

What to expect from your audit

AUDIT NEW ZEALAND

Mana Arotake Aotearoa



Contents

What you can expect in this brochure.....	1
What is a public sector audit?	2
Who carries out public sector annual audits?	3
How does a public sector audit differ from a private sector audit?.....	4
What are the key milestones in the audit cycle?	5
What is the purpose of the Audit Arrangements Letter?	6
What are the main areas covered in the audit?	7
How do the auditors examine those areas?	8
Are there limits to what the audit will identify?	9
What if my entity requires a broader scope in some areas?	10
How are audit fees set?	11
What are the outputs of the annual audit?	12
How can my entity get greater value from the annual audit?	13

What you can expect in this brochure.

Audit New Zealand has been appointed by the Controller and Auditor-General (the Auditor-General) to carry out the annual audit of your entity.

This brochure explains the purpose and scope of the annual audit, our role, and what to expect during your audit.

This information will help you and your organisation to:

- be well prepared for the annual audit;
- work effectively and efficiently with the audit team; and
- derive maximum benefit from your audit.

You can find out more about Audit New Zealand, our people, and ways we can help you on our website – www.auditnz.govt.nz.

This brochure is intended as an introduction, but please always feel free to discuss specific questions with your Audit Director or a member of the audit team.

What is a public sector audit?

Public entities are accountable to Parliament and the public for their use of public resources and powers conferred by Parliament.

The Auditor-General provides independent assurance that public entities are operating, and accounting for their performance, in keeping with Parliament's intentions.

Under the Public Audit Act 2001, the Auditor-General is required to carry out annual audits of all public entities, and may also carry out performance audits and inquiries.

In conducting and reporting on the annual audits of public entities, the Auditor-General seeks to "improve the performance of, and the public's trust in, the public sector". This is done by ensuring that an entity:

- is delivering what it has been asked to;
- has operated lawfully and honestly, and has not been wasteful; and
- has fairly reported its performance.

This level of scrutiny is important because public sector organisations provide services for all New Zealanders. All appointed auditors are required to meet the Auditor-General's auditing standards. The standards are based on the ethical and professional standards used by New Zealand Institute of Chartered Accountants members who conduct audits, as well as additional standards that are unique to the public sector audit environment.

A private sector audit examines financial performance so that shareholders in a company can see how well it did. A public sector audit is carried out so all New Zealanders can see how publicly funded organisations performed – and that includes more than just the financial statement numbers.

Who carries out public sector annual audits?

Under the Public Audit Act 2001, the Auditor-General is the auditor of all public entities.

These include:

- the Crown;
- government departments;
- Crown entities;
- State-owned enterprises;
- local authorities and their subsidiaries;
- district health boards;
- tertiary education institutions;
- schools;
- statutory boards;
- licensing trusts; and
- other public bodies.

The Auditor-General appoints an auditor from Audit New Zealand or a private sector accounting firm to be the “appointed auditor” and carry out the annual audit on her behalf.

The Auditor-General selects the provider best suited for the needs of a particular audit. The appointed auditor oversees the audit team working on the annual audit and then signs the audit opinion.

An appointed auditor is generally appointed to audit a public entity for a three-year term, which can be renewed for a further term. The maximum term for an appointed auditor and other senior audit staff is six years.

How does a public sector audit differ from a private sector audit?

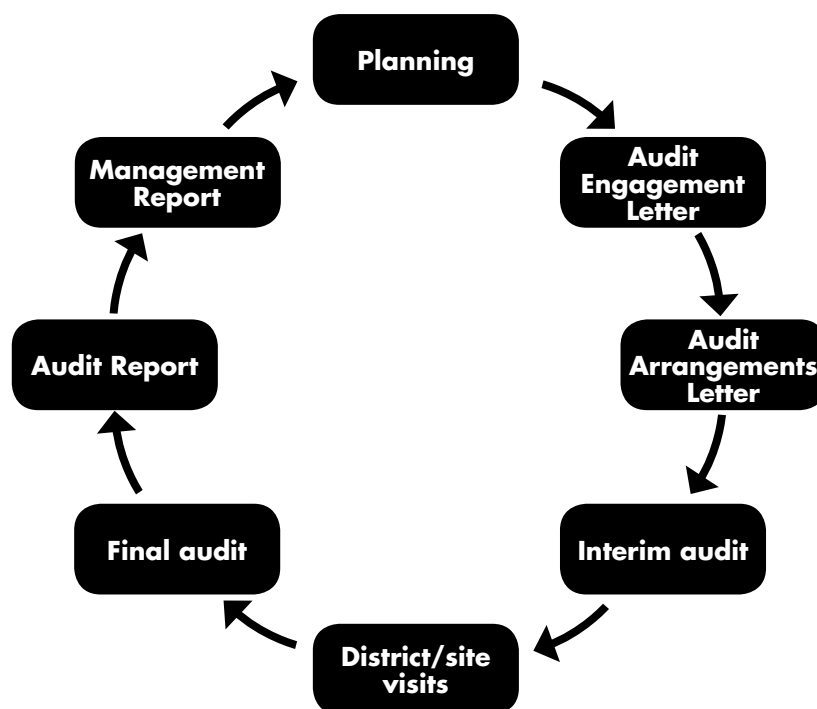
It's important to recognise that public sector annual audits are broader in scope than "normal" private sector annual audits.

A public sector annual audit is an audit of the financial statements and other information (such as non-financial performance information) that a public entity is required to have audited. In carrying out a public sector annual audit, we also assess the entity's compliance with statutory obligations.

In addition, we audit areas of sensitive expenditure and we maintain alertness for and awareness of issues and risks related to the Auditor-General's concerns over effectiveness and efficiency, waste, and a lack of probity or financial prudence.

Auditor-General's mandate and wider concerns	Areas of focus for public sector audits
Annual audit: Do public entities' financial statements and statements of service performance comply with generally accepted accounting practice and give full and accurate public accounts of their performance and position?	Financial statements Statement of Service Performance
Statutory obligations: Are activities being carried out, and accountability requirements met, within the authority granted by Parliament?	Policies Delegations Legislative compliance
Sensitive expenditure: Has expenditure by a public entity have the potential to (or be perceived to) provide private benefit to an individual member of a public entity? Is the expenditure by a public entity unusual for the entity's purpose and/or functions?	Sensitive expenditure Management of conflicts of interest
Effectiveness and efficiency: Are services and activities being carried out efficiently, and achieving their intentions and their desired effect on outcomes or objectives?	Statement of Service Performance Reporting of impacts and outcomes Financial management
Waste: Are taxpayers' dollars and public resources being wasted? Do governance and management arrangements ensure that public entities obtain and apply resources in an efficient and economical way?	Procurement practices Asset management
Probity or financial prudence: Are public entities meeting Parliament's and the public's expectations of an appropriate standard of behaviour? Has a public entity committed to a course of action that may be beyond its means, that may reflect reckless behaviour, or that may reflect an act or omission in bad faith or in disregard of their functions?	Sensitive expenditure Standards of behaviour: the "front page of the newspaper" test Management of conflicts of interest

What are the key milestones in the audit cycle?



Planning – Based on our knowledge of your entity and its business, we will begin to plan for your audit.

Audit Engagement Letter – Issued to your entity’s governing body or Chief Executive to confirm the terms of the annual audit engagement. This usually happens every three years, but if there are significant changes to the terms of your audit, we will issue a new letter.

Audit Arrangements Letter – Issued annually. It details specifics about your audit. You can read more about this letter on the next page.

Interim audit – Depending on the size and complexity of your entity, we may conduct an interim audit during the year to look at the control environment.

District/site visits – We may visit your entity’s regional offices or sites to conduct specific audit work.

Final audit – Carried out after the end of your financial year. The timing of this varies between sectors.

Audit Report – Our opinion on your financial statements and, for some entities, statement of service performance.

Management Report – Key findings from our audit, and recommendations for areas where we’ve identified potential improvements.

What is the purpose of the Audit Arrangements Letter?

Before each annual audit begins, we send an Audit Arrangements Letter to your entity's governing body.

The Audit Arrangements Letter is intended to help you and your staff prepare for the audit team's visit. It sets out the proposed audit arrangements, including:

- the scope of the audit;
- the business and audit risks that we have identified from our planning;
- our proposed audit response to the identified risks;
- confirmation of audit fees (including how the fees will be billed);
- the information we require (documents that we will need to examine during the audit);
- a list of who will be on the audit team; and
- a timetable for completing the audit.

What are the main areas covered in the audit?

The objectives of the annual audit are:

- to give an independent opinion on your entity's financial statements and, as required, statement of service performance; and
- to report on other matters relevant to your entity's financial and other management systems that come to our attention.

To do this, we audit your financial statements and other financial information, for example:

- revenue;
- expenditure;
- personnel/payroll;
- fixed assets;
- depreciation;
- accounts payable/receivable;
- investments;
- borrowings; and
- Controller function and appropriation audit (for central government).

We also audit non-financial information for some entities, such as:

- statement of service performance;
- outcome and impact performance information; and
- legislative compliance.

In performing our audit, we consider:

- governance arrangements;
- the control environment, including aspects such as budgetary control;
- conflicts of interest and transactions with related parties;
- procurement policies; and
- other policies and procedures (such as fraud and sensitive expenditure).



How do the auditors examine those areas?

The audit team will carry out much of your annual audit on-site, where it can readily access your entity's information.

Our work generally includes:

- determining whether significant financial and management controls are in place, are working, and can be relied on to produce complete and accurate data;
- verifying samples of transactions and account balances;
- performing analyses to identify anomalies in reported data;
- reviewing significant estimates and judgements made by your entity's governing body/senior management;
- confirming year-end balances;
- drawing on our in-house specialist assurance services as needed to audit your entity's procurement, contract management, and asset management systems;
- determining whether accounting policies are appropriate and consistently applied; and
- determining whether all financial statement and service performance disclosures are adequate.

In sectors where we audit non-financial performance information, our audit work may also include:

- assessing appropriateness of the non-financial performance framework, including the performance measures that will be reported externally;
- reviewing and testing controls over performance reporting; and
- verifying reported performance for important performance measures.

Our Information Systems Audit and Assurance specialists work with our audit teams to ensure that entities have appropriate information technology controls in place.

In some instances, we may request data sets from your entity to use computer-assisted audit techniques. This allows us to perform data analysis to gain reasonable assurance over account balances and transactions.

Are there limits to what the audit will identify?

An external annual audit is not designed to identify all significant weaknesses in your entity's accounting and internal control systems.

However, our audit will help you to understand how well your policies and controls are working. Your entity's control environment is your best safeguard against fraud and error.

We review systems and controls only to the extent required to design audit procedures and to enable us to express an opinion on the financial statements and, as required, statement of service performance.

We do not examine every transaction and cannot guarantee complete accuracy of the financial statements or the statement of service performance.

An audit provides reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error, but an audit is not intended to detect all fraud or errors that may exist. The governing body and management have primary responsibility for detecting and preventing fraud and errors.

To maintain our independence, we will not become involved in your entity's decision-making processes. However, we are happy to be consulted on issues identified by you during the audit.

We also cannot act in any way that might restrict our ability to exercise the powers conferred on us by law.



What if my entity requires a broader scope in some areas?

If your entity requires additional independent assurance, our Specialist Assurance Services team can be contracted separately, or we can extend the scope of the annual audit (by agreement). This includes areas such as:

- procurement (policies and practices);
- asset management;
- contract management;
- project management;
- conflict of interest;
- risk management practices;
- procedures and protocols for grant programmes;
- performance management and reporting;
- governance arrangements;
- delegations and funding arrangements;
- sensitive and discretionary expenditure;
- activity/output-based funding and costing; and
- sensitive reviews or inquiries related to potential issues with probity, fraud, ethical conduct, or a failure to comply with organisational or government policy or procedures or industry good practice.

Ask your Audit Director or visit our website (www.auditnz.govt.nz) for more information about Specialist Assurance Services.

How are audit fees set?

We charge a fee for the annual audit. The fee is agreed (usually by direct negotiation between your entity and us) at the beginning of the audit contract. This agreement is recorded in an Audit Proposal Letter, which usually covers a three-year period. The fee is confirmed each year in the Audit Arrangements Letter.

In determining the fee, we take into account:

- your entity's track record in preparing the annual accounts for audit and responding to our information requests;
- your entity's management control environment and systems of internal control, including financial controls and risk management;
- the extent to which we can use the work of your entity's internal audit team;
- your entity's size and geographical location(s);
- the effect of changes to mandatory accounting and/or auditing standards on the work we need to complete;
- the effect of changes to legislation specific to your entity;
- the effect of any changes in the operational scale or structure of your entity on audit time or risk; and
- the Auditor-General's expectation about other areas of audit focus.

This information helps us to decide the staff mix and the amount of time required to complete the audit, which in turn helps us to set the audit fee.

If audit fees cannot be agreed, they can be set by the Auditor-General under the Public Audit Act 2001.

Fee over-runs and recovery

The agreed fee is based on the expectations outlined in the Audit Arrangements Letter and the Audit Proposal Letter. If these expectations are not met, and additional audit costs are incurred, then your appointed auditor may seek to recover these costs from you through additional fees.

What are the outputs of the annual audit?

The annual audit results in two types of report.

The **Audit Report** details our findings on your entity's published financial statements and, as required, statement of service performance.

Our audit opinion is part of the Audit Report. We express an opinion on whether the financial statements (and, as required, the statement of service performance) comply with generally accepted accounting practice and fairly reflect the entity's performance and position. The audit opinion is designed to give readers reasonable assurance about the reliability of the information presented.

The Audit Report accompanies your entity's financial statements and, as required, statement of service performance in your entity's annual report.

Our **Management Report** is issued to your entity's governing body and details our key findings and recommendations about significant matters arising from the audit. We may also provide a more detailed report to the management of your entity.

For some of our clients, our Management Report also provides the basis for the letter to your entity's Minister on significant matters arising from the audit.

How can my entity get greater value from the annual audit?

Take an active role during the planning stage

At the audit planning stage, we identify business and audit risks and our proposed response to them. These main risks are documented in our Audit Arrangements Letter and we discuss these with you before finalising our audit plan. You can make this stage of the work as effective as possible by discussing the issues and questions that concern you and how we can address them together.

We encourage you to inform us of changes to your entity's operating environment, business systems, or processes, and any other matters that may be relevant to your audit.

Help to make the audit as productive as possible

We encourage you to discuss with us how you can help improve the efficiency of the audit, perhaps by streamlining your own procedures, improving documentation, or changing the way that your internal audit team operates.

To enable us to carry out the annual audit efficiently and within the proposed audit fee, we expect that, before our audit team arrives, you will:

- have prepared financial statement account balances and disclosures or performance information results with supporting documentation, clearly showing the main transactions making up each balance or result;
- have prepared robust variance explanations (comparing this year's actual results with last year's results and also the budget) for the income statement, the balance sheet, and the statement of cash flows;
- have ensured that your people are available when our audit team is on-site, to answer their questions and provide additional information and records in a timely manner; and
- have done an appropriate level of quality control review over the draft financial statements and statement of service performance before providing them to us for auditing.

Respond to audit findings promptly

We encourage you to respond promptly to any significant findings that we raise with you as a result of the audit. We also suggest that you develop action plans to implement recommended improvements and monitor those actions and the resulting improvements.

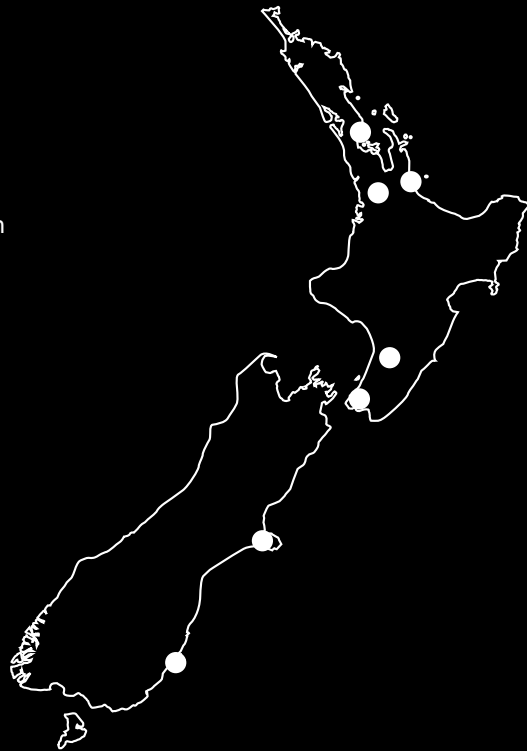
Use us as a sounding board

We encourage you to consult with us about accounting or auditing issues and problems in advance to avoid surprises and resolve issues early. We will be as helpful as possible without compromising our independence.

Our locations

Audit New Zealand has around 200 staff in seven locations: Auckland, Hamilton, Tauranga, Palmerston North, Wellington, Christchurch, and Dunedin.

Our National Office is in Wellington.



Contact us

For more information, please contact your Audit Director on their mobile DDI or on our Freephone number:

0508 AUDITNZ (0508 283 4869)

In Wellington, please ring 04 496 3099.

You can also visit our website www.auditnz.govt.nz.

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