

The Audit Office
Te Tari Whakamatau, Arotake

Annual Report
for the year ended 30 June 2001

Presented to the House of Representatives pursuant to
section 37 of the Public Audit Act 2001 and section 39 of
the Public Finance Act 1989





Rt Hon Jonathan Hunt
Speaker
House of Representatives
WELLINGTON

Mr Speaker

This report has been prepared pursuant to the requirements of section 37 of the Public Audit Act 2001 and section 39 of the Public Finance Act 1989. It covers the operations of the Audit Office for the year ended 30 June 2001.

Yours sincerely

A handwritten signature in blue ink, reading 'D J D Macdonald'.

D J D Macdonald
Controller and Auditor-General

Wellington
21 September 2001



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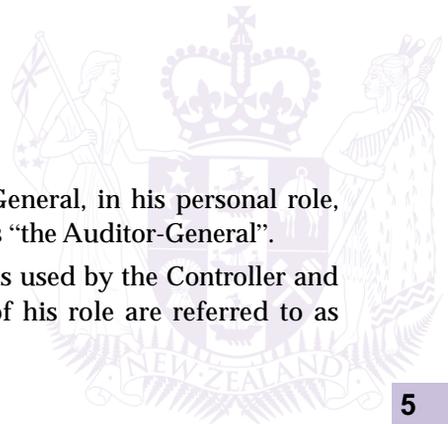
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Note on Terminology

Throughout this report:

- The Controller and Auditor-General, in his personal role, is usually referred to simply as “the Auditor-General”.
- The organisation and resources used by the Controller and Auditor-General in pursuit of his role are referred to as “the Audit Office”.





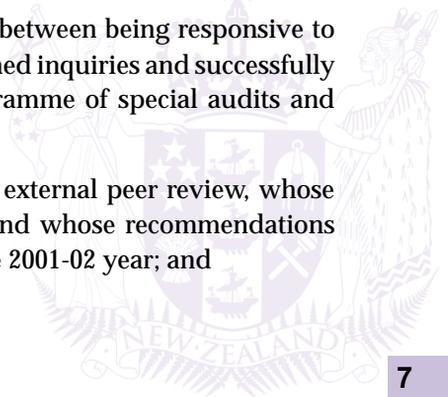
The Year in Review



I have much pleasure in presenting our report on the Audit Office's performance for the 2000-01 financial year.

I am pleased to be able to report positively on all of the issues which I identified last year as high on my list of things to achieve. In particular the Office:

- maintained high levels of productivity – publishing 12 substantive reports, and completing 4,007 annual audits;
- assisted with the passage into law of the Public Audit Act 2001, and began to implement the consequent changes;
- maintained a suitable balance between being responsive to increasing demand for unplanned inquiries and successfully completing our planned programme of special audits and studies;
- successfully commissioned an external peer review, whose findings were very positive, and whose recommendations we will be responding to in the 2001-02 year; and



- improved our capability – particularly in the area of knowledge management, but also through identifying more accurately our future needs and beginning to take steps towards meeting those needs.

Public Reports

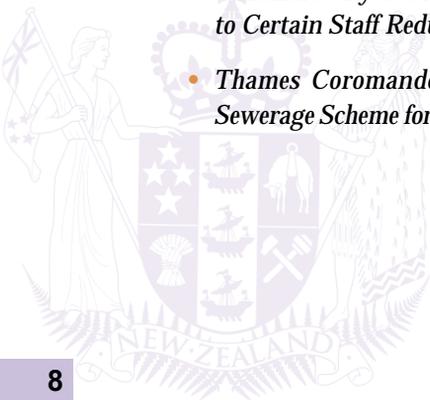
Highlights			
	2001	2000	1999
Number of public reports	12	13	10
Cost (\$000)	2,339	2,342	2,558

Once again we had a busy and successful year. We produced 12 substantive public reports – covering the results of annual audits, planned special audits and unplanned special investigations. One report achieved a particularly high public profile – *Members of Parliament: Accommodation Allowances for Living in Wellington – Interim Report* (March 2001).

Responding to Local Concerns

We produced three public reports during 2001, and numerous reports to individual Councils, on significant local issues raised during the year. Most of these identified issues which the Councils needed to address. The three public reports were:

- *Auckland City Council's Management of its Responsibilities in the Hauraki Gulf* (October 2000);
- *Waitakere City Council: Payments and Associated Issues Relating to Certain Staff Redundancies* (October 2000); and
- *Thames Coromandel District Council: Actions Relating to a Sewerage Scheme for Cooks Beach and Ferry Landing* (June 2001).



Governance Issues

We continued to encourage the Executive, select committees and various other groups to debate and implement our previously published reports on governance issues such as *Governance Issues in Crown Entities* (November 1996) and *The Accountability of Executive Government to Parliament* (June 1999).

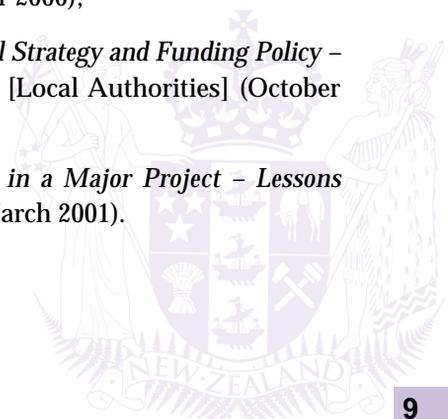
It is disappointing that the Government's initiative to produce new legislation for Crown entities has been given lower priority this year. However, it is pleasing that the State Services Commission and the Treasury have been making good progress on addressing the "capability" and "outcome reporting" issues we raised in *The Accountability of Executive Government to Parliament*.

In respect of the Local Government sector, we produced a major report entitled *Local Authority Governance of Subsidiary Entities* (March 2001). This report canvasses a range of both general and specific governance issues in local government – such as governance of trusts, commercial trading enterprises, and major service entities such as Infrastructure Auckland. The report makes a number of recommendations on roles and responsibilities, structures, and monitoring and accountability arrangements.

Supporting Better Practice

We produced three reports aimed at providing positive guidance to particular sectors of our audit portfolio:

- *Auditing a Long-term Financial Strategy – Opotiki District Council Pilot Project* (September 2000);
- *Reviewing a Long-term Financial Strategy and Funding Policy – Experiences of the “Early Nine”* [Local Authorities] (October 2000); and
- *Good Practice for Involvement in a Major Project – Lessons from the Opuha Dam Project* (March 2001).



Two further “good practice” reports were circulated widely in draft during the year, and published early in 2001-02:

- *Reporting Public Sector Performance* (July 2001); and
- *Procurement: A Statement of Good Practice* (draft published on our web site, July 2001).

Although most of these reports used “live” case studies, our primary aim was to provide “good practice” guidance for entities embarking on similar projects in the future.

Emphasising Environmental Issues

We continued to give emphasis to environmental issues. We published a report entitled *Meeting International Environmental Obligations* in May 2001, which examined New Zealand’s approach to four significant international environmental agreements it is party to. These agreements related to the ozone layer, wetlands, trade in endangered species, and climate change.

Reporting Audit Results and Sectoral Issues

Each year we produce compendium reports, primarily summarising the results of financial statement audits in the Central Government and Local Government sectors. In 2000-01, these were published in December 2000 and June 2001 respectively, and covered a wide range of issues.

Highlights of the reports included questions about the Supplementary Estimates process which had taken place in 1999-2000, and a follow-up report on the Papakura District Council’s management and monitoring of its water and wastewater franchise.

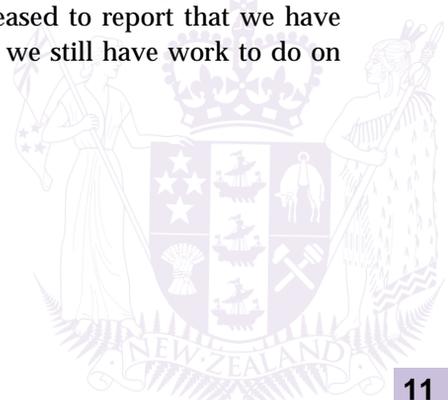


Financial Statement Audits

Highlights			
	2001	2000	1999
Audits completed	4,007	4,272	3,960
Audit costs (\$m)	31.362	30.407	29.014
Timeliness of audit reports (excluding schools)	68%	61%	62%
Timeliness of management reports	95%	88%	86%
Audits outstanding at year end	395	646	1,038

Our public reports provide the visible side of our activity. However, about 85% of what we do relates to financial audits of the more than 3,700 public sector organisations that we audit. I am again pleased to report that the arrears situation for these audits has significantly improved. Audits outstanding have reduced from 646 to 395, an improvement of 643 on two years ago. This is the result of strenuous efforts over the last two years (on the part of auditors in the field and staff in the Office of the Auditor-General) to encourage entities to produce their statements in a more timely manner, and then to complete the audits.

The timeliness of work has improved dramatically in the last year. I noted in last year's annual report my intention to take steps to improve performance in the timely issue of audit management letters, and am pleased to report that we have been successful here. However, we still have work to do on timeliness of audit reports.



Achieving Our Goals

Highlights

- 4 audit tender rounds successfully completed.
- Peer review of the Audit Office completed in March 2001.
- Public Audit Act 2001 passed in April 2001.

Part 2 of this report details our performance in achieving the three goals we set ourselves for 2000-01. Items that deserve special mention here are:

Continuing to Deliver Excellent Audit Services

As already mentioned, we were particularly successful in making major improvements in the problem areas of “audit arrears” and the timely issue of audit reports and management letters.

We aim to carry out quality assurance reviews of each Approved Auditor’s performance once during their three-year contract period. We remain on target to achieve this coverage. Our reviews found that, generally, work was of a good quality. For the few exceptions, we took appropriate follow-up action.

We continued to place emphasis on communicating effectively with those interested in our work. We gave numerous briefings to select committees and other audiences on our reports, and also began considering how we can better evaluate the impact of the reports.

Adjusting to Reflect our Changing Environment

Obtaining and processing intelligence about developments in the public sector is a core part of our business. This year, we put special effort into:

- developing our relationships with central agencies;

- understanding the impact of “E-Government”, both generally on the public sector and specifically on audit requirements; and
- beginning a project to enable auditors to report to us electronically.

Leading by Example

We continue to try to demonstrate best practice as a public entity in the areas of performance, financial management and accountability. Highlights for the year were:

- We continued with our policy of exposing a significant part of our audit portfolio to competitive tendering. Four tender rounds were held this year – resulting in 4 tenders being won by Audit New Zealand, 10 by private sector auditing firms, and 106 entities electing to renegotiate with their existing audit service provider.
- We take seriously the proposition that, to lead by example, we must practice what we preach. This year, we undertook a systematic review of our own processes in relation to relevant reports we have issued over the last decade. We identified some minor areas for reconsideration of our processes in the areas of telephone use, fraud policy, and asset disposal policies.
- We continued to develop processes for measuring our own outcomes, and we report on some of these measures in this report.
- The Public Audit Act 2001 was enacted on 6 April 2001 and came into force on 1 July 2001. This marked the completion of a process of debate and reform which had lasted since the late 1980s. Since the Bill was introduced, a lot of work has been done to prepare for its implementation – as it extends both the portfolio of entities we audit and our mandate in those entities. In the current financial year we will publish auditing standards under the Act, finalise arrangements for the audits of entities newly added to our portfolio, and undertake some work under our extended mandate.

- In February-March 2001, member officers of the Australasian Council of Auditors-General undertook a peer review of our activities. I am very pleased that the overall findings present the Office in an excellent light and we are committed to responding positively to the review findings and recommendations.

Management Performance

Highlights

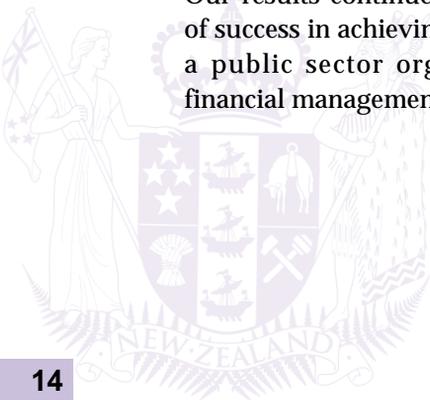
- We achieved a surplus of \$351,000 on total spending of \$35,543,000.
- Output Class D3 was overspent by \$277,000.
- The OAG developed capability action plans.
- Audit New Zealand implemented computer-assisted audit support tools.

Part Three of the report highlights our performance under the headings of:

- financial performance; and
- human resources.

It then discusses how the two business units of the Office – the Office of the Auditor-General (OAG) and Audit New Zealand – have met their respective key objectives for 2000-01 as set out in our Forecast Report.

Our results continue to demonstrate an encouraging degree of success in achieving our goal of being a leading example of a public sector organisation in terms of performance, financial management and accountability.



Financial Performance

We achieved a surplus of \$351,000, compared with a forecast surplus of \$237,000.

We incurred unappropriated expenditure of \$277,000 in Output Class D3 – Non-contested Audit Services. This was because costs associated with the audits of public reserves, cemeteries, and the disestablishment of health entities were under-budgeted, and indirect costs were higher than budget because of lower-than-forecast activity in Output Class D4, which lead to Output Class D3 having to carry a higher burden of indirect or overhead costs. The unappropriated expenditure was funded by revenue from third parties, and so did not result in any cost to the Crown.

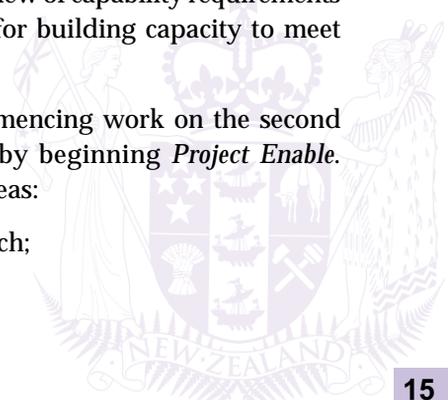
In recent years we have successfully managed within static appropriations for the discretionary part of our business (Output Class 1). However, this has placed increasing strain on the Office, and we have not always been able to achieve all we planned or have been asked to do.

We approached the Officers of Parliament Committee with a new business plan late last year. The plan successfully sought additional funding to help us satisfy the increasing demands from Parliament and external enquirers, and the impact of increased responsibilities under the Public Audit Act 2001.

Human Resources

In the past year we continued our development of human resource and professional development policies and practices. Major areas of emphasis were:

- for the OAG, undertaking a review of capability requirements and agreeing to action plans for building capacity to meet future needs;
- for Audit New Zealand, commencing work on the second phase of its people strategy by beginning *Project Enable*. This project focuses on four areas:
 - refocusing the audit approach;
 - reshaping the business;



- improving business processes; and
- leading change in culture, competencies and behaviour.

Staff turnover in both the OAG and Audit New Zealand increased this year to 17.8% and 25.9% respectively. The increases reflect an increasingly competitive market for skilled and experienced staff and are of particular concern to Audit New Zealand. Audit New Zealand is developing strategies to address and cope with this level of turnover.

While overall staff turnover has been high, I am pleased to report that there was no turnover at senior levels in either the OAG or Audit New Zealand during the year.

OAG Management Objectives

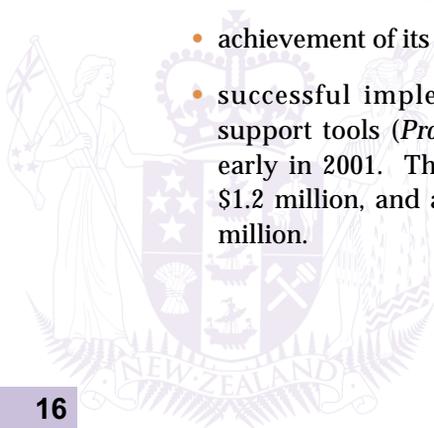
The OAG has reported against its six key management and development objectives set out in the Forecast Report. Highlights not covered above include:

- beginning to work with the new sub-committee of the Finance and Expenditure Committee on consideration of our reports; and
- further development of our knowledge management systems, including beginning work on exchanging information with our audit service providers electronically.

Audit New Zealand Management Objectives

Audit New Zealand has also reported against its five key management and development objectives as set out in the Forecast Report. Highlights not covered above include:

- achievement of its surplus target; and
- successful implementation of computer-based audit support tools (*Project Assist*) on time and within budget, early in 2001. This was funded by a capital injection of \$1.2 million, and a reduction in the surplus target of \$0.8 million.



Input to Public Sector Accounting and Auditing Development

The Office continues to play a leading role in the development of public sector accounting and auditing standards – both in New Zealand and internationally.

This year has again been a busy one. Highlights include:

- Continuing participation by one of my Assistant Auditors-General, Kevin Simpkins, as New Zealand's representative on the Public Sector Committee of the International Federation of Accountants.
- Continuing participation in international working groups on environmental auditing and the development of accounting standards.
- Continuing duties as Secretary of the South Pacific Association of Supreme Audit Institutions (SPASAI).
- Continuing participation of senior staff in the technical committees of the Institute of Chartered Accountants of New Zealand.

In addition, I attended the second meeting of the Auditors-General Global Working Group in Washington in February 2001. This working group was set up to promote informal dialogue among the Auditors-General of a small number of countries facing similar issues and challenges. New Zealand will host the next meeting in February 2002.

Looking Forward to 2001-02

The following issues – which are set out in detail in the Office's *Forecast Report 2001-2002* – are high on my list of things to achieve before my term of office expires in late-April 2002:

- implementing the portfolio and mandate changes that came into force when our new legislation was enacted;
- responding to the recommendations of the external peer review of the Office conducted in February-March 2001; and

- maintaining the high productivity of the Office while ensuring that our capability is maintained and enhanced, and in particular ensuring that the additional funding received by the Office is effectively used.

Appreciation

Finally, I thank my Deputy, Assistant Auditors-General, Directors of Audit New Zealand and the OAG and all my staff for their hard work and dedication in contributing to what I believe has been another particularly successful year for the Office.



Part One

About the Audit Office



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Purpose, Role and Outcomes of the Audit Office

Purpose

The Audit Office exists as a constitutional safeguard to maintain the financial integrity of New Zealand's parliamentary system of government.

The Audit Office plays a key part in the system of checks and balances between Parliament and public entities:

- Public entities (as defined in section 5 of the Public Audit Act 2001) are *accountable* to Parliament and to other constituencies for their use of the resources and powers conferred by Parliament.
- The Audit Office provides *assurance* to Parliament and to other constituencies that the entities are operating, and accounting for their performance, in a manner consistent with Parliament's intentions. We also seek to foster *improvement* in their performance and accountability.

The Audit Office, as an Office of Parliament, is *independent* of the Executive Branch of Government.



Desired Outcomes

If the Audit Office has done a good job:

- Parliament and the public will be *confident* that public entities:
 - are delivering what they have been asked to;
 - have operated lawfully and honestly, and have not been wasteful;
 - have fairly reported their performance;and know that, if this is not the case, we will tell them.
- The Government and public entities will effect *improvements* in public sector performance and accountability in areas where we have advised that there is potential for improvement.



Outputs

The Audit Office provides assurance through:

Parliamentary and Public Reports –

Which contain those matters arising from audits that warrant the attention of Parliament or other constituencies.

Controller Certifications –

Which ensure that funds released from the Crown Bank Account are for purposes consistent with Parliament's intentions.

Audit and Assurance Reports –

Which express an opinion on the financial statements and results of the audit of over 3,700 public entries, and also provide further assurance on aspects of management performance at the request of the entities.

Flowing from the conduct of audits, the Audit Office provides advice to:

Parliamentary select committees
Taxpayers and ratepayers
The Government
Audited entities
Related professional bodies



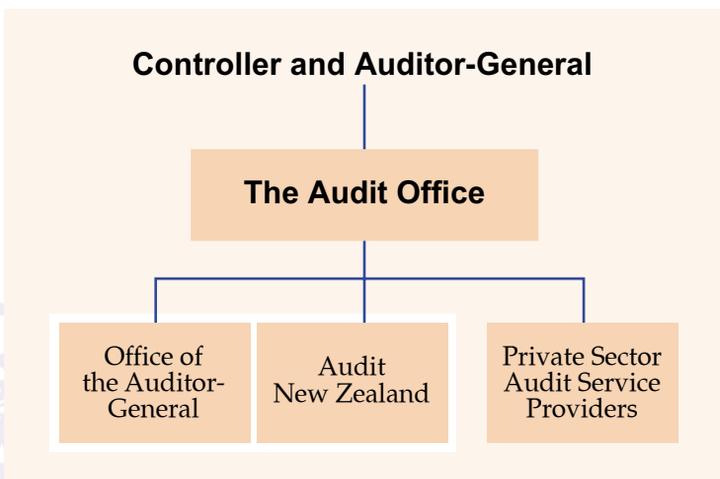
Organisational Arrangements

The Controller and Auditor-General is a corporation sole established by section 10(1) of the Public Audit Act 2001, and is an Office of Parliament for the purposes of the Public Finance Act 1989.

To plan, conduct and report on the results of over 3,700 audits each year, the Controller and Auditor-General has three major sources of assistance: two internal business units (the Office of the Auditor-General and Audit New Zealand) and private sector auditing firms.

“The Audit Office” is the term used in this report to refer to the whole of these resources and activities. It includes the Controller and Auditor-General as a person, and all those authorised by the Controller and Auditor-General to carry out any particular function, duty or power.

*Figure 1
Organisation of the Audit Office*



The roles of the two internal business units are as follows:

The Office of the Auditor-General¹ –

Is responsible for providing strategic audit planning, setting standards, determining who will undertake audits, overseeing auditor performance, carrying out special audits and studies, and parliamentary reporting and advice.

Audit New Zealand –

Carries out audits that it has won the right to conduct on behalf of the Auditor-General in competition with private sector auditors, as well as those audits not awarded under the contestable audit arrangements, and offers additional assurance services to public entities.

Because of the potential conflict between the Auditor-General's purchase interest and his ownership responsibilities, an advisory board for Audit New Zealand assists him in discharging those responsibilities. The board comprises three non-executive directors and is responsible for:

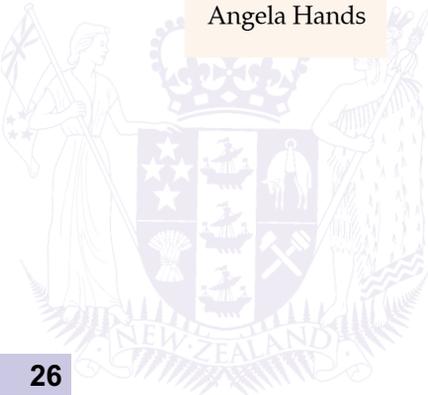
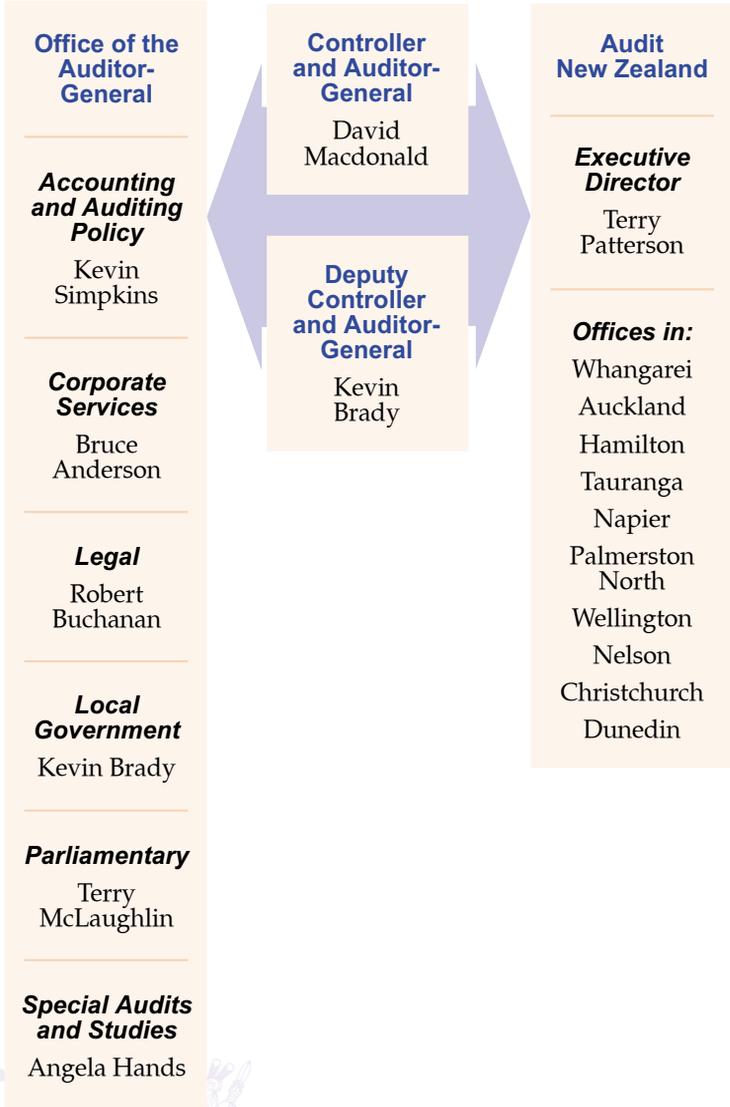
- endorsing a strategic focus for Audit New Zealand's business, and a business plan which is consistent with this focus; and
- monitoring service delivery against the plan.

The Auditor-General approves the plan annually, and the advisory board periodically reports to him on progress against the plan.

1 Usually abbreviated to "OAG" in the rest of this report.



Figure 2
Management Structure



Part Two

Achievement of Goals



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Part Two of our *Forecast Report 2000-2001* set out our three goals for the year and the strategies we considered appropriate for achieving those goals.² This part of this report describes what we achieved.

Goal 1: Continuing to Deliver Excellent Audit Services

Strategy 1. *We will continue to plan and conduct all audits professionally, and having regard to the full mandate of the Office.*

Auditing Standards

The *OAG Auditing Standards* consist of the Institute of Chartered Accountants of New Zealand (ICANZ) Auditing Standards and Audit Guidance Statements, supplemented by the Audit Office Statements and Specific Standards (where an ICANZ standard does not exist). The *OAG Auditing Standards* establish the minimum standards to be applied to annual audits conducted on behalf of the Audit Office.

During the year, we completed the process of aligning the Audit Office's standards with the ICANZ standards. This was achieved when we issued OAG Statement 208: *Consideration of Laws and Regulations in an Audit* in September 2000.

² Parliamentary paper B.28FR(00), pages 18-19.

Training and Support for Our Auditors

Manual for Audit Service Providers

Our primary vehicle for formally communicating with Appointed Auditors³ is our *Manual for Audit Service Providers*. The *Manual* was first published in 1993 and includes:

- background information to assist auditors;
- the *OAG Auditing Standards*; and
- annual audit plans (known as “audit briefs”) issued by the Auditor-General for all major sectors, together with sector information where appropriate.

The *Manual* also contains guidance for auditors in the form of statements of general policy on matters that, for example, affect entities in more than one sector or are unique to the public sector. Audit Service Providers contribute to these statements by reporting issues that they encounter during audits, and raising issues at periodic Technical Forum meetings.

We have undertaken significant development towards providing access to the *Manual* in electronic form in the 2001-02 year.

Support for Audit Service Providers

During 2000-01 we continued to provide advice and support to Appointed Auditors – both individually on request and collectively – on a range of accounting and auditing issues. We conducted 7 seminars for school auditors throughout the country and eight special seminars for auditors undertaking local government audits. Towards the end of the year we also presented five seminars on the Public Audit Act 2001.

3 An “Appointed Auditor” under section 32 or section 33 of the Public Audit Act 2001 is the person appointed to be in charge of and responsible for all aspects of a particular audit. An “Audit Service Provider” – either Audit New Zealand or a private sector auditing firm – supplies the staffing resources and the audit methodology that the Appointed Auditor needs to use.

We keep in touch with Appointed Auditors in a less formal way through a periodic newsletter - *The Watchdog* – four editions of which were published in 2000-01. Extracts from issues of *The Watchdog* can be seen on our web site (www.oag.govt.nz).

Reviewing Our Auditors' Performance

We aim to review each Appointed Auditor's performance once during their three-year contract period. Follow-up reviews may be initiated if we identify a need for improvement.

Our quality assurance programme:

- focuses on ensuring that auditors fulfil the requirements of the *OAG Auditing Standards* and relevant audit briefs;
- is part of the continuous improvement programme within the OAG; and
- provides feedback to our policy, sector, and technical managers.

We undertake desk reviews of audit files, and also visit Appointed Auditors in their offices to:

- review the systems they have developed to ensure compliance with the standards set; and
- review working paper files for evidence of compliance with those standards.

During 2000-01 we proposed to review the quality of the work of 50 Appointed Auditors, and we achieved this target (1999-2000: 50 reviews). Our 2001-02 target has been set at 45 reviews, which is a sufficient number to ensure that we achieve our desired coverage.

We visited 41 auditors (1999-2000: 38 visits) to review their work, and we conducted desk reviews on a further 9 auditors (1999-2000: 12 desk reviews) involved primarily in the audit of schools. Consistent with previous years, the work we reviewed was, with only a few exceptions, of good quality. For the exceptions, we took appropriate follow-up action.

ACHIEVEMENT OF GOALS

Goal 1: Continuing to Deliver Excellent Audit Services

Another way of reviewing the quality of auditor performance is in the process of issuing a non-standard audit report.⁴ If an Appointed Auditor is considering modifying the audit report because of a major issue (for example, where there are doubts that the going concern assumption is appropriate), they submit the matter to the OAG, stating the grounds for the proposed modification. Forty-seven such submissions were made and responded to during the year (1999-2000: 53). Overall, the quality of the submissions was sound.

Strategy 2: *We will continue to target our audits at critical areas of performance and accountability in the public sector.*

Strategic Audit Plans

Information to prepare a strategic audit plan for each broad sector group is gathered from the results of previous audits, developments in different parts of the public sector, changes in legislation, and other environmental factors. In 2000-01, we supplemented this information with formal papers on environmental and E-Government issues.

The plans cover a period of three years, and are updated annually. They are subject to internal critical review so that priorities can be determined – given the limited resources we have available to do discretionary work. Planned and likely projects are published annually in our *Forecast Report*, for scrutiny by parliamentarians and other interested stakeholders. From next year a draft annual plan, containing material from the strategic audit plans, must be submitted to the Speaker for consideration by the House of Representatives before it is finalised.

⁴ Non-standard audit reports are those where the auditor has:

- qualified the audit opinion due to a disagreement or a limitation on scope;
- drawn attention to a breach of law; or
- drawn attention to a fundamental uncertainty.

In all special audit projects we identified the skills needed and, where appropriate, made use of advisers to ensure that specialist skills were available to the team undertaking the project. This is especially important during both the planning and the report-drafting stages of a project.

In the Local Government sector, as in previous years, we consulted widely with individual councils, sector groups and a number of organisations with an interest in local government. We analysed the issues raised through consultation as well as the complaints that have been brought to our attention, to ensure we have focused on areas where we are able to add the greatest benefit by our audit work in the sector. Our strategic audit plan was also subject to review by the Auditor-General's Local Government Advisory Group.

Audits of Annual Financial Statements

Some 85% of our work relates to conducting audits of annual financial statements. Elements of that audit programme are subject to explicit direction by way of audit briefs issued by the Auditor-General.

The prime objective of each audit is to perform the work necessary to form an opinion and issue an audit report on the financial statements. In addition, however, audit briefs may identify matters of particular interest which the Approved Auditor is required to look into and report back on. Typical examples of matters we looked at during 2000-01 were:

- Central Government –
 - compliance with Cabinet expenditure delegations;
 - departmental reporting on “Closing the Gaps”; and
 - managing employee fraud.
- Local Government –
 - sale and lease of land;
 - review of long-term financial strategies and funding policies;
 - Councils' reporting on changes to plans and policies.

Special Audits and Studies

Apart from any additional coverage required as part of the annual financial statement audits, we develop a programme of special audits and studies from our office-wide and sector strategic audit planning processes.

The Crown funds the costs of special audits and studies. The results are reported either in one of our general reports to Parliament⁵ or in a separate report (which is usually also presented to the House).

The areas we focused on in 2000-01 are set out on pages 39-47.

Strategy 3: *We will place particular emphasis on completing all audits that we are required to perform.*

Audits Completed

We completed 4,007 audits of public sector entities in 2000-01. This figure compares well with the excellent result of 4,272 completed in the previous year, and enabled us to make another significant reduction in the number of audits outstanding.

Audit reports and management letters have also been issued in a more timely way – in most sectors and overall.

The tables on page 107 for Output Class D3 and page 112 for Output Class D4 show the results on a sector basis.

⁵ Those bearing the shoulder number series B.29.

Audits Outstanding

During 2000-01 we continued to put a lot of effort into reducing the number of audits outstanding, building on the work done in previous years.

We reduced the number of audits outstanding from 646 to 395 during the year. Often, the audits outstanding are not within our control, because the entity has not produced financial statements for audit. However, following the work done in 1999, 2000 and 2001 to persuade entities to produce financial statements, there has been a significant reduction in the number of audits outstanding this year.

The outstanding audits were made up as shown in Figure 3 below:

Figure 3
Audits Outstanding

	Audits Outstanding As at 30 June	
	2001	2000
Major Statutory Bodies	6	15
Other Local Authorities	38	92
School Boards of Trustees	153	112
Miscellaneous Public Bodies	74	158
Audits without fees	124	269
TOTAL	395	646

The reduction in the audits outstanding over the last four years is shown in Figure 4 on the next page, and the status of non-school audits which were outstanding at 30 June 2001 is shown in Figure 5 also on the next page.

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Goal 1: Continuing to Deliver Excellent Audit Services

*Figure 4
History of Audits Outstanding*

	30 June 2001	30 June 2000	30 June 1999	30 June 1998
Schools	153	112	255	376
Other entities	242	534	783	881
TOTAL	395	646	1,038	1,257

*Figure 5
Status of Non-school Audits Outstanding*

Sector	Audits Outstanding ¹	Financial Statements:		
		Provided to Auditors ²	Expected soon ³	Not provided ⁴
Government Departments and Officers of Parliament	-	-	-	-
Major Statutory Bodies	6	5	1	-
Regional, City and District Councils	-	-	-	-
Other Local Authorities	38	15	23	-
Miscellaneous Public Bodies	74	54	20	-
Audits without fees	124	61	43	20
TOTAL	242	135	87	20

1 These figures exclude the 153 school audits currently outstanding, which make up the total arrears of 395 audits. The school audits outstanding comprise mainly 31 December 2000 audits plus the financial statements of some Schools which closed in earlier years.

2 These figures comprise instances where the financial statements have been made available to the Appointed Auditors. Some of them have been provided, and some of the audits have been completed, since 30 June 2001.

3 These figures comprise instances where we are in contact with the entities and expect the financial statements to be made available shortly.

4 Despite all our efforts, there are 4 entities where we have been unsuccessful in obtaining financial statements relating to a number of years. In some instances, we have been unable to make contact with those responsible for the governance of the entities. Parliament needs to be aware of the names of these entities. We have also passed this information on to the responsible Government department.

Entities Which have Failed to Provide Financial Statements for Audit

The entities which have failed to provide financial statements for audit are:

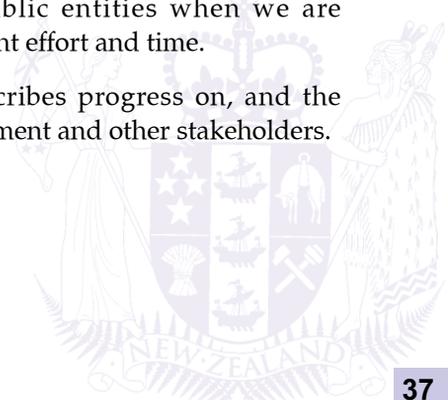
- Bunnythorpe Cemetery Trustees for the 5 years ended 31 March 1996, 1997, 1998, 1999 and 2000;
- Charleston Goldfields Hall Board for the 5 years ended 30 June 1996, 1997, 1998, 1999 and 2000;
- Okuru Hall Board for the 2 years ended 30 June 1999 and 2000; and
- Oparure Public Hall Board for the 8 years ended 30 June 1993, 1994, 1995, 1996, 1997, 1998, 1999 and 2000.

Strategy 4: *We will place particular emphasis on communicating effectively with those who have a key interest in the results of our work.*

Emphasis on Communication

We place great emphasis on effective communication with our various audiences. Liaison arrangements with stakeholders (such as select committees, individual enquirers, and sector groups), and operating on a professional “no surprises” basis with public entities when we are reporting on them, take significant effort and time.

This section of the report describes progress on, and the contents of, our reports to Parliament and other stakeholders.



Annual Audits

Government Departments, Crown Entities and State-owned Enterprises

The results of our audits of the 1999-2000 financial statements of the Government and of government departments were reported in our report *Central Government: Results of the 1999-2000 Audits*.⁶ That report also contained the results of the following audit examinations carried out during 1999-2000:

- Compliance with Cabinet Expenditure Delegations;
- Departmental Reporting on “Closing the Gaps”;
- Managing Employee Fraud;
- Funding Arrangements with Non-government Organisations;
- Disclosing Fiscal Risks on Defence Capital Projects;
- Student Loan Debt; and
- The Supplementary Estimates for 1999-2000.

Local Government

The results of our audits of the 1999-2000 financial statements of regional and territorial local authorities were reported to Parliament in our report *Local Government: Results of the 1999-2000 Audits*.⁷ That report also contained the results of other audit examinations carried out, or issues identified, during the 1999-2000 audits:

- Management of and Accounting for Infrastructural Assets;
- Setting Operating Revenues to Cover Operating Expenses;
- Timeliness of Annual Reporting;
- Legal Compliance;
- Separate Properties and Rating Apportionments;

⁶ Parliamentary paper B.29[00c], December 2000.

⁷ Parliamentary paper B29[01a], June 2001.

- Reporting Chief Executive Officer Remuneration;
- Reporting Severance Payments;
- Competing with the Private Sector;
- Defamation Costs;
- The Local Authorities (Members' Interests) Act 1968 – Discussing and Voting When Interested;
- Long-term Contracts for Services; and
- Papakura District Council – Managing and Monitoring the Water and Wastewater Franchise.

Special Audits and Studies

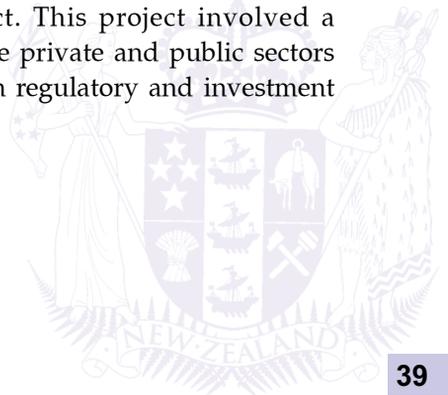
We completed work from our Forecast Reports for 2000-01 and earlier years in the following areas:

Long-Term Financial Strategies in Local Government

We undertook a pilot project to audit the long-term financial strategy of the Opotiki District Council and separately reported on that task. The methodology developed for the pilot project was also tested with the Western Bay of Plenty District Council. We also reviewed the experiences of six other councils to enable us to share them with the rest of the Local Government sector.

Good Practice for Involvement in a Major Project (Opuha Dam)

The purpose of our review of the Opuha Dam project was to see what messages for good practice we could find by looking at a large scale project. This project involved a number of entities from both the private and public sectors and their interests included both regulatory and investment interests.



Local Authority Governance of Subsidiary Entities

We reviewed the governance arrangements for subsidiary entities with a number of councils. The purpose of the study was to identify and analyse current and emerging issues about how local authorities govern their subsidiary entities. We also highlighted the risks when governance arrangements do not work effectively, and recommended and illustrated good practice for proper accountability and effective governance.

Meeting International Environmental Obligations

We selected four specific multilateral environmental agreements to report on whether Crown resources used to implement government policy on the four agreements had been applied effectively to meet New Zealand's obligations. We set out what we considered to be the key elements for successful implementation of, and ongoing compliance with, the obligations. We also commented on the quality of reporting to Parliament about the agreements.

Civil Aviation Safety Audits

We completed a follow-up audit on our 1997 audit of the Civil Aviation Authority's (CAA's) conduct of safety audits of operators in the civil aviation industry.

We noted that the CAA had made some progress in identifying high risk areas and improving the quality of safety audits. However, we identified areas in the CAA's operations that need to be addressed if the CAA is to play a full part in improving New Zealand's air safety performance.

Franchising of Water Services in Papakura

In 1998 we published a report on our review of the franchising agreement the Papakura District Council had entered into with United Water International Pty Limited to operate the water and wastewater services within the Papakura district. During 2000 we carried out a follow-up audit to look at how the Council had managed and monitored the franchise agreement and whether any of the issues we had raised in our 1998 report remained a matter for concern.

We also responded to a range of requests from a number of stakeholders in the public sector, including Ministers of the Crown and Members of Parliament:

Auckland City Council: Administration of the Gulf Islands

In February 2000 Mr Owen Jennings MP presented to the House a number of documents relating to Auckland City Council and its dealings with the residents of Great Barrier and Waiheke Islands. We conducted an inquiry to ascertain whether the Auckland City Council had complied with its statutory responsibilities, and its own policies, in its administration of the Islands of the Hauraki Gulf.

Staff Redundancies at Waitakere City Council

During August 1997 to September 1999 a number of employees of the Waitakere City Council had been made redundant. We reviewed the redundancy payments to ascertain whether the payments and the processes were appropriate.

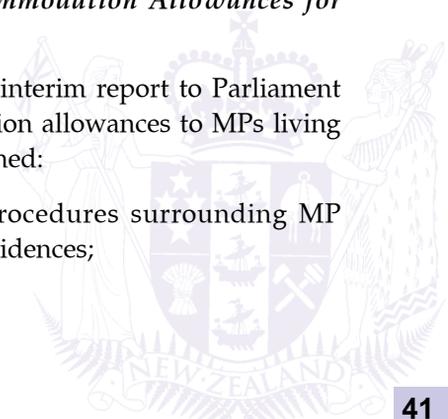
A Sewerage Scheme in Thames Coromandel District

We reviewed the manner in which the Council resolved to undertake a sewerage reticulation project to service properties at Cooks Beach and Ferry Landing. We reported our views on whether the Council had complied with the legislative requirement and whether the views of ratepayers on the sewerage options were adequately sought.

Members of Parliament: Accommodation Allowances for Living in Wellington

In March 2001 we provided an interim report to Parliament on the payment of accommodation allowances to MPs living in Wellington. The report examined:

- the systems, policies and procedures surrounding MP allowances and Ministerial residences;



- the eligibility of Ms Marian Hobbs MP and Ms Phillida Bunkle MP for the Wellington accommodation allowance; and
- the allocation of a Ministerial residence to Ms Bunkle.

We presented a final report on parliamentary salaries, allowances and other entitlements to Parliament in July 2001. The final report set out our detailed recommendations as to how the system surrounding MP entitlements can be improved.

We made good progress on the following areas indicated in our *Forecast Report 2000-2001*:

Police Clearance of Property Crime

The particular category of property crime selected for study was burglaries from residential dwellings. This form of offending is of significant concern to the public and comprises about one in ten of all recorded offences. The Police have made burglary one of their priority areas and successive governments have provided them with additional resources to tackle the problem. The study looks at different approaches being used in different Police districts, with a particular focus on the quality of performance information and the evaluation of effectiveness. The study was complete by the end of the 2000-01 year, and a report will be tabled in the House in September 2001.

Providing and Caring for School Property (referred to in the Forecast Report as “Property Management in the Education Sector”)

State-owned school property is one of the Crown’s largest capital investments and it is important that the investment is well managed. This study considers the Ministry of Education’s performance in managing the property portfolio. We focused on the management arrangements in place between the Ministry and school Boards of Trustees, the processes for funding capital works and the processes for ensuring that school property is adequately maintained. The study was undertaken at a time when the Ministry of Education was introducing new planning processes and a new

capital funding framework for school property, and our report will also comment on the new system and the benefits it aims to achieve. This report will also be tabled in the House in September 2001.

Contracting Arrangements for Primary Healthcare

The field work for this study is complete, and will be shaped into a report which will be useful for District Health Boards, the Minister and Ministry of Health, and the Health Select Committee. It will report on:

- arrangements for the funding, purchasing and monitoring of primary health care;
- the changing structural arrangements in the sector; and
- lessons learned from a range of contracting arrangements undertaken by the Health Funding Authority and its predecessors, the Regional Health Authorities.

Preparedness for the Deployment in East Timor

Field work has been completed on this study, our report on which will be published later this year. It examines the preparedness of the New Zealand Defence Force for the first part of the multinational deployment known as INTERFET. The study covers the period from early 1999 to February 2000, when the INTERFET phase was replaced by the United Nations Transitional Administration. The study assesses whether the Defence Force met its stated capability requirements in practice, including:

- planning effectively for a possible military operation; and
- assembling and deploying a force which would enable it to carry out its assigned mission, in accordance with the Government's objectives.

A second study is considering in detail the operations of two elements of the deployed force – helicopters and the medical unit. This study will provide information about the impact of deployment on these particular force elements, and their sustainability.

Biosecurity Risk Management (referred to in the Forecast Report as “Border Control”)

This study is looking at how MAF manages biosecurity risks. The study focuses on procedures and policies in place to prevent biosecurity breaches and how MAF applies risk analysis to determine the conditions on which animals and goods can enter New Zealand. Our report on this study will contain a number of case studies illustrating MAF’s policies and procedures in practice. Case studies are likely to include Foot and Mouth disease, the Varroa Bee Mite, the Southern Saltmarsh Mosquito, the Glassy Winged Sharp Shooter and the Red Imported Fire Ant.

We also made good progress on a number of studies not foreshadowed in our *Forecast Report 2000-2001*:

Reporting Public Sector Performance

Late in 1999 we began a follow-up study to *The Accountability of Executive Government to Parliament*⁸, focusing on performance reporting in the public sector as a whole. This study describes the current situation and suggests future directions for non-financial reporting to stakeholders. The report was issued in July 2001⁹, and includes practical advice for entities or individuals being required to produce performance reports, as well as more general advice on the way forward.

Military Purchasing: Light Armoured Vehicles and Light Operational Vehicles

We began this inquiry late in 2000 at the request of the Secretary for Defence, and our report was published in August 2001. It examines the acquisition process followed for the purchase of the Light Armoured Vehicles, and the process being used for the purchase of the Light Operational Vehicles. It makes recommendations for improvements in these processes.

8 Parliamentary paper B.29[99c], June 1999.

9 ISBN 0 477 02877 2.

Procurement: A Statement of Good Practice

During the year we updated the good practice guidelines for purchasing that we had originally published in 1995. The new guidelines cover a wider range of public sector purchasing activities, and include commentary on current issues such as syndicated procurement, outsourcing, and E-procurement. The report is now available in draft form on our web site (www.oag.govt.nz).

Governance, Risk Management and Legislative Issues in the New Zealand Fire Service

We made substantial progress in this study in 2000. However, there have been delays, and we now plan to report later in 2001. The proposed study initially encompassed other subject areas, including long-term financial planning, treasury management, and fleet management in the Service. We expect to cover these subjects in a subsequent report.

Relationships between Local Authority Chief Executives and their Councils

For some time we have been concerned about the relationships between Chief Executives and their Councils. The local government environment has changed since our 1994 report on these issues. We are therefore surveying all Chief Executives and Mayors/Chairpersons and a number of Councillors to update our knowledge of the environment and provide guidance to the sector on how relationships can be better established.

Speed Cameras

We commenced an audit of New Zealand's speed camera programme. The study is focusing on management and operation of the programme, and looks at:

- the selection of speed camera sites;
- how the Police allocate speed cameras to particular sites;
- whether the Police undertake regular evaluations of the programme;

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- whether speed camera technology is operated in a manner which maximises effectiveness; and
- enforcement of speed camera fines.

The audit team also proposes to compare New Zealand's programme with those operating in Victoria and Queensland, with a view to making recommendations based on "best practice".

We have made limited progress on, or do not intend to pursue, the following areas indicated in our *Forecast Report 2000-2001*:

Custodial Sentence Administration

The Department of Corrections is implementing a new system of Integrated Offender Management that changes fundamentally its approach to the administration of custodial sentences. The Department believes that this new approach will achieve a reduction in re-offending rates. The process of implementation is taking longer than originally expected, and is currently not scheduled to be completed before the end of the 2001-02 year. We have therefore discontinued work on the study. We will review the position when the new system has been fully implemented.

Capability in the Public Sector

The OAG maintained its representation on the Capability, Accountability and Performance (CAP) project sponsored by the SSC. This project has involved five public sector departments – and the SSC itself – in examining different methods of capability assessment and developing more comprehensive and better quality departmental reporting. In addition, the Office began preliminary work on scoping a study of strategic human resource capability in the public sector.

Robustness of Forecasts for Demand-Driven Output Classes

We have not been able to make progress on this subject because of resource constraints. However, it remains an area for future study, with progress being dependent on available resources and other competing priorities.

Accuracy of Social Security Benefit Payments Taxpayer Audit Activity in the Inland Revenue Department

These project proposals have been included in our 2001-02 programme and work has commenced on researching and scoping the first of them. We did not make progress earlier because of other priorities.

Licensing and Enforcement of the Commercial Transport Industry

Some preliminary scoping work was undertaken in 2000 for a range of studies in the licensing and enforcement area of commercial transport. This work was replaced by the study on Speed Cameras referred to above.

Monitoring of Effectiveness for Maori

During 1998-99, we reported to the House on our suggested audit model for testing the capability of departments for delivering effective outcomes for Maori. In 1999-2000, we began work on applying this model to the State Services Commission, and we are considering the most effective way to make further progress.

Governance and Risk Issues in Crown Entities

Preparedness for Emergency Management

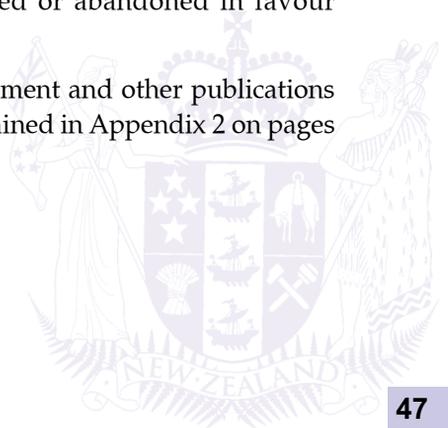
Crown Management of Treaty Settlements

The Use of Benefit-Cost Analysis in Government Investment Decisions

Service Delivery in Government Departments

These studies have been deferred or abandoned in favour of other priorities.

A full list of our reports to Parliament and other publications produced during the year is contained in Appendix 2 on pages 139-140.



Goal 2: Adjusting to Reflect our Changing Environment

Strategy 1. *We will maintain sound awareness of developments and changes in the public sector.*

The Local Government and Parliamentary Groups in the OAG obtain and process a large amount of intelligence about developments and changes in the public sector, from public entities and from our field auditors, as a core part of their business. This intelligence forms the basis for our strategic audit planning process, referred to earlier in this report. The Auditor-General's Local Government Advisory Group also provides us with an excellent sounding board for developments in that sector.

In 2000-01, we complemented this ongoing effort by:

- putting further effort into developing relationships with central agencies;
- maintaining involvement in the SSC's Capability, Accountability and Performance project;
- setting up an in-house "E-government" group, to provide intelligence on developments in this area; and
- developing an inventory of our private sector contacts, to ensure that we remain aware of relevant developments.

Strategy 2. *We will improve our mechanisms for learning as an organisation.*

The new initiatives identified above provide additional intelligence, but this is only raw material. In order to improve our mechanisms for learning, we have also undertaken a number of initiatives in the OAG and Audit New Zealand, including:

- implementation of computerised audit working papers, which both reduce paper documentation and approve accessibility of audit information;
- making good progress on projects to improve Approved Auditor access to key information obtained by the OAG (the database of audits and the *Manual*);
- beginning a project to obtain returns from auditors electronically, rather than in paper form; and
- in the OAG, doing further development work on our intranet and our electronic document management system, and developing action plans on how to improve our capacity for innovation and learning.



Strategy 3. *We will undertake projects targeted at increasing our understanding of specific areas or issues in the public sector, and at developing suitable audit products for the changing needs of the sector.*

During 2000-01, we developed and considered a number of internal issues papers in pursuit of this strategy, on the following subjects:

- the impact of developments in information and communications technology on the public sector, and on the auditing profession;
- probity, and the audit of probity in the public sector; and
- forensic auditing (this was completed after the end of the year).

The OAG will continue to develop a small number of issues papers in these and similar areas each year.



Goal 3: Leading by Example

Strategy 1. *We will fulfil a leadership role where it is appropriate to do so, particularly in the development of public sector accountability arrangements and performance reporting.*

During 2000-01, we pursued this strategy in a number of ways:

- by undertaking speaking engagements on a range of subjects in a range of forums, particularly on general accountability arrangements, the development of public sector performance reporting, and the impact of the new Public Audit Act;
- by liaising with our national and international peers and professional organisations; and
- by completing a major study on Public Sector Performance Reporting (published in July 2001).

We receive a wide range of visitors from countries who have an interest in New Zealand public sector reform, particularly our legislative, accountability and audit arrangements. We have also expanded our links with Australia, contributing to a number of forums on financial management and local government.

We have continued our involvement as a member of the INTOSAI Environmental Audit Committee, participated in an ASOSAI regional workshop on environmental auditing held in China, and continued to administer the SPASAI training programme funded by the Asian Development Bank and the International Development Initiative of INTOSAI.

The Contestable Audit Policy

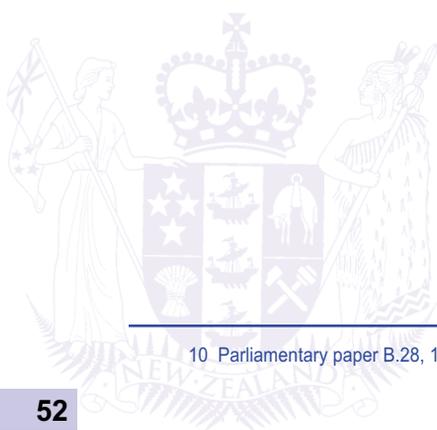
Another way in which we try to lead by example is through our policy of exposing a significant part of our audit portfolio to competitive tendering. Entities comprising approximately 89% (by audit hours) of the portfolio have now been invited to participate in the contestability arrangements.

The contestable audit policy means that audits are carried out by Appointed Auditors from either:

- **Audit New Zealand**, which is the auditing business unit of the Audit Office, and operates under a combination of a purchase agreement for some audit services and individual contracts for specific audits; or
- **private sector auditing firms**, which are contracted by the Auditor-General to conduct specific audits on behalf of the Audit Office.

As at 30 June 2001, 145 individual Appointed Auditors from 74 private sector firms and Audit New Zealand were conducting audits and signing audit reports on behalf of the Auditor-General. Of these, 67 Appointed Auditors and 56 firms audit only schools or other small organisations.

We gave a full description of the tendering and contracting process in our 1996-97 *Annual Report*.¹⁰ Figure 6 on page 54 of this report illustrates the process leading to appointment of an Appointed Auditor, and Figure 7 on page 55 illustrates the post-appointment procedures applying to an audit.



¹⁰ Parliamentary paper B.28, 1997, pages 41-45.

Continuing the Implementation of the Contestable Audit Engagement Policy

We have recently written to further entities inviting them to participate in the contestable audit policy by December 2001. Their responses will enable us to plan tenders having regard to:

- the market;
- the ability of appropriate tenderers to meet the volume of requests for tenders; and
- the stability of individual entities.

We have held back invitations to some selected groups of entities, pending events such as the completion of structural changes in the Health sector. In a very small number of cases, we have also held back invitations as a result of ownership considerations, where the Auditor-General believed that Audit New Zealand would be unreasonably at risk of losing critical mass in a sector, subject, or geographical area if they lost the audit.

In addition, we do not intend to offer the opportunity of a contestable audit to:

- some small entities where the costs of tendering are so high in relation to the audit fee as to outweigh any benefit; and
- a small group of entities where we require very high level security clearance of all staff, and where audit staff may be privy to information of major national economic or strategic significance.

We have discussed these matters with all the affected entities.

With the above exceptions, and subject to unforeseen matters requiring revision in individual cases, the contestable audit policy will be fully implemented by December 2001. Before June 2002, we will complete an impact evaluation of the contestability regime, in order to brief the incoming Auditor-General.

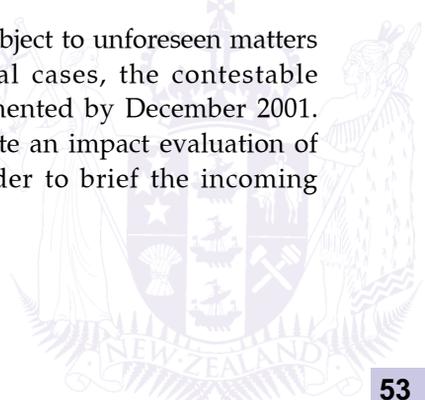


Figure 6
The Audit Tender Process

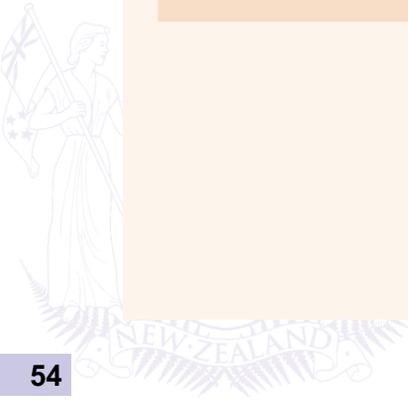
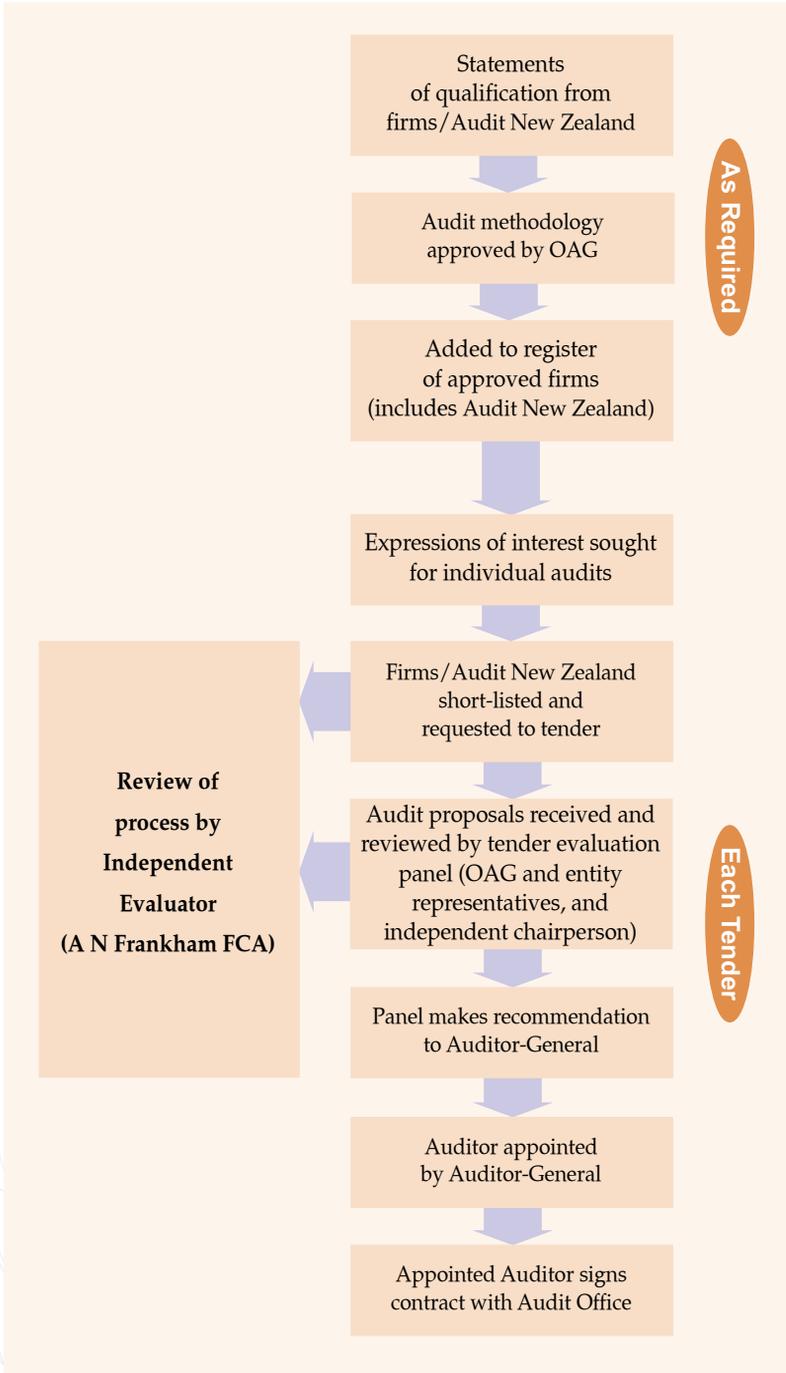
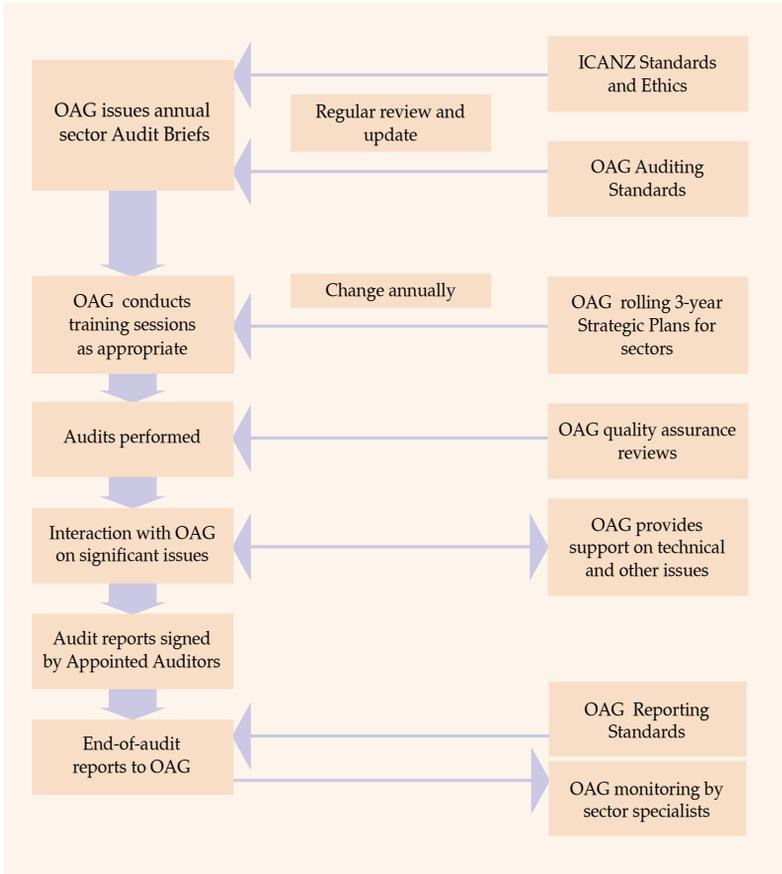


Figure 7
The Conduct of Audits



Tender Rounds Completed in 2000-01

During 2000-01 we made new or renewed audit arrangements for a wide range of entities within our mandate which have been subject to the contestable audit process for some years, and had the option this year of again participating in a tender. In addition, tenders were conducted for 3 entities that had not previously been invited to participate in a tender, and for 11 entities that had already been included in the contestable audit process.

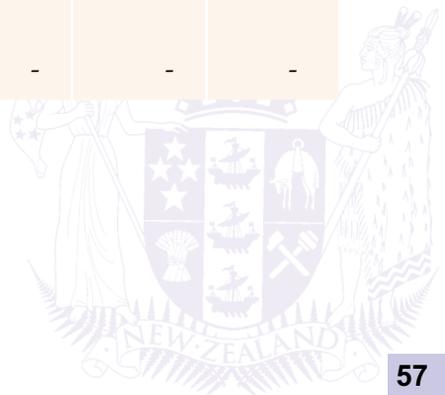
A total of 120 entities were invited to participate in tenders. Of those, 106 elected to negotiate terms for a three-year contract with their current audit service provider, rather than subjecting their audit to a tender process. In our view, that result continues to indicate a sufficiently high level of satisfaction with the service provided by our audit service providers – and with the competitiveness of fees proposed in negotiations for renewal of contracts.

The new and renewed audit arrangements were achieved through four projects. The results are set out in Figure 8 on the opposite page.



Figure 8
Audit Tender Outcomes 2000-2001

Tender Timing	Renegotiated	Tendered	Tender Outcomes	
			Audit New Zealand	Other
June 2000 - September 2000 <i>Universities</i>	-	2	1	1
September 2000 - February 2001 <i>Energy Companies, Local Authorities, Crown Entities, Government Departments, Crown Companies</i>	35	10	3	7
March 2001 - June 2001 <i>Government Departments, Polytechnics, Port Company</i>	9	2	-	2
June 2000 - November 2000 <i>A wide range of entities with audit contracts due for renewal, that chose to negotiate with existing auditors</i>	62	-	-	-



Report of the Independent Evaluator

Mr Anthony N Frankham FCA has continued to act as an independent evaluator to assist in ensuring that any tendering performed by the Audit Office is seen to be rigorous, objective, and unbiased. Mr Frankham's summary report on the integrity of the process for the four tender rounds completed during the year is reproduced below.

A N T H O N Y N F R A N K H A M



Chartered Accountants

Associate
Brendan Lyne

23 July 2001

The Controller and Auditor-General
PO Box 3928
Wellington

Annual Report of the Independent Reviewer of Audit Tender Processes

1. You have retained me as an independent evaluator of the processes for tendering audits by the Office of the Auditor-General ("OAG"). I confirm that I am independent of the OAG and Audit New Zealand and the other tendering audit firms. My terms of reference are to evaluate the audit tender processes established and implemented and report on their probity and objectivity. I have reported in the past on eight tender bid rounds and on specific processes relating to the tender of school audits.
2. Since my report dated 6 July 2000 I have undertaken further independent reviews of the policies and processes adopted during the period and followed by the OAG. I have reviewed further groups of audit tenders involving a range of statutory bodies, SOEs, energy companies, CRIs, government departments, crown entities and TLAs. My review has involved the consideration of existing and emerging policies and their implementation. I have had discussions with you and your staff and with the independent panel chairs. I have reviewed reports of the panels that have met and have made recommendations to you. I have not considered it necessary to participate in all panel meetings to observe the process in operation. No limitation has been placed on the manner in which I carry out my assignment.
3. In my opinion the policies for awarding audit assignments to the delegates of the Auditor-General and renewal of existing contracts over the period to the date of this report dealt with by the documentation I have examined and the process I have observed, were fair and appropriate having regard to:
 - The objectives of the contestability arrangements
 - The experience of previous tender rounds
 - The rights, interests and obligations of the parties involved.
4. I have reported separately to the OAG on specific matters which have arisen or been referred for my attention during the period. None of these matters relate to issues which cause me to alter the view I express in this report.
5. I have kept you informed of all matters coming to my attention where I consider there were elements of sensitivity or processes or behaviours that were challenged or may have given rise to challenge. There have been no changes in policy or process during the period coming to my attention from my review that I consider should have been subject to your further review.

Yours faithfully

(Anthony N Frankham)

LEVEL 7 TOWER 2 SHORTLAND CENTRE SHORTLAND ST AUCKLAND 1 NEW ZEALAND
P.O. BOX 701 AUCKLAND 1 DX CP20505 TELEPHONE 09 300 5800 FAX 09 300 5805

Strategies 2 and 3: *We will continue to practise what we preach to others, and we will operate under a philosophy of continuous improvement.*

We take seriously the proposition that, to lead by example, we must practise what we preach.

This year, we undertook a systematic review of our own processes in relation to relevant reports we have issued over the last decade. We identified seven recently issued reports which we thought might have particular relevance to us, and did a careful assessment of our practices in relation to them. We identified some minor areas for reconsideration of our processes, in the areas of use of telephones, fraud policy (OAG only), and asset disposal policies (Audit New Zealand only). In the first half of 2001-02, we will reassess our processes in the light of these findings.

We continually look for ways to improve our performance – both externally and internally – and to report on our activities in a comprehensive and open manner.

The information contained in this report presents a succinct picture of the performance targets we set ourselves for the year, and the extent to which we met those targets. We have exceeded some targets (such as the number of reports prepared, and reduction in audit arrears), and some we have not met (such as the timeliness of audit reports, and promptness in clearing enquiries). Generally, we have met or exceeded most of our targets for the year, and have improved on the prior year in almost all areas.



Strategy 4: *We will place additional emphasis on measuring and reporting achievement of our goals and desired outcomes.*

A core part of our role is advocacy of improved measurement and reporting of results by public entities. With the intention of trying to lead by example, in 1999-2000 we began to develop new measures of our achievements and our capability as an Office. We identified a possible series of measures and, in our *Forecast Report 2000-2001*¹¹, committed to reporting on some or all of them at the end of the 2000-01 financial year. The results of work to date, including some direct measurement of outcomes, are set out below:

- *Surveying stakeholder assurance and confidence:* As stakeholders' interests are variable and complex, and assurance is also a complex concept, we decided that there was little information value in broad-based surveys of stakeholders at this stage. We developed initial specifications for the use of focus groups – to tell us what assurance meant to them, and how the Audit Office contributes to this. During 2001-02 we will undertake a trial using at least two focus groups with professional facilitators, one on the general issue of “assurance” and one on the assurance given by specific reports or products. We will also do further work on systematising the results of the liaison discussions we have with stakeholders.
- *Select Committee use of our material:* A desirable outcome for the Audit Office is that Select Committees use the briefing material we provide to them – not only to review public entities, but also to report and recommend to the Government. We successfully piloted an approach to measuring these outcomes during the year, and found that they were measurable, internally useful, and externally reportable. The actual result of our six pilots was an average 70% uptake of issues raised by the Audit Office

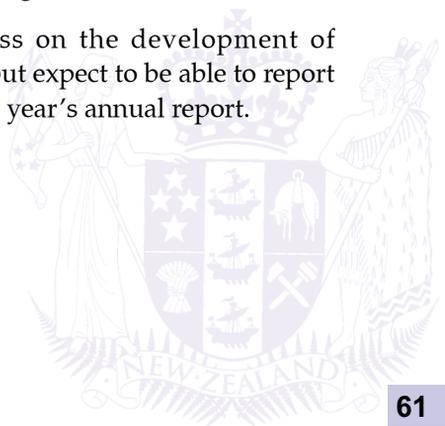
11 Parliamentary paper B.28FR(00).

in Select Committee reports, with a range of 56% to 88%. We believe that, initially, this is a reasonable range to expect. We will undertake independent assessments of 40 briefings during 2001-02, and plan to publish the results in next year's Annual Report.

- **Outcomes of annual audits:** We designed an approach to assessing (although not yet measuring) the effects that our annual audits have – namely, the recommendations that are implemented, the changes in financial practice that result, and the outcomes in terms of more effective and efficient use of public money. We piloted this on a small number of audits, and will extend the pilot in 2001-02 to about 20 audits. We plan to report on these in next year's Annual Report.
- **Outcomes of special audits and studies:** We identified numerous ways of assessing the impacts of studies, and we developed a template which has now been adopted for all special audits and studies. This template helps us to consider information that needs to be collected, the processes that need to be used, and the follow-up required, to help assess the impact the study has had.
- We also made some progress on improving the five “management aspects” which we use to report on financial management performance in the central government and crown sector, and on the more general research question of how to measure outcomes in terms of the legislative audit model enshrined in the Public Audit Act 2001.

During the year, we also analysed the outcomes of audits in terms of the types of audit reports issued. The results of this analysis are summarised on page 108.

We made only limited progress on the development of measures of capability and risk, but expect to be able to report on the results of this work in next year's annual report.



Strategy 5: *We will be suitably prepared for the coming into force of the revised legislative mandate for the Auditor-General.*

The Public Audit Act 2001 was enacted on 6 April 2001, and came into force on 1 July 2001. This marked the completion of a process of debate and reform which had lasted since the late 1980s. Obviously, the passage of the Act was a very significant event for the Office.

The Act achieves three objectives:

1. Both the Controller and Auditor-General and the Deputy Controller and Auditor-General become Officers of Parliament. The Act confirms their independence and redefines their constitutional relationship with Parliament.
2. The Audit Department, which previously existed to provide staff and administrative services to the Audit Office, has been abolished. The Auditor-General is established as a corporation sole and an Office of Parliament.
3. The law relating to the audit of public sector organisations is modernised and updated. In particular:
 - the range of entities subject to public audit is defined in a single provision – previously the Auditor-General’s portfolio was defined by more than 80 different statutes; and
 - the public auditing mandate is set out in a comprehensive and accessible way and applied consistently across the portfolio.

A lot of work is being done to prepare for the new era, some of which was completed by 30 June 2001 and some of which is still in progress. The work includes:

- comprehensively reviewing the portfolio on a “before and after” basis;

- incorporating the full auditing mandate into our strategic audit planning processes;
- developing internal policies to underpin the functions and powers which the Act confers;
- revising our *Manual* and our contracts with Approved Auditors;
- preparing the first publication containing the auditing standards to be used for audits and inquiries under the Act;
- instituting a staff training programme and a series of seminars for audit service providers; and
- completing arrangements for transfer of the Audit Department's assets from the Crown to the Auditor-General as a corporation sole.

As we signalled in last year's annual report, our three-year business plan was rewritten to take account of the operational implications of the Act for the Office. We presented our revised plan to the Finance and Expenditure and Officers of Parliament Committees in late November 2000. The plan included proposals for additional funding – not only to take account of the extension of our mandate under the Act but also to deal with other unresolved issues, such as the impact of increased demand, the cost of audits for which no fees were payable, and the Office's seasonal cashflow problem. In the 2001-02 Estimates round, the Officers of Parliament Committee approved significant new funding for the Office, comprising:

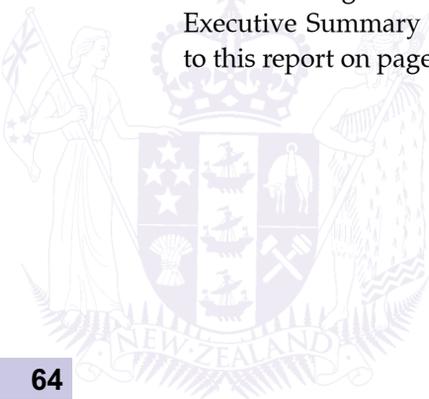
- an additional \$175,000 per annum to cope with increased demand;
- an additional \$700,000 per annum (\$350,000 in 2001-02) to undertake additional performance audits in the Crown sector;
- an additional \$100,000 per annum as a contribution towards audits for which fees were not payable; and
- formally setting Audit New Zealand's annual surplus target at 1% of revenue (approximately \$200,000) compared with the previous, informal target of 2-3%.

The increased activity under the Act will occur on a graduated basis over the next 18 months. The new definition of “public entity” (which defines the Auditor-General’s portfolio) and the wider public auditing mandate (including the power to do performance audits and conduct inquiries) apply from 1 July 2001. However, the duty to undertake financial report audits applies only to balance dates which occur on or after that date.

Strategy 6: *We will successfully commission, and respond to the findings of, an external peer review.*

In February-March 2001, at our request, member offices of the Australasian Council of Auditors-General undertook a peer review of our activities. The four review team members were from the Western Australia, Victoria and New South Wales State Auditors-General’s Offices and the Australian National Audit Office. They spent two weeks reviewing both the Office of the Auditor-General and Audit New Zealand. Their comprehensive report and our responses have been presented to the Officers of Parliament Committee and the Finance and Expenditure Committee for their information and consideration, and are available on our web site (www.oag.govt.nz).

The overall findings present the Office in an excellent light and we are committed to responding positively to the review findings and recommendations. The Introduction and Executive Summary sections of the report are in Appendix 3 to this report on pages 141-151.



Strategy 7: *We will maintain a capability which delivers excellent administrative, corporate and technical support to the Office.*

No major initiatives were undertaken during this year under this strategy.

The Corporate Services area of the OAG undertook a benchmarking exercise early in the year, which identified a number of good practice areas and some areas where improvements could be made. The suggestions made as a result of the benchmarking exercise have been built into our plans for development for the 2001-02 year.

In Audit New Zealand, *Project Enable* is reviewing business processes, including support functions, and the results of the review are being considered during 2001-02.



Part Three

Management Performance



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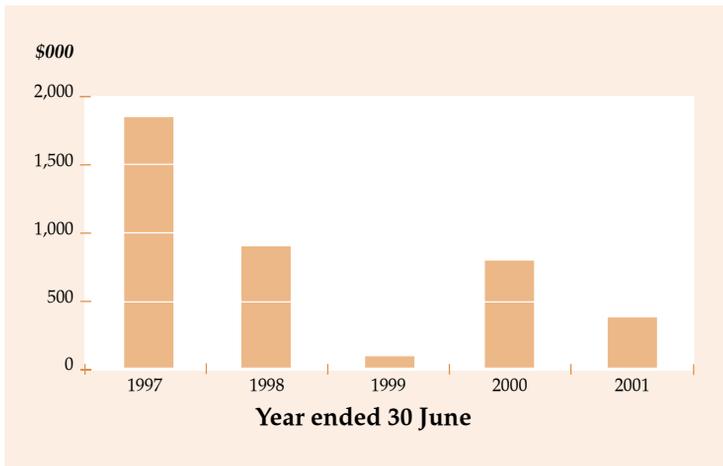
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Financial Performance

Surplus

A surplus of \$351,000 has been achieved for the year. The graph shows how this result compares with the operating results for previous years. The main contributor to this year's surplus is Audit New Zealand's achievement of its surplus target of \$181,000 (actual result \$193,000).

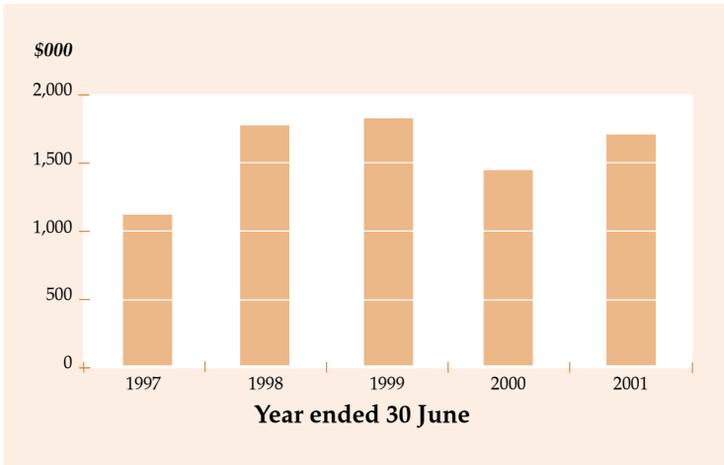
Operating Surplus 1997-2001



Working Capital

This year we have continued to maintain our year-end working capital level. While payables outstanding are higher than last year, the increase is offset by an improved cash position at 30 June 2001 resulting from an active campaign to improve our collection of accounts receivable. This improvement also helped us manage the working capital difficulties we experience in the second half of every year as a result of highly seasonal cashflows. We expect to have finalised new arrangements for managing these seasonal cashflows before 2002.

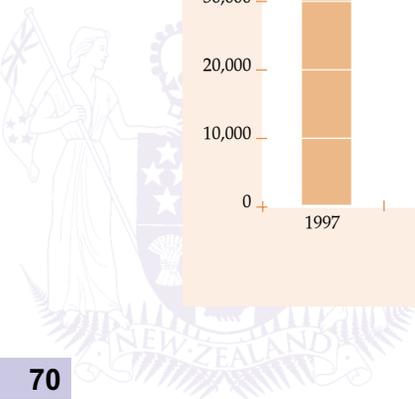
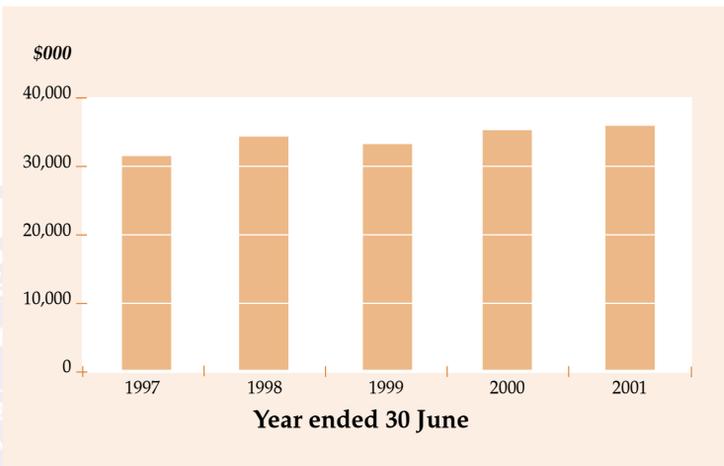
Working Capital 1997-2001



Expenditure

The expenditure out-turn on the Vote (see page 125) shows that total output expenditure at \$35.543 million is 95.9% of the estimate, and compares with \$34.599 million in 1999-2000. One of the four output classes, D3 – Non-contested Audit Services, is overspent for the financial year, for the reasons given on page 126.

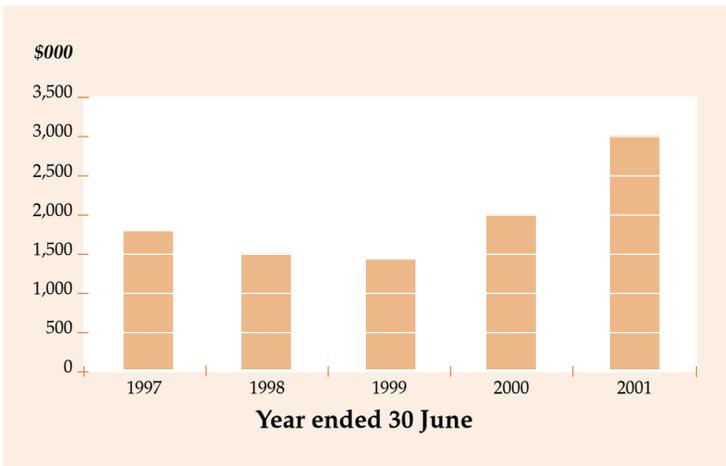
Operating Expenses 1997-2001



Financial Position

The level of physical assets has increased by \$1,046,000, representing the net result of additions, disposals and depreciation expense during the year. The major addition to physical assets was the purchase and implementation of computer-based audit support tools for Audit New Zealand. This increase was funded by a capital injection of \$1.2 million from the Crown.

Physical Assets 1997-2001



Human Resources

Good Employer Requirements

Clause 9 of Schedule 3 to the Public Audit Act 2001 requires the Auditor-General to operate policies that comply with the principle of being a “good employer”. Such policies must provide for the fair and proper treatment of employees in all aspects of their employment.

We continue to strive for ways to improve our human resources policies and practices.

Developing and Implementing Sound Professional Development Policies and Practices

During the year we continued to focus on the professional development of staff. This included:

- Helping staff to meet the membership requirements of the Institute of Chartered Accountants of New Zealand by continuing Audit New Zealand’s professional development programme. This programme ensures that Audit New Zealand fulfils its obligations as an Approved Training Organisation.
- Running formal study programmes, providing training relevant to an individual’s needs, giving on-the-job coaching, and organising in-house courses to meet the business and professional requirements of the OAG and Audit New Zealand. Specific learning initiatives developed for Audit New Zealand staff have included:
 - a customised assessment process for management which incorporates 360-degree feedback on leadership and client relationship skills;
 - a leadership enablement programme for senior management;

- strategic management development for targeted senior staff; and
- a revised graduate induction programme.
- Creating secondment opportunities for staff within the Office to enhance their knowledge and experience outside of their normal job requirements. Secondment opportunities have also been created with Audit Offices in the United Kingdom, Canada, Australia and Thailand.
- Sending one senior staff member of the OAG to a senior management development course, and another to participate in the Management Development Centre's "Centre for Individual Management Development".

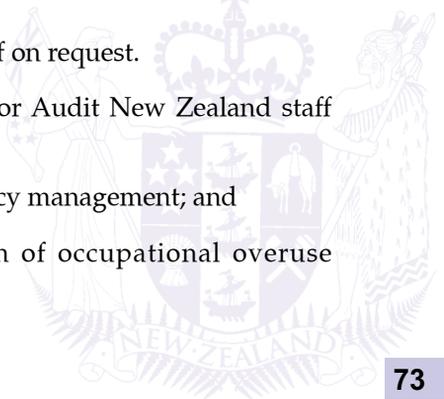
Continuing to Improve the Working Environment of our Employees

The Audit Office is required by the Health and Safety in Employment Act 1992 to safeguard the health and well-being of all staff and visitors to the Office. During the year we have continued to:

- develop programmes and equipment to help ensure the safety of employees should a civil defence emergency or bomb alert occur;
- identify any hazards within our premises;
- develop effective emergency plans;
- replace old furniture with ergonomically designed furniture;
- provide a confidential Employee Assistance Programme to all staff; and
- provide flu vaccinations to staff on request.

We have implemented training for Audit New Zealand staff in areas of:

- disaster recovery and emergency management; and
- management and prevention of occupational overuse syndrome (OOS).



Audit New Zealand has also revised its health and safety procedures.

We continue to apply family-friendly work practices.

Continuing to Encourage Diversity Within Our Organisation

We recognise that understanding and knowledge of different perspectives enhance the performance of our employees and hence of the Office. We are endeavouring to achieve this through:

- complying with the Human Rights Act 1993 and the New Zealand Bill of Rights Act 1990;
- ensuring that all employees have equal access to employment opportunities;
- continuing to operate a Maori scholarship programme; and
- continuing to operate a Pacific Island scholarship programme.

Four students were awarded scholarships during the year.

We are continuing to review our Maori responsiveness strategy and will be identifying key initiatives to be introduced during the next twelve months.



Figure 9
Composition of Staff by Gender

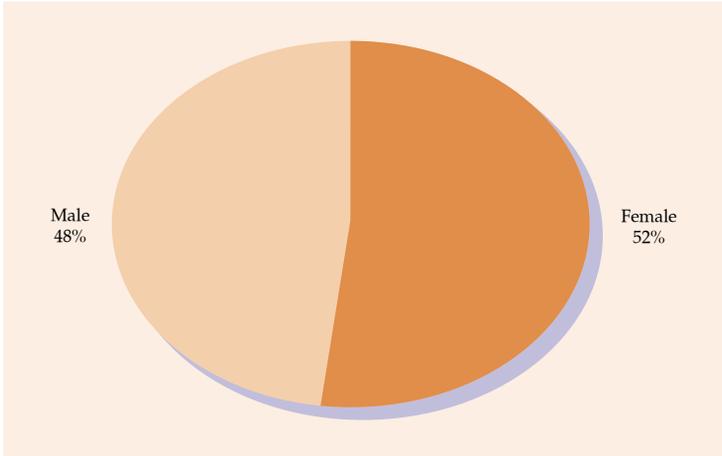
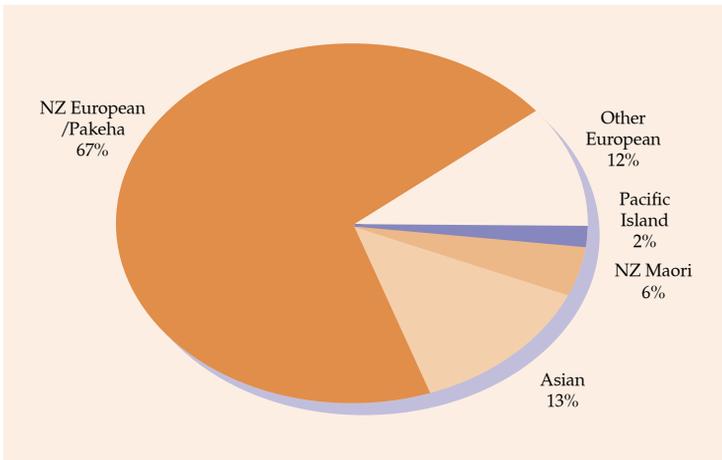


Figure 10
Composition of Staff by Ethnicity



Ensuring Our Human Resource Policies Support the Achievement of Our Objectives

We are continuing to improve our human resources policies and practices so that these support the achievement of our corporate objectives. In particular, this year we have:

- continued to ensure that our performance management and remuneration policies and practices reflect accepted benchmark practices;
- continued to review our recruitment, retention and reward systems so that we are able to attract and retain the skilled staff needed to meet the business needs of the entities we audit;
- implemented internal procedures for dealing with Protected Disclosures;
- reviewed the OAG's Human Resources activities against external benchmark practices;
- reviewed the OAG's policy on flexible work arrangements;
- reviewed Audit New Zealand's HR management procedures to ensure their alignment with strategic direction and legislative requirements; and
- undertaken a project to review the OAG's capability. This project identified ways in which the OAG could maintain its capacity to deliver outputs and results, and identify and cope with future requirements. Action will be taken in the following areas:
 - skill requirements;
 - recruitment;
 - operating systems;
 - staff training;
 - performance management; and
 - general management.

Operational Capacity

Total staff numbers of 271 full time equivalents (FTEs) at 30 June 2001 were 2.9% less than the 279 at 30 June 2000. Staff turnover within the OAG has increased from 12.4% in 1999-2000 to 17.8% in 2000-01, and in Audit New Zealand from 23.4% to 25.9%.

This increase in staff turnover reflects an increasingly competitive employment market for skilled and experienced audit staff. While the effect on the OAG has been limited so far, Audit New Zealand, in common with many accounting firms, is having some difficulty maintaining its level of staff capability.

Figure 11
Staff Numbers (FTEs) 1997-2001

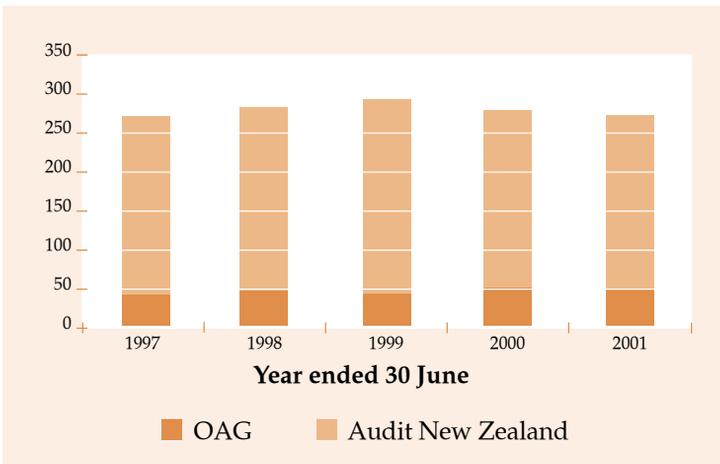
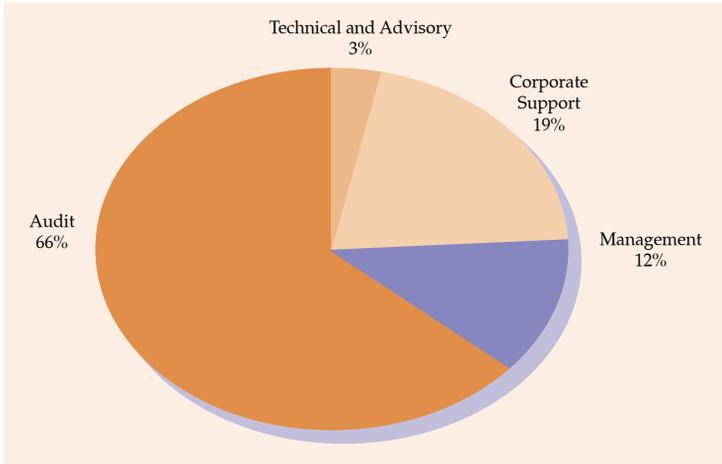


Figure 12
Composition of Staff by Function



Office of the Auditor-General

The major development area for the OAG this year was preparation for, and implementation of, the Public Audit Act. Associated with this was development of a new business plan, and obtaining increased funding. Our six key management and development objectives for 2000-01 were set out in the Office's *Forecast Report*.¹² Four of them have been discussed in Part Two of this report:

- being ready to implement the Public Audit Act (pages 62-64);
- continuing to develop the Office's overall strategic processes, including improving measurement of our outcomes, capability and risk (pages 48-50 and pages 60-61);
- continuing to reduce the backlog of audits (pages 35-36); and
- successfully commissioning an external peer review (page 64).

We report on the two remaining objectives below:

Objective 3:

Communicating more effectively with Parliamentarians.

The Finance and Expenditure Committee sub-committee has met once to consider our report *Central Government: Results of the 1999-2000 Audits*. We intend to provide six-monthly reports to the sub-committee in the future in order for them to consider the status of our reports – for example, whether they had been considered by other Committees or have received a government response.

¹² Parliamentary paper B.28FR(00), pages 30-34.

Other Committees have also had briefings on our reports tabled in the 2000-01 year, including *Meeting International Environmental Obligations*, *Civil Aviation Authority Safety Audits*, and the results of Central and Local Government annual audits.

Objective 5:

Continue to develop our knowledge management systems.

This year has seen a number of our systems consolidated and some new developments begin.

We are consolidating on and building up our use of Silent One, which is our Electronic Document Management System (EDMS), and our Intranet (CAGNet). Particular developments included:

- implementing a linked, web-based database of precedents to support advice given to auditors (the Technical Advice Register);
- moving our internal Policy and Procedures Manual into Silent One, for easier access;
- improving the ability of OAG staff to obtain remote access to Silent One; and
- beginning to develop CAGNet as a management tool, which will have home-pages and key performance indicators.

The new developments that have begun are particularly focused on our commitment to work electronically with our business partners, in particular our contracted auditors:

- **Audit Status Database (ASD) OnLine:** The ASD OnLine is a web-based interface for our contracted auditors and their teams to input data from the annual audits they conduct on our behalf.

Specification for this system occurred from June to December 2000 and Stage 1 – the Analysis and Design phase – was completed in July 2001. Stage 2 (in about 18 months time) will allow users to attach images and files as part of the audit completion process and send those to us electronically, to be collected, indexed and put into our EDMS automatically.

- *OnLine Manuals:* As part of working with our auditors electronically (rather than through hard copy), we are developing a system to make the *Manual* they use available on our web site.

The usual benefits of savings in distribution costs for the hard copy manual, availability of a consistently up-to-date version, and easier provision of updates, will flow from implementation of this system.



Audit New Zealand

Audit New Zealand continued to make significant progress on a range of fronts during the year. Its five key objectives for management and development in 2000-01 were set out in the Office's *Forecast Report*¹³, and its actual achievements are described below:

Objective 1:

Take a more strategic approach to managing the business through continuing to communicate a shared understanding of the organisation's vision, mission and values.

The National Management Team reviewed and confirmed Audit New Zealand's purpose, values, vision and brand. They then reviewed the key focus areas for 2001-02 and developed the following key focus areas:

- refocusing the audit approach;
- reshaping the business;
- improving business processes;
- achieving revenue targets; and
- maintaining capability.

Subsequently, the National Management Team was disestablished and replaced by a smaller National Change Team that will assume the governance role for the key focus areas, which have been branded as *Project Enable*.

¹³ Parliamentary paper B.28FR(00), pages 35-36.

Three project teams were established: one to refocus the audit approach, another to reshape the business and the third to review business processes. The first two projects were reported to the National Change Team early in July 2001.

The strategic direction and key focus areas have been communicated to all staff, and staff also receive regular *Project Enable* communications.

Objective 2:

Increase efficiency and improve client value by implementing electronic audit support tools in conjunction with an updated audit methodology.

The implementation of electronic audit support tools (*Project Assist*) was completed and formally handed over to the business early in 2001. This project was completed on time and within budget.

A post-implementation review of *Project Assist* has been conducted by the external auditors of the Audit Office, Grant Thornton International. The report was very positive and confirmed that this was a successful implementation.

Objective 3:

Improve service delivery through client service planning and co-ordination of audit and assurance work throughout the organisation.

Work continues on identifying opportunities to add value to clients by offering a range of audit and assurance services. This is helped by the use of client planning and independent client satisfaction surveys.

Objective 4:

Continue to improve the capability and capacity of the organisation through targeted recruitment, retention and staff development systems.

Two directors visited a number of Asian audit offices with a view to seconding staff between the offices and to establish a senior management sabbatical. A total of 8 secondees have started: 6 from Thailand (4 for 3 months and 2 for a year) and 2 from Poland (both for 3 months).

Secondment opportunities with the Australian National Audit Office are now in place, and the recruitment programme continues to emphasise employing staff with a wide range of skill sets.

A staff survey was completed and high level results analysed. There was a 76% response rate from staff. Staff were most positive about overall job satisfaction and clarity of vision and purpose. They were least positive about satisfaction with the organisation and their degree of involvement. On average, staff were mildly positive across all dimensions.

Objective 5:

Achieve revenue targets by client retention, growth, and extending assurance-based services.

A total of 10 existing Audit New Zealand clients were involved in the 2000 tender round – 7 were lost and 3 retained. One client that was previously audited by competitors was regained.

Client satisfaction surveys have been completed for the Office of the Auditor-General, and key clients in the Auckland and Wellington Regions.

Part Four

Financial Statements

2000-01



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The Audit Office
Te Tari Whakamatau, Arotake

Financial Statements
for the year ended 30 June 2001

Statement of Responsibility

As Chief Executive of the Audit Office, I am responsible for the accuracy of and judgements used in the preparation of the Financial Statements, and the establishment and maintenance of systems of internal control designed to provide ongoing assurance of the integrity and reliability of financial reporting.

Appropriate systems of internal control have been employed to ensure that:

- all transactions are executed in accordance with authority;
- all transactions are correctly processed and accounted for in the financial records; and
- the assets of the Office are properly safeguarded.

In my opinion, the information set out in the statements and attached notes to those statements fairly reflects the service performance, financial activities and cash flows of the Audit Office for the year ended 30 June 2001 and its financial position as at that date.



D J D Macdonald
Controller and Auditor-General
31 August 2001



(Countersigned)
D E Atkin
Finance Manager
31 August 2001

Audit Report



**TO THE READERS OF THE FINANCIAL STATEMENTS OF
THE AUDIT OFFICE
FOR THE YEAR ENDED 30 JUNE 2001**

We have audited the Financial Statements of the Audit Office on pages 90 to 134. The Financial Statements provide information about the past financial and service performance of the Audit Office and its financial position as at 30 June 2001. This information is stated in accordance with the accounting policies set out on pages 115 to 119.

Responsibilities of the Controller and Auditor-General

Section 35 of the Public Finance Act 1989 requires the Controller and Auditor-General to prepare annual Financial Statements in accordance with generally accepted accounting practice and which fairly reflect the financial position of the Audit Office as at 30 June 2001 and the results of its operations, cash flows and service performance achievements for the year ended on that date.

Auditor's Responsibilities

Section 40 of the Public Finance Act 1989 requires the auditor appointed by the House of Representatives to audit the Financial Statements presented by the Controller and Auditor-General. It is the responsibility of the auditor to express an independent opinion on the Financial Statements and report its opinion to you.

Basis of Opinion

An audit includes examining, on a test basis, evidence relevant to the amounts and disclosures in the Financial Statements. It also includes assessing:

- the significant estimates and judgements made by the Controller and Auditor-General in the preparation of the Financial Statements; and
- whether the accounting policies are appropriate to the Audit Office's circumstances, consistently applied and adequately disclosed.

We conducted our audit in accordance with New Zealand Auditing Standards. We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to obtain reasonable assurance that the Financial Statements are free from material misstatements, whether caused by fraud or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the Financial Statements.

Other than in our capacity as auditor, we have no relationship with or interests in the Audit Office.

Unqualified Opinion

We have obtained all the information and explanations we have required.

In our opinion the Financial Statements of the Audit Office on pages 90 to 134:

- comply with generally accepted accounting practice; and
- fairly reflect:
 - the financial position as at 30 June 2001; and
 - the results of its operations and cash flows for the year ended 30 June 2001; and
 - the service performance achievements as measured in relation to the performance targets and other measures set out in the forecast report for the year ended on that date.

Our audit was completed on 21 September 2001 and our unqualified opinion is expressed as at that date.

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Statement of Objectives and Service Performance For the Year Ended 30 June 2001

Departmental Output Classes

The Audit Office has four output classes. The extent to which we have met our objectives for each output class (as set out in our *Forecast Report 2000-2001*¹⁴) is reported below.

Output Class D1 – *Reports and Advice arising from the Exercise of the Function of Legislative Auditor*

This class of outputs has six elements, each relating to the Audit Office's constitutional function of assisting Parliament to ensure accountability for public resources.

The products and services contained in this class of outputs are either demand-driven (e.g. ratepayer enquiries or advice to select committees), or are subject to the discretion of the Auditor-General as to the particular audit undertaken and reported (e.g. special studies).

Desired Outcomes

- 1 Maintenance of the integrity of:
 - public sector accounting and reporting systems; and
 - reports on financial and non-financial performance by public bodies.
- 2 Better use of public resources.

I Reports to Parliament and other constituencies on matters arising from annual audits, programmed special audits and studies, and unprogrammed special investigations

Performance Results

<i>Actual 1999-00</i>		<i>Actual 2000-01</i>	<i>Estimate 2000-01</i>
	<i>Quantity</i>		
2	• Results of annual audits	2	At least 2 reports
7	• Results of programmed special audits and studies	6	At least 6 reports
4	• Results of unprogrammed special investigations	4	-
	<i>Quality</i>		
All	• All reports will be prepared with due professional care and be subject to: <ul style="list-style-type: none"> • internal peer review; • substantiation; and • entity confirmation of factual accuracy. 	All	All
	<i>Timeliness</i>		
Substantially achieved	• Reports will be completed in a manner which ensures that the subjects being reported are timely and relevant.	Substantially achieved	
<i>\$000</i>		<i>\$000</i>	<i>\$000</i>
2,342	<i>Value of resources applied</i>	2,329	2,411

Commentary on Performance

We presented to Parliament two omnibus reports on the results of Central Government and Local Government audits, and the following six single-issue reports:

- Auditing a Long-term Financial Strategy – Opotiki District Council Pilot Project
- Civil Aviation Authority Safety Audits – Follow-up Audit
- Good Practice for Involvement in a Major Project – Lessons from the Opuha Dam Project

- Members of Parliament: Accommodation Allowances for Living in Wellington – Interim Report
- Local Authority Governance of Subsidiary Entities
- Meeting International Environmental Obligations.

We also published the following major reports and distributed them to relevant audiences:

- Auckland City Council’s Management of its Responsibilities in the Hauraki Gulf
- Waitakere City Council: Payments and Associated Issues Relating to Certain Staff Redundancies
- Reviewing a Long-term Financial Strategy and Funding Policy – *Experiences of the Early Nine*
- Thames Coromandel District Council: Actions Relating to a Sewerage Scheme for Cooks Beach and Ferry Landing.

The number and coverage of reports was similar to last year. We expect to increase the number of reports issued over the next two years as a result of additional funding provided.

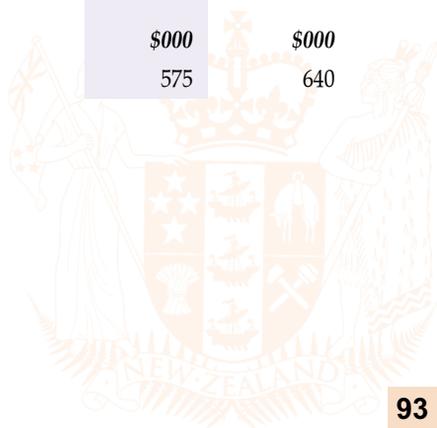
See pages 38-42 for more detail and commentary on reports issued.



II Reports and advice to select committees and Ministers

Performance Results

Actual 1999-00		Actual 2000-01	Estimate 2000-01
	<i>Quantity</i>		
	• Reports to select committees:		
96	• financial reviews	85	110
29	• estimates examinations	90	40
26	• other.	34	20
113	• Reports to portfolio Ministers on the results of annual audits.	136	110
	<i>Quality</i>		
7	• All select committees will be surveyed as to their satisfaction with the quality of our reports and advice.	13	13
All	• All reports and advice will be prepared with due professional care by an appropriately qualified person and, where the circumstances require it, be subject to:	All	All
	• internal peer review;		
	• substantiation; and		
	• entity confirmation of factual accuracy.		
	<i>Timeliness</i>		
All	• Reports presented to select committees at least two days before their examination, unless otherwise agreed with the committee.	All	All
All	• Reports presented to portfolio Ministers before select committee scrutiny of departmental and Crown entity performance.	All	All
\$000		\$000	\$000
572	<i>Value of resources applied</i>	575	640



Commentary on Performance

Quantity

The overall number of reports is up on the previous year, because the Estimates examinations for 2000-01 only began in late-June 2000, while the 2001-02 Estimates examinations began early in June 2001.

Quality

Select committee chairpersons were interviewed in August/September 2000 and asked to comment on their satisfaction with the OAG's performance in relation to estimates advice, financial reviews and any other interactions between committees and the OAG. A consistently high level of satisfaction was expressed in relation to the content and quality of OAG advice to committees. This was corroborated by the Peer Review carried out in February-March 2001 (see page 64).



III Responding to enquiries from taxpayers, ratepayers and Members of Parliament

Performance Results

Actual 1999-00		Actual 2000-01	Estimate 2000-01
	<i>Quantity</i>		
	• Enquiries received from:		
45	• taxpayers	21	60
172	• ratepayers	177	180
66	• Members of Parliament.	51	60
	<i>Quality</i>		
All	• All reports and advice will be prepared with due professional care by an appropriately qualified person and, where the circumstances require it, be subject to:	All	All
	• internal peer review;		
	• substantiation; and		
	• entity confirmation of factual accuracy.		
	<i>Timeliness</i>		
80%	• Initial response within five working days.	88%	100%
79%	• Cleared within 30 working days, unless otherwise advised.	82%	100%
<i>\$000</i>		<i>\$000</i>	<i>\$000</i>
403	<i>Value of resources applied</i>	420	300

Commentary on Performance

This is a demand-driven activity, the quantity of enquiries received being beyond our control.

Although many of these enquiries can be responded to relatively promptly, others identify more significant issues and can lead to major or ongoing investigations. Enquiries that lead to major studies have an impact upon both response times and costs per enquiry. Examples this year included:

- Members of Parliament: Accommodation Allowances for Living in Wellington – Interim Report.

- Auckland City Council's Management of its Responsibilities in the Hauraki Gulf.
- Waitakere City Council: Payments and Associated Issues Relating to Certain Staff Redundancies.
- Thames Coromandel District Council: Actions Relating to a Sewerage Scheme for Cooks Beach and Ferry Landing.

The target of clearing 100% of inquiries within 30 working days is aspirational, and has been amended to an 80% hurdle target from 2001-02.



IV *Advice to government bodies and other agencies on auditing, accountability and financial management in the public sector*

Performance Results

<i>Actual 1999-00</i>		<i>Actual 2000-01</i>	<i>Estimate 2000-01</i>
	<i>Quantity</i>		
*	<ul style="list-style-type: none"> • Responding to specific requests from, and participating in working parties on matters related to financial management and accountability with, organisations including: <ul style="list-style-type: none"> • central agencies; • government departments, local authorities and other public sector entities; • professional bodies such as the Institute of Chartered Accountants of New Zealand; • sector organisations such as Local Government New Zealand and the Society of Local Government Managers; • foreign delegations; and • other audit institutions and related organisations, such as INTOSAI. 	*	*
	<i>Quality</i>		
All	<ul style="list-style-type: none"> • All advice will be prepared with due professional care by an appropriately qualified person and, where the circumstances require it, be subject to internal peer review. 	All	All
	<i>Timeliness</i>		
	<ul style="list-style-type: none"> • As requested 		
<i>\$000</i>		<i>\$000</i>	<i>\$000</i>
595	<i>Value of resources applied</i>	542	700

*This is a demand-driven activity for which there are no wholly satisfactory quantity measures.

Commentary on Performance

We continue to provide a wide range of high-quality advice on financial management and accountability issues. Most is directed to governmental or sector organisations, but our involvement with professional bodies in New Zealand, and receiving international audit agencies and other international delegations, also consumes considerable time.

The advice given to professional bodies relates mainly to:

- submissions made to the Institute of Chartered Accountants of New Zealand on the Auditing Standards and Guidance Statements and Financial Reporting Standards; and
- our participation in the activities of the Public Sector Committee of the International Federation of Accountants.

Our ongoing involvement with international audit agencies relates to:

- Continuing participation in two international working groups of the International Organisation of Supreme Audit Organisations (INTOSAI) – on auditing activities with an environmental perspective, and accounting standards.
- Participation in the Auditors-General Global Working Group, which was initiated by the Comptroller General of the United States to promote informal dialogue among the Auditors-General of a small number of countries facing similar issues and challenges.
- Regular contact with our Australian colleagues through a forum known as the Australasian Council of Auditors-General (ACAG).
- Our role as Secretary to the South Pacific Organisation of Supreme Audit Organisations (SPASAI).

The Office continues to receive many delegations from other countries, not all of which are confined to audit-related matters. The international reputation of New Zealand's public sector reforms undoubtedly contributes significantly to this sustained high level of international interest.

V *Administering the provisions of the Local Authorities (Members' Interests) Act 1968*

Performance Results

<i>Actual 1999-00</i>		<i>Actual 2000-01</i>	<i>Estimate 2000-01</i>
	<i>Quantity</i>		
81	<ul style="list-style-type: none"> • Responding to specific requests in relation to the Audit Office's powers to: <ul style="list-style-type: none"> • approve increased limits for contract payments; • grant dispensations in certain circumstances from the prohibition against discussing and voting where members have a pecuniary interest; and • consider alleged breaches of the Act. 	71	90
	<i>Quality</i>		
All	<ul style="list-style-type: none"> • All reports and advice will be prepared with due professional care by an appropriately qualified person and, where the circumstances require it, be subject to internal peer review. 	All	All
	<i>Timeliness</i>		
89%	<ul style="list-style-type: none"> • Initial response within five working days. 	92%	100%
83%	<ul style="list-style-type: none"> • Cleared within 30 working days, unless otherwise advised. 	86%	100%
<i>\$000</i>		<i>\$000</i>	<i>\$000</i>
60	<i>Value of resources applied</i>	69	50



Commentary on Performance

The number of enquiries reduced this year, and our overall timeliness in completing them improved slightly. However, the actual cost per enquiry increased significantly, because:

- we received more requests for dispensations, some of which concerned issues of major public importance to the districts concerned – in these cases, we had to give detailed consideration to whether it was in the public interest that all members (including those with pecuniary interests) should be entitled to participate in the decision-making process; and
- we had to undertake a number of complex investigations into alleged breaches of the rule against discussing and voting where a member has a pecuniary interest.



VI *Transition to the new Public Audit Act 2001*

Performance Results

<i>Actual 1999-00 \$000</i>	<i>Actual 2000-01 \$000</i>	<i>Estimate 2000-01 \$000</i>
-	7	75

Commentary on Performance

Parliament has appropriated an additional \$75,000 for each of the 2000-01 and 2001-02 years, to contribute to the costs of transition to the Public Audit Act 2001. The funding is to be spent on making arrangements for the audit of new entities in the Audit Office's portfolio.

The additional funds were provided in the expectation that about 170 energy, community and miscellaneous trusts would be added to the portfolio. In the event, community trusts were not added and the status of energy trusts was still to be resolved at 30 June 2001. As a result of these uncertainties, only a small amount of work was done during 2000-01 on setting up new audit arrangements. The unused funding was returned to the Crown by way of additional surplus in the output class.



Financial Performance of Output Class D1

<i>Actual</i> 1999-00 \$000		<i>Actual</i> 2000-01 \$000	<i>Estimate</i> 2000-01 \$000
4,042	Revenue - Crown	4,172	4,171
8	- Other	73	15
(3,972)	Expenditure	(3,942)	(4,176)
78	Surplus	303	10

Commentary on Financial Out-turn of Output Class D1

The cost of producing the output in this class was appropriately covered by revenue for the year. On-going attention to cost efficiencies in producing the outputs, and the unused funding for costs of transition to the Public Audit Act 2001, resulted in a larger surplus than forecast.



Output Class D2 – Certification of Authority to Release Funds from the Crown Bank Account

This class of outputs relates to the controller function under section 22 of the Public Finance Act 1989. The function is to act as a monitor, on behalf of Parliament, to control the issue of funds from the Crown Bank Account. Operationally this includes monitoring departmental and Crown financial reporting systems to ensure that releases of funds are supported by appropriations and are for lawful purposes.

Desired Outcome

Legal disbursement of public funds.

Performance Results

Actual 1999-00		Actual 2000-01	Estimate 2000-01
	<i>Quantity</i>		
13	• Warrants issued	7	15
247	• Controller statements issued	243	240
	<i>Quality</i>		
All	• Authorities will be issued once correct documentation is received.	All	All
All	• Issues from the Crown Bank Account will be within the appropriations and other lawful authorities granted by Parliament.	All	All
No payments made without authority	• All payments not within a warrant from the Governor-General will be refused.	No payments made without authority	No payments made without authority
	<i>Timeliness</i>		
99%	• Controller statements signed before 12 noon on day of submission.	99%	100%
\$000		\$000	\$000
220	<i>Value of resources applied</i>	239	240

Commentary on Performance

The volume of controller statements issued continues at a similar level to that of previous years. It is pleasing to note that concerns we raised in 1999-2000 about fluctuation in the quality of statements presented were addressed, and the average quality of statements presented remained sound during 2000-01.

Financial Performance of Output Class D2

<i>Actual</i> 1999-00 \$000		<i>Actual</i> 2000-01 \$000	<i>Estimate</i> 2000-01 \$000
220	Revenue – Crown	239	240
(220)	Expenditure	(239)	(240)
Nil	Surplus	Nil	Nil

Commentary on Financial Out-turn of Output Class D2

This small but important constitutional function has been effectively carried out within the funding provided by the Crown.



Output Class D3 – *Provision of Non-contested Audit Services*

The Audit Office has a statutory duty to conduct an audit of the financial statements of more than 3,700 public entities. The Office of the Auditor-General establishes the standards by which audits will be carried out.

This class of outputs relates to the provision of those audits which have not been allocated to audit service providers by a contestable process. These are:

- audits of national sensitivity; or
- audits where the Auditor-General considers that subjecting particular audits to contestability at this time is potentially too disruptive to the entity; or
- those audits which have yet to be subject to competitive tender.

The work is carried out by Audit New Zealand.

The two significant outputs in this class are:

- **Audit Reports** – on whether the financial statements fairly reflect the financial and non-financial performance of the entity subject to audit; and
- **Management Reports** – to the management and governing bodies of these entities, on issues arising from the audit.

Desired Outcomes

- 1 Maintenance of the integrity of:
 - public sector accounting and reporting systems; and
 - reports on financial and non-financial performance by public entities.
- 2 Better use of public resources.

Performance Quality

<i>Standard</i>	<i>Achievement</i>
1 Work will be conducted with due professional care; ensuring adherence to standards of appropriateness, quality, efficiency and independence as set out in the Institute of Chartered Accountants of New Zealand's standards and other standards which the Auditor-General deems appropriate for the public sector.	Done
2 A quality assurance programme will be carried out on audit arrangements and work undertaken.	Programme undertaken, the results of which are reported on pages 31-32.

Commentary on Performance

A key goal set for 2000-01 was to continue to reduce audit arrears. We set a target of 25% for this output class. As a result of a sustained effort, arrears were actually reduced by 60% in this output class.

As a result of measures set in train last year and continued this year, the timeliness of both audit opinions and management reports for current year audits improved.



Statement of Performance for Output Class D3 – Non-contested Audit Services
Performance Quantity and Timeliness¹

Sector	Quantity			Timeliness			
	Audit Status			Timely Issue of Audit Reports		Timely Issue of Management Reports	
	Total Entities in Group	Carried Out	Audit Arrears at Year End	Target ²	Actual	Target ³	Actual
Government Departments and Offices of Parliament	20	20	-	100%	100%	100%	95%
1999-2000	20	20	-	100%	100%	100%	90%
Major Statutory Bodies ⁴	60	62	6	100%	81%	100%	91%
1999-2000	69	64	14	100%	82%	100%	85%
Other Local Authorities ⁵	44	61	4	100%	91%	100%	85%
1999-2000	71	101	26	100%	65%	100%	55%
Miscellaneous Public Bodies ⁶	156	178	59	75%	66%	100%	98%
1999-2000	179	181	78	75%	59%	100%	88%
Audits for which fees will not be charged ⁷	165	292	124	75%	31%	100%	99%
1999-2000	172	361	269	75%	14%	100%	95%
TOTALS	445	613	193		58%		97%
1999-2000	511	727	387		50%		86%

1 Figures may not balance exactly, or may vary from those presented in the Forecast Report and last year's Annual Report, because of in-year changes and corrections to the audit portfolio.

2 Audits will be completed and audited financial statements will be available within statutory deadline or within 5 months of balance date.

3 Management reports and letters will be issued within 6 weeks of the date of the audit report.

4 Comprising State-owned Enterprises, Tertiary Education Institutions, Producer Boards, Hospitals and Health Services, Crown Research Institutes and major Crown Entities.

5 Comprising Licensing Trusts, Airports, LATEs, Energy Companies, Port Companies and Sinking Fund Commissioners.

6 Comprising mainly Maori Trust Boards, smaller Crown Entities, and subsidiaries of major statutory bodies.

7 Comprising Cemetery Trustees, Hall and Reserve Boards, Racecourse Trustees, and Patriotic Funds.

Commentary on Performance: Audit Outcomes

The following table gives an analysis of all non-standard audit reports³² issued in the 1999-2000 and 2000-01 years.

1999-00				2000-01		
Schools	Other	Total		Schools	Other	Total
88	44	132	Unqualified, with explanatory paragraph on breach of law	73	111	184
5	13	18	Full Disclaimer	1	14	15
4	-	4	Partial Disclaimer	1	55	56
2	7	9	Adverse	1	4	5
43	73	116	Except for	24	30	54
142	137	279	Total non-standard audit reports	100	214	314
2,959	1,481	4,440	Total all audit reports	2,597	1,410	4,007

There has been a slight increase in non-standard audit reports as a proportion of all audit reports issued during the year – from 6.5% in 1999-2000 to 7.8% in 2000-01.

This increase is largely due to:

- the need to draw attention to the dissolution of a number of health sector entities in their audit reports for the periods to 30 June 2000 and 31 December 2000 (40 audit reports with explanatory paragraphs); and
- the issue of a number of partial disclaimers for entities such as cemetery trustees and reserve boards who had not maintained adequate accounting records (55 audit reports in 2000-01).

A reduction in “Except for” opinions from 116 in 1999-2000 to 54 in 2000-01 partly offset these increases. This was because a smaller number of entities omitted budget figures or performance information when required to do so, and there were fewer departures from generally accepted accounting practice.

³² Non-standard audit reports are those where the auditor has

- qualified the audit opinion due to a disagreement or a limitation on scope;
- drawn attention to a breach of law; or
- drawn attention to a fundamental uncertainty.

Whenever a non-standard audit report is likely to be issued, we encourage entities to take appropriate action. In some cases, action taken can remove the need for a non-standard audit report. In others – for example, some limitations in scope and breaches of law – resolving the issue will only affect audit reports for future years.

Financial Performance of Output Class D3

<i>Actual 1999-00 \$000</i>		<i>Actual 2000-01 \$000</i>	<i>Estimate 2000-01 \$000</i>
5,430	Revenue – Other	5,361	5,214
(5,006)	Expenditure	(5,392)	(5,133)
424	Surplus/(Deficit)	(31)	81

Commentary on Financial Out-turn of Output Class D3

The expenditure for this output class for the year was greater than the estimate, resulting in unappropriated expenditure (refer to the Statement of Unappropriated Expenditure on page 126). Revenue was greater than estimate because fees forecast to complete the health disestablishment audits were under-budgeted. Costs associated with these audits, plus extra work on domains and cemeteries, and higher indirect costs allocated to the output, resulted in a small deficit for the year.



Output Class D4 – *Provision of Contested Audit Services*

The Audit Office has a statutory duty to conduct an audit of the financial statements of more than 3,700 public entities. The Office of the Auditor-General establishes the standards by which audits will be carried out.

This class of outputs relates to the provision of audits or audit-related services awarded through a competitive tender process or under the threat of competition. This class of output is appropriated on a Mode B net basis, and the work is carried out by Audit New Zealand and private sector auditing firms on contract to the Auditor-General.

The two significant outputs in this class are:

- **Audit Reports** – on whether the financial statements fairly reflect the financial and non-financial performance of the entity subject to audit; and
- **Management Reports** – to the management and governing bodies of these entities, on issues arising from the audit.

Desired Outcomes

- 1 Maintenance of the integrity of:
 - public sector accounting and reporting systems; and
 - reports on financial and non-financial performance by public entities.
- 2 Better use of public resources.

Performance Quality

<i>Standard</i>	<i>Achievement</i>
1 Work will be conducted with due professional care; ensuring adherence to standards of appropriateness, quality, efficiency and independence as set out in the Institute of Chartered Accountants of New Zealand's standards and other standards which the Auditor-General deems appropriate for the public sector.	Done
2 A quality assurance programme will be carried out on audit arrangements and work undertaken.	Programme undertaken, the results of which are reported on pages 31-32.

Commentary on Performance

A key goal set in 2000-01 was to continue to reduce audit arrears. We set a target of 15% for this output class. As a result of a sustained effort, arrears were actually reduced by 22% in this output class. We expect to hold the level of arrears at no more than 50 audits (other than schools) in the future.

As a result of measures set in train last year and continued this year, the timeliness of both audit opinions and management reports improved.

Commentary on the outcomes of audits (types of audit report issued) is set out on pages 108-109.



Statement of Performance for Output Class D4 – Contested Audit Services
Performance Quantity and Timeliness¹

Sector	Quantity				Timeliness			
	Audit Status		Timely Issue of Audit Reports		Timely Issue of Management Reports		Timely Issue of	
	Total Entities in Group	Carried Out	Audit Arrears at Year End	Target ²	Actual	Target ³	Actual	
Government Departments and Offices of Parliament	28	28	-	100%	100%	100%	100%	
1999-2000	28	28	-	100%	96%	100%	92%	
Major Statutory Bodies ⁴	71	73	-	100%	99%	100%	87%	
1999-2000	69	73	1	100%	96%	100%	69%	
Regional, City and District Councils	86	86	-	100%	99%	100%	95%	
1999-2000	86	86	-	100%	94%	100%	82%	
Other Local Authorities ⁵	302	350	34	100%	79%	100%	91%	
1999-2000	337	375	66	100%	69%	100%	74%	
School Boards of Trustees	2,640	2,597	153	50%	29%	100%	96%	
1999-2000	2,653	2,797	112	50%	29%	100%	91%	
Miscellaneous Public Bodies ⁶	189	260	15	75%	65%	100%	89%	
1999-2000	196	186	80	75%	49%	100%	75%	
TOTALS	3,316	3,394	202		40%		95%	
1999-2000	3,369	3,545	259		38%		88%	

1 Figures may not balance exactly, or may vary from those presented in the Forecast Report and last year's Annual Report, because of in-year changes and corrections to the audit portfolio.

2 Audits will be completed and audited financial statements will be available within statutory deadline or within 5 months of balance date.

3 Management reports and letters will be issued within 6 weeks of the date of the audit report.

4 Comprising State-owned Enterprises, Tertiary Education Institutions, Producer Boards, Hospitals and Health Services, Crown Research Institutes, and major Crown Entities.

5 Comprising Licensing Trusts, Airports, LATEs, Energy Companies, Port Companies and Sinking Fund Commissioners.

6 Comprising mainly Maori Trust Boards, smaller Crown Entities, and subsidiaries of major statutory bodies.

Financial Performance of Output Class D4

<i>Actual</i> 1999-00 \$000		<i>Actual</i> 2000-01 \$000	<i>Estimate</i> 2000-01 \$000
25,703	Revenue – Other	26,049	27,672
(25,401)	Expenditure	(25,970)	(27,526)
302	Surplus	79	146

Commentary on Financial Out-turn of Output Class D4

The financial out-turn for this output class for the year is within estimate and the result is a surplus. While revenue did not increase as much as forecast because added assurance targets were not achieved, the costs relating to the conduct of audits were held effectively.



Financial Performance Indicators For the Year Ended 30 June 2001

Details of the actual performance of the Audit Office against performance measures established in the *Forecast Report* are summarised below.

<i>Actual</i>		<i>Actual</i>	<i>Final</i>	<i>Forecast</i>
<i>1999-00</i>		<i>2000-01</i>	<i>Estimates</i>	<i>Report</i>
<i>\$000</i>		<i>\$000</i>	<i>2000-01</i>	<i>2000-01</i>
			<i>\$000</i>	<i>\$000</i>
	Operating Results			
	Revenue: other than			
	Crown and			
	departmental audit			
24,743	fees	25,616	25,949	29,394
34,599	Output expenses	35,543	37,075	40,365
	Surplus before capital			
1,042	charge	592	536	541
803	Surplus	351	237	242
	Working Capital			
	Management			
	Current assets less			
1,474	current liabilities	1,694	1,011	1,423
136%	Current ratio	140%	131%	148%
	<i>Average receivables and</i>			
51 days	<i>work in progress</i>	49 days	44 days	36 days
	<i>Average payables</i>			
35 days	<i>outstanding</i>	43 days	43 days	32 days
	Resource Utilisation			
	<i>Physical assets:</i>			
	Total physical assets at			
1,985	year end	3,031	3,307	2,633
	<i>Additions as % of</i>			
63%	<i>physical assets</i>	66%	68%	75%
	Taxpayers' funds			
2,386	Level at year-end	3,586	3,586	3,586
	Net Cash Flows			
	Surplus on operating			
1,510	activities	1,966	856	1,205
	(Deficit) on investing			
(1,129)	activities	(1,823)	(2,171)	(1,795)
	Surplus/(deficit) on			
(629)	financing activities	397	397	631
	Net increase/(decrease)			
(248)	in cash held	540	(918)	41

Statement of Accounting Policies For the Year Ended 30 June 2001

Reporting Entity

These are the financial statements of the Audit Office prepared pursuant to section 35 of the Public Finance Act 1989.

The Audit Office comprises the Auditor-General, the Deputy Auditor-General, and those resources provided by the Audit Department.

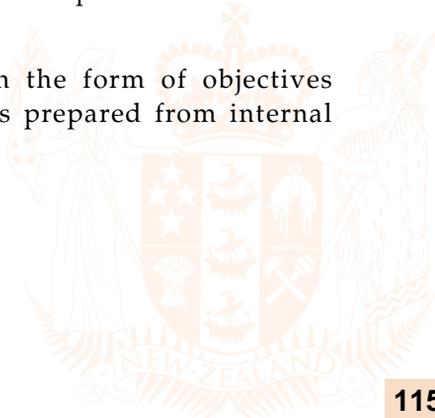
The Audit Department is a department of state established by section 15 of the Public Finance Act 1977 to provide resources to the Audit Office to enable it to perform its functions and duties. The Auditor-General is the Chief Executive of the Audit Department. Departmental activities include the work undertaken by chartered accounting firms on contract to the Auditor-General.

The activities of the Audit Office and the Audit Department are reported here as one entity, referred to as “the Audit Office”, consistent with the definition of that term in section 2 of the Public Finance Act 1989.

Measurement Base

Generally accepted accounting practice is used to measure and report the activities and financial position of the Audit Office on an historical cost basis.

Non-financial information, in the form of objectives and performance measures, is prepared from internal management information.



Accounting Policies

Revenue

The Audit Office derives revenue from the Crown for outputs provided to Parliament, from audit fees for services to third parties, and from other assurance work undertaken by Audit New Zealand at the request of audited entities.

Expenses

The salaries of the Auditor-General and the Deputy Auditor-General, which are a charge against a permanent appropriation in terms of sections 18 and 21 of the Public Finance Act 1977, are recognised as expenses of the Audit Office.

Output Cost Allocation

Definitions

- *Direct costs* are those costs which are directly attributable to a single output.
- *Indirect costs* are all other costs. These costs include: payroll costs; variable costs such as travel; and operating overheads such as property costs, depreciation, and capital charges.

Method of Assigning Costs to Output Classes

- *Direct costs* that can readily be identified with a single output are assigned directly to the relevant output class. For example, the cost of audits carried out by contract audit service providers is charged directly to Output Class D4.
- *Indirect costs* are allocated according to the time charged to a particular activity.

Receivables and Work in Progress

Receivables and work in progress are stated at estimated realisable value, after providing for non-recoverable amounts.

Leases

The Audit Office leases office premises and office equipment. As substantially all of the risks and rewards of ownership are retained by the lessor, these leases are classified as operating leases. Operating lease costs are expensed on a systematic basis over the period of the lease.

Physical Assets

The initial cost of a physical asset is the value of the consideration given to acquire or create the asset and any directly attributable costs of bringing the asset to working condition for its intended use.

All physical assets costing more than \$500 are capitalised.

Depreciation

Depreciation of physical assets is provided on a straight-line basis so as to allocate the cost of the assets, less their residual value, over their expected useful lives. The estimated useful lives are:

Furniture and fittings	4 years
Office equipment –	
Computer hardware and software	2.5 years
Other office equipment	4 years
Motor vehicles	5-7.5 years

Provision for Employee Entitlements

Annual leave and time off in lieu of overtime worked are recognised as they accrue to employees based on current rates of pay. Long service leave and retiring/resigning leave are recognised on an actuarial basis. In calculating the present value of the estimated future cash outflows, the assumptions used in valuing the Government Superannuation Fund liability have been adopted.

Foreign Currency

Foreign currency transactions, relating primarily to subscriptions and travel, are paid for at the New Zealand dollar exchange rate at the date of the transaction.

Financial Instruments

Financial instruments primarily comprise bank balances, receivables and payables, which are recognised in the Statement of Financial Position. Revenue and expenses in relation to all financial instruments are recognised in the Statement of Financial Performance.

Goods and Services Tax (GST)

Amounts in the financial statements are reported exclusive of GST, except for:

- Payables and Receivables in the Statement of Financial Position, which are GST-inclusive.
- Figures in the Statement of Appropriations, which are GST-inclusive unless noted.

The amount of GST owing to or from the Inland Revenue Department at balance date, being the difference between Output GST and Input GST, is included in Payables or Receivables (as appropriate).

Income Tax

The Audit Office, as an institution of the Crown, is exempt from the payment of income tax in terms of the Income Tax Act 1994. Accordingly, no charge for income tax has been provided for.

Commitments

Future payments are disclosed as commitments at the point at which a contractual obligation arises. Commitments relating to employment contracts are not disclosed unless they had vested at balance date, in which case they are reflected in the item "Provision for employee entitlements" in the Statement of Financial Position.

Contingent Liabilities

Contingent liabilities are disclosed at the point at which the contingency is evident.

Changes in Accounting Policies

There have been no changes in accounting policies, including cost allocation accounting policies, from those contained in the last audited financial statements.



Statement of Financial Performance For the Year Ended 30 June 2001

Description of Statement

The Statement of Financial Performance details the revenue and expenses relating to all outputs (goods and services) produced by the Audit Office. Supporting statements showing the revenue and expenditure of each output class are on pages 101, 104, 109 and 113.

1999-00 Actual		Notes	2000-01 Actual	2000-01 Final Estimates ¹
\$000			\$000	\$000
	Continuing Activities –			
	Revenue			
4,261	Crown	2	4,411	4,411
31,141	Other	3	31,483	32,901
<u>35,402</u>	Total Revenue		<u>35,894</u>	<u>37,312</u>
	Expenses			
18,188	Personnel costs		18,233	19,001
15,553	Operating costs	4	16,305	16,926
619	Depreciation		764	849
239	Capital charge	5	241	299
<u>34,599</u>	Total Expenses		<u>35,543</u>	<u>37,075</u>
<u>803</u>	Surplus		<u>351</u>	<u>237</u>

¹ See Note 1 on page 128.

The accompanying accounting policies and notes form part of these statements.

Statement of Movements in Taxpayers' Funds (Equity) For the Year Ended 30 June 2001

Description of Statement

The Statement of Movements in Taxpayers' Funds combines information about the surplus with other aspects of the financial performance of the Audit Office to give a degree of measure of comprehensive income. This statement, together with the Statement of Financial Position, provides information for assessing the return on investment in the Audit Office.

1999-00 Actual \$000		Notes	2000-01 Actual \$000	2000-01 Forecast \$000
2,386	Taxpayers' Funds brought forward at 1 July		2,386	2,386
803	Movements during the year			
	Surplus		351	237
803	Total Recognised Revenues and Expenses for the Year		351	237
	Flows to and from the Crown			
-	Capital Contribution	6	1,200	1,200
(803)	Provision for payment to the Crown	7	(351)	(237)
(803)			849	963
2,386	Taxpayers' Funds at 30 June		3,586	3,586

The accompanying accounting policies and notes form part of these statements.

Statement of Cash Flows For the Year Ended 30 June 2001

Description of Statement

The Statement of Cash Flows summarises the cash movements in and out of the Audit Office during the year. It takes no account of money owed to the Office or owing by the Office, and therefore differs from the Statement of Financial Performance.

1999-00 Actual \$000	Notes	2000-01 Actual \$000	2000-01 Forecast \$000
Operating Activities			
Cash received from:			
4,261		4,466	4,411
31,408		31,548	23,669
Cash disbursed on:			
(31,582)		(31,654)	(25,210)
(2,338)		(2,153)	(1,715)
(239)		(241)	(299)
<u>1,510</u>	13	<u>1,966</u>	<u>856</u>
Investing Activities			
Cash received from:			
130		163	73
Cash disbursed on:			
(1,259)		(1,986)	(2,244)
<u>(1,129)</u>		<u>(1,823)</u>	<u>(2,171)</u>
Financing Activities			
Cash received from:			
		1,200	1,200
Cash disbursed on:			
(629)		(803)	(803)
<u>(629)</u>		<u>397</u>	<u>397</u>
(248)		540	(918)
1,193		945	945
<u>945</u>		<u>1,485</u>	<u>27</u>

The accompanying accounting policies and notes form part of these statements.

Supplementary Information For the Year Ended 30 June 2001

Statement of Commitments

This statement records those expenditures to which the Audit Office is contractually committed at 30 June 2001 and which will become liabilities if and when the terms of the contracts are met.

The Audit Office had no capital commitments as at 30 June 2001 (2000 – nil).

The Audit Office has long-term leases on its premises. The annual property lease payments are subject to regular reviews, ranging from 3-yearly to 6-yearly.

Equipment lease commitments include leases of computer equipment, telephone exchange systems, facsimile machines and photocopiers.

30/6/2000 Actual \$000		30/6/2001 Actual \$000
	Operating Lease Commitments	
	Property Lease Commitments	
1,440	Less than one year	1,214
1,431	One to two years	1,342
3,720	Two to five years	3,419
1,589	More than five years	536
<u>8,180</u>	Total Property Lease Commitments	<u>6,511</u>
	Equipment Lease Commitments	
598	Less than one year	537
537	One to two years	209
231	Two to five years	21
<u>1,366</u>	Total Equipment Lease Commitments	<u>767</u>
<u>9,546</u>	Total Operating Lease Commitments	<u>7,278</u>

The accompanying accounting policies and notes form part of these statements.

Statement of Contingent Liabilities

This statement discloses situations which exist at 30 June 2001, the ultimate outcome of which is uncertain and will be confirmed only on the occurrence of one or more future events after the date of approval of the Financial Statements.

The Audit Office did not have any contingent liabilities as at 30 June 2001 (2000 – nil). There is potential for claims to arise against the Audit Office as a result of defalcations and other losses within entities of which the Auditor-General is the auditor. No demands for compensation have been made by any party as at the date of these financial statements. The Audit Office has professional indemnity insurance.

There were no contingent assets as at 30 June 2001 (2000 – nil).

Statement of Appropriations¹

	2000-01	
	Output Expenses \$000	Appropriations \$000
Annual Appropriations		
<i>Mode B Gross</i>		
D1 Reports and advice to Parliament	4,018	4,245
D2 Controller function	269	270
D3 Non-contested audit services	6,062	5,785
Total Annual Appropriations	10,349	10,300
<i>Less GST</i>	1,180	1,155
Total Annual Appropriations GST-exclusive	9,169	9,145
Other Appropriations		
<i>Mode B Gross</i>		
D1 Reports and advice to Parliament ²	404	404
<i>Mode B Net</i>		
D4 Contested audit services ³	29,226	30,985
<i>Less GST</i>	3,256	3,459
Total Mode B Net Annual Appropriations GST-exclusive	25,970	27,526
Total Other Appropriations GST-exclusive	26,374	27,930
Total Output Expenses as reported in the Statement of Financial Performance	35,543	37,075

1 Amounts in the Statement of Appropriations are GST-inclusive, except for Other Appropriations (Mode B Gross) which are exempt from GST.

2 Costs incurred pursuant to sections 18 and 21 of the Public Finance Act 1977.

3 Costs incurred pursuant to section 10 of the Public Finance Act 1989.

The accompanying accounting policies and notes form part of these statements.

Statement of Unappropriated Expenditure

This statement discloses expenditure and costs incurred in excess of appropriation for the year.

	2000-01		
	<i>Actual Expenses</i>	<i>Appropriation</i>	<i>Unappropriated Expenditure</i>
	\$000	\$000	\$000
Vote: Audit Output Class D3 – Non-contested Audit Services	6,062	5,785	277

Unappropriated expenditure in Non-contested Audit Services occurred because:

- The costs associated with work on the audits of domains and cemeteries and health disestablishment audits were under-budgeted.
- Higher indirect costs were allocated to the output class than budgeted. Indirect costs are allocated between output classes on a “chargeable hours” basis. Lower than forecast activity in Output Class D4: Provision of Contested Audit Services resulted in proportionally more indirect costs being allocated to Output Class D3.

The unappropriated expenditure is matched by third-party revenue and is therefore fiscally neutral.

There was no unappropriated expenditure during the year ended 30 June 2000.



Statement of Trust Money

On 1 November 1996 the Audit Office was appointed Secretary-General of the South Pacific Association of Supreme Audit Institutions (SPASAI). SPASAI exists to encourage, promote and advance cooperation among its members in the field of public audit.

A trust account records the financial transactions undertaken by the Audit Office on behalf of SPASAI. All trust money transactions are recorded on a cash basis.

1999-00 Actual \$000		2000-01 Actual \$000
251	Opening balance at 1 July	89
359	Receipts	4
610		93
(521)	Payments	(49)
<u>89</u>	Closing balance at 30 June	<u>44</u>

The accompanying accounting policies and notes form part of these statements.



Notes to the Financial Statements For the Year Ended 30 June 2001

Note 1: Budget Estimates

The table below shows the main budget for the year as reflected in the *Estimates of Appropriations* approved by Parliament, the changes made in conjunction with the *Supplementary Estimates* approved by Parliament, and the aggregate budget estimates.

	<i>2000-01 Main Budget Estimates \$000</i>	<i>2000-01 Supplementary Estimates Changes \$000</i>	<i>2000-01 Final Estimates (Forecast) \$000</i>
Revenue			
Crown	4,261	150	4,411
Other	36,346	(3,445)	32,901
Total Revenue	<u>40,607</u>	<u>(3,295)</u>	<u>37,312</u>
Expenses			
Personnel costs	18,883	118	19,001
Operating costs	20,052	(3,126)	16,926
Depreciation	1,131	(282)	849
Capital charge	299	-	299
Total Expenses	<u>40,365</u>	<u>(3,290)</u>	<u>37,075</u>
Surplus	<u>242</u>	<u>(5)</u>	<u>237</u>

Note 2: Crown Revenue

Revenue is provided by the Crown to meet the costs of the Audit Office in assisting Parliament in its role of ensuring accountability for public resources. The services provided to Parliament include reports to Parliament and other constituencies, reports and advice to select committees, responding to taxpayer and ratepayer enquiries, advice to government bodies and other agencies, and administering the provisions of the Local Authorities (Members' Interests) Act 1968.

Note 3: Other Revenue

1999-00 Actual \$000		2000-01 Actual \$000	2000-01 Forecast \$000
6,398	Audit fees – departments	5,867	6,952
24,735	Audit fees – other	25,609	25,934
8	Miscellaneous	7	15
31,141	Total Other Revenue	31,483	32,901

Note 4: Operating Costs

Operating costs include:

1999-00 Actual \$000		2000-01 Actual \$000	2000-01 Forecast \$000
25	Asset write-offs	-	-
(63)	Loss/(profit) on sale of physical assets	13	-
(68)	Increase/(decrease) in provision for doubtful receivables	17	-
55	Fees to auditors for audits of the Financial Statements	55	60
7	Fees to auditors for other services provided	14	5
408	Equipment lease costs	387	388
1,271	Property lease costs	1,445	1,471
8,912	Fees paid to contracted auditors	9,765	12,373

Note 5: Capital Charge

The Audit Office pays a capital charge to the Crown on its average taxpayers' funds as at 30 June and 31 December each year. The capital charge rate for the year ended 30 June 2001 was 10 percent (2000 – 10 percent).

Note 6: Capital Contribution

The Audit Office received a capital contribution during the year of \$1.2 million for the selection, purchase and implementation of computer-based audit support tools for Audit New Zealand.

Note 7: Provision for Payment to the Crown

Departments are not permitted to retain operating surpluses. Thus, the surplus for this year of \$350,666 is fully repayable to the Crown.

If there is an operating deficit, any interest received and any profit made on the sale of a physical asset are both returned to the Crown.

30/6/2000 Actual \$000		30/6/2001 Actual \$000
803	Surplus	351
<u>803</u>	Total Provision for Payment to the Crown	<u>351</u>

Note 8: Receivables

30/6/2000 Actual \$000		30/6/2001 Actual \$000
3,286	Trade receivables	2,911
(197)	Provision for doubtful receivables	(214)
<u>3,089</u>	<i>Net Trade Receivables</i>	<u>2,697</u>
-	Crown debtor	(55)
86	Other receivables	99
<u>3,175</u>	Total Receivables	<u>2,741</u>

Note 9: Physical Assets

30/6/2000 Actual \$000		30/6/2001 Actual \$000
	Furniture and Fittings	
2,536	At cost	2,548
(1,806)	Accumulated depreciation	(2,010)
<u>730</u>	<i>Furniture and Fittings at Net Carrying Value</i>	<u>538</u>
	Office Equipment	
2,690	At cost	4,296
(1,962)	Accumulated depreciation	(2,348)
<u>728</u>	<i>Office Equipment at Net Carrying Value</i>	<u>1,948</u>
	Motor Vehicles	
699	At cost	738
(172)	Accumulated depreciation	(193)
<u>527</u>	<i>Motor Vehicles at Net Carrying Value</i>	<u>545</u>
<u>1,985</u>	Total Physical Assets at Net Carrying Value	<u>3,031</u>

Note 10: Payables and Provisions

30/6/2000		30/6/2001
Actual		Actual
\$000		\$000
1,393	Trade payables	1,919
112	Provisions	72
<u>1,505</u>	Total Payables and Provisions	<u>1,991</u>

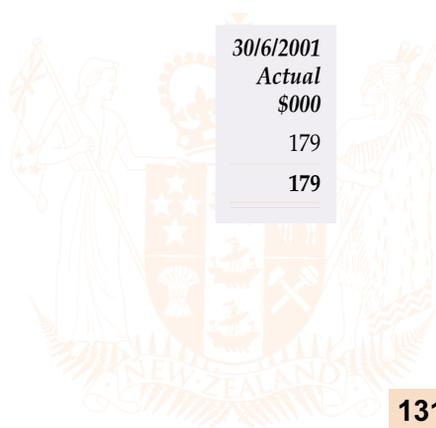
Note 11: Provision for Employee Entitlements

30/6/2000		30/6/2001
Actual		Actual
\$000		\$000
	Current Liabilities	
1,058	Annual leave	1,098
9	Long service leave	-
109	Time off in lieu of overtime worked	74
580	Salary and other accruals	633
-	Retiring leave	80
<u>1,756</u>	Total Current Liabilities	<u>1,885</u>
	Term Liabilities	
96	Long service leave	16
795	Retiring/resigning leave	944
<u>891</u>	Total Term Liabilities	<u>960</u>
<u>2,647</u>	Total Provision for Employee Entitlements	<u>2,845</u>

Note 12: Property Lease Liabilities

Property lease liabilities consist of the unamortised value of lease inducements received.

30/6/2000		30/6/2001
Actual		Actual
\$000		\$000
182	Term liabilities	179
<u>182</u>		<u>179</u>



Note 13: Reconciliation of Surplus to Net Cash Flow from Operating Activities

This reconciliation discloses the non-cash adjustments applied to the Surplus reported in the Statement of Financial Performance on page 120 to arrive at the Net Cash Flow from Operating Activities disclosed in the Statement of Cash Flows on page 123.

1999-00 Actual \$000		2000-01 Actual \$000	2000-01 Forecast \$000
803	Surplus	351	237
	Non-cash Items		
619	Depreciation	764	849
619	Total Non-cash Items	764	849
	Working Capital Movements		
73	(Increase)/decrease in prepayments	38	(25)
(570)	(Increase)/decrease in receivables	434	369
837	(Increase)/decrease in work in progress	(315)	(18)
(645)	(Decrease)/increase in payables	486	561
189	(Decrease)/increase in employee entitlements	129	(776)
(116)	Total Net Working Capital Movements	772	111
	Investing Activity Items		
(38)	Loss/(profit) on sale of physical assets	13	-
(38)	Total Investing Activity Items	13	-
	Other Items		
24	Increase/(decrease) in term employee entitlements	69	(421)
182	Increase/(decrease) in property lease liabilities	(3)	80
36	Other items	-	-
242	Total Other Items	66	(341)
1,510	Net Cash Flow from Operating Activities	1,966	856

Note 14: Financial Instruments

The Audit Office is a party to financial instrument arrangements as part of its everyday operations. These include instruments such as bank balances, receivables and payables.

Credit Risk

In the normal course of its business, the Audit Office incurs credit risk from receivables and from transactions with financial institutions and the New Zealand Debt Management Office of the Treasury.

The Audit Office has no significant concentrations of credit risk. No collateral or security is held or given to support financial instruments.

Interest Rate Risk

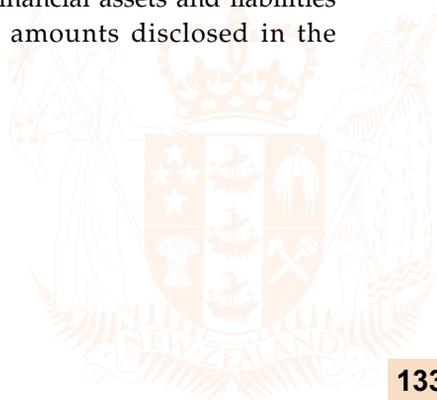
The Audit Office has no interest rate risk, as all cash funds that earn interest are managed as part of the Crown's banking arrangements.

Currency Risk

The Audit Office has no exposure to currency risk, as all financial instruments are in New Zealand dollars.

Fair Values

The estimated fair values of all financial assets and liabilities are equivalent to the carrying amounts disclosed in the Statement of Financial Position.



Note 15: Related Party Information

The net assets of the Audit Office are owned by the Crown. Although the net assets belong to the Crown, the Audit Office is protected through its legislation from undue influence and significant control by the Government.

Some 12% of the Office's revenue is provided by the Crown directly (see Note 2) and a further 16% indirectly through fees for the audit of Government departments (see Note 3). These transactions are not considered to be related-party transactions, as all transactions are on an arm's-length basis with the interests of each party being completely independent.

Note 16: Office Accommodation Statistics

The following statistics for the year ended 30 June 2001 are provided in accordance with directives issued by the Government to chief executives in 1991 on the management of departmental accommodation.

30/6/2000 Actual		30/6/2001 Actual
6,435m ²	Area	6,435m ²
279	Number of staff	271
23m ²	Space allocation per person	24m ²
\$1,270,534	Total costs of leased office accommodation	\$1,445,068
\$3,991	Rent costs per person	\$4,466
\$283	Utility costs per person	\$258
-	Vacant accommodation	-



Appendices



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Appendix 1

Directory of Offices

Office of the Auditor-General

Level 5, Hitachi Data Systems House
48 Mulgrave Street
Private Box 3928
Wellington
Phone (04) 917-1500
Fax (04) 917-1549
Web site: www.oag.govt.nz

Audit New Zealand

National Office

Level 8, St Paul's Square, 45 Pipitea Street
Private Box 99, Wellington
Phone (04) 496-3099 Fax (04) 496-3095

Whangarei

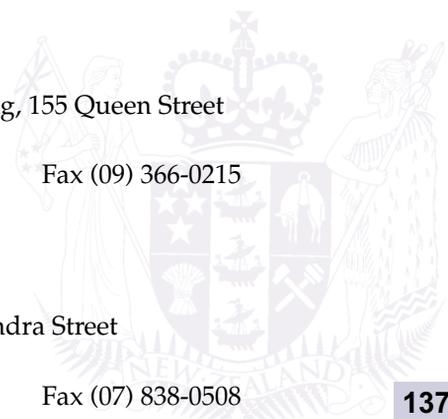
Level 2, State Insurance Building, 96 Bank Street
Private Box 395, Whangarei
Phone (09) 430-3083 Fax (09) 430-3084

Auckland

Level 10, Dynasty Pacific Building, 155 Queen Street
Private Box 1165, Auckland
Phone (09) 373-5457 Fax (09) 366-0215

Hamilton

Level 5, KPMG Centre, 85 Alexandra Street
Private Box 256, Hamilton
Phone (07) 839-3349 Fax (07) 838-0508



Tauranga

Ford Electrical Building, 34 Chapel Street
Private Box 621, Tauranga
Phone (07) 578-8400 Fax (07) 577-9321

Napier

Unit 3, Munroe Court, 62 Munroe Street
Private Box 224, Napier
Phone (06) 835-0663 Fax (06) 835-0348

Palmerston North

292 Featherston Street
Private Box 149, Palmerston North
Phone (06) 354-9702 Fax (06) 356-7794

Wellington

Level 8, St Paul's Square, 45 Pipitea Street
Private Box 99, Wellington
Phone (04) 496-3099 Fax (04) 496-3195

Nelson

Level 1, WINZ Building, 22 Bridge Street
Private Box 13, Nelson
Phone (03) 546-8054 Fax (03) 546-8053

Christchurch

Level 2, Charles Luney House, 250 Oxford Terrace
Private Box 2, Christchurch
Phone (03) 379-8774 Fax(03) 377-0167

Dunedin

Level 5, Forsyth Barr House, 165 Stuart Street
Private Box 232, Dunedin
Phone (03) 477-0657 Fax (07) 479-0447

Appendix 2

Reports Issued During the Year Ended 30 June 2001

Reports to Parliament

General Reports of the Controller and Auditor-General

Central Government: Results of the 1999-2000 Audits – B.29[00c]	20/12/00
Local Government: Results of the 1999-2000 Audits – B.29[01a]	27/6/01

Programmed Special Reports

Auditing a Long-term Financial Strategy – Opotiki District Council Pilot Project	25/9/00
Civil Aviation Authority Safety Audits – Follow-up Audit	20/12/00
Good Practice for Involvement in a Major Project – Lessons from the Opuha Dam Project	13/3/01
Local Authority Governance of Subsidiary Entities	30/3/01
Meeting International Environmental Obligations	8/5/01

Unprogrammed Investigation Reports

Members of Parliament: Accommodation Allowances for Living in Wellington – Interim Report	22/3/01
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Accountability Reports of the Audit Office

Annual Report 1999-2000 – B.28	29/8/00
Forecast Report 2001-2002 – B.28FR(01)	24/5/01

Other Reports And Publications

Programmed Special Reports

Reviewing a Long-term Financial Strategy and Funding Policy – <i>Experiences of the Early Nine</i>	27/10/00
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Unprogrammed Investigation Reports

Auckland City Council's Management of its Responsibilities in the Hauraki Gulf	11/10/00
Waitakere City Council: Payments and Associated Issues Relating to Certain Staff Redundancies	17/10/00
Thames Coromandel District Council: Actions Relating to a Sewerage Scheme for Cooks Beach and Ferry Landing	21/6/01

Other

A Digest of Local Authorities and Their Ownership of Other Entities (Second Edition)	18/8/00
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These reports and publications can be viewed on our web site (www.oag.govt.nz).

Copies of these publications may be ordered from:

Reports Group
The Audit Office
Private Box 3928
WELLINGTON
Ph: (04) 917-6534
Fax: (04) 917-1515
E-mail: reports@oag.govt.nz

Appendix 3

Extracts from *Peer Review of the New Zealand Audit Office*, March 2001

Introduction

The Australasian Council of Auditors-General (ACAG) was established following the 19th Bicentennial Conference of Australasian Area Auditors-General in Perth in 1993. ACAG provides consultative arrangements for the structured sharing of pertinent information and intelligence between Auditors-General. Membership of ACAG is open to the Auditors-General of all audit jurisdictions within Australia, New Zealand, Fiji and Papua New Guinea.

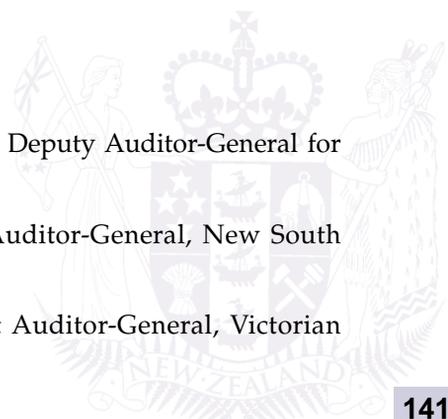
The objectives of ACAG are to foster and promote the development of Public Sector Auditing in the Australasian Region. Promoting the development of a professional quality assurance peer review programme for participating Offices is included among these objectives.

This report describes the findings of the first such peer review of the New Zealand Audit Office, conducted between 26 February and 10 March 2001.

Review Team Members

Review Team members were:

- Dr Gordon Robertson, retired Deputy Auditor-General for Western Australia;
- Mr Phil Thomas, Assistant Auditor-General, New South Wales Audit Office;
- Mr Russell Walker, Assistant Auditor-General, Victorian Audit Office; and



- Mr David McKean, Executive Director, Australian National Audit Office.

Scope and Approach

A significant difference between the New Zealand Audit Office and those of other jurisdictions is the division of the Audit Office into two separate business units:

- the **Office of the Auditor-General (OAG)**, which provides technical advice and oversight of all audit activities; and
- **Audit New Zealand**, which is a quasi-independent business unit that undertakes audit assurance work on the Auditor-General's behalf along with private sector audit service providers.

The ACAG review addressed the Audit Office, most aspects of the Office of the Auditor-General and aspects of Audit New Zealand.

The approach included :

- Extensive briefings from and interviews of senior staff;
- Interviews of key external stakeholders; and
- Review of documents and files.

The Controller functions of the Controller and Auditor-General were not addressed by this review.

Structure of the Report

The report¹⁵ is split into two parts:

- Office of the Auditor-General (sections 2 and 3); and
- Audit New Zealand (sections 4 and 5).

Both parts have an individual Executive Summary and a Detailed Review.

¹⁵ The complete report, including responses to *Opportunities for Improvement* can be found on the OAG website (www.oag.govt.nz).

In addition, the responses of the Office of the Auditor-General and Audit New Zealand to the ‘*Opportunities for Improvement*’ set out in the report are detailed in Section 6.

OAG Executive Summary

Effectiveness of the Auditor-General

The Auditor-General operates as a constitutional safeguard to maintain the financial integrity of New Zealand’s parliamentary system of government. The Auditor-General has no executive power. However, he provides assurance that the 3,900 public entities he audits are operating in a manner consistent with Parliament’s intentions, and can report publicly where this is not the case or where he sees room for improvement. The perceptions of stakeholders, especially the Members of the Parliament to whom he reports and the leaders of the sectors with whom he interacts, are therefore of vital importance to the effectiveness of his function.

The review found that the Auditor-General is effectively meeting the needs of key stakeholders.

Parliament

The Auditor-General is highly regarded by Members of the New Zealand Parliament and his integrity, credibility and authority were described as being without question. The Members interviewed perceive him to be unbiased and fair, and indicated that they place great reliance on his work. His reports to Parliament are widely read by both government and agencies and are seen to contribute to improvement in public administration. Briefings provided to Parliamentary Committees by the Auditor-General’s staff are well received and highly valued, and the quality of explanations in the briefs was described as exceptional. Inquiries conducted by the Auditor-General are also well regarded, with Members expressing the view that the integrity of his inquiries is without question.

Local Government

Representatives of local government similarly hold the Auditor-General in high regard. Both the OAG and Audit New Zealand have a reputation within the local government sector for being incorruptible and are regarded as being measured, sensitive and balanced when dealing with local government issues. Management of local authorities value the assistance provided by the OAG when implementing changes arising from new legislation. They are particularly appreciative of the OAG's good practice guides.

Central Government Agencies

Central government agencies described their relationship with the Auditor-General as satisfactory and the level of consultation taking place as appropriate. There was reluctant acceptance by central agencies of the role for the Auditor-General's staff in providing advice to Parliamentary Committees, although the view was expressed that auditors should be more cautious when framing questions in that environment. Nonetheless, the credibility of the Auditor-General is high and his ability to conduct inquiries, particularly those involving questions of probity, is seen by central agencies to be very important. Central agencies also view the Auditor-General's reports as making a useful contribution to debates on finance and accountability, but felt that the Auditor-General needs to be more transparent about how special studies are chosen. They have a high level of confidence in the financial accounting expertise, professional astuteness and competence within the OAG, and its activities are seen as being proactive and useful in financial matters.

Auditing Non-financial Information

While financial audit opinions are well regarded by all stakeholders, the audit of non-financial information may need some attention. Some reservations were expressed as to the competence of auditors to adequately address non-financial matters.

Operation of the Auditor-General's Office

Legislative Base

The new Public Audit Act, which will take effect from 1 July 2001, is of great significance, as it will give a firm base upon which the Auditor-General will be able to achieve his purpose. The legislation strengthens the independence of the Auditor-General and expands his mandate to include every public entity in New Zealand. The legislation also regularises customary reporting relationships by enabling the Auditor-General to report to Parliament or its Committees, Ministers, public entities or any person.

Funding

Under the New Zealand system of Output Based Management, the Audit Office is funded to produce four Output Classes: Reports and Advice which includes undertaking and reporting on special audits of public entities as well as reporting to and advising parliamentarians on results of audits and investigations; Controller Certifications of authority to release funds from the Crown bank account; Non-Contested Audit Services to approximately 500 public entities where the audit is not allocated by contestable process; and Contested Audit and Assurance Services where the audit is allocated by contestable process. The last of these Output Classes is funded on the Mode B Net basis, enabling costs to be incurred up to the amount of revenue generated, which the review team recognised as essential in the contestable environment.

Structure

The OAG has been structured along sectoral and functional lines that are appropriate for the legislative and environmental framework within which it operates. These comprise: a Parliamentary Group, which deals with the central government sector; a Local Government Group which deals with the local government sector; and groups that deal with Special Audits and Studies, Accounting and Auditing Policy, Legal, and Corporate Support functions.

The review team concluded that the structure is appropriate for the legislative and environmental framework within which the OAG operates.

Audit Process

The OAG has in place a comprehensive strategic audit-planning framework that enables it to gather and distil intelligence on all aspects of public sector activities. From this it develops detailed, rolling, three-year Strategic Audit Plans for both its Parliamentary and Local Government Groups. These plans are used to support decisions to proceed with selected audit interventions such as special studies, a focus incorporated into annual assurance audit work, or best practice guides.

Overall, the review team was impressed by the comprehensiveness and quality of these plans. However, the review team has suggested improving the criteria for selecting audit interventions and improving reporting of the rationale behind selection, thereby satisfying the desire expressed by a number of stakeholders to have a better understanding of how special audit studies in particular are selected.

Special Audits and Studies

Topics for special audits can arise from the Strategic Audit Plans, the OAG policy of following up previous studies, topics emerging from other studies or from special investigations for Parliament on behalf of Select Committees. The Special Audits and Studies Group conducts 7-9 of the special audits undertaken by OAG each year. Other OAG staff, Audit New Zealand, or external consultants, undertake 3-4 of the special audits each year.

Once an audit proposal is formally approved, the methodology followed by the Special Audits and Studies Group in conducting a special audit is sound, containing sufficient guidance to be useful while avoiding excessive prescription. In the files examined by the review team, the methodology was closely followed and appropriately documented. The evidential standards underpinning the special audit studies were good and internal quality assurance was satisfactory.

The review team identified some opportunities for improvements in the areas of project management and report writing.

Enquiries, Complaints and Inquiries

The Auditor-General may inquire, either on request or on his own initiative, into any matter concerning a public entity's use of its resources. Approximately 20 percent of enquiries originate from Members of Parliament. Taxpayers account for a further 20 percent, while ratepayer enquiries account for 60 percent. A number of enquiries lead to major inquiries or special studies separately reported to Parliament by the Auditor-General.

Inquiries undertaken by the Special Audit and Studies group follow their procedure manual. However, there are no established procedures for inquiries undertaken by other groups within the Office. An examination of a limited number of inquiry files showed adequate documentation of the process followed but did not record approvals for the inquiry to proceed. The review team identified an opportunity to improve the procedures surrounding enquiries and complaints.

Contestability

While the New Zealand public sector was undergoing extensive reform in 1992, the then Auditor-General introduced a system of contestability for public sector auditing. The private sector is now involved in about 39 percent of the audit effort and further expansion of contestable audits is planned. The OAG has detailed procedures in place for managing the contestability process, which include oversight of the tendering process by an independent evaluator, the provision of highly regarded Auditing Standards and Guidelines and a number of quality assurance checks.

The review team examined the contestability model in some detail and concluded that it is working as designed. However, monitoring of the outcomes of the contestability regime would be improved by introducing more comprehensive management metrics and it is timely for a formal evaluation

of the benefits and costs of the regime to be undertaken. The review team was also of the view that a retendering policy is needed to limit the duration of the association between individual entities and audit service providers, while addressing equity and fairness to marketplace participants.

Administration

The OAG has in place a comprehensive strategic business plan that addresses its overall operational capacity and links its goals with strategies for all deliverables for both external and internal deliverables. It also has a Board of Management, which meets regularly, making decisions on all significant matters, effectively tracking progress against targets and monitoring financial and other aspects of performance.

The review team concluded that the overall management control framework is both strong and effective and saw only minor areas for improvement.

The corporate support framework provides a comprehensive system of information management and, although there is some room for improvement in the integration of data systems, the information technology, financial, human resources and asset management systems are appropriate for the OAG's needs.

Audit New Zealand Executive Summary

Overview

Audit New Zealand is a business unit within the Audit Office, which carries out audits that it has won the right to conduct on behalf of the Auditor-General in competition with private sector auditors, as well as those audits not awarded under the contestable audit arrangements. It also offers additional assurance services to public entities.

In 2000-01, Audit New Zealand had an annual operating budget of \$21.4 million, and about 220 staff operating from 10 locations. Audit New Zealand is currently of sufficient size to maintain the critical mass needed to support adequate

technical capability and development. However, the review team was advised that significant further reduction in its audit base could jeopardise its future viability.

Management Practices

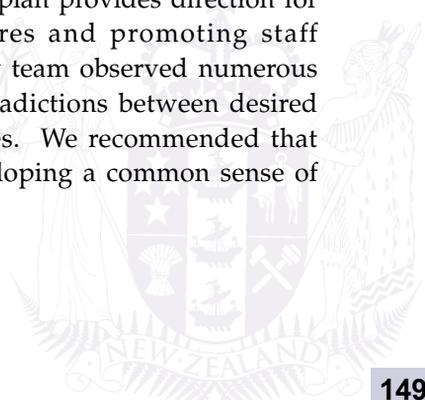
Essentially, Audit New Zealand is market-driven, and its performance measures relate primarily to bottom-line results. However, Audit New Zealand is currently introducing a Balanced Scorecard approach to management reporting, which should improve its focus on audit clients, staff and internal processes.

There are satisfactory procedures in place to enable Audit New Zealand to actively pursue continuous improvement in its management practice. Innovation is part of its strategic plan.

The administrative support structure is adequate to service Audit New Zealand's needs. The time recording system is closely linked to billings and tracks actual time and cost versus budget. There have, however, been examples of budget over-runs and the review team found indications of under-recording of time. We recommended that Audit New Zealand develop a culture that actively discourages non-recording of time.

Under the prevailing highly competitive labour market conditions for auditors, Audit New Zealand has been experiencing a 25 per cent staff turnover per annum. Losses have been mostly within its junior ranks and in the regions. Current staffing numbers are, however, adequate to meet current needs.

The development of the strategic plan provides direction for aligning policies and procedures and promoting staff innovation. However, the review team observed numerous instances where there were contradictions between desired behaviour and current procedures. We recommended that greater attention be paid to developing a common sense of purpose in staff.



Quality Control

Audit New Zealand undertakes suitable assessments of risks associated with its client base. The review team noted that introduction of regular client satisfaction surveys, linked to mechanisms to respond to client concerns, would improve Audit New Zealand's ability to maintain its position in the marketplace.

Audit New Zealand has suitable processes to give it assurance that staff maintain professional independence and the necessary levels of skill and competence to conduct audits. It is currently developing a competency-based human resource model that should integrate strategic direction, recruitment, training and performance assessment.

Audit Policies and Procedures

Audit New Zealand has documented quality control procedures and these are effectively monitored. It also has a professional policies manual that ensures each audit is adequately reviewed. Audit files include comprehensive information about the entity and all relevant correspondence, and also record advice provided to the entity.

Audit New Zealand has suitable systems for determining its personnel requirements, assigning staff to audit engagements and scheduling its work. Staff supervision within assignments is satisfactory.

Audit New Zealand's workflow has a pronounced seasonal variation, with large peaks of effort occurring after the end of the financial year. Greater use of interim audit work could significantly reduce the seasonal peaks in audit workload and associated resource requirements.

Examination of Audit Engagements

The review team examined a number of audit engagements in detail.

There was a high level of compliance with OAG Standards and with Audit New Zealand's methodology. However, the review team gained the impression that methodology is seen

as the law, rather than as a tool to support professional judgement.

Audit New Zealand's unit costs are low, but the hours expended are high. There was some evidence that more realistic assessments of risk may have reduced the audit effort, and in particular the assessment of sample sizes for substantive testing.

We recommended that audit effort be reviewed, to identify areas for improvements in efficiency, and that the methodology be adapted to incorporate better risk assessment, and place greater reliance on client systems, computer audit assurance and internal audit.

The review team had reservations about the relatively low audit effort directed to the audit of non-financial information in comparison to that directed to the audit of financial statements.

The review team also examined a special audit of payroll and expenditure that had been conducted by Audit New Zealand for the OAG. It was satisfactorily planned and executed. The Auditor-General should consider arranging a further review of other assurance services provided by Audit New Zealand, as these were not adequately addressed in this review.



