



The Controller and Auditor-General

Tumuaki o te Mana Arotake

Draft Annual Plan for the year ending 30 June 2005

**Prepared as required by
section 36(1) of the Public Audit Act 2001**

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Speaker's Foreword

Introduction by the Controller and Auditor-General

I am pleased to submit my Draft Annual Plan for 2004-05 under section 36(1) of the Public Audit Act 2001.

Over the past nine months, we have undertaken a significant amount of work on creating our Strategic Plan for the five years 2005 to 2009 (being the balance of my term as Auditor-General). This work has provided us with a robust understanding of our environment and stakeholder needs, and our current capability to respond. On the basis of this understanding, we have developed our strategies and actions for the next five years. This Draft Annual Plan outlines our specific actions for 2004-05.

The Officers of Parliament Committee has signified its willingness to invest in our future capability through its recommendation that Parliament provide additional funding for us to undertake ongoing research and development, and product development, and to build depth into our capabilities and capacity to be more responsive and timely. This Draft Annual Plan reflects the recommended new level of funding agreed by Parliament and sets out how, over the forthcoming financial year, we will maximise this funding to enhance our outcomes.

This Draft Annual Plan is designed to follow the “Statement of Intent” model – and we have built a comprehensive measurement framework to better measure the difference we make.

We circulated our “Preliminary Draft Annual Plan” to all select committees in December 2003. This document is the statutory Draft Annual Plan and incorporates our response to the feedback already received on that preliminary draft. I thank Members for that feedback and invite any further feedback the House may have under section 36(3) of the Public Audit Act by 30 April 2004.

Kevin Brady
Controller and Auditor-General
00 April 2004

Statement of Responsibility

The forecast financial and other statements for the Controller and Auditor-General for the year ending 30 June 2005 contained in this Draft Annual Plan have been prepared in accordance with section 36(1)(b) of the Public Audit Act 2001 and sections 34A and 40 of the Public Finance Act 1989.

As Controller and Auditor-General, I acknowledge, in signing this statement, that I am responsible for the forecast output information and financial statements contained in this Draft Annual Plan.

The forecast financial statements, which include objectives for output and financial performance, are consistent with the plans considered by the Officers of Parliament Committee when it examined (on behalf of the House of Representatives) the 2004-05 budgetary estimates for the Auditor-General submitted pursuant to section 17 of the Public Finance Act 1989.

We, the undersigned, certify that the information contained in this Draft Annual Plan is consistent with the appropriations contained in the *Estimates* for the year ending 30 June 2005 that are to be laid before the House of Representatives under section 9 of the Public Finance Act 1989.

K B Brady
Controller and Auditor-General
00 April 2004

D E Atkin
Finance Manager
00 April 2004

Part One

Strategic View

Background

Our Role

The office of Auditor-General is a statutory office created by the Public Audit Act 2001. The office exists as **a constitutional safeguard to maintain the financial integrity of New Zealand's parliamentary system of government.** The Auditor-General is an officer of Parliament, and in that capacity is independent of the executive government and Parliament in discharging the functions of the office, but answerable to Parliament for his stewardship of the public resources entrusted to him.

In New Zealand's system of government, Parliament is supreme – all authority for governmental activity ultimately stems from Parliament. Public sector organisations are therefore accountable to Parliament for their use of public resources and powers it has conferred on them.

Parliament seeks independent assurance that public sector organisations are operating, and accounting for their performance in accordance with Parliament's intentions. There is also a need for independent assurance in local government – local authorities are accountable to the public for using the resources they fund through rates. As an Officer of Parliament, the Auditor-General provides this independent assurance to both Parliament and the public.

The **Auditor-General's key concerns** are a reflection of his mandate under the Public Audit Act. His key concerns are:

- **Performance** – *Have public entities undertaken activities in accordance with Parliament's intentions, and in an effective and efficient manner?*
- **Authority** – *Have activities, resourcing and accountability requirements been undertaken within the authority granted by Parliament?*
- **Waste** – *Have resources been obtained and applied in an economical manner? That is, taxpayers' dollars are not being wasted.*
- **Probity and Financial Prudence** – *Are entities meeting parliamentary and public expectations of an appropriate standard of behaviour in the public sector?*
- **Accountability** – *Have entities given full and accurate accounts of their activities, and of their compliance with Parliament's intentions, through the annual reporting cycle? Are governance and management arrangements suitable to address the concerns identified above?*

Our Structure

The Auditor-General employs staff and engages private sector auditing firms to carry out his functions in relation to public entities. This combination of internal and external resources we refer to as “the Audit Office”. The current Auditor-General has recently introduced an “audit resourcing model” which replaces the previous contestable model for selecting auditors to carry out annual audits of public entities.

The audit resourcing model allows the Auditor-General greater choice and flexibility in the allocation of his work to the auditors who carry out annual audits. The introduction of this new way of working has created opportunities for greater collaboration between the organisations that make up the Audit Office. These organisations can be represented as follows:

The **Office of the Auditor-General** (the OAG) undertakes –

- Strategic audit planning;
- Policy development and standard setting;
- Appointing auditors and overseeing their performance;
- Carrying out performance audits;
- Parliamentary reporting and advice; and
- Inquiries and other special studies.

Audit New Zealand (ANZ) –

is the operating arm of the Auditor-General and carries out annual audits allocated to it under the resource allocation model. ANZ also provides other assurance services within the Auditor-General’s mandate to public entities.

Other **Audit Service Providers** (ASPs) –

are private sector accounting firms which carry out annual audits allocated to them under the resource allocation model. ASPs also offer wider assurance services to public entities.

Our Strategic Direction

This Statement of Intent builds from the work we have undertaken recently on developing our five-year Strategic Plan. Through this process, we have gained a comprehensive understanding of our environment, our stakeholder needs and our current capability to respond (these are outlined on the following pages).

As a result, we have clarified our outcome statements and our internal operating vision and strategy.

The **end outcome** we strive to contribute to is:

TRUST IN AN EFFECTIVE PUBLIC SECTOR

This end outcome and our intermediate outcomes are described fully on pages 18 and 19.

In order to successfully achieve our outcomes, we have chosen an **internal operating vision and strategy**.

We want “**to set the benchmark for design and delivery of independent assurance services**”. This means we want to be acknowledged as the innovators in designing public sector independent assurance services and high quality deliverers of such services. We refer to this internally as being “product leaders”.

To do this, we will focus our efforts on maximising how we develop and use the “best people” within the broader Office (OAG, ANZ and our other ASP colleagues) to create the “best products and services”.

Operating Environment

Ongoing Changes

There is a very wide range of issues in our environment with audit implications. The key issues fall broadly into the significant and ongoing changes in:

- the accounting and auditing profession;
- public entities' legislative and operating environments; and
- information and reporting requirements and methods.

Accounting and Auditing Profession

- Credibility of the profession under pressure after major international corporate collapses.
- “Back to basics” response from the accounting and auditing profession – e.g. increased emphasis on risk and quality, audit methodologies being reappraised, firms rationalising service lines, increased ratio of senior staff to junior staff, increased emphasis on core auditing and accounting skills, resultant increases in audit fees.
- Implementation of standards based on International Financial Reporting Standards (IFRSs) in the public sector by 2007.

Public Entities' Legislative and Operating Environments

- Considerable flow-on audit implications arising from ongoing legislative changes (e.g. Local Government Act 2002, Public Finance Act amendments, Crown Entity legislation, Land Transport Management Act 2003) and significant decisions (e.g. that New Zealand will adopt IFRS-based accounting standards).
- Increased level of scrutiny on the activities of the NZ public sector, particularly in the areas of NGO contracting, governance and accountability.
- New and different ways of doing business, e.g. e-government/business.

Information and Reporting Requirements and Methods

- Significant changes in reporting requirements and methods – e.g. Long Term Council Community Plans, XBRL, Sustainable Development Reporting, Managing for Outcomes/Statements of Intent, etc.
- Information is becoming more complex – e.g. inter-generational equity, spending choice, capability, and value for money.
- Entities are being asked to enhance their reporting – particularly in non-financial areas – and they are looking for enhanced external reporting on probity and waste, capability and risk.
- Our stakeholders are asking for more help in navigating their way through information, new legislative requirements, and reporting.

- They are also looking for us to make use of our sector knowledge to provide best-practice information, where appropriate.

Stakeholders' Needs

Our key external stakeholders are Parliament, local constituencies and public entities within the Auditor-General's mandate.

We have some well-established stakeholder validation and feedback mechanisms, including the Auditor-General's meetings with Select Committee Chairpersons, Parliamentary Party Leaders and public entities; client satisfaction surveys undertaken by Audit New Zealand and other Audit Service Providers; and the Local Government Advisory Group. We also recently carried out a pilot focus group exercise. In addition, we receive extensive feedback from our ongoing liaison with sectors and entities.

We intend to continue to develop our stakeholder validation and feedback mechanisms over the next three years.

Our stakeholders are telling us that:

WE ARE DOING WELL AT –

- Preserving our independence and maintaining our credibility
- Servicing Parliament's assurance needs
- Maintaining strong sector relationships
- The depth in our relationships with public entities
- The robustness of our standards
- The knowledge and quality of our people.

THEY WOULD LIKE MORE –

- Performance audits (value for money assurance)
- Help to navigate through information and understand and apply legislative changes
- Best practice guidance.

WE COULD DO BETTER BY –

- Improved timeliness, especially for inquiries and performance audits
- Greater responsiveness, and innovation.

Each of these is described in detail in our Five-year Strategic Plan, pages 15-16, which can be viewed on our web site at www.oag.govt.nz .

Key Strategic Issues

Based on our environmental assessment, we have concluded that, over the next three to five years, we will need to deal with the following key strategic issues:

- the significant and ongoing changes in the accounting and auditing profession, in public entities' legislative and operating environments, and in information and reporting requirements and methods;
- the current desire for more of what we do;
- the improved timeliness sought by our stakeholders, especially for inquiries and performance audits;
- our stakeholders' desire for us to show greater responsiveness and innovation;
- the increasing scrutiny of the public sector;
- the opportunities created by the change in the way we choose the auditors who carry out annual audits; and
- our desire to use the best people (internally and externally).

As part of our response to these issues, we have recently prepared a Three-year Business Plan for the Officers of Parliament Committee. This document sought additional baseline funding in the following areas:

- to maintain our existing state capability;
- to implement our Strategic Plan initiatives (capacity for the Office to undertake research and development, and product development; and increased capability for performance audits and inquiries); and
- for other funding priorities.

The Officers of Parliament Committee has proposed to Parliament that it approves this additional baseline funding. The proposed increases are included in the Statement of Objectives in our Forecast Financial Statements in Part Three.

Strategic Risk Framework

As part of our strategic planning, we have undertaken a comprehensive assessment of our strategic risks and developed appropriate mitigation and/or management strategies. We have also developed indicators to monitor the success of our risk management strategies. (Some of these measures, by their very nature, are a subset of our outcome, output or capability measures.) These are:

Strategic risk	We will measure how we have managed/mitigated this risk by:	Key measures we will use:
Not maintaining our credibility and reputation	Assessing whether there has been any damage – real or perceived – to the credibility and/or reputation of the Audit Office; and Assessing whether our mitigation strategies have been effectively implemented	<ul style="list-style-type: none"> ▪ No instances where our credibility/reputation is badly damaged or litigation action taken against the Office ▪ Sample stakeholders' assessment of perceptions of the Office's credibility and reputation ▪ Our risk mitigation strategies are substantially implemented (90% completed)
Not meeting our stakeholders' expectations	Assessing whether our stakeholders perceive we add value, are timely and are relevant	<ul style="list-style-type: none"> ▪ Sample stakeholders' assessment of the value we add, our timeliness and our relevance
Not maintaining and building our capability	Assessing the Office's ability to attract and retain suitably qualified staff, and to maintain its investment in their development	<i>Covered by our capability measures (refer page 29)</i>
Failure to successfully implement our five-year Strategic Plan	Assessing the extent of implementation of our Strategic Plan activities	<ul style="list-style-type: none"> ▪ Our Strategy Implementation Plan is substantially implemented (90% completed)
Not maintaining our independence	Assessing whether there have been any failures of independence of the Audit Office – this includes both breaches of independence in the work we undertake (i.e. breaches of AG-100) and breaches of independence by the people working for the Audit Office	<ul style="list-style-type: none"> ▪ Our risk mitigation strategies are substantially implemented (90% completed) ▪ There are no failures of AG-100 ▪ Independence Declarations for all OAG and Audit New Zealand staff are completed every six months
Serious audit failure	Assessing whether we have robust professional standards, quality assurance regimes, audit methodologies, peer review and substantiation processes; and the quality and training of our people; and the sufficiency of Professional Indemnity Insurance	<ul style="list-style-type: none"> ▪ Our risk mitigation strategies are substantially implemented (90% completed)

Intended Outcomes

Outcome Framework

Our outcome framework is modelled on the “Managing for Outcomes” approach, as depicted in the diagram on the opposite page.

The **logic flow and definitions** of our outcome framework (and therefore, this Plan) are as follows:

end outcome The desired situation sought. The result that the Office intends to achieve over time. Others may play a part in the achievement of the end outcome.

intermediate outcome(s) Contributing outcome(s) to the end outcome. The “vital few” – those where the Office will have a major impact.

outputs The activities planned by the Office which support the achievement of the intermediate outcomes (and ultimately lead to the end outcome). Classified as “output classes”.

business strategies¹ The strategies that the Office will undertake to assist in achievement of the intermediate outcome(s). This includes strategies relating to capability.

actions The specific actions that the Office will implement over the term of the Strategic Plan to give effect to the business strategies. (The actions relating to 2004-05 are detailed in Part Two: Proposed Work Programme on pages 47-49.)

The diagram on the next page details the outcome framework and shows the linkage between our outputs and intermediate outcomes, and the end outcome. Each of these is discussed further on the following pages.

¹ Sometimes called “interventions”.

[insert diagram from separate file]

The End Outcome

The “end outcome” is the desired situation sought as the result of our (and others’) work. While aspirational in nature, it is nevertheless achievable. Others will also play a part in its achievement.

Below we identify the end outcome to which the Audit Office contributes, and provide a fuller “vivid description” of the desired state. We also identify others who play a key role in the achievement of this end outcome.

End outcome	TRUST IN AN EFFECTIVE PUBLIC SECTOR
Description of the desired state –	<p>“<i>Trust in ...</i>” – being where Parliament and the public know whether public entities (including central and local government entities, and others such as schools) are –</p> <ul style="list-style-type: none">• carrying out their activities effectively, efficiently, and appropriately;• using public funds wisely; and• reporting their performance accurately –• and know that, if this is not the case, we will tell them. <p>“... <i>an effective public sector</i>” – being where public entities operate effectively and with a focus on continual improvement and innovation.</p>
Other contributors –	<p>Others who contribute to the achievement of this end outcome are:</p> <ul style="list-style-type: none">• Central Agencies – i.e. SSC, DPMC and Treasury; and• Public sector entities – through their actions and behaviours.

Intermediate Outcomes

Our “intermediate outcomes” are the outcomes we can directly influence which will significantly contribute to the achievement of the end outcome. They are also known as “impacts”.

The desired situation we aim to create as the direct result of our work is where there is:

- Independent assurance that public entities are acting legally, ethically, and with probity;
- Advice to improve public entity operations; and where
- Parliament has control of expenditure.

We achieve this desired situation through the provision of two intermediate outcomes:

- Independent assurance and advice; and
- Parliamentary control of expenditure, delivered through our “controller function” activities.

Independent assurance and advice

We help to ensure the legality, ethicality, and probity of entity actions by being vigilant for any behaviour below expectations, and highlighting and fully investigating any irregularities we come across in the course of our work.

We contribute to improved public entity operations by:

- assessing entity operations (through our assurance activities), and then
- telling relevant stakeholders (through our reporting and advisory activities) about:
 - the sufficiency and appropriateness of public entity information systems;
 - the effectiveness and efficiency of entity operations; and
 - the accuracy and adequacy of entity reporting.

Parliamentary control of expenditure

We play a key role in ensuring parliamentary control of expenditure through our “controller function” activities. These activities ensure that public money released from the Crown bank account is applied only for purposes that are lawful and are within the appropriations voted by Parliament.

Outputs

In order to achieve our impacts, we intend to deliver the following outputs. Full details of the outputs are set out in the Proposed Work Programme on pages 30-53 and the Statement of Objectives on pages 58-72.

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

- Reporting to and advising parliamentarians – either in Select Committees, or as Ministers or individual MPs – on the results of audits and investigations. The bulk of this is done through Financial Reviews and Estimates Examinations.
- Responding to enquiries from taxpayers, ratepayers or individual Members of Parliament on matters that we think appropriate to investigate. Nearly 300 enquiries are received each year.
- Undertaking and reporting on performance audits of public agency operations. These audits examine questions such as entity performance, the quality of accountability to Parliament, and the probity of activities. Subjects for the audits are chosen using the Strategic Audit Planning process (see pages 34-35).

Under the Public Audit Act 2001, this activity now covers almost all of the public sector. The quality of this work is ensured by rigorous internal procedures, including peer review and substantiation of major reports. Principles of natural justice are applied in the clearance of published reports, so that public agencies and affected individuals have an opportunity to check the factual accuracy of the findings and comment on the conclusions drawn.

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

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 Parliamentary appropriations and are for lawful purposes. A key part of this activity is checking that warrants issued by the Governor-General for the release of funds, and daily amounts released to Departments to fund their activities, are supported by appropriations.

Note: The Public Finance (State Sector Management) Bill, if enacted, will change the mix of our work in Controller activities in the future.

Output Class D3 – Provision of Non-contested Audit Services

Output Class D4 – Provision of Contested Audit and other Assurance Services

Both Output Classes D3 and D4 relate to the conduct of the annual audits of public entity financial reports. The Auditor-General has a statutory duty to conduct an audit of more than 4,000 public entities. These audits are undertaken by either Audit New Zealand or by private sector auditors.

Annual audits result in –

- **Audit Reports** – on whether the financial reports fairly reflect the financial and non-financial performance of the agencies; and
- **Management Reports** – to the management and governing bodies of agencies, on issues arising from the audit.

Audit service providers also provide other auditing and assurance services to public entities, at their request.

Both Output Class D3 and D4 are funded mainly by fees paid by the public entities being audited. The difference in output classes relates to the method by which the audit service provider has been selected – D4 can involve a competitive tender process.

The quality of audit and assurance work carried out under these two output classes is maintained by:

- being subject to the **Auditor-General’s Auditing Standards²**;
- provision of detailed guidance on audit risks and issues;
- training of auditors; and
- post-audit quality control which evaluates every auditor’s work at no more than three-yearly intervals.

Note: The move to resource allocation may result in changes to these output classes over time.

²

See www.oag.govt.nz

Measuring Our Outcomes

To enable us to assess how well we are progressing in achieving our outcomes, we have continued the development of performance measures for impact evaluation for our end outcome and intermediate outcomes. (This forms part of our overall measurement framework.)

Our impact evaluation considers whether the desired state has been achieved (i.e. maintained and/or improved).

Below we describe how we would assess our impact or contribution to outcomes.

	End outcome	Intermediate outcome 1	Intermediate outcome 2
	<i>TRUST IN AN EFFECTIVE PUBLIC SECTOR</i>	<i>INDEPENDENT ASSURANCE AND ADVICE</i>	<i>PARLIAMENTARY CONTROL OF EXPENDITURE</i>
We will assess our impact/ contribution to this by:	<ul style="list-style-type: none"> ▪ Assessing the extent of improvements over time in Parliament and public perceptions of public sector performance and trustworthiness 	<ul style="list-style-type: none"> ▪ Assessing whether real change and improvement is happening as a result of our work ▪ Assessing whether the Audit Office is perceived by its stakeholders as an essential part of the system 	<ul style="list-style-type: none"> ▪ Assessing whether breaches of parliamentary control of expenditure have occurred
Key measures we will use:	<ul style="list-style-type: none"> ▪ New Zealand maintaining or improving its Transparency International ranking ▪ Improvements in aspects of entity management (as measured through our assessments) 	<ul style="list-style-type: none"> ▪ The actions others take as a result of our work ▪ Stakeholder assessment of our relevance and timeliness, and the value we add ▪ Reduction over time in the recurrence of key themes in inquiries we conduct 	<ul style="list-style-type: none"> ▪ All funds released from the Crown bank account will have appropriate parliamentary approval (100% compliance)

Business Strategies

To enhance the achievement of our outcomes, we have developed **three business strategies**. These strategies have emerged from our work on our five-year Strategic Plan and cover both of our intermediate outcomes. The strategies are:

- **Shaping our services** to anticipate and respond to Parliament and other stakeholders' needs and our changing environment;
- **Building our capability** to create and deliver our services; and
- **Fostering relationships and ways of working** that support our strategy.

These mean:

Shaping our services

Having the “best” independent, public sector assurance products and services, which constantly evolve to meet the needs of Parliament and our other stakeholders and to respond to the ongoing and significant changes in our environment.

Building our capability

Investing in the future capability of the Audit Office through targeted attraction, retention and development strategies. Having systems and processes which support the work of the Office. And, having access to the “best people” across the wider Audit Office (i.e. OAG, ANZ and our other ASP colleagues).

Fostering relationships and ways of working

Encouraging and valuing behaviours which support across-Audit Office working and innovation.

For each strategy, we have identified specific **areas of focus** which we will concentrate on over the next three to five years. These are:

Shaping our services –

- Ongoing research and development and product development, and innovation;
- Changes to the breadth and depth of our current assurance products and services; and
- Enhancement of our Strategic Audit Planning process and deployment of our full range of assurance interventions around issues/risks.

Building our capability –

- Continual adaptation of our organisation (including enhancing our capabilities).

Fostering relationships and ways of working –

- Facilitating opportunities for collaborative working.

Each of these areas is described in the following paragraphs.

STRATEGY ONE: SHAPING OUR SERVICES

ONGOING RESEARCH AND DEVELOPMENT AND PRODUCT DEVELOPMENT, AND INNOVATION

- In the last decade, we have had an over-reliance on Audit Service Providers to develop assurance approaches. This did not happen to the extent needed – primarily due to their limited sector coverage and lean pricing of audits.
- The Audit Office now intends to lead its own product development. This requires a significant investment in establishing the infrastructure to support research and development and product development, and accessing the right capability.

CHANGES TO THE BREADTH AND DEPTH OF OUR CURRENT ASSURANCE PRODUCTS AND SERVICES

- We believe most of what the Audit Office does now (refer to our “activities” on pages 35-36) is the right work. However, we believe more breadth and depth is required, particularly in the areas of annual audits and performance audits. In addition, our stakeholders are seeking improved timeliness of performance audits and inquiries.
- We will develop the capability of ASP’s to deliver enhanced annual audits, and increase our capability for performance audits and inquiries. We will also improve our timeliness.

ENHANCEMENT OF OUR STRATEGIC AUDIT PLANNING PROCESS AND DEPLOYMENT OF OUR FULL RANGE OF ASSURANCE INTERVENTIONS AROUND ISSUES/RISKS

- Our Strategic Audit Planning process is among the best internationally. However, there are opportunities for greater involvement, communication and knowledge sharing between people working in and for the Audit Office. In addition, we wish to enhance the extent of integration of our assurance responses around issues/risks.
- We will maximise effort and simplify processes/systems. We intend to pilot an enhanced Strategic Audit Planning process prior to full implementation.

STRATEGY TWO: BUILDING OUR CAPABILITY

CONTINUAL ADAPTATION OF OUR ORGANISATION (including enhancing our capabilities)

- Changes to the way we choose auditors who do the annual audits opens the way for many of our processes and systems to be simplified across the Office. We are committed to “practising what we preach”, and maintaining operational excellence.
- We will also enhance our capabilities through the attraction, development and retention of high performing people.

STRATEGY THREE: FOSTERING RELATIONSHIPS AND WAYS OF WORKING

FACILITATING OPPORTUNITIES FOR COLLABORATIVE WORKING

- The removal of contestability allows the organisations that make up the Audit Office to work closer and to share knowledge and resources.
- We will identify opportunities to facilitate the exchange of knowledge and resources.
- We will also encourage and value collaborative behaviours.

The specific actions we propose to take during 2004-05 are detailed on pages 48-50 of this document.

Capability

Current Capability

The Audit Office's ability to currently deal with these changes in our environment and to respond to stakeholders' needs can be characterised as follows:

Strengths

- Our independence
- Reputation and credibility
- Clear mandate from the Public Audit Act 2001
- Knowledge and expertise of our people
- Sector knowledge and presence
- Strong knowledge of the accounting and auditing profession
- Well-developed standards, policies and sector information
- Rigorous Strategic Audit Planning process
- Depth of relationships with sectors and public entities
- Contribution to our international colleagues, particularly those in the South Pacific
- Our standing with Parliament.

Weaknesses

- Light mix of performance audits compared to financial report audits, and compared to our international counterparts
- Capability for performance audits is lean
- Timeliness variable (inquiries and performance audits)
- Not adequately resourced or funded to respond to increased complexity and volume of inquiries
- Limited product development/innovation occurring
- No knowledge management strategy for the Office as a whole
- Sharing of auditing best practice and sector knowledge inhibited under contestability
- Limited ability to invest (capital adequacy)
- Tension between innovation and task/productivity focus
- Level of work in non-financial reporting and waste, probity, governance and accountability in annual audits needs increasing
- Over-reliance on Audit Service Providers to develop audit approaches.

Opportunities

- Introduction of Resource Allocation Model for provision of annual audits
- Enhanced integrated Strategic Audit Planning involving all Audit Service Providers and strategically deploying the full range of assurance interventions around risks/issues
- Increased collaboration (knowledge and resource sharing) internally and within the auditing market
- Freeing up of senior time for product development and innovation.

Threats

- Failure to respond to the key changes in our environment or to meet stakeholders' needs
- Impact on the Office of challenges to the credibility of the accounting and auditing profession
- Reputational risk through our wide exposure and coverage of work
- Competition for people and resources
- Difficulties in maintaining currency and sustainability of audit methodology
- Inefficiency or loss of quality.

In addition to the changes in our environment and our stakeholders' needs, the Office itself desires to:

- Use the best people (internally and externally);
- Work collaboratively (OAG – ANZ – ASPs);
- Gain sector consistency;
- Invest in our future;
- Build depth;
- Maintain ongoing efficiency;
- Continue delivering to Parliament, local constituencies and public entities;
- Manage through all the changes;
- Become more innovative;
- Restore and build capability; and
- Grow and develop our people.

Already we have made some progress, e.g. the changes in the way we choose the auditors who carry out annual audits – moving from a market model to a planned approach (the “audit resourcing model”) – will enable us to do the first three bullet points better. But it only goes part of the way, and we need to make further changes and investments.

The SWOT analysis on the previous page also tells us that the Office is under stress and we have some significant challenges to deal with. The indicators of this are:

- We are struggling to maintain our capability and market competitiveness;
- We are continually having to apply senior resources to deal with unplanned work, i.e. inquiries;
- We have limited ability to invest in product development;
- We have insufficient depth in our senior staff;
- Our timeliness is variable, especially for inquiries and performance audits; and
- Our ability to invest in the capability development of our staff is limited.

Capability Requirements

On pages 25 and 26, we outlined our current capability to respond to the issues in our environment and our stakeholders' needs. For the Office to achieve its business strategies and ultimately its outcomes, we have the following capability requirements:

OUR PEOPLE

- Increased capability and capacity to:
 - Undertake research and development, and product development;
 - Carry out performance audits – including building a critical mass of professionals working in this area (for peer support, training, peer review and the development of robust methodologies and approaches); and
 - Undertake inquiries.
- Strengthening our core capabilities/skills in:
 - Professional leadership of public sector auditing and accounting;
 - Relationship management (to further build relationships with our key stakeholders and work collaboratively with others); and
 - Strategic leadership.
- Encouragement and recognition of the following behaviours:
 - Office-thinking;
 - Joint working – internally and externally; and
 - Innovation.

OUR PROCESSES

- The creation of more flexible access to the “best people”;
- The ability to backfill roles;
- The ability to better balance productivity with innovation and create “headspace” to think; and
- Greater alignment of our Corporate Support strategies and processes across the OAG and Audit New Zealand.

OUR SYSTEMS

- Design and implementation of a Knowledge Management strategy and an Information Systems Strategy; and
- Improved project management disciplines.

How we intend to respond to these requirements is outlined in Part Two under “Strategic Plan Implementation” on pages 48-50.

Measuring Capability Success

We have developed capability measures to assess the success of our capability strategies. There are three dimensions of our assessment:

- People – measuring the extent of staff development, retention and utilisation that has been achieved;
- Culture – measuring the extent of changes to the way people work together; and
- Processes/Systems – measuring the effectiveness of our processes and systems, including governance and accountability mechanisms.

Strategic risk	We will measure how we have built capability for the future by:	Key measures we will use:
People – staff development, retention and utilisation	Assessing our ongoing ability to attract, develop and retain suitably qualified staff	<ul style="list-style-type: none"> ▪ Average staff tenure ▪ Retention targets ▪ % of ready successors for key roles ▪ Hours and \$ spent on staff development ▪ Pass rates for technical accounting exams ▪ Equal Employment Opportunity initiatives substantially implemented (90% completed) ▪ Effectiveness for Maori initiatives substantially implemented (90% completed) ▪ New staff resources (for performance audits) substantially recruited ▪ Audit New Zealand ratio of senior to junior staff
Culture – changes to the way people work together	Assessing whether our staff perceive that the Office creates an environment which supports them to be innovative and work collaboratively	<ul style="list-style-type: none"> ▪ Staff assessment of the extent of innovation and collaborative working that occurs and is encouraged
Processes/Systems	Assessing how effective the Office's processes and systems are in supporting the work of the Office (including the governance and accountability mechanisms)	<ul style="list-style-type: none"> ▪ Benchmark peer comparators ▪ Strategy Implementation Plan substantially achieved ▪ Staff assessment of quality and usefulness of business processes/systems

Part Two

Proposed Work Programme

Introduction

Section 36 of the Public Audit Act 2001 requires our Draft Annual Plan to include the Auditor-General's proposed work programme for the coming financial year.

In previous years, we have identified:

- special areas of focus we will be asking our auditors to look at during the annual audits;
- proposed performance audits and special studies; and
- other contributions the Office will make to better public sector administration.

This year, we will extend our proposed work programme to include two additional areas:

- How the Audit Office intends to implement its Strategic Plan initiatives over the coming year; and
- Our proposed research and development, and product development programme for the year.

We believe the addition of these two areas in our proposed work programme will assist Parliament to better understand the work of the Office and provide the platform for the Auditor-General to be properly accountable for the achievement of our Strategic Plan, particularly in relation to the further funding by Parliament recommended by the Officers of Parliament Committee.

Strategic Audit Planning

Prior to developing our proposed audit/assurance work programme, we undertake a robust Strategic Audit Planning process. This is acknowledged as being a leading process by our international counterparts. We have, however, identified that there are opportunities for this process to be enhanced through greater involvement, communication and knowledge sharing between people working for and with the Audit Office. Over the coming year, we intend to pilot a revision of our Strategic Audit Planning process.

The current Strategic Audit Planning process can be represented as follows (how we go about each step in the process is further outlined on pages 33-34):

[insert diagram from separate file]

STEP ONE: ENTITY AND SECTOR ENVIRONMENTAL SCANNING

All public entities are grouped into “sectors”. There are two broad sector groupings – Parliamentary and Local Government.

The entities within the Parliamentary Group’s oversight are organised along the same lines as the parliamentary “subject” Select Committees. Entities within the Local Government Group are organised in a similar fashion. Each sector within a group is the responsibility of a Sector Manager who has ongoing responsibility for consulting with stakeholders and monitoring all significant activities within the sector.

Audit New Zealand and the other ASPs also have sector specialists. (Part of our revisions to the Strategic Audit Planning process over the coming years will be to facilitate more involvement from, and communication with, these sector specialists).

To initiate the Strategic Audit Planning process, Sector Managers review changes and trends in:

- Legislation;
- Governance and accountability requirements;
- The accounting and auditing profession;
- Information and reporting; and
- Entity management practices.

They then:

- Survey current and forecast activities by all entities within the sector; and
- Consult with stakeholders.

STEP TWO: KEY ISSUES/RISKS IDENTIFICATION

On the basis of this environmental scanning, further work is then done to:

- Analyse these trends, changes and activities for key issues and risks, and, where possible, the causes of these;
- Identify what other relevant work is being done by other agencies, and what the Office has already done in respect of that issue or related issues.

STEP THREE: DETERMINING ASSURANCE RESPONSES

Having identified and given priority to the most important issues and risks impacting on entities within our mandate, we then:

- Identify possible assurance responses that will address the issue or mitigate the risk;
- Subject the possible responses to a thorough process of peer review;
- Compare and rank the proposed responses; and
- Select the most appropriate responses on the basis of agreed criteria.

The **types of assurance “responses”** we might initiate include:

- Identifying areas to be given particular emphasis in the course of annual audits;
- Conducting and following up performance audits and special studies;
- Commissioning additional audit-related work that is specific to a particular entity;
- Gathering information and intelligence;
- Conducting sector-wide surveys;
- Developing and promulgating “best practice” guidelines; and
- Drawing particular matters to the attention of stakeholders and decision-makers.

The criteria we use to rank possible assurance responses

Currently, the criteria we use to rank possible assurance responses are:

- the likely benefits to the community (national or local) of improvements in public sector performance, where such improvements appear possible; and
- the extent to which an assurance action might be useful.

Because Parliament is our primary client, we may also apply a secondary criterion – our assessment of the extent of parliamentary or community interest.

CONSULTATION WITH PARLIAMENT

Under section 36 of the Public Audit Act 2001, our proposed work programme is subject to parliamentary consultation. As noted in the Controller and Auditor-General’s introduction to this Draft Annual Plan, we also seek preliminary feedback on an early draft of the work programme. We then review and amend our programme based on the feedback we receive.

Key Issues and Risks 2004-05 and Beyond

Emerging from our recent Strategic Audit Planning, we have identified the following as the key issues/risks likely to impact on sectors and entities within our mandate over the next 1-3 years:

Accounting and auditing

- **Implementation of changes to Generally Accepted Accounting Practice** (“GAAP”), including new requirements relating to accounting for controlled entities, and the implementation of standards based on International Financial Reporting Standards.
- The likely increase in **Public-Private Partnerships** (PPPs).

Legislation

- **Local Government Act 2002** – specific audit implications arising from: audits of summary financial reports; implementation of new rating legislation; and auditing of Long Term Council Community Plans (LTCCPs).
- Likely changes from enactment of the **Public Finance (State Sector Management) Bill**.

Information and Reporting

- **Performance reporting** – application of the “Managing for Outcomes” reporting framework in the Crown sector; and the move to “Quadruple Bottom Line Reporting” for local government.

Governance and accountability/entity management practices

- Perceptions and examples of poor **Risk Management** in the Local Government sector.
- Increasing evidence of **Conflicts of Interest**.
- **Asset Management** – the requirement to audit LTCCPs; and the extent of planned significant capital spending by Central Government organisations.

Other/topical issues

- Guidance on **advertising and other communications** at the time of parliamentary and local government elections.
- Increase in **e-government initiatives**.

In addition, we have identified a range of **entity-specific issues and risks**. These cover such things as implementation of government initiatives and cross-agency interaction and effectiveness.

Assurance Responses

To deal with these identified issues and risks, we have proposed a range of assurance “responses”. We have consulted with Parliament on our draft work programme for 2004-05.

On page 31, we outlined the possible range of assurance responses which we may use to address the key issues/risks we identify through our Strategic Audit Planning process. We also set out the criteria we use to rank possible assurance responses.

As we review and extend our Strategic Audit Planning process over the next few years, we intend to better deploy the full range of our assurance responses around issues/risks.

Our proposed assurance responses for 2004-05 are presented in two parts:

1. Sector-wide key issues/risks and the proposed assurance responses; and
2. Entity-specific and cross-entity performance audits – being our proposed assurance responses to the “sector-wide” key issues and risks identified on page 34, and our planned performance audits relating to identified entity or cross-entity specific issues.

It is important to note that the majority of the work performed by the Office is in relation to Annual Audits (i.e. the audits of financial and, in many cases, non-financial statements). This accounts for approximately 85% of our current work effort.

The Officers of Parliament Committee (OPC) has recently supported an increase in the number of performance audits (or “value-for-money”, efficiency/effectiveness audits) as it views this as an important tool for providing greater breadth and depth of assurance. In addition, the OPC has acknowledged the impact of major inquiries on the Office’s ability to deliver its programmed work and, accordingly, has proposed additional funding for this work.

SECTOR-WIDE KEY ISSUES/RISKS AND THE PROPOSED ASSURANCE RESPONSES

On page 34, we identified the “sector-wide” key issues and risks likely to impact on the entities within our mandate in the coming 1-3 years. We propose to address or mitigate these issues/risks by:

	Key issues/risks	Proposed assurance responses
Accounting and auditing	Implementation of changes to GAAP	<ul style="list-style-type: none"> ▪ Focus area for 2004-05 annual audits ▪ Implementation of a strategy to assist public entities and ensure that our auditors are prepared
	Public-private partnerships	<ul style="list-style-type: none"> ▪ Development of guidance for our auditors on accounting appropriately for public-private partnerships ▪ Learning from other jurisdictions
Legislation	Local Government Act 2002	<ul style="list-style-type: none"> ▪ Focus area for 2003-04 annual audits ▪ LTCCP project (research and development, product development, implementation and training) ▪ Development of audit approach for auditing summary financial reports
	Public Finance (State Sector Management) Bill	<ul style="list-style-type: none"> ▪ Maintain an active interest in progress of this Bill
Information and reporting	Performance reporting	<ul style="list-style-type: none"> ▪ Focus area for 2004-05 annual audits ▪ Ongoing research and development, and product development ▪ Performance audit proposed for 2005-06 on departmental strategic planning
Governance and accountability/ entity management practices	Risk management in local government	<ul style="list-style-type: none"> ▪ Scoping study on risk management in local government to be considered in 2005-06
	Conflicts of interest	<ul style="list-style-type: none"> ▪ Focus area for 2004-05 annual audits ▪ Provision of guidance to elected members in local government
	Asset management	<ul style="list-style-type: none"> ▪ Focus area for 2004-05 annual audits ▪ Performance audit on long-term financial planning in central government already underway ▪ Ongoing work with local government re LTCCPs
Other/topical issues	Advertising guidelines	<ul style="list-style-type: none"> ▪ Review existing guidelines in this area
	E-government	<ul style="list-style-type: none"> ▪ Focus area for 2004-05 annual audits ▪ Performance audit reviewing progress with e-government programme

Mapping these same sector-wide key issues/risks by our range of assurance products/services highlights the extent to which we have currently deployed our products/services to respond to these issues/risks.

As we review our Strategic Audit Planning process, we intend to enhance the deployment of our full range of assurance products/services around issues/risks.

[insert table from separate file]

ENTITY-SPECIFIC AND CROSS-ENTITY PERFORMANCE AUDITS

In addition to the assurance responses designed to address or mitigate the “sector-wide” key issues/risks, we have also identified entity-specific and cross-entity issues which would benefit from detailed study. These generally relate to entity reviews of the implementation of government initiatives, reviews of cross-agency interaction and effectiveness in the delivery of government initiatives, or other topical matters and consider effectiveness and efficiency and value-for-money dimensions. We respond primarily to these entity-specific/cross-entity issues by carrying out a “performance audit”.

Performance audits are planned pieces of work which are resource intensive. They often span more than one year.

The OPC has supported the Office to conduct more performance audits, acknowledging the greater depth and breadth on issues that can be gained from a performance audit which is not available from annual audits. The Office currently delivers approximately 10 performance audits per year. Over 2004-05, the OPC has proposed that Parliament fund an additional 5 performance audits, and the Office itself, through internal efficiency and productivity gains, intends to deliver an additional 2 performance audits. This totals 17 performance audits. In 2005-06 and 2006-07, the OPC has proposed that Parliament fund an additional 4 performance audits – making a total of 21 performance audits in three years. This will enable the Office to build capability for more performance audits and respond better to the needs of its key stakeholders.

There are a number of performance audits already in progress. In addition, prior to 30 June 2004 it is likely a further number of performance audits will be started. On the following pages, we list all “active” and “intended” performance audits for the 2004-05 year.

Performance Audits Currently in Progress

The following performance audits are either in progress or having their scope determined, and a number will be completed by 30 June 2004 (for a full description on these audits please refer to pages 52 to 61 of our 2003-04 Annual Plan):

- ACC Case Management
- Hazardous waste management
- Collaborative initiatives between local authorities
- Information requirements for the sustainable management of fisheries
- Civil Aviation Authority
- New Zealand Defence Force – acquisition of light armoured vehicles
- Transport safety
- Department of Conservation’s land holding and purchasing policies.

Performance audits likely to be allocated in the balance of the 2003-04 year

The following performance audits have been scheduled for commencement prior to 30 June 2004. Again, full detail on each study can be found in our 2003-04 Annual Plan.

- Resource Management Act 1991
- Contracting/funding Non-Government Organisations
- Long-term financial planning in central government
- SOE governance and the role of the Crown Company Monitoring and Advisory Unit
- Economic Development initiatives
- Overseas Development Assistance
- Regional Council water management.

Performance Audits Planned for 2004-05

The following performance audits were the high-ranking audits arising from our recent Strategic Audit Planning process. Feedback from Parliament has confirmed the following priority and ranking of these studies.

1. Sea container surveillance (follow-up study)
2. Public-private partnerships – learning from other jurisdictions
3. Fines collection – efficiency and effectiveness
4. Health sector IT – progress against the WAVE report
5. Ministry of Fisheries – enforcement of compliance with the Quota Management System
6. Management of Heritage Collections
7. Quality in Tertiary Education – effectiveness and efficiency of the quality of assurance arrangements for Tertiary Education Institutions (“TEI’s”) and Private Training Establishments (“PTE’s”)
8. Update to Institute of Internal Auditors Sensitive Expenditure Guidelines
9. Human Resource Management
10. Housing New Zealand Corporation – property portfolio management
11. The Treasury – effectiveness for Maori
12. Prisoner mental health treatment
13. E-government – review progress against objectives and targets
14. Schools – Foreign fee-paying students
15. Inland Revenue Department Taxpayer Audit (Follow-up study)
16. Roll-out and evaluation of Primary Health Organisations (“PHO’s”)
17. Youth at risk

Each of these is described in detail below and on the following pages. Note: Following feedback from Parliament, we intend to extend our descriptors of each study in future years to include rationale for its ranking and priority.

Sea container surveillance

In November 2002, we published the findings from an audit of biosecurity risk management, which included concerns about sea container surveillance capability in particular.

The subsequent government responses include additional funding to improve sea container scrutiny. We propose this audit as a follow up to our 2002 audit of biosecurity risk management, which we anticipate would take place about 12 months after the introduction of the container surveillance response.

Public-private partnerships – learning from other jurisdictions

In addition to developing guidance for our auditors on accounting appropriately for various public-private partnerships, we intend to draw on expertise from other jurisdictions, such as Australia and the United Kingdom, to prepare for a possible audit of a significant partnership.

Fines collection – efficiency and effectiveness

Now that the COLLECT information technology system has been completed, a special study will be conducted of the effectiveness and efficiency of the fines collections operations of the Collections Unit of the Ministry of Justice.

Health sector IT – progress against the WAVE Report

We are aware of significant gaps in the national information available about the health of the population and about the inputs, processes, outputs and related costs aimed to address health outcomes. A major review of health information systems, Project WAVE, indicated the need for a plan for health information management and technology across the entire sector.

In October 2001, the WAVE Advisory Board published its Health Information Management and Technology Plan, Working to Add Value through E-Information (WAVE). We propose a study that would focus on the Ministry of Health's progress against the WAVE Report recommendations as set out in "From Strategy to Reality: the WAVE Project".

Ministry of Fisheries – enforcement of compliance with the Quota Management System

This study was originally recognised in 1999 as the third phase of the audit of sustainable management of fisheries.

Government policy is now bringing new species onto the Quota Management System (QMS) at an increasing rate. The successful operation of the QMS depends on fishers, licensed fish receivers, and quota holders providing accurate returns to the Ministry of fish caught and landed. Also, recent Select Committee and SSC inquiries into the scampi fishery have highlighted how bringing new species onto the QMS is dependent on accurate baseline catch records.

Management of Heritage Collections

We propose an audit of the effectiveness and efficiency of the management of heritage collections within local authorities and their controlled entities. The audit would probably also cover risk management aspects.

Quality in Tertiary Education – effectiveness and efficiency of the quality of assurance arrangements for Tertiary Education Institutions (TEI's) and Private Training Establishments (PTEs)

Accreditation of institutions and approval of courses, and monitoring of the quality of those courses, is critical to the quality of tertiary education and training. Accreditation and monitoring falls to several groups dependent on the sub-sector, and there is a risk that quality is uneven across sub-sectors. The New Zealand Qualifications Authority (NZQA) (and New Zealand Vice Chancellors' Committee (NZVCC) for the universities) need to provide comparable assurance services in this respect.

We envisage a high level special study to examine the monitoring and quality assurance arrangements in place in the tertiary sector (in Tertiary Advisory Monitoring Unit (TAMU), Tertiary Education Commission (TEC), NZQA, Associations of Polytechnics in New Zealand (APNZ), NZVCC, and Association of Colleges of Education in New Zealand (ACENZ)).

Update to Institute of Internal Auditors Sensitive Expenditure Guidelines

We intend to develop and publish updated and clear guidance about key sensitive expenditure items. This guidance would establish our expectations for use by auditors of all public entities and in the conduct of probity inquiries. We expect the guidance would be valued by public entities as well.

Human Resource Management

This audit would examine how well departments individually – and the public sector generally – are performing the strategic human resource management function. Failures of strategic human resource planning can result in the inefficient delivery of public services, or in serious service failures, especially in areas which are potentially of high cost to the economy and society.

Housing New Zealand Corporation – property portfolio management

A special study to examine the way in which Housing New Zealand Corporation forecasts demand for rental accommodation and operates its acquisition and disposal function. This option has been made more material by Government funding decisions in 2003-04. Significant capital contributions have been made in 2002-03 and 2003-04 for the acquisition and modernisation of the Corporation's rental housing stock.

The Treasury – Effectiveness for Maori

This audit would involve the application to the Treasury of our model for assessing the capability of departments to deliver effective outputs for Maori.

Prisoner Mental Health Treatment

Evidence indicates that psychiatric morbidity among prison inmates is a serious problem and a significant contributor to subsequent criminal offending. However, psychiatric services are not provided by the Department for Corrections, but by local health authorities. A special study could follow up the 1999 report *The National Study of Psychiatric Morbidity in New Zealand Prisons* and examine the way in which psychiatric services are being provided to inmates. This study would be cross-sectoral, between the Health and Justice sectors.

E-government – review progress against objectives and targets

A special study is proposed that will review progress on the e-government programme against original objectives and targets identified when the programme was mooted. This would involve considering the original intentions of the e-government programme, how those intentions may have changed over the intervening period, and the progress made to date.

Schools – Foreign Fee-paying Students

It is planned that the 2003 schools audits will give special emphasis to the risks arising from the enrolment of foreign fee-paying students (“FFPS”). This exercise will be relevant only to the audits of those schools where FFPS activity is material in relation to the remainder of the school’s activities. At this stage, it is considered that between 100 and 500 audits of the total of 2,500 would be involved. The exercise will focus in particular on stewardship of the funds, and ensuring that a consistent standard of audit review and reporting is applied in the relevant schools.

Inland Revenue Department Taxpayer Audit (follow-up audit)

This will be a follow-up of our 2003 report: *Inland Revenue Department: Performance of Taxpayer Audit*.

Introduction and evaluation of Primary Health Organisations (PHOs)

We propose a study that would focus on the Ministry of Health’s introduction and measurement of the success of the PHO initiative. It would focus on how the Ministry takes account particularly of:

- Concerns about PHO development; and
- Management of information needs and impact assessment.

Youth at Risk

The co-ordination of services to at-risk youth is an important issue and is a significant strategic focus for *New Directions*. The Department of Child, Youth and Family Services operates a “youth at risk” strategy and the Government *Youth Offending Strategy* is currently being implemented. A cross-sectoral study could be conducted of the quality, co-ordination, effectiveness and efficiency of services to youth.

Feedback from Parliamentary Consultation

Under section 36 of the Public Audit Act 2001, our proposed work programme is subject to parliamentary consultation. As noted earlier, we have sought preliminary feedback on an early draft of the work programme. This feedback:

- Largely supported the priority and ranking of proposed studies; and
- Provided us with guidance as to the scope and relative emphases we should place on many of our proposed studies.

We thank Parliament for this feedback and will ensure that it is incorporated into our scoping of the respective studies.

In addition, the following suggestions were proffered for future studies:

- Department of the Prime Minister and Cabinet – Effectiveness for Maori.
- Follow-up study on Police handling of burglaries.

We will ensure that these suggestions are considered as part of our Strategic Audit Planning process later this year.

Other Contributions to Better Public Sector Administration

The Office plays an important role in enhancing accountability and in the development of professional and technical standards for accounting and auditing. It does this through:

- Commenting and making submissions on draft legislation;
- Making senior staff available for membership on committees of ICANZ – including the Professional Practices Board and the Financial Reporting Standards Board;
- Considering and making submissions on proposed New Zealand, and, where appropriate, international financial reporting, auditing and ethical standards;
- Participating in committees and working groups of public sector auditing bodies – such as the International Organisation of Supreme Audit Institutions (INTOSAI) and the Australasian Council of Auditors-General (ACAG);
- Liaising with the Auditor-General’s appointed auditors on accounting, auditing and policy developments; and
- Liaising with, and assisting, government agencies (including the Treasury and the State Services Commission), the Society of Local Government Manager, and others on public sector accountability and reporting issues.

We intend to continue our contribution in all these areas.

Strategic Plan Implementation

The Officers of Parliament Committee (the OPC) has proposed to Parliament to further invest in the future capability of the Audit Office through the provision of additional parliamentary baseline funding for the next three years.

The basis for this additional funding was our five-year Strategic Plan. In that plan, we outlined our Strategy to better respond to our stakeholders' needs and the changes in our environment.

We intend to provide the OPC and Parliament with greater detail on how we will utilise this additional funding to enhance the achievement of our outcomes. This will afford the OPC and Parliament greater certainty over their investment and enable them to hold the Office to account.

Each year, we will therefore include as part of our proposed annual work programme a section on Strategic Plan activities to be implemented over the planning period. (Note: Our Strategic Plan activities are consistent with our business strategies as outlined on pages 22-24.)

In this section, therefore, we outline the specific actions we will take in 2004-05 to give effect to our Strategic Plan.

Subject to Parliamentary approval, we will have available the first of the additional parliamentary baseline funding on 1 July 2004. This represents Phase One of the implementation of our Strategic Plan.

This phase involves primarily "building of the infrastructure" to support the achievement of our Strategic Plan. This includes:

- Establishing clear governance and accountability for our strategy;
- Putting in place the mechanisms (process, systems) to support our strategy;
- Increasing our resources and capacity in areas where funding has been received;
- Looking for ways to maximise efforts across the Audit Office;
- Enhancing our capabilities;
- Continuing to work together in ways which encourage innovation and collaborative working; and
- Delivering what we have committed to.

Over 2004-05, therefore, we intend specifically to:

GOVERNANCE AND ACCOUNTABILITY

- Embed our new governance and leadership structure; and
- Align our accountability frameworks across the Office.

MECHANISMS TO SUPPORT OUR STRATEGY

- Implement a “project office” approach; and
- Develop strategies, processes and systems for turning ideas into action.

INCREASE OUR RESOURCES AND CAPACITY

- Put more resources into our performance audit team and implement ways to better access capacity for inquiries.

MAXIMISE EFFORTS ACROSS THE OFFICE

- Pilot a revision of our Strategic Audit Planning process (as outlined on page 29); and
- Continue to streamline our Corporate Support strategies and processes.

ENHANCE OUR CAPABILITIES

- Fully implement the “Associate Director” pilot in Audit New Zealand;
- Continue to implement our EEO and EFM initiatives; and
- Review our capability development model for senior staff.

WORK TOGETHER BETTER

- Implement a project to maximise our “sector” efforts.

DELIVER WHAT WE HAVE COMMITTED TO

- Undertake research and development, and product development as outlined in our proposed programme on pages 51-54;
- Improve our timeliness in performance audits and inquiries; and
- Continue delivering our core business.
- Produce a history of the Audit Office.

Relating these actions back to our business strategies and areas of focus shows the alignment between our Strategic Plan and our outcome framework in the table on the next page.

Business Strategy	Area of focus	Proposed actions 2004-05
Shaping our services	ONGOING RESEARCH AND DEVELOPMENT AND PRODUCT DEVELOPMENT, AND INNOVATION	<ul style="list-style-type: none"> ▪ Develop strategies, processes and systems to turn ideas into action; and ▪ Undertake research and development, and product development as outlined on pages 52-54.
	CHANGES TO THE BREADTH AND DEPTH OF OUR CURRENT ASSURANCE PRODUCTS AND SERVICES	<ul style="list-style-type: none"> ▪ Put more resources into our performance audit team and implement ways to better access capacity for inquiries; ▪ Improve our timeliness in performance audits and inquiries; and ▪ Continue delivering our core business.
	ENHANCEMENT OF OUR STRATEGIC AUDIT PLANNING PROCESS AND DEPLOYMENT OF OUR FULL RANGE OF ASSURANCE INTERVENTIONS AROUND ISSUES/RISKS	<ul style="list-style-type: none"> ▪ Pilot a revision of our Strategic Audit Planning process.
Building our capability	CONTINUAL ADAPTATION OF OUR ORGANISATION (including enhancing our capabilities)	<ul style="list-style-type: none"> ▪ Embed our new governance and leadership structure; ▪ Implement a “project office” approach; ▪ Align our accountability frameworks across the Office; ▪ Continue to streamline our Corporate Support strategies and processes; ▪ Fully implement the “Associate Director” pilot in Audit New Zealand; ▪ Continue to implement our EEO and EFM initiatives; and ▪ Review our capability development model for senior staff.
Fostering relationships and ways of working	FACILITATING OPPORTUNITIES FOR COLLABORATIVE WORKING	<ul style="list-style-type: none"> ▪ Implement a project to maximise our “sector” efforts.

Research and Development, and Product Development

Subject to parliamentary approval, new funding for the purposes of carrying out timely and relevant research and development, and product development will be available. This is to enable the Office to be more responsive to our stakeholders' needs and to the changes in our environment through the design and development of innovative assurance products and services.

We wish to maintain transparency with Parliament and will therefore publish our proposed research and development, and product development programme annually as part of our work programme.

We have determined our proposed research and development, and product development programme by examining the key issues/risks and common themes emerging from our Strategic Audit Planning process, as outlined earlier.

Our proposed research and development, and product development programme for 2004-05 is as follows:

Research/product development subject	Description	Implementation date
Local Government Act 2002, Long-Term Council Community Plans ("LTCCP's")	We have a new requirement to audit LTCCP's under the Local Government Act 2002. This requirement comes into effect in 2006. We have already commenced development work through our "Auditing the Future" project. We need to undertake further research and development to enable the Office to credibly and usefully audit LTCCPs in 2006.	December 2005
	We are required to audit summary financial reports under the Local Government Act 2002. The first of these will be audited towards the end of 2004 but the majority of councils will be audited for the first time in the latter half of 2005. We need to undertake research to ensure a consistent level of work is done to audit summaries and to ensure the effectiveness of our reporting on these documents.	August 2005
Public Finance (State Sector Management) Bill and "Managing for Outcomes" in Central Government	<p>The Public Finance (State Sector Management) Bill is intended to come into effect from 1 July 2005. The Audit Office has been appointed advisors to the Finance and Expenditure Committee (alongside Treasury and SSC) for this Bill. There are a wide range of technical amendments to the Public Finance Act that will require specific audit responses, including appropriations, vote and output structures and reporting, statements of intent, changes to imprest supply and changes to the controller function.</p> <p>In addition, there are significant changes in relation to the governance, accountability and reporting of Crown entities. We need to ensure our auditors have a thorough working knowledge of the Act through centralised development of audit responses and through training.</p> <p>Our development work in this area will subsume the ongoing developments in "managing for outcomes".</p>	Ongoing

Research/product development subject	Description	Implementation date
Adoption of standards based on International Financial Reporting Standards ("IFRS")	<p>We need to ensure our own people and our ASPs are prepared for the significant change to IFRS-based standards over the next three years. This work will involve training, development of models and tools, and support to public entities.</p> <p>We have already established a project team to lead this area and have adopted a "minimum fuss" approach together with a focus on collaboration with other interested parties. It is also likely that a partnership (or a series of partnerships) with the major CA firms will underpin our strategic response to this.</p>	Various dates up to 30 June 2007
Likely introduction of International Standards of Auditing ("ISAs")	<p>There are two related developments which will affect us over the next few years. Firstly, it is likely that New Zealand standards will be even more strongly based on ISAs than in the past. In essence a similar approach to that being taken with IFRS is likely.</p> <p>The Public Sector Committee of the International Federation of Accountants is handing over full responsibility for the public sector dimensions of the ISAs to the International Auditing and Assurance Standards Board. However, INTOSAI has established a process to ensure appropriate public sector input to those standards. It is likely that we will need to make significant changes to our auditing standards and also to our general policies on auditing matters over the next three years.</p>	Ongoing, expected by 30 June 2007
Performance Reporting/Non-financial reporting/Sustainable Development Reporting ("SDR")	<p>We have frequently expressed our disappointment at the lack of progress made in non-financial reporting in New Zealand. We have been constrained however in the amount of effort we have been able to put into this. Our report in 2001 entitled "<i>Reporting Public Sector Performance</i>" remains of value though we need to do much more.</p> <p>We are beginning to see the introduction of sustainability development reporting in financial reports and we need to respond to this development as well as ensure auditors have the necessary tools to audit this information when it falls within the scope of our audit responsibility.</p>	Ongoing, by 30 June 2006

Research/product development subject	Description	Implementation date
Increased scope of annual audit to extend audit work on waste, probity, governance and accountability	Our strategy signals, and it is the Auditor-General's intention, that we extend our work in the annual audit in areas of waste, probity, governance, and to some extent, accountability. To ensure progress we need to develop practical audit approaches this will require the use of experienced people in developing guidance and training auditors.	Ongoing
Conflicts of interest	There has been increasing evidence of conflict of interest issues outside of those which we already oversee in our role under the Local Authorities (Members' Interests) Act 1968. We need to research these issues with a view to providing guidance that can be made available, particularly in the local government sector.	Ongoing
Auditing sensitive expenditure	In recent times we have come across evidence that indicates that sensitive expenditure in the public sector needs greater scrutiny. It would be desirable for us to contribute to the development of guidance which could be made available to public entities in clarifying what is appropriate in relation to these types of expenditure. Furthermore we need to develop audit responses to ensure we identify issues earlier than we have been in the recent past.	Ongoing
Review of the "Five Management Aspects"	The 5 management aspects are perceived as having high value by Select Committees. We need to refresh them and consider the possibility of applying them in other sectors in the future. A revised rating system also presents an opportunity to reinforce and complement other research and development/product development initiatives as outlined above.	Ongoing

Part Three

Forecast Financial Statements

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Introduction

The Audit Office's forecast financial statements have been prepared in accordance with section 34A of the Public Finance Act 1989 and are consistent with generally accepted accounting practice. The purpose of the forecast financial statements is to facilitate parliamentary consideration of the appropriations for, and planned performance of, the Audit Office. Use of this information for other purposes may not be appropriate. Readers are cautioned that actual results are likely to vary from the information presented here and that the variations may be material.

These forecast financial statements have been prepared on the basis of assumptions as to future events that the Auditor-General reasonably expects to occur associated with the actions he reasonably expects to take as at the date this information was prepared.

These statements have been prepared also in the context of the budgetary process.

It is not intended that this published information will be updated.

Forecasts should be contrasted with projections. Projections are based on one or more hypothetical assumptions.

Statement Of Significant Underlying Assumptions

The forecast financial statements on pages 58-86 have been compiled on the basis of existing Government policies and after consultation by the Audit Office with the Speaker and the Officers of Parliament Committee. The main assumptions are that:

- ◆ The Audit Office's *portfolio of entities* will remain substantially the same as for the previous year.
- ◆ The Audit Office will continue to deliver the *range of products* currently provided and will also position itself to deliver new products, or existing products in new ways, to cope with changing demands.
- ◆ The scale of *annual audits* will remain substantially the same.
- ◆ The balance of activity associated with *performance audits, advice to Parliament and others, and inquiries* will continue to be variable because of increases in demand and the effects of the Public Audit Act.
- ◆ The Auditor-General will continue to utilise audit expertise from both Audit New Zealand and the private sector.

These assumptions are adopted as at 00 April 2004.

Statement of Objectives for Output Class D1 –

Reports and Advice Arising from the Exercise of the Function of Legislative Auditor

Description

Output Class D1 includes the following products and services of the Audit Office:

Reports to Parliament and other constituencies –
on matters arising from annual audits, programmed performance audits and special studies,
and unprogrammed inquiries.

Reports and advice to Select Committees –
to assist in their reviews of performance, estimates examinations, or other inquiries
for which our assistance is sought.

Reports to portfolio ministers on the results of annual financial report audits.

Responses to enquiries from taxpayers, ratepayers and
Members of Parliament.

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

Administration of the provisions of the Local Authorities (Members' Interests) Act 1968.

Development of a written history of the Audit Office

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. performance audits). Given the discretionary element in this class of outputs, we have provided additional detail in our Proposed Work Programme (see Part Two on pages 40-44).

Planned Activities and Costs

Reports to Parliament and Other Constituencies

\$000

Results of annual audits:

- ◆ Audit results for central government, local government, and selected other sectors
- ◆ Specific issues arising from particular audits or in relation to sectors generally

Results of programmed performance audits and special studies
(see pages 62-63 for more detail)

Matters arising from unprogrammed inquiries³ initiated in response to particular concerns brought to the attention of the Audit Office during 2003-04

5,117

Reports and Advice to Select Committees⁴/Ministers

\$000

Advice to Select Committees/Ministers to assist their financial reviews of:

- ◆ Government departments and Offices of Parliament
- ◆ State-owned enterprises and Crown entities
- ◆ Reports to portfolio Ministers on the results of annual financial report audits

Advice to Select Committees to assist their examination of the *Estimates*

Advice or assistance (as requested) for other inquiries conducted by Select Committees

730

³ Spare capacity is not held for such investigations. The extent of the resource usage on unprogrammed enquiries will directly affect the resource availability for other planned activities.

⁴ The extent and cost of these activities is largely determined by the demands made by Select Committees.

FORECAST FINANCIAL STATEMENTS FOR 2004-05
Objectives for Output Class D1

**Responses to Enquiries from Taxpayers, Ratepayers,
and Members of Parliament**

\$000

Acknowledgement, investigation⁵ and reporting the results of enquiries directed to the Audit Office by:

- ◆ Taxpayers
- ◆ Ratepayers
- ◆ Members of Parliament

1,050

Advice to Government Bodies and Other Agencies

\$000

Responding to specific requests from, and participating in working parties on matters related to financial management and accountability with, organisations including⁶:

- ◆ Central agencies
- ◆ Government departments, local authorities, and other public 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
- ◆ Other audit institutions and related organisations, such as INTOSAI

730

⁵ Not all enquiries will result in an investigation. Enquiries assessed as warranting investigation may be considered either at the time of the next annual audit or by way of an immediate, specific enquiry.

⁶ The cost associated with each area of advice is difficult to predict with any reliability, as it is largely demand-driven. Accordingly, the cost of these activities has been estimated, based on past experience.

FORECAST FINANCIAL STATEMENTS FOR 2004-05
Objectives for Output Class D1

Administration of the Provisions of the Local Authorities (Members' Interests) Act 1968 *\$000*

Responding to specific requests in relation to the Audit Office's powers to:⁷

- ◆ Approve increased limits for contract payments
- ◆ Grant dispensations in certain circumstances from the prohibition against discussing and voting where members have a pecuniary interest
- ◆ Consider alleged breaches of the Act

75

History of the Audit Office⁸ *\$000*

Development of a written history of the Audit Office in conjunction with the Ministry for Culture and Heritage

50

⁷ This activity is demand-driven. The nature and extent of the activity is determined by the number and complexity of the requests made to the Audit Office.

⁸ This is a new activity this year planned to take 3 years to complete.

Performance Measures and Targets

Output	Quantity ⁹	Cost \$000	Timeliness ¹⁰	Quality
1. Reports to Parliament and other constituencies, comprising results of: <ul style="list-style-type: none"> ◆ annual audits ◆ programmed performance audits and special studies ◆ unprogrammed enquiries ◆ other activities. 	We expect to deliver at least: <ul style="list-style-type: none"> ◆ 2 reports on the results of annual audits. ◆ 17 reports covering programmed performance audits, special studies, and unprogrammed enquiries. Performance auditors will spend a minimum of 22,100 hours undertaking performance audits. We will complete at least 90% of the R&D and product development plans as set out in our Annual Plan. We will implement a pilot of the enhanced Strategic Audit Planning process.	5,117	All reports will be provided within the deadlines agreed in the: <ul style="list-style-type: none"> ◆ terms of reference for enquiries; ◆ performance audit and special study audit plans. We will complete the pilot of the enhanced Strategic Audit Planning process by 30 June 2005.	We will complete an independent review of our performance audits and special studies. We will develop and pilot a survey covering a range of stakeholders to ascertain the quality, relevance and responsiveness of our reporting and advice.
2. Reports and advice to Select Committees/Ministers, comprising: <ul style="list-style-type: none"> ◆ financial reviews ◆ estimates examinations ◆ reports to portfolio Ministers on the results of annual financial report audits ◆ other reports. 	We expect to deliver: <ul style="list-style-type: none"> 100 reports 40 reports 20 reports 20 reports 	730	All reports will be provided: <ul style="list-style-type: none"> ◆ at least 2 days before an examination, unless otherwise agreed with a Committee. ◆ to Ministers before Select Committee scrutiny of departmental and Crown entity performance. ◆ according to the terms of reference for other reports. 	

⁹ The quantity of reports and enquiries handled, and their consequent cost, are largely demand-driven. Accordingly, these figures have been estimated based on past experience.

¹⁰ “Working days” are as defined in the Official Information Act 1982.

<p>3. Responses to enquiries from:</p> <ul style="list-style-type: none"> ◆ taxpayers ◆ ratepayers ◆ Members of Parliament. 	<p>60 enquiries 180 enquiries 60 enquiries</p>	<p>1,050</p>	<p>We will:</p> <ul style="list-style-type: none"> ◆ provide an initial response within 5 working days ◆ complete 80% within 30 working days ◆ advise 100% if the enquiry will take longer than 30 working days. 	
<p>4. Advice to government bodies and other agencies.</p>	<p>We will provide advice on demand</p>	<p>730</p>	<p>We will deliver the advice in accordance with the terms of reference agreed.</p>	
<p>5. Administration of the provisions of the Local Authorities (Members' Interests) Act 1968.</p>	<p>80 enquiries</p>	<p>75</p>	<p>We will:</p> <ul style="list-style-type: none"> ◆ provide an initial response within 5 working days ◆ complete 80% within 30 working days ◆ advise 100% if the enquiry will take longer than 30 working days. 	
<p>6. Audit Office history.</p>	<p>Over the next 3 years we will produce a written history of the Audit Office, in conjunction with the Ministry for Culture and Heritage.</p>	<p>50</p>	<p>The written history will be completed within the agreed timetable.</p>	<p>We will use personnel with the appropriate professional skills, qualifications and experience to undertake the history project.</p>
<p>TOTAL COST</p>		<p>7,752</p>		

Statement of Objectives for Output Class D2 –

Certification of Authority to Release Funds from the Crown Bank Account

Description

Output Class D2 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.

Performance Measures and Targets

Quality

The Controller and Auditor-General will ensure that:

- ◆ Warrants and controller statements will only be certified once correct documentation is provided by the Treasury to support the certification of a warrant or the release of funds from the Crown bank account.
- ◆ Issues from the Crown bank account will only be certified if the issue is supported by appropriation by Parliament or other lawful authorities granted by Parliament.
- ◆ All payments not within a warrant from the Governor-General will be refused.

Quantity¹¹

Number of warrants and controller statements expected to be certified:

- ◆ 6 Governor-General warrants.
- ◆ 245 controller statements.

Timeliness

- ◆ All valid certifications will be provided promptly on the day that documentation is provided by the Treasury for certification.

¹¹ The quantity of Governor-General warrants and controller statements is determined by the Treasury. Accordingly, these figures have been estimated based on past experience.

Cost

- ◆ The cost will not exceed \$144,000.

Statement of Objectives for Output Classes D3 and D4

Provision of Audit Services

Description

These two output classes relate to the conduct of the annual audits of public entity financial reports. The Auditor-General is the statutory auditor of more than 4000 public entities. These audits are undertaken by either Audit New Zealand or private sector auditors.

Annual audits result in:

Audit Reports –

On whether the financial statements fairly reflect the financial and non-financial performance of these entities.

Management Reports –

To the management and governing bodies of these entities, on issues arising from the audit.

The difference between the output classes relates to the method by which the audit service provider has been selected:

Output Class D3 – Non-contested Audit Services

Output Class D4 –

Contested Audit and Other Assurance Services

Both Output Classes D3 and D4 are funded mainly by fees paid by the entities being audited or to which other assurance services are being provided.

Output Class D4 is appropriated on a mode B net basis.

Statement of Objectives for Output Class D3 – Non-contested Audit Services

Performance Measures and Targets

Group	Total Entities in Group	Estimated Number of Audits in Arrears as at 30/6/04	Planned Audit Completions in 2004-05	Expected Number of Audits in Arrears as at 30/6/05	Timely Issue of Audit Reports Target ¹²	Timely Issue of Management Reports Target ¹³
Government Departments and Offices of Parliament	11	-	11	-	100%	100%
Major Statutory Bodies ¹⁴	29	5	29	5	100%	100%
Other Local Authorities ¹⁵	23	5	23	5	100%	100%
Miscellaneous Public Bodies ¹⁶	120	60	120	60	75%	100%
Audits for which fees are not directly charged ¹⁷	155	72	155	36	75%	100%
Totals	338	142¹⁸	338	106		

¹² Audits will be completed and audited financial statements available within statutory deadline or within 5 months of balance date.

¹³ Management reports and letters will be issued within 6 weeks of the date of the audit report.

¹⁴ State-owned Enterprises, Tertiary Education Institutions, Producer Boards, District Health Boards, Crown Research Institutes and major Crown entities.

¹⁵ Licensing Trusts, Airports, LATEs, Energy Companies, Port Companies and Sinking Fund Commissioners.

¹⁶ Mainly Maori Trust Boards, smaller Crown Entities, and subsidiaries of major Crown entities.

¹⁷ Those entities where there is no statutory right to charge an audit fee or no realistic possibility of obtaining a fee. These entities include Cemetery Trustees, Hall and Reserve Boards, Racecourse Trustees and Patriotic Funds. (From 2004-05, the crown is funding up to \$190,000 of the cost of these audits.)

¹⁸ An estimated 130 bodies have audits in arrears, some for a number of years, and the 110 audits in the final category represent only 44 bodies. Most have not prepared financial statements for the periods involved.

Statement of Objectives for Output Class D4 – Contested Audit and Other Assurance Services

Performance Measures and Targets

Group	Total Entities in Group	Estimated Number of Audits in Arrears as at 30/6/04	Planned Audit Completions in 2004-05	Expected Number of Audits in Arrears as at 30/6/05	Timely Issue of Audit Reports Target ¹⁹	Timely Issue of Management Reports Target ²⁰
Government Departments and Offices of Parliament	36	-	36	-	100%	100%
Major Statutory Bodies ²¹	93	-	93	-	100%	100%
Regional, City and District Councils	86	-	86	-	100%	100%
Other Local Authorities ²²	477	20	477	20	100%	100%
School Boards of Trustees	2,582	140	2,582	140	95%	100%
Miscellaneous Public Bodies ²³	450	20	450	20	75%	100%
Totals	3,724	180²⁴	3,724	180		

¹⁹ Audits will be completed and audited financial statements available within statutory deadline or within 5 months of balance date.

²⁰ Management reports and letters will be issued within 6 weeks of the date of the audit report.

²¹ State-owned Enterprises, Tertiary Education Institutions, Producer Boards, District Health Boards, Crown Research Institutes and major Crown entities.

²² Licensing Trusts, Airports, LATEs, Energy Companies, Port Companies and Sinking Fund Commissioners.

²³ Mainly Maori Trust Boards, smaller Crown Entities, and subsidiaries of major statutory bodies.

²⁴ An estimated 150 bodies have audits in arrears, some for more than one year. Most of the arrears are schools whose audits for the 31 December 2003 year will not have been completed at 30 June 2004.

Performance Measures and Targets (continued)

Audits in Arrears

The number of audits to be completed during the year will fluctuate according to the readiness of each entity to present its financial statements for audit. The number of audits actually finished during the year will relate mainly to those financial statements due in the year, plus some not presented for audit in earlier years. Where entities have not presented their financial statements for audit in previous years, the term “audit arrears” is used to describe the outstanding audits. Most arrears are from small bodies such as school boards of trustees, cemetery trustees, or minor subsidiaries of a parent body. Because an entity might have arrears for a number of years, the number of audit entities with arrears is lower than the arrears numbers shown.

The Audit Office measures and reports the number of audit entities with one or more audits in arrears as at each balance date as well as the total number of audits in arrears.

Performance Measures of Quality

Quality Assurance Reviews

The Audit Office will ensure that audits are conducted with due professional care – ensuring that standards of appropriateness, quality, efficiency and independence are adhered to as set out in the auditing standards issued by the Institute of Chartered Accountants of New Zealand and (where additional standards are required) other standards approved by the Auditor-General for application to public sector audits. These other standards recognise the particular requirements of the public sector and are designed to cover the audit of service performance information, legislative compliance, waste, and probity matters.

Compliance with these standards is tested by a programme of quality assurance reviews conducted by the Audit Office. The programme seeks to review every approved auditor at least once during their 3-year contract period. The Audit Office intends to review the work of 45 auditors during the year, the results of which will be reported in our Annual Report for the year ending 30 June 2005.

Stakeholder Satisfaction

As the largest audit service provider (ASP), Audit New Zealand undertakes a survey of its clients’ satisfaction with the quality of work completed. We will measure and report on the levels of satisfaction achieved.

Ratio of Non-financial to Financial Work Performed

The degree of non-financial audit work performed is expected to increase over time as non-financial information becomes an important part of public sector reporting. We will use this year as a benchmark for the future measurement of this trend.

Ratio of Senior to Junior Audit Staff

The Audit Office will measure and report on the quality of audit staff used on audits. We would expect to see an increasing ratio showing more senior to junior staff over time as a mitigation of risk and an increase of the quality output from the audits.

FORECAST FINANCIAL STATEMENTS FOR 2004-05

Objectives for Output Classes D3 and D4

Performance Measures of Timeliness

Completion of audits is influenced largely by the quality of records and financial statements subject to audit. The Auditor-General expects, however, that the majority of audited entities will meet the statutory deadlines for completing their annual financial statements, so as to allow completion of the audits within deadline also.

The Audit Office therefore measures:

- ◆ The number (and percentage) of audit reports issued within statutory deadlines during the reporting period, or within 5 months of balance date if there is no statutory deadline. It should be noted that not all sectors perform uniformly well. Consequently, the performance standards for each group of entities are:
 - 100% for government departments, Offices of Parliament, major statutory bodies, regional, city and district councils, and other local authorities;
 - 75% for miscellaneous public bodies, and audits for which fees will not be charged; and
 - 30% for school boards of trustees.
- ◆ The number (and percentage) of audit management reports issued within 6 weeks of issuing the audit report. The performance standard for this measure is 100%.

Performance Measures of Effectiveness

The Audit Office will report on the trend in types of non-standard audit reports issued up to and including the current year.²⁵

²⁵ 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.

FORECAST FINANCIAL STATEMENTS FOR 2004-05
Objectives for Output Classes D3 and D4

Cost

	<i>\$000</i>
◆ Cost of services for Output Class D3 – Non-contested Audit Services	4,098
◆ Cost of services for Output Class D4 – Contested Audit and Other Assurance Services	29,161

Statement of Accounting Policies

Reporting Entity

These are the forecast financial statements of the Auditor-General prepared pursuant to section 34A of the Public Finance Act 1989.

The 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.

The Auditor-General's activities include the work undertaken by private sector auditors appointed by the Auditor-General.

In this report, the activities of the Auditor-General are referred to as those of "the Audit Office", consistent with the meaning of that term in section 52 of the Public Audit Act 2001.

Measurement Base

Generally accepted accounting practice (GAAP) 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 remuneration of the Auditor-General and the Deputy Auditor-General, which are a charge against a permanent appropriation in terms of clause 5 of Schedule 3 of the Public Audit Act 2001, 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 such as client travel, and direct labour costs.
- ◆ *Indirect costs* are all other costs including 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 proportion of direct labour costs 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 premises and office equipment. Except for laptop leases, as substantially all of the risks and rewards of ownership are retained by the lessor, leases are classified as operating leases. Operating lease costs are expensed on a systematic basis over the period of the leases.

FORECAST FINANCIAL STATEMENTS FOR 2004-05

Accounting Policies

Leases of laptop computers are classified as finance leases because the useful life of the laptops equates to the lease term. Assets under finance leases are recognised as physical assets in the Statement of Financial Position. They are recognised initially at the lower of the present value of the lease payments or their fair value. A corresponding liability is established and each lease payment allocated between the liability and finance expense. Leased assets are depreciated on the same basis as the equivalent office equipment.

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	2.5-5 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 Prospective Financial Position. Revenue and expenses in relation to all financial instruments are recognised in the Statement of Prospective Financial Performance.

FORECAST FINANCIAL STATEMENTS FOR 2004-05

Accounting Policies

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 is exempt from the payment of income tax in terms of section 43 of the Public Audit Act 2001. Accordingly, no charge for income tax has been provided for.

Changes In Accounting Policies

During the year the Audit Office has changed their accounting policy with respect to accounting for laptop computer leases. Under the new policy, laptop computer leases are recognised as finance leases. Formerly all leases were treated as operating leases.

This change in policy has resulted in \$518,000 added to physical assets and a corresponding liability.

There have been no other changes in accounting policies, including cost allocation accounting policies, from those contained in the annual financial statements of the Audit Office for the year ended 30 June 2003 as laid before the House of Representatives under section 37 of the Public Audit Act 2001.

Statement of Prospective Financial Performance²⁶

For The Year Ending 30 June 2005

Description Of Statement

The Statement of Prospective Financial Performance details the revenue and expenses relating to all outputs (goods and services) produced by the Audit Office. A statement showing the revenue and expenses of each output class appears on page xxxx.

	2003-04		2004-05 Forecast
	<i>Budgeted</i> ²⁷	<i>Estimated Actual</i> ²⁸	
	\$000	\$000	\$000
Continuing Activities			
Revenue			
Crown	5,637	5,637	8,084
Departments	6,947	6,947	6,947
Other	<u>26,722</u>	<u>26,722</u>	<u>26,378</u>
Total Revenue	<u>39,306</u>	<u>39,306</u>	<u>41,409</u>
Expenses			
Personnel costs	18,805	18,805	20,135
Operating costs	18,712	18,712	19,158
Depreciation	1,230	1,230	1,575
Capital charge	<u>305</u>	<u>305</u>	<u>287</u>
Total Expenses	<u>39,052</u>	<u>39,052</u>	<u>41,155</u>
Surplus	<u><u>254</u></u>	<u><u>254</u></u>	<u><u>254</u></u>

²⁶ Prepared in accordance with section 34A(3) of the Public Finance Act 1989.

²⁷ Budgeted figures incorporate both the Main Estimates and Supplementary Estimates appropriations for 2003-04.

²⁸ The amounts in this column reflect actual results to 29 February 2004 and the forecast results for the remaining four months to 30 June 2004.

FORECAST FINANCIAL STATEMENTS FOR 2004-05
Movements in Taxpayers' Funds (Equity)

Statement of Prospective Movements in Taxpayers' Funds (Equity)

For the Year Ending 30 June 2005

Description of Statement

The Statement of Prospective 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 Prospective Financial Position, provides information for assessing the return on investment in the Audit Office.

	<i>2003-04</i>		<i>2004-05</i>
	<i>Budgeted</i>	<i>Estimated Actual</i>	<i>Forecast</i>
	<i>\$000</i>	<i>\$000</i>	<i>\$000</i>
Taxpayers' Funds brought forward at 1 July	<u>3,586</u>	<u>3,586</u>	<u>3,586</u>
Movements during the year			
Surplus	<u>254</u>	<u>254</u>	<u>254</u>
<i>Total Recognised Revenues and Expenses for the Year</i>	<u>254</u>	<u>254</u>	<u>254</u>
Flows to and from the Crown			
Provision for payment to the Crown	(254)	(254)	(254)
Taxpayers' Funds at 30 June	<u>3,586</u>	<u>3,586</u>	<u>3,586</u>

FORECAST FINANCIAL STATEMENTS FOR 2004-05
Financial Position

Statement of Prospective Financial Position

As at 30 June 2005

Description of Statement

The Statement of Prospective Financial Position reports the total assets and liabilities of the Audit Office. The difference between the assets and liabilities is called Taxpayers' Funds.

	<i>Budgeted Financial Position as at 30/6/04 \$000</i>	<i>Estimated Actual Financial Position as at 30/6/04 \$000</i>	<i>Forecast Financial Position as at 30/6/05 \$000</i>
Taxpayers' Funds			
General funds	<u>3,586</u>	<u>3,586</u>	<u>3,586</u>
Total Taxpayers' Funds	<u>3,586</u>	<u>3,586</u>	<u>3,586</u>
Represented by:			
Current Assets			
Cash and bank balances	1,458	1,458	1,518
Prepayments	290	290	290
Work in progress	1,750	1,750	1,750
Receivables	<u>3,650</u>	<u>3,650</u>	<u>3,650</u>
<i>Total Current Assets</i>	<u>7,148</u>	<u>7,148</u>	<u>7,208</u>
Non-current Assets			
Physical assets	<u>2,410</u>	<u>2,410</u>	<u>2,005</u>
<i>Total Non-current Assets</i>	<u>2,410</u>	<u>2,410</u>	<u>2,005</u>
Total Assets	<u>9,558</u>	<u>9,558</u>	<u>9,213</u>
Current Liabilities			
Payables and provisions	2,029	2,029	2,114
Provision for payment to the Crown	254	254	254
Provision for employee entitlements	2,150	2,150	2,150
Other short term liabilities	<u>345</u>	<u>345</u>	<u>173</u>
<i>Total Current Liabilities</i>	<u>4,768</u>	<u>4,768</u>	<u>4,681</u>

Term Liabilities			
Provision for employee entitlements	860	860	860
Property lease liabilities	171	171	86
Other term liabilities	<u>173</u>	<u>173</u>	<u>-</u>
<i>Total Term Liabilities</i>	<u>1,204</u>	<u>1,204</u>	<u>946</u>
Total Liabilities	<u>5,972</u>	<u>5,972</u>	<u>5,627</u>
Net Assets	<u>3,586</u>	<u>3,586</u>	<u>3,586</u>

Statement of Prospective Cash Flows

For The Year Ending 30 June 2005

Description Of Statement

The Statement of Prospective 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 Prospective Financial Performance.

	<i>2003-04</i>		<i>2004-05</i>
	<i>Budgeted</i>	<i>Estimated</i>	<i>Forecast</i>
	<i>Actual</i>	<i>Actual</i>	
	<i>\$000</i>	<i>\$000</i>	<i>\$000</i>
Operating Activities			
Cash received from:			
The Crown	5,637	5,637	8,084
Departments	6,947	6,947	6,947
Others	14,727	14,727	14,303
Cash disbursed on:			
Production of outputs	(25,727)	(25,727)	(27,563)
Capital charge	(305)	(305)	(287)
<i>Net Cash Flow from Operating Activities</i>	<i>1,279</i>	<i>1,279</i>	<i>1,484</i>
Investing Activities			
Cash received from:			
Sale of physical assets	160	160	170
Cash disbursed on:			
Purchase of physical assets	(1,245)	(1,245)	(1,340)
<i>Net Cash Flow from Investing Activities</i>	<i>(1,085)</i>	<i>(1,085)</i>	<i>(1,170)</i>
Financing Activities			
Cash disbursed on:			
Payment to the Crown	(151)	(151)	(254)
<i>Net Cash Flow from Financing Activities</i>	<i>(151)</i>	<i>(151)</i>	<i>(254)</i>
Total net increase/(decrease)			
in cash held	43	43	60
Add Opening cash balance at 1 July	1,415	1,415	1,458
Closing cash balance at 30 June	1,458	1,458	1,518

FORECAST FINANCIAL STATEMENTS FOR 2004-05
Reconciliation of Surplus to Net Cash Flow

Reconciliation of Surplus in the Statement of Prospective Financial Performance to the Prospective Net Cash Flow from Operating Activities

For the Year Ending 30 June 2005

Description of Statement

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

	<i>2003-04</i>	<i>2004-05</i>	
	<i>Budgeted</i>	<i>Estimated</i>	<i>Forecast</i>
	<i>\$000</i>	<i>Actual</i>	<i>\$000</i>
	<i>\$000</i>	<i>\$000</i>	<i>\$000</i>
Surplus	<u>254</u>	<u>254</u>	<u>254</u>
Non-cash Items			
Depreciation	<u>1,230</u>	<u>1,230</u>	<u>1,575</u>
Total Non-cash Items	<u>1,230</u>	<u>1,230</u>	<u>1,575</u>
Working Capital Movements			
(Increase)/decrease in prepayments	54	54	-
(Increase)/decrease in receivables	28	28	-
(Increase)/decrease in work in progress	52	52	-
Increase/(decrease) in payables	(324)	(324)	85
Increase/(decrease) in current employee entitlements	<u>(19)</u>	<u>(19)</u>	<u>-</u>
Total Net Working Capital Movements	<u>(209)</u>	<u>(209)</u>	<u>85</u>
Other Items			
Increase/(decrease) in property lease liabilities	4	4	(430)
Total Other Items	<u>4</u>	<u>4</u>	<u>(430)</u>
Net Cash Flow from Operating Activities	<u>1,279</u>	<u>1,279</u>	<u>1,484</u>

Forecast Details of Physical Assets by Category

As at 30 June 2005

	<i>As at 30 June 2004</i>		<i>Forecast Position as at 30 June 2005</i>		
	<i>Budgeted Net Book Value \$000</i>	<i>Estimated Actual Net Book Value \$000</i>	<i>Cost \$000</i>	<i>Accumulated Depreciation \$000</i>	<i>Net Book Value \$000</i>
Furniture and fittings	57	57	2,356	2,298	58
Office equipment	1,942	1,942	5,688	5,048	1,640
Motor vehicles	411	411	731	424	307
Totals	<u>2,410</u>	<u>2,410</u>	<u>9,775</u>	<u>7,770</u>	<u>2,005</u>

FORECAST FINANCIAL STATEMENTS FOR 2004-05
GST Status of Appropriations

Prospective GST Status of Appropriations

For the Year Ending 30 June 2005

Description of Statement

This statement reconciles, for expenses and repayment of debt, the amounts reported GST-exclusive in the Statement of Prospective Financial performance (on page xxx) and the Forecast Output Class Operating Statements (on the previous page) with the GST-inclusive amounts of the corresponding appropriations appearing in Part B1 of Vote Audit for 2004-05 in the *Estimates of Appropriations* (parliamentary paper B.5 Vol.1).

	<i>GST-Exclusive (Annual Plan)</i> \$000	<i>GST</i> \$000	<i>GST-Inclusive (Vote)</i> \$000
<i>Departmental Output Classes</i>			
Mode B Gross			
Output Class D1			
◆ Annual appropriation	7,171	897	8,068
◆ Other appropriation	<u>581</u>	<u>-</u>	<u>581</u>
	7,752	897	8,649
Output Class D2	144	18	162
Output Class D3	4,098	<u>524</u>	<u>4,622</u>
Total Mode B Gross Output Classes	<u>11,994</u>	<u>1,439</u>	<u>13,433</u>
Mode B Net			
Output Class D4	<u>29,161</u>	<u>3,665</u>	<u>32,826</u>
Total Mode B Net Output Classes	<u>29,161</u>	<u>3,665</u>	<u>32,826</u>
Total Departmental Output Classes	<u>41,155</u>	<u>5,104</u>	<u>46,259</u>
Repayment of Debt			
Net Overdraft Repayment	<u>500</u>	<u>-</u>	<u>500</u>
Total Repayment of Debt	<u>500</u>	<u>-</u>	<u>500</u>
Totals	<u>41,655</u>	<u>5,104</u>	<u>46,759</u>

Forecast Output Class Operating Statements²⁹ For the Year Ending 30 June 2005

<i>Departmental Output Class</i>	<i>Description</i>	<i>Revenue Crown \$000</i>	<i>Revenue Depts \$000</i>	<i>Revenue Other \$000</i>	<i>Total Revenue \$000</i>	<i>Total Expenses \$000</i>	<i>Surplus \$000</i>
Mode B Gross							
D1	Reports and advice arising from the exercise of the function of legislative auditor.	7,750	-	4	7,754	(7,752)	2
D2	Certification of authority to release funds from the Crown Bank Account.	144	-	-	144	(144)	-
D3	Provision of non-contested audit services.	<u>190</u>	<u>1,667</u>	<u>2,333</u>	<u>4,190</u>	<u>(4,098)</u>	<u>92</u>
Total Mode B Gross Output Classes		<u>8,084</u>	<u>1,667</u>	<u>2,337</u>	<u>12,088</u>	<u>(11,994)</u>	<u>94</u>
Mode B Net							
D4	Provision of contested audit and other assurance services.	-	5,280	24,041	29,321	(29,161)	160
Total Mode B Net Output Classes		-	5,280	24,041	29,321	(29,161)	160
Totals		<u>8,084</u>	<u>6,947</u>	<u>26,378</u>	<u>41,409</u>	<u>(41,155)</u>	<u>254</u>

²⁹Details of the forecast performance for each class of outputs are set out on pages 58-72 of this report.

FORECAST FINANCIAL STATEMENTS FOR 2004-05
Financial Indicators

FORECAST FINANCIAL INDICATORS

For the Year Ending 30 June 2005

	<i>2003-04</i>		<i>2004-05</i>
	<i>Budgeted (after Supplementary Estimates)</i>	<i>Estimated Actual</i>	<i>Forecast</i>
	<i>\$000</i>	<i>\$000</i>	<i>\$000</i>
Operating Results			
Revenue: other than Crown	33,669	33,669	33,325
Output expenses	39,052	39,052	41,155
Surplus before capital charge	559	559	541
Surplus	254	254	254
Working Capital			
Net current assets ³⁰	2,380	2,380	2,527
Current ratio ³¹	150%	150%	154%
Average receivables and work in progress	59 days	59 days	59 days
Average payables outstanding	46 days	46 days	45 days
Resource Utilisation			
Physical assets			
Total physical assets at year-end	2,410	2,410	2,005
Additions as % of physical assets	52%	52%	67%
Taxpayers' funds			
Level at year-end	3,586	3,586	3,586
Forecast Net Cash Flows			
Surplus on operating activities	1,279	1,279	1,484
Deficit on investing activities	(1,085)	(1,085)	(1,170)
Deficit on financing activities	(151)	(151)	(254)
Net increase/(decrease) in cash held	43	43	60

³⁰ Current assets minus current liabilities.

³¹ Current assets as a proportion of current liabilities.