

Occasional Paper

Developing an Effective Approach to Public Auditing

26 April 2000

Pat Barrett
Auditor-General for Australia

INTRODUCTION

I would like to describe, at the outset, the purpose and structure of this paper. This paper is, essentially, a 'think piece' aimed at both improving primarily the performance of the Australian National Audit Office (ANAO) and generating greater understanding of, and contribution to, the related issues and environment in the broader community of interest. It is not a research effort or an exhaustive treatise nor indeed, an analysis, of current management, administrative and audit practices in the public sector.

It is my intention to use this paper as a basis for discussion with interested stakeholders which I hope will provide a test of the degree of perceived commonality of public audit interests and related future directions. I expect the latter to be a shared interest and the outcome of mutual advantage for strategic planning and better understanding of the public audit function by all concerned.

While the focus of the paper is clearly on the Australian environment, the issues canvassed may have relevance for public audit institutions (notably Supreme Audit Institutions – SAIs – as national bodies) in other countries. The support of the International Organisation of Supreme Audit Institutions (INTOSAI) and its regional groups, particularly through their committees and working parties, is essential for the maintenance of the independence, professionalism and public credibility of SAIs.

The first part of the paper examines some of the pressures for change in public administration of which Audit Offices are an integral part, including as a contributor. I will then describe broad environmental trends in Australia which will help to signpost the way forward. This will be followed by a discussion about what auditors 'do' and may need to do in the future if they are to continue to be valued. Finally, I will conclude with a discussion about how we measure our performance and the necessity of demonstrating our continuing credibility, relevance and indispensability in the medium to longer term.

MAIN POINTS

The following are some simply expressed but significant issues for public audit institutions as I see them in today's/tomorrow's public sector environment. Firstly, we have to recognise we are an integral part of that environment and have to provide assurance about its financial management, operations and performance. Consequently, it is an imperative to know and understand, as well as contribute to, that changing environment. This has to be an important element of our comparative advantage as a public sector auditor.

Secondly, we have to act, and be seen to act, in a completely independent fashion. That depends importantly on our legislation but also on our relationships with our main stakeholders, such as the Parliament, the Government and public sector agencies and entities. Achieving respect and support for our independence from all our stakeholders is a major ongoing challenge. Again, it has to be central to our comparative advantage which distinguishes us from, say, private sector auditing firms.

Periods of significant change bring both opportunities and risks. For many constituencies, this is no more apparent than with the greater involvement of the private sector in both the provision, and delivery, of products and services to, and on behalf of, the public sector. Parallel to this development is the greater availability, and potential, of communications and computing technology which is changing the way we do business and how we perform our functions. Such developments present both internal and external challenges for audit offices and courts of audit not least in the areas of accountability and corporate governance.

We need to be credible, relevant and indispensable to our stakeholders, particularly the Parliament and its Committees. In large part, this will depend on the relationships we establish with them and the confidence we engender. The latter largely depends on the relevance, timeliness, quality and cost of our products and the professionalism and responsiveness of our people. Greater assurance will come from a more focussed and integrated approach to audit selection reflecting both the emerging environment and the circumstances of individual agencies and entities. Nevertheless, we continue to be subject to the basic requirements of providing assurance and assessing performance and the need to address any expectation gaps in the audit process.

In a more complex and demanding environment, we need to build positive and supportive partnerships with other public sector auditors, including within the framework of INTOSAI, and with the accounting and auditing profession. The latter includes professional bodies, both national and international, the academic community and private sector accounting and auditing firms. Such partnerships may also greatly assist in dealing with any problems of 'critical mass', particularly where specialised skills and information are involved, as well as technology-based demands in a more knowledge-intensive society. Better communication and sharing may be essential strategies to our survival as credible public audit institutions.

Benchmarking and identification of better practice, coupled with continuous improvement, are becoming central elements of performance. We will be judged not just on what we do but also on how we do it. The latter will depend on both our people as well as the tools and opportunities for development of personal capabilities provided. More innovative approaches and more determined efforts are required to both recruit and retain suitable

and committed staff. Such approaches also have to address how we actually perform the audits, and on what basis, reflecting the use of greater electronic processing. A particular challenge will be how best to address the varying demands and capabilities of our client population within our resource endowments.

RESPONDING TO CHANGE

The future is here

Public Sector reforms in many countries are demanding a more responsive public service. In essence, this means not only adapting to change but also contributing to it. It follows that public auditors, in order to remain relevant, will also have to adapt and respond to a continually changing and unpredictable environment. Adaptability will be a major key to our survival. Conversely, a failure to adapt will lead to loss of credibility and marginalisation. Being 'adaptable' is not without risk. Public Audit Institutions are generally required to be a 'moral exemplar' when it comes to issues of accountability, fairness and probity which are seen to be immutable. Put simply, principles do not often change but practices frequently do.

There is a risk that adaptation may steer us away from our prime purpose so that, in the end we find that we have become something quite different from what was intended. In short, we have to be careful we do not lose sight of our 'reason for being' and the expectations of those who provided our legislation and supported our central role in relation to the Parliament and the general community. The ANAO is indeed fortunate to have clear, comprehensive and supportive legislation (*Auditor-General Act 1997*) which will serve us well in an environment of change. Such legislation is virtually a pre-condition for the success of any public audit institution in the environment being discussed.

Public Audit Institutions will need to have clarity about their role. It will also help if they have a sound knowledge and understanding of the environment in which they operate and can relate to the 'big picture', including how they can contribute to it. And they have to be able to bridge the gap between largely values-based expectations of sound governance and the practical realities of public administration. Borrowing on observed private sector experience, it has been noted that:

*'Companies that enjoy enduring success have core values and a core purpose that remain fixed while their business strategies and practices endlessly adapt to a changing world.'*¹

The authors of this statement go on to suggest that a well-conceived vision consists of two major components : core ideology and an envisioned future. In turn, an organisation's core ideology consists of two distant parts: core

values, a system of guiding principles and tenets; and core purpose, the organisation's most fundamental reason for existence.² These two aspects should present no real problems for Public Audit Institutions where they are largely defined in legislation and other public documentation. But they do need to be stressed and reinforced. The daunting challenge is to create an envisioned future. More about that later. Nevertheless, for now, it is important to keep in mind the need to distinguish core ideology (and core purpose) from longer-term goals that are concrete yet aspirational but, importantly, to ensure their complete alignment for best results.

While public auditors, traditionally, do not comment on matters of Government policy (at least that is the case in Australia) we are nevertheless obliged to offer opinions and - if necessary - guidance on issues of governance. In that sense, we are seen as an important element of the maintenance of democratic governance. The real asset in this respect is our 'independence' which should underpin our 'indispensability'. That is why we should be constantly vigilant to preserve, and guard against any diminution of, that asset.

Complexity will increase

We have to recognise that the world is growing in complexity - this is no less true for political and societal issues than it is for the physical world. And like the physical world, we are really only just beginning to understand the underlying patterns and relationships that give rise to social and political phenomena. For a start, cause and effect is not confined by borders. Developments in one part of the world can lead to a chain of events elsewhere. Trends and movements in public expectations, market behaviour, policy responses and management practice are mobile, are adopted and adapted, possibly mutate but eventually give way to new ideas. I suspect that if one were to apply an epidemiological model to main currents in public policy and public administration over the past twenty years, it would be possible to map the progress and mutation of ideas and practices both geographically and temporally. This would largely be the result of both better communications and the impact and influence of international bodies such as the International Monetary Fund and World Bank.

It has been said that Australia and New Zealand have been in the 'fortunate' position to benefit from the adoption of mature technologies by virtue of the combined effects of geographical distance and a relatively small market. Certainly, we in Australia have been the beneficiaries of notions of governance, models of public administration, management practices and business processes originating in the Northern Hemisphere. We have adopted and adapted these models to meet our needs and, in the process, we have given them our particular character.

Instant communication is increasingly making geographic distance less relevant. Consequently, the lag period between the initiation of an idea in one part of the globe and its application in another is correspondingly diminishing. In addition, the time period between the implementation of a policy or management solution and a full realisation of its actual impacts may often exceed the time required for the transmittal of an idea from one country to another. To employ another medical analogy, it is possible that particular solutions and approaches are being adopted and implemented before the results of the 'clinical trials' are known.

More than ever, public auditors need to be aware of international trends and developments. This means cultivating and consolidating strong, constructive collegial relationships between Supreme Audit Institutions in various countries, particularly in the context of INTOSAI and its regional groups, and between Public Audit Institutions and centres for research and development, such as universities, 'think tanks' and professional bodies within countries. So, to 'adaptiveness' we need to add the notion of 'preparedness'. We as auditors cannot simply be reactive (that is, reacting to events, innovations or technologies as and when they occur) – we also need to anticipate and contribute to change as well as being *prepared to respond* positively to our stakeholders.

Expectations change continually

We cannot be confident about predicting trends in public administration. There are no irreducible formulae or prognostic instruments available to us. However, while there will always be risk of miscalculation, if we build our knowledge base and develop as broad an informational base as possible, we should be somewhere in the ball park. Of course, we have to recognise that the behaviours of people, markets and governments, whose role it is to regulate and guide society and markets, are not inherently rational (economically or otherwise). Such behaviours are shaped as much by belief, perception and attitude as by the rational calculation of costs and benefits. That is the nature of the political environment which we could do well not to forget.

Furthermore, beliefs, perceptions and attitudes are volatile and changeable. As governments well know, voters are increasingly undecided – sometimes alienated – and even fickle. Although loyalty to particular political parties remains a feature of the political landscape, at least in the Western democracies, there appears to be a growing number of voters who remain steadfastly uncommitted. These are the so-called 'swinging voters' who are increasingly the primary target of political communication – especially during elections. It is this group of electors to whom appeals for support are now largely directed.

Although a decline of traditional political allegiances based on geography or socio-economic factors may be indicative of an electorate which is less willing than previous generations of voters to accept the dictums of political institutions, this does not necessarily herald a more aware or informed political culture. Although I have not seen empirical evidence to this effect, social and political commentators in Australia have observed that the Australian public is not especially well informed about Australia's key public institutions or public service culture. For example, there would be some doubt that a majority of Australians of voting age fully understand the role and functions of an Auditor-General.

Therefore, should Public Audit Institutions have a duty to raise the overall level of civic awareness in their respective communities? For my part, I consider that, by logical extension, my statutory responsibility to inform the Parliament constitutes an obligation to inform fully the Australian community. Perhaps, we also need to consider how best to prepare the community to understand the significance of what we do? I have already indicated that public auditors have a particular role in the custodianship of the principles of propriety and ethical behaviour in relation to public administration. In environments where communities consider that their public institutions are becoming less responsive and less capable, and they perceive that the interface between the community and the apparatus of government is more difficult to manage, the public audit function acquires a salience beyond that which is dryly prescribed in its enabling legislation but is increasingly reinforced by its proponents.

The risk, and the challenge, for auditors in such an environment rest on both the reality and the perception of their essential impartiality. Therefore we cannot afford to risk any politicisation of the public audit role. A practical issue is whether politicisation can be entirely avoided. In the environment just described, public auditors also face the challenge of remaining relevant to the general public. For example, where governments commission audits into matters of public administration which have become politically contentious, there is a risk that the general public may perceive the public auditor as being 'coopted' in some way, or complicit in the selling of a particular message. Lack of understanding often comes with complexity, both in terms of the political environment and the nature and subject matter of our audits (whether performance or financial audits). Audit institutions, by and large, do not go out of their way to draw attention to themselves. However, we need to ask ourselves seriously whether we are immune to the dictum '*market or perish*', particularly in a more contestable environment.

Adaptability is a key to survival

The foregoing comments inevitably bring us back to the initial premise about the inevitability of change and the importance of adapting to change. Should we be 'tooling up' in anticipation of events and circumstances which possibly

have not occurred yet, or is the future already here? In either case, we need to identify the particular factors that are likely to impact on what we do and how we do it. In most Western democracies we have witnessed a convergence in the policy platforms of the major political parties to the extent that political analysts and the voters themselves have increasingly found it difficult to distinguish between them (a related phenomenon is the increased voter attractiveness of many of minor or even micro-parties and independents, as well as the increasing 'foot-looseness' of major party support).

Public policy and public administration in much of the developed world have been increasingly shaped by a strong focus on fiscal performance and economic efficiency. Often the preferred policy responses have embraced strategies of public sector downsizing, privatisation, commercialisation and corporatisation. However, there is evidence in a number of jurisdictions – including Australia – that electorates are questioning the results of some reforms. The intentions have largely been to make the public sector more business-like and to involve the private sector more in the provision of public services either in partnership or in competition with the public sector. It is also clear that there is a broad perception that some parts of the community have borne a disproportionate share of the social, economic and structural costs of reform (for example, in Australia, many contemporary political and social observers in Australia would say this is indicative of much of the non-metropolitan areas in general and of the welfare sector in particular).

There appears to be an emerging demand for a greater differentiation in the political 'product'. As a result, we see in some jurisdictions attempts by major political parties to reinvent themselves in an effort to get back in touch with their 'traditional' – but apparently disaffected – constituencies by being seen, through their rhetoric and policy formulations, to clearly diverge from the so-called 'economic rationalist' approach. At least there is ongoing debate of the issues as there is of the liberal market philosophy involved. Some see such a move as a belated reaction to significant change while others perceive it as the next stage of the transition to the global economy with its challenges to the ability of government to govern, not least in the preservation of their tax base.

In an increasingly global environment, the question of competitiveness and/or contestability of the public sector against similar elements in the private sector, including benchmarking of performance, would seem to suggest that our attention should be more outwardly than inwardly focused in the future at least, if not now. External pressures may require the development of 'real' partnerships between the public and private sectors in the interests of maintaining national sovereignty and global competitiveness. The imperative would then be to develop a highly performing public sector to complement the private sector rather than just compete with it. In this respect, it is interesting to consider the United Kingdom (UK) 'Modernising Government' approach which stresses 'partnership delivery' by all parts of

government as well as with the private sector.³ The UK National Audit Office subsequently reported on its response (and strategies) to that policy, including the notion of 'joined-up' government.⁴ The latter also reflects the impact of technology, particularly in the use of the Internet and moves to E-Commerce, on service delivery, transactions and data sharing involving greater networking within and outside the public sector.

In a similar context, a recent article by Professor Mark Considine and an associate noted the emerging image of 'network bureaucracy' stressing co-production of results as against 'market bureaucracy' with its emphasis on contracting-in and introduction of quasi-markets.⁵ The move to an output/outcomes framework for managing resources and measuring performance at the Federal Government level has engendered discussion about 'shared outcomes' and the strategic and other relationships between outputs that contribute to those outcomes and those organisations responsible for both. Nevertheless, while recognising there are debates, for example, about transactions costs issues associated with contracts and markets, academic writers have also pointed out the limitations of trust-based relationships, longer-term instability of inter-organisational networks, unintended consequences such as fraud and corruption and resistance to innovation and protection for under-performing organisations⁶. The issues are not simple and require wide-ranging debate but many might support the view that:

*'... the choice between markets, hierarchies and networks should be a matter of 'practicality' instead of 'ideological' conviction.'*⁷

And what does this mean for public auditors? We need to be part of any transition process in our areas of expertise, particularly in relation to public administration, both as a contributor to the direction, nature and timing of such change as well as being the auditor, evaluator and facilitator of the inevitable environmental and organisational impacts. As in the past, there will be no return to the 'good' or 'bad' old days. There will only be 'new' days, new systems, new structures, new demands and expectations and new configurations of risk and results. Our interest is mainly in accountability for performance and helping to ensure that the accountability framework is sound and effective. Interestingly, the UK 'cross-cutting approach', which refers to any policy or service where there is, or should be, joint working between government departments and agencies, as part of 'joined-up' government, not only encourages auditors to support and encourage sensible risk taking but also wants them to minimise any barriers or disincentives to the approach due to audit.⁸

We, as public sector auditors, have to be prepared also to respond to changing governance arrangements as part of the bureaucracy. We also have to respond as part of the profession of accounting and auditing working closely with the relevant professional bodies and associations. The challenges may

well be beyond the resource endowments of many, if not most, public audit offices. The prospects of developing contributory partnerships both with private and other public sector organisations have to be fully investigated as to the possibilities for shared contributions while maintaining the credibility and legitimacy of the independent public sector auditor. History shows that non-government organisations are prepared to cooperate and contribute to shared purposes and visions in the public interest as good corporate citizens.

LEARNING THE LESSONS OF YESTERDAY AND TODAY

While there is no necessary expectation that the past will provide answers for the future nor any indication of what will be the likely challenges of tomorrow, we should at least explore what lessons we have learned to be as well prepared as we can be to deal with the uncertainties already discussed. There is no doubt that has been a period of significant change in public administration in most countries. We have come to accept that change is a continuous process. If we are to do what is necessary to engender the culture, the professionalism and the flexibility in our organisations to be able to adjust quickly and credibly to change, we have to be sensitive to the direction and speed of that change. I will be largely using the Australian situation as an illustration of what might be needed to achieve that outcome.

The impetus for reform

The Australian Public Service (the APS) reform agenda has spanned almost two decades. As with many other democracies, Australian governments have been under increasing pressure to achieve a better performing public service and less costly, more tailored - or better focussed - and higher quality services for their communities. Accordingly, the Australian Public Service has been steadily evolving towards a more private sector orientation with a particular emphasis now on:

- the contestability of services;
- the outsourcing of functions which the private sector can undertake more efficiently;
- ensuring a greater orientation towards outcomes, rather than just on process; and
- an accent on continuous improvement to achieve better performance in an environment of devolved authority and greater management flexibility.

These developments have given rise to a focus by many politicians, public servants and academics on what constitutes 'core' public sector activities as opposed to 'non-core' ones. The Minister Assisting the Prime Minister for the Public Service has stated that the Government's objective:

'has been to focus the APS on its core activities of policy development, legislative implementation and the contracting and oversight of service delivery'.⁹

That is, what are those functions which can, and should, only be performed and delivered by government. Clearly, the size of the core is shrinking as evidenced by outsourcing and privatising in areas which, hitherto, were considered traditional public sector activities. Just how small the core can

become is very much open to debate. But even areas where the public sector has traditionally held a monopoly, such as the provision of policy advice, are becoming increasingly open to competition from the private sector. This action has literally meant the creation of a market for public sector service delivery, such as employment services, resulting in greater choice and more competition with adverse consequences, more recently, for the sole public sector provider. The implications of the latter depend largely on why a public sector provider is retained in a competitive environment. A broader question is what is the sustainable critical mass necessary to retain a credible and effective public sector as part of sound democratic governance in the longer term.

A more 'business-like' approach

A major impetus for the changes we have witnessed to date has been the fundamental questioning of what government does, or should do, allied with a perception of inefficient (costly) and ineffective (lacking client focus) delivery of public services due to its monopoly provision and/or other constraints of public sector administration. Reform efforts have focused on core government activities, as indicated above in the Minister's statement, that is: policy development; legislative implementation and the contracting and oversight of service delivery. The implementation of the reform agenda has involved organisational restructuring, business re-engineering, outsourcing, commercialisation, privatisation and/or the transfer or abandonment of functions and services.

Put simply, the prevailing rationale is that public services would be provided more efficiently and effectively, with greater client satisfaction, in a more market-oriented environment which provides greater flexibility for management decision-making and the discipline of competition. Indeed, history shows varying support for such a view but with reservations, for example, about market imperfections and public goods arguments (to use economic terminology). Concerns have been expressed about the maintenance of public service values and ethics, as well as issues such as probity, privacy, security, equity and transparency. The New Zealand Auditor-General recently observed that:

*'There is a special relationship between the user of a public service and the provider of that service – dependency, the force of law, and a lack of choice are all factors that distinguish public from private services.'*¹⁰

One of the greatest challenges for government organisations in implementing the reforms has been in the area of program delivery. Implementation of the purchaser-provider dichotomy, often as part of a policy/administration split, along with a greater emphasis on client focus and public service responsiveness, have changed the way in which government programs are delivered. These changes have been most apparent in the areas of

employment, health care and social welfare. Such observations have to be qualified to the extent that computing and communications technology, for example, are also having, and will increasingly have, a marked impact on the way public services are being delivered. Nevertheless, in a more contractually-oriented environment, there are concerns about the impact of transactions costs involving, for example, communications, information, monetary and financial management systems, as well as costs that cannot be measured. The following quote puts such concerns in a broader perspective:

*'The transaction costs of the market-oriented public service are considerable. They may be justified on the grounds that they are offset by the gains that are made in the efficiency and effectiveness of the public service, but the immediate effect is likely to be seen by many as the growth of a new form of bureaucracy, established to manage the market.'*¹¹

These kinds of issues are more about public management than public administration. Nevertheless, there are also some fundamental questions about the latter as the following discussion will indicate.

The need for 'adaptive' management systems and culture

Not only has the nature of program delivery changed but so have the management systems that support it. For example, there has been a steady devolution of responsibility and authority away from central agencies so that Chief Executives of operational agencies now have greater autonomy in their decision-making, as well as greater flexibility in how they manage their resources and affairs.

Greater responsibility and flexibility in decision-making need to be matched by a commensurate focus on strengthening the associated accountability arrangements to ensure that decisions are appropriately made and that those people making decisions can be properly called to account should questions of accountability arise. To provide such assurance, public sector entities need to have robust corporate governance arrangements, including financial management and other control structures in place. More robust controls are required in an era of devolution of authority to individual agencies and entities. The work of the INTOSAI Internal Control Standards Committee is proving, and will continue to prove, useful for audit assessments and evaluations of such controls.

Particular Parliamentary concerns have been expressed about the protection, and proper use, of public resources and ethical (values-based) conduct of those delivering them. As well, there is concern that the terminology of the Commonwealth's financial management legislation should be more consistent with that used in the private sector.¹² While there is acceptance of greater risk management reflecting approaches taken in the private sector, emphasis has been placed on commensurate accountability, including the systematic

identification, privatisation, assessment, treatment and monitoring of risks, in the public sector environment.

Underpinning the changes to both program delivery, and its supporting systems, is the evolution of a more contract-oriented and contestable public service. In Australia, a number of federal government entities have outsourced service delivery functions, information technology services and corporate management functions. Consequently, the following observation is not surprising:

*'Contract has become the most significant mechanism for the ordering of public resources and the delivery of services, both to the public and to the government itself. It has replaced traditional public administration in significant areas of government.'*¹³

Because accountability is fundamental to a democratic system, the privatisation of the public sector requires the transparent demonstration of accountability for the stewardship of public resources particularly in a more contractually-oriented public sector.

Importantly, the privatisation of the public sector does not obviate, or limit, the need for accountability to stakeholders. To the contrary, less direct relationships (such as the introduction of the private sector service provider in the accountability chain) and devolved decision-making strengthen that need. The question is, who is accountable for what and to whom? How we answer that question will largely determine the success or otherwise of an increasingly results-oriented public sector and the public confidence that engenders.

A convergence of the public and private sectors

As a direct consequence of greater contestability of services, outsourcing of functions and a stronger APS orientation towards the notions of outcomes¹⁴, outputs¹⁵ and continuous improvement, we are witnessing an apparent convergence, or reconvergence in a historical sense, between the private and public sectors.

This convergence offers opportunities for enhancing partnerships and sharing of concepts but also brings into clearer focus the distinctions between the two sectors. In particular, convergence raises issues about the nature of accountability in this changing environment - the public sector accountability relationship with the Parliament and the community 'imperatives' versus the commercial 'realities' of operating in the marketplace. A recent paper has also drawn attention to differences in legal responsibilities, particularly in the context of the *Corporate Law Economic Reform Program (CLERP) Act* and the *Commonwealth Authorities and Companies (CAC) Act 1997*.¹⁶

This is not the place to examine the wide range of accountability issues that any convergence may involve, which I partly did last year.¹⁷ However, the growing use of private finance in operational areas such as infrastructure, property, defence and information technology (IT) is raising a range of issues of both management and audit interest. In particular, risk transfer is seen as a major driver of the Private Finance Initiative (PFI) in the United Kingdom.¹⁸ For example, in contracting the funding, design and management of IT and infrastructure projects to the private sector, the associated transfer of risk to private sector managers is being justified on the basis that they are better able to manage the risks involved. Mr Le Marechal CB, Deputy Controller and Auditor General of the United Kingdom (UK) National Audit Office, noted in correspondence with me on an early draft of this paper that:

'In practice, on IT projects in particular, we have seen considerable naivety on the part of government departments as to the extent to which they can actually transfer risk'.¹⁹

Mr Marechal pointed out that departments have found out too late that it is their job to sort out problems and get results if essential public systems do not work properly. He went on to observe that:

'Under heavy public and political pressure to get systems working properly, departments are then reluctant to take a hard line on their contractual rights and so sour relationships with the very contractors whose cooperation is essential'.²⁰

This point was emphasised by a Report commissioned by the UK Treasury which indicated that some invitations to negotiate by public sector bodies included risks that could not realistically be best managed by the contractor.²¹ Nevertheless, the UK National Audit Office itself concluded that:

'Appropriate risk allocation between the public and private sectors is the key to achieving value for money on PFI projects.'²²

The National Audit Office, not surprisingly, went on to advocate an approach involving the 'optimum' transfer of risk, which simply means allocating individual risks to those best placed to manage them. As usual, the devil is in the detail but experience is indicating some useful means of deciding on an appropriate allocation of such risks.

Periods during which any revised accountability arrangements and changed organisational structures are having to be bedded down present the greatest risk to effective decision-making. In my view, such risk is accentuated as a result of:

- greater involvement of the private sector in contractual arrangements;
- loss of corporate memory in agencies with downsizing of the public sector;

- the greater use of computing technology with attendant control and fraud related issues (particularly when outsourced);
- a lack of project and contract management skills in the public sector; and
- insufficient experience generally in managing on an accrual accounting and full costing basis.

The notion of accountability is not exclusive to the public sector. No one doubts, for example, that the boards of private sector corporations are accountable to their shareholders who want a return on their investment. It is the nature, extent and complexity, particularly in relation to Ministers and the Parliament, of that accountability which public sector commentators would contend distinguishes the two sectors. Of note, is that the adoption or adaptation of private sector approaches, methods and techniques in public service delivery, has highlighted the issue of trade-offs between the nature and level of accountability and private sector cost efficiency and, perhaps, pricing.

Managing outsourcing while maintaining accountability

It is important to recognise that the provision of public services is not just about realising the lowest price, or concepts of profit, or shareholder value. It is about maximising overall 'value for money' for the taxpayer and ensuring proper accountability for use of public resources and achievement of agreed results which often involve a significant non-monetary element. The latter requires consideration of issues other than production costs, such as client satisfaction, the public interest, fair play, honesty, justice and equity.

Although the public sector may contract-out service delivery, this does not equate to contracting-out the responsibility for the delivery of the service or output. It is the responsibility of the agency to ensure that the service delivery is both cost-effective and acceptable to individual recipients and key stakeholder groups. I am also indebted to Mr Le Marechal for the observation that:

*'The trend towards more diverse forms of delivering public programmes comes as much from a wish to evade rigorous public accountability as it does from considerations of managerialism.'*²³

Mr Le Marechal also referred me to a relevant quote by Sir Robin Butler, the UK Cabinet Secretary of the time:

'The panoply of Parliament, elections and public accountability, is put in place to give citizens control over those functions performed on their general behalf by the people whom they elect. Yet, judging by the extent to which we put in layer after layer of further safeguards on the exercise of such functions by our democratic representatives, far greater than the

*controls we put over the exercise of functions by others, whether quangos or in the private sector, it might be concluded that it is this structure of democratic control in which we have the least confidence of all. Perhaps that huge overhead of accountability and redress which we impose on Government is another of the factors which underlies the trend towards privatisation in recent years.'*²⁴

A related [view was expressed](#) by the Australian Joint Committee of Public Accounts and Audit (JCPAA) in relation to a review of one of my reports as follows:

*'... Some agencies may see a benefit in the reduced accountability that can occur when services are outsourced to the private sector.'*²⁵

In essence, this was a criticism, not an observation.

The planning, negotiation and ongoing management of contracts needs to be undertaken in the context of other relevant public sector reforms such as output/outcomes based accrual accounting and budgeting. In purchaser/provider environments, it is critical to define clearly how the services delivered by the provider contribute to the outcomes (and in some cases, outputs, where the services are of an intermediate nature) of the purchaser.

Experience has shown that, while government entities should aim to work in partnership with the private sector, any successful outsourcing arrangement must be based on sound tendering processes and an enforceable contract. To be enforceable, the contract must specify:

- the level service and performance required;
- the relationship between the parties, including identification of respective responsibilities; and
- the mechanisms for monitoring performance, including penalties and incentives.

There should not be any equivocation about required performance nor about the obligations of both parties. This is as much about achieving the desired outcome as it is about meeting accountability requirements for the efficient, effective and ethical use of resources no matter who delivers the particular outputs/outcomes.

Striking the right balance

There is a need to strike a balance between the appropriate nature, and level, of accountability and the imperative to achieve cost-effective outcomes. Such a balance is the decision-making prerogative of the Government and Parliament or Legislature. It is not an issue to be determined by agencies or

entities, particularly by default where no guidance has been provided by any of the foregoing authorities. A clear indication of the accountability requirements in the changing environment would be very helpful to agency management at all levels. The ways agencies can better manage this process themselves include:

- emphasising the importance of project and contract management skills for public sector managers;
- basing commercial relationships on sound tendering and administrative processes and an enforceable contract; and
- ensuring that public accountability is not eroded, virtually by default through, for example, contracting-out that reduces external scrutiny through public reporting and the activities of Auditors-General.

An important part of appropriate and transparent accountability arrangements for contract management is the capacity for agencies and public auditors to have adequate access to contractors' records and premises (to this end, the [Australian National Audit Office](#) ANAO has developed a set of standard access clauses for inclusion in contracts with the private sector).

Commercial confidentiality

Virtually all traditional accountability mechanisms rely on the ready availability of reliable and timely information. As a result of contracting-out to the private sector, there has been a marked tendency by various agencies to restrict the flow of information available to assess performance and satisfy accountability requirements. This situation has arisen where performance data is held exclusively by the private sector or through claims of commercial confidentiality that seek to limit or exclude data in agency hands from the scrutiny of Parliaments and other Legislatures. Parliamentary concerns have been expressed that accountability can be impaired where outsourcing reduces openness and transparency in public administration. For this reason, the issue of commercial confidentiality is likely to be of increasing importance to public accountability as the extent and scope of outsourcing grows with the accompanying tensions and potential conflicts with private sector providers/suppliers.

My view is that the question as to whether or not commercial-in-confidence information should be disclosed to the Parliament or Legislature should start from the general principle that information should be made public unless there is a good reason for it *not* to be. In other words, there should be, in effect, a reversal of the principle of onus of proof, which would require the party that argues for non-disclosure to substantiate that disclosure would be harmful to its commercial interests.

The Australasian Council of Auditors-General²⁶ has developed a statement of Principles for Commercial Confidentiality and the Public Interest. As an example, one of the Principles concludes that:

*'Some private and public sector bodies are instinctively apprehensive and protective about the disclosure of any commercial information. But such views often overstate the implied risks to an entity that might be occasioned by the release of commercial data. After-the-event commercial information has significantly less value than commercial information concerning events that have yet to occur. But even where commercial information might have commercial value to others, there are often overriding obligations that require it to be released. This is so for commercial information held in the private sector and, a fortiori, it applies to the public sector.'*²⁷

The issues indicated in the above conclusion reflect a number of considerations which have exercised the minds of fellow Australian State Auditors-General in addressing commercial-in-confidence material. A particular concern has been the insertion of confidentiality clauses in agreements/contracts which can impact adversely on Parliament's 'right to know' even if they do not limit a legislatively protected capacity of an Auditor-General to report to Parliament. The latter can create tensions when Parliamentarians are frustrated by their requests under Freedom of Information legislation being denied and they then look to the auditor to provide the information. Not surprisingly, Auditors-General actively promote the maximum possible availability of information in the interests of accountability.

At the heart of this debate is the on-going problem of clearly defining the 'public interest'. The public interest is, of course, fundamental to democratic governance and is an issue that public officials, including auditors, continually grapple with. Section 37(2) of the *Auditor-General Act 1997* provides some guidance in this respect. Again, the challenge is about striking the right balance between public and private interests.

One of the difficulties in addressing commercial confidentiality issues is that of precise definition as to what is being covered by such an umbrella description. While there is broad understanding of the kinds of information which contractors might regard as commercially confidential, the question is how best to ensure adequate accountability for the use of public funds while ameliorating any justifiable 'confidentiality' concerns. Such concerns were evident in a recent recommendation for draft guidelines to be prepared for the scrutiny by Parliamentary Committees of commercially confidential issues relating to Government Business Enterprises.²⁸

Recent legal decisions have reiterated the importance of maintaining 'proper confidentiality' of tendering proposals.²⁹ With the growing convergence between the private and public sectors in many countries, and the

considerable associated increase in contracting, the issue has become a matter of practical importance and some urgency for resolution. A particular concern is that agencies may too readily agree to treat contractors' documents as confidential, notwithstanding the wide access powers that may be provided to the Auditor-General and possible publication of any restriction in an audit report in the public interest.

Another challenge for Auditors-General in the move to increased contracting with the private sector for the provision of government services is our actual ability to access the relevant records. At present I do not have a legislative provision similar to that which I understand applies in the United States that guarantees access by government auditors to the private sector service providers' premises. Mr Le Marechal, in correspondence referred to earlier, also observed that, in the UK, whatever their motivation, Ministers and senior civil servants have shown little enthusiasm for modernising the access rights of the National Audit Office to reflect the different ways in which public business is done.³⁰

As also indicated earlier, my Office is currently encouraging the inclusion of a suitable access to premises clause in contracts with the private sector. Such a clause is not necessary to enable me to seek access to information as that access is available under Section 32 of the *Auditor-General's Act 1997*. It is seen as important in flagging to contractors that they must give full access to the Auditor-General for proper accountability. In my view it is a matter of educating both parties, whether in the public or private sector, to the requirements of a successful relationship or contract.

The lesson here is that external scrutiny (through public reporting and the activities of Auditors-General) is an essential element in ensuring that public accountability is not eroded, by default, through contracting-out. Just as it is incumbent upon public sector agencies to ensure they have a sound understanding of the commercial nature of any contract, private sector entities need to recognise that there are overlaying public accountability issues, not present in purely private sector transactions, that need to be addressed, particularly if there is any apparent conflict.

Implications for Public Audit Institutions

If we look back on the preceding decades and the progression of circumstances and related events which have defined our present day environment, it becomes clear that the 1980s and the 1990s represented a considerable paradigm shift in the social, economic and political construction of the approach to government programs and service delivery. Moreover, when we look closely at those events, we see that the change has not occurred as a gradual, incremental progression, rather – to borrow a term from evolutionary theory – change has been more akin to a 'punctuated equilibrium' model. This means that change has occurred in 'bursts', impelled

by precipitating events. Most of the changes in public administration have been adaptive and some not. All were calculated to respond to a changing social, economic and political 'ecology' increasingly being impacted by 'globalisation'.

A punctuated equilibrium model of change also means that the speed and direction of change are hard to anticipate and, consequently, the effects difficult to extrapolate. Approaches to public administration gain ascendancy – or suffer decline – in a dynamic environment. More often than not, the ascendancy of ideas about governance and public administration depends more on political dynamics (and the underlying social and economic conditions which shape public perceptions) than on the application of the latest management theories, although the latter may subsequently be part of the 'political package'.

Such is the environment we have to work in. Assumptions which we previously regarded as 'given' are rendered less certain and less relevant by ongoing events. Adaptations which conferred an 'evolutionary' advantage yesterday, can become an encumbrance tomorrow. The one persistent 'truth' in public administration is the requirement for accountability: that and the need for the appropriate intellectual and practical tools to demonstrate accountability in action. Public sector managers and auditors have been increasingly challenged in the latter part of the 1990s to come to grips with the new environment, its demands and often unfamiliar disciplines – particularly as a consequence of the greater convergence of the public and private sectors and the accompanying adoption/adaptation by public sector organisations of commercial concepts and practices.

Public sectors in Australia (and I include Public Audit Institutions) are still in transition. Public service culture has proved to be somewhat of a road block because of the individual and collective adjustments needed to be made and perhaps too few, or indistinct, road signs to follow. In a changing environment, it is unlikely that there will be too much comfort for public sector managers in respect to the latter. The same holds true for public sector auditors. Nevertheless, there is a legislative requirement for Chief Executives to ensure the ethical use of resources for which they are responsible.

What we all have in common is a legislated set of public service values (*Public Service Act 1999*) and codes of ethical conduct which complement them. These are our collective touchstone and are one of the major factors which distinguish us from the private sector. The latter relates mainly to the values rather than the existence of codes of conduct per se. However, questions have been raised whether public administration needs a new set of ethics reflecting 'entrepreneurial values' in a more private sector oriented environment.³¹ On the other hand, it is argued that such an environment makes it more vital to underpin public interest with enduring ethical standards 'grounded in law and constitutional democracy'³². The tension is similar to that with the

question of any accountability trade-off which, as indicated earlier, is one largely for Parliament and the Government to resolve.

MAKING PUBLIC AUDIT MORE RELEVANT AND INDISPENSABLE

Public Audit Institutions do not exist in an environment which is separate, or separable, from the broader pressures on governments, the economy, society or the public sector itself. If public audit practices are to remain relevant and viable, we need to have an acute awareness about our own practices, business processes and deliverables and a good understanding about the changing public sector environment.

Audit Offices, like any other public sector entity, have to achieve identified outputs and outcomes within legislative, as well as human and other resource, constraints. Audit Offices are not some kind of interested on-looker to an environment to which we have to contribute. They have to be an integral element of that environment to support its credibility and viability and the confidence and trust of all stakeholders. The ANAO is confronting this 'reality' and is endeavouring to adjust its business practices and systems to at least maintain, if not improve, its relevance and performance. It is not easy, partly because we have not fully 'exploited' our independence nor fully demonstrated our 'indispensability'. We need to be more than valued, important as that might be.

The role of Auditors-General

While there are variations in the mandate, focus and operating arrangements across countries, the fundamental role of Auditors-General, or their equivalents in democratic systems of government, is substantially the same. That role is broadly to provide the elected representatives of the community (the Parliament or Legislature) with an independent, apolitical and objective assessment of the way the government of the day is administering their electoral mandate and using resources approved by democratic processes, albeit under differing governance frameworks.

In most, if not all, systems of government, the concept of accountability is of fundamental importance to governance, as I have stressed earlier. By accountability I mean a direct authority relationship within which one party accounts to a person or body for the performance of tasks or functions conferred, or able to be conferred, by that person or body.

Auditors-General have to be seen to be an essential element in the accountability process by providing a unique blend of independence, objectivity and professionalism to the work they do. This has been expressed, in a practical sense, by the four national audit agencies making up the Public Audit Forum in the United Kingdom as follows:

'... there are three fundamental principles which underpin public audit:

- *the independence of public sector auditors from the organisations being audited;*
- *the wide scope of public audit that is covering the audit of financial statements, legislatively (or legality), propriety (or probity) and ~~{delete full stop}~~ value for money; and*
- *the ability of public auditors to make the results of these audits available to the public, and to democratically elected representatives.'*³³

In short, the role of the Auditors-General today includes providing independent assurance on the overall performance and accountability of the public sector in delivering the government's programs and services and implementing effectively a wide range of public sector reforms. And I cannot overstate the importance of the independence of the Auditor-General in those respects. As the public and private sectors converge; as the management environment becomes inherently riskier; and as concerns for public accountability heighten; it is vital that Auditors-General have all the professional and functional freedom required to fulfil, fearlessly and independently, the role demanded of them. I would place some emphasis on the sufficiency of resources but also recognise the need to be realistic in this respect in the environment we face with demands for lower taxes and smaller government.

I would argue that the role of Auditors-General is more important to effective, accountable and democratic governance today than at any time in the past. I would also suggest that, as we move into the future, and as the pace of change remains unabated, this trend will not decline. Rather, it is likely to increase as the roles and responsibilities of the public and private sectors converge and, perhaps, the differences between the two become more critical to define, explain and accept as opposed to the concepts and approaches those sectors might share.

An integrated audit service

To achieve our outputs and outcomes and meet our other responsibilities to the Parliament as well as to the Government, audit clients and the general public, the ANAO produces a comprehensive range of audit reports and related products and services. Our main products are financial statement and performance audits, complemented by audits of financial control and administration, and assurance control and assessment audits, as well as better practice guides (see Attachment) and other audit-related services but not in competition with the private sector. I stress audit-related in a narrow sense as I am sensitive to perceptions about any apparent conflicts with public audit independence. I will also explain later the audit-related value of better practice guides, both as a benchmarking exercise and as a vehicle for providing audit assurance, to the Parliament and its Committees.

The development and delivery of our products and services are based on an integrated strategic approach at two levels:

- at the broader level across the public sector, we need to ensure that our product mix and coverage are tailored to the environment in which we operate and to the accountability/assurance needs of our principal client, the Parliament; and
- at the agency or entity level, we aim to ensure audit services of those organisations' reflect their individual circumstances to assist them to improve their performance while minimising duplication or overlap with other reviews to the maximum extent possible.

The ongoing challenge is to maintain an appropriate balance of audit activity across the public service to fulfil our statutory obligations while meeting the particular demands of Parliament and of individual public sector organisations for, say, audit assurance and/or advice. A key to achieving the right activity mix is understanding, and acting on, the Parliament's apparent priorities. Recently there was a recommendation that a consolidated series of charts and tables comparing the performance of all Commonwealth Agencies against a range of key performance ratios should be tabled in Parliament on an annual basis³⁴. Only one State and one Territory have legislation requiring audit of performance indicators. With greater Parliamentary interest in performance information, we need to give consideration as to how best to provide any opinion and/or comment that may be sought on such information.

The ANAO makes a considerable effort to ensure that we maintain a strong relationship with the Parliament through interaction with parliamentary committees and individual parliamentarians. The views of parliamentary committees and public sector entities are sought when audits are being planned, and suggestions from individual Parliamentarians are welcomed. Nevertheless, it is clear that the final decisions about the audit workplan are the responsibility of the Auditor-General.

The timeliness, cost effectiveness and quality of program delivery and contestable service provision were overriding themes of our 1998-99 audit program. A measure of our success has been the extent of Parliamentary and media interest in our audit reports, particularly those that have examined issues associated with the negotiation, administration and value for money of major contracts. Perhaps, not surprisingly, these have engendered considerable debate and comment. They point to the need for the ANAO to be prepared to deal with emerging issues as they arise, such as Budget performance, including performance information on an outputs/outcomes basis in an accrual accounting and budgeting framework; and the taking of evidence under oath or affirmation with its various ramifications, for example

in relation to **individuals'** rights (natural justice) and legal complexities, including duty of care considerations.

As previously indicated, in addition to audits of Government entities' financial statements and performance audits, the ANAO also produces Better Practice Guides (BPGs) aimed at promoting better practices in public sector management and as a basis for providing later audit assurance when applying those BPGs to agency practices. Allied to our BPGs are the range of audit-related advisory services we provide to entities. For example, we are currently undertaking a benchmarking study of the finance function in a number of Australian federal government agencies. This is a particularly important function underpinning a range of managerial decision-making responsibilities, using accrual-based information, and including the monitoring and review of contract performance.

The ANAO also undertakes protective security audits which are 'across-the-board' studies that examine control frameworks and use established better practice criteria to evaluate agency performance. The three key aspects of security that are examined in these audits are information , personnel and physical security.

We present client seminars on topical issues, such as controlling performance and outcomes, and make presentations to, and with, other stakeholders and interested parties, for example the Australian Society of Certified Practising Accountants (ASCPAs) and the Institute of Public Administration Australia (IPAA). We also have strong involvement, for example on Corporate Governance and other professional issues, with the Institute of Chartered Accountants in Australia (ICAA). We value the links established with a number of tertiary institutions, in particular the Canberra and Australian National Universities. Of growing importance are the 'partnership' arrangements we have with major consulting firms in the areas of accounting and auditing, as well as on legal and constitutional issues that contribute significantly to our being able to deliver a credible integrated audit service.

Contributing to standards setting

Setting Auditing Standards

Under the *Auditor-General Act 1997*, I am required to set auditing standards with which individuals performing Auditor-General functions must comply. In setting the Standards, I acknowledge the commonality of professional requirements between private and public sector auditors and as such, the ANAO Auditing Standards are formulated with regard to the Auditing Standards issued by the Auditing and Assurance Standards Board of the Australian Accounting Research Foundation (AARF).³⁵ Consistency with the INTOSAI Auditing Standards is also a consideration in setting the Standards. The INTOSAI Code of Ethics for Auditors in the Public Sector, produced by

the INTOSAI Auditing Standards Committee in 1998, is a necessary and useful complement to those Standards.

The current ANAO Auditing Standards incorporate the codified Auditing Standards and Auditing Guidance Statements issued by the AARF. Amendments to standards and guidance statements are automatically incorporated into the ANAO Standards. In this context, and our broader role in the accounting environment, it is important for the ANAO to contribute to the process of setting these Standards.

The issue of new or revised Auditing Standards requires the exposure of proposals for change to interested parties for their comments. My Office comments on all proposals in conjunction with the Auditors-General of the Australian States and Territories under the auspices of the Australasian Council of Auditors-General. Where possible, the Auditors-General seek to express a consensus view, although if necessary, dissenting views may be noted. There is no formal consultative process for the issue of Auditing Guidance Statements.

The Auditing and Assurance Standards Board has 11 members, including my Deputy Auditor-General and the Auditor-General of Western Australia. Other members are from each of the 'big five' accounting firms, a number of second tier firms and an academic. Appointments are personal rather than as representatives of special interest groups.

Setting Accounting Standards

Until recently, the Accounting Standards have been made and amended by the Australian Accounting Standards Board³⁶ and the Public Sector Accounting Standards Board.³⁷ The ANAO had, until recently, a senior representative on the Public Sector Accounting Standards Board.

The development and amendment of the Accounting Standards follows a process of public consultation, where changes are released as exposure drafts for public comment. Australian Auditors-General contribute as a matter of course to the development of Standards through this process.

To complement this framework, an Urgent Issues Group has been established with a shorter consultative process to allow it to respond quickly to issues raised. The Group conducts public meetings, seeking issue proposals for consideration from concerned parties and inviting submissions on any issue proposals that proceed to adoption. The ANAO formerly had a senior representative on this Group; public sector auditors are currently represented by the Auditor-General of Tasmania.

This standard-setting process is changing following the enactment of the *Corporate Law Economic Reform Act 1999* on 1 January 2000. The Act

establishes a Financial Reporting Council (FRC) and a new Australian Accounting Standards Board (AASB).

The key functions of the FRC are to advise the Government on the accounting standard setting process and the development of international accounting standards. The FRC determines the broad strategic direction of the AASB, gives it directions, advice and feedback on matters of general policy, and is responsible for approving its priorities, business plan, budget and staffing arrangements. However, the FRC cannot influence the AASB's technical deliberations and hence the content of particular accounting standards.

The members of the FRC are appointed by the Treasurer from nominations by stakeholder groups. Current members represent a number of private sector business and accounting bodies, the Australian Stock Exchange, the Securities Institute, the Federal, State and Territory Treasuries and the Commonwealth Department of Finance and Administration. At this stage there is no public sector audit representation on the Board.

The AASB is responsible for developing a conceptual framework for evaluating proposed standards; making standards for the purposes of the Corporations Law and for other purposes; and participating and contributing to the development of a single set of standards for world wide use. Members of the AASB must have knowledge of, or experience in, business, accounting, law or government to qualify them for the appointment. This is important if there is a move to cover assurance services such as has occurred for the Assurance Standards Board in Canada. In Australia, the Auditing Standards Board mandate was also expanded in 1998 and was renamed the Auditing and Assurance Standards Board.

The mechanisms through which the ANAO and State Auditors-General will be able to contribute to the Standards under this new framework are yet to be established. The responsibilities of the FRC include establishing appropriate consultative mechanisms and monitoring the operation and effectiveness of the AASB's consultative arrangements. To fulfil these responsibilities, the FRC may establish committees and advisory groups in which public sector auditors could participate. The FRC has already committed to establishing Project Advisory Panels that will address stakeholder interests for each project undertaken by the AASB.

A project to harmonise Australian Standards with International Standards issued by the International Accounting Standards Committee is currently being undertaken within this standard-setting framework. The aim is to ensure that compliance with Australian Accounting Standards results in compliance with International Accounting Standards. A problem is that International Standards, as they currently stand, are compromises which allow alternative treatment, with many running counter to well established standards in Australia.

In addition, the International Standards make no mention of government or the particular requirements of public sector auditing. While, in principle, there would be support for a common set of standards for the public and private sectors, there are also concerns that specific public sector requirements are recognised either through particular standards and/or using public sector illustrations as well in generic standards. The INTOSAI's Committee on Accounting Standards is playing, and can increasingly play, a significant role in the development of suitable standards that can be applied sensibly in the public sector and in any transition/harmonisation process from a cash to accrual basis of accounting and budgeting.³⁸

Some other issues have arisen in the context of the harmonisation process. There are currently thirteen projects outstanding in the Australian Boards' Harmonisation Project; exposure drafts have been issued for nine of these. The extent of the differences in the remaining projects varies. There are as yet, for example, no Australian equivalent standards on *Provisions and Contingencies* or *Investment Properties*. Following harmonisation, significant differences are likely to exist in a number of standards, for example in the context of revaluations of non-current assets, accounting for internal reconstructions, and standards dealing with business combinations that, under the International Standards, qualify as unitings of interests.

Delivering our audit services

The ANAO's strategic planning framework is integral to our ability to deliver our services and meet our clients' needs in the most efficient, effective and ethical manner possible. We are guided in this regard by the ANAO Corporate Plan 1998-2001 which outlines the broad key result areas against which my office measures its performance. Linked to the Corporate Plan, is the ANAO's integrated Business Plan which details the approach for delivering the components of our Corporate Plan. As well, the ANAO is currently developing a series of Product Plans to focus on individual outputs. A number of other plans, such as the Workplace Diversity Plan, complement our core planning framework.

A vital key to our success is how effectively we manage and develop our people. An ongoing challenge for the ANAO has been in the area of recruitment, particularly the ability to attract and retain assurance audit staff. This has been due mainly to the changing nature of the Australian Public Service (APS), the implementation of accrual budgeting, the consequently high demand for financial skills and the fact that ANAO staff are well regarded both across the APS and in the private sector. We know we are increasingly subject to pressures of the marketplace and well appreciate that:

'The object is not to prevent water from flowing out but to control its direction and its speed'.³⁹

Unfortunately, we have limited capacity to tailor our audits to the retention requirements for various staff and to the level of demand for them in the marketplace. That limited capacity also applies to salary packages which extends to the 'futility of golden handcuffs'.⁴⁰ Nevertheless, we still offer a wide range of interesting, demanding and professionally satisfying audit experience and the opportunity to make a difference in nationally important issues and programs. That not only contributes to personal development but also provides a very satisfying and fulfilling work environment.

The ANAO has also maintained a strong internal focus on contestability, including outsourcing activities where the private sector can provide better value for money. For example, over a third of our financial statement audit budget is used for audits contracted to the private sector, with the ANAO maintaining a project management and oversight role. As well, we contract-in relevant expertise to assist in the audit process, particularly where the area involved is of a highly technical or specialist nature.

The ANAO's information technology (IT) services were contracted-out in July 1997 following a comprehensive market testing exercise. In 1998, the ANAO engaged a contractor to provide typesetting, editing and printing services for all ANAO reports and publications. In future, opportunities will continue to be identified for the contracting-out of services where it is cost-effective to do so and where it is consistent with the ANAO's strategic direction set out in its corporate and business plans. At the same time, we will continue to examine issues of organisational critical mass, retention of corporate knowledge and skills and the ability to maintain control and credibility in relation to our core business.

The ANAO fully costs most of its products through the application of charge out rates which aim to recover, either actually or notionally, all relevant costs including the attribution of overhead costs with an exception related to our national role. Our resource management practices aim to ensure that the costs of our products are comparable to those of other relevant audit bodies while recognising our limited authority to conduct any work outside our audit coverage. While this is a disadvantage compared to the flexibility available to private sector accounting and auditing firms, there is a real issue of the impact of such work on our independence. Moreover, a similar concern is increasingly being raised in relation to audits and consulting engagements in the private sector.

Our capacity to ensure that our products and services are contestable is underpinned by a performance monitoring framework and a commitment to the processes of benchmarking, quality assurance, peer review and continuous improvement. We assess the quality and impact of our services through a range of qualitative and quantitative mechanisms, including surveys of Parliamentarians and our audit clients. But the question is whether this is sufficient in a changing environment.

The potential for benchmarking

The delivery of relevant, timely, credible and professionally rendered audit services relies on having in place a management framework which is flexible, intelligent, responsive, effective and efficient. This involves a process of continuous analysis and construction. Moreover, it is a process which demands a capacity to apply the same level of scrutiny to ourselves as we apply to the organisations we audit. We need to be able to demonstrate that we are managing ourselves well.

I consider there is considerable potential for public sector auditors to benchmark their performance in relation to the management of inputs and the quality of outputs. Benchmarking – and the identification of better practices as a result – could occur, for example, in relation to financial management; human resource management (including industrial relations practices and professional development); the utilisation (and harmonisation) of technology; and productive processes (including the application of relevant audit tools, the use of external consultants and relative costs of production).

The ANAO has been committed to benchmarking its operations for a number of years. Internal reviews and external benchmarking activities with relevant national and international counterparts are used to refine processes, contain costs and strive towards better practice. For example, a consultant was engaged to examine the processes of planning and scoping of performance audits and report quality indicators. In addition, an external evaluation was undertaken of the ANAO's competitive tendering and contract management practices in relation to outsourced financial statement work.

Our Assurance Audit area is currently involved in two benchmarking reviews of financial statement audits: one with a major private sector accounting firm and one with the Office of the Auditor-General of Western Australia. The ANAO also participated in the Australasian Council of Auditors-General benchmarking exercise of Australian audit office activities in December 1998. We are considering opportunities to develop a strategic benchmarking partnership of our performance audits with another comparable overseas audit office and a peer review exercise with the Office of the Auditor-General of New Zealand.

There has also been a number of significant developments in the business management area which support the effective delivery of services, such as the following:

- ongoing implementation of major elements of our management information system (MIS) occurred this year, including our finance system (Finance 1) time-recording and payroll; and

- refinement of the ANAO's corporate governance framework, following the implementation of the recommendations of an external review of the ANAO's governance arrangements.

Case studies in adaptive change

To illustrate how the ANAO has sought to adapt to a changing environment, it may be instructive to examine how we have sought to demonstrate our contribution and relevance by adapting our audit practices and tools to issues of inter-agency benchmarking and performance audits of privatisation.

Benchmarking is a widely adopted approach for bringing about business performance improvements. The existence of benchmarking databases enables ready and cost effective access to data from many organisations. Performance metrics provide interested parties with the ability to focus relatively quickly on the areas needing improvement.

Privatisation has been a significant feature of the public sector reform agenda in Australia at all levels of government. Privatisation is a significant issue in creating a more competitive environment, and one which excites the interest of both Parliamentarians and the general public. Privatisation, in all its various dimensions, also has implications for almost all aspects of our audit practice. A number of those implications were canvassed in a paper I presented to the International Organisation of Supreme Audit Institutions (INTOSAI) Working Group on the Audit of Privatisation late last year.⁴¹ Specific privatisation issues relating to both financial statement and performance audits are discussed later in this paper.

The major role of the ANAO is to promote excellence in administration and accountability in the Australian public sector. Our Business Assurance Services Group (BASG) has started to develop a benchmarking service capability. Our first benchmarking study, the study of Internal Audit in the Commonwealth, was undertaken using the Global Auditing Information Network (GAIN) data collection instrument and database developed by the American Institute of Internal Auditors. The study is to be completed over three years. In 1998, the ANAO commenced its second benchmarking study, that is, benchmarking of the finance function. This project, which is in its pilot phase, involves collecting data (mainly quantitative) on the finance function and comparing the results with those in the private sector and with other Commonwealth agencies. Our intention is to extend benchmarking services to other areas of public administration.

Benchmarking of the Finance Function Project

The ANAO is undertaking the above-mentioned pilot benchmarking study of finance function operations in a number of Commonwealth Government agencies in conjunction with an external provider of benchmarking

instruments and relevant data. If the results justify it, the pilot will be extended into a full benchmarking study.

Recent Government reforms aim to improve financial practices in Commonwealth agencies by making them comparable in terms of time, cost and quality with best practice in the private sector. Agencies are encouraged to identify, measure, and compare their performance with other organisations, private and/or public. Benchmarking is one of the means to accomplish this.

The choice of the finance function was influenced by several reasons. The finance function is of particular interest to organisations as it plays an important role in supporting organisational transition to the new operating environment with accrual accounting and market contestability principles in operation. There is evidence that the role of the finance function in private organisations has changed from maintaining the figures to business decision support. Research from the private sector also indicates that finance is a relatively expensive function in organisations with significant scope for performance improvement. Therefore, benchmarking the finance function in APS agencies offers an opportunity to learn from other Australian Federal and State Government agencies and from private sector practices.

- The objective and scope of the study

The objective of the project is to obtain, over time, qualitative and quantitative benchmarks for the finance function as it operates in Australian Federal Government agencies and entities. There are several models of the finance function which were used by others to conduct benchmarking studies in the private sector, but none was created specifically for the purpose of the public sector. The ANAO had to research and construct a model to reflect the APS context. The scope of the study was restricted primarily to the transaction processing element of the finance function as research indicated that most benefits are obtained from comparing data related to this part of the finance function. As well, data should be more readily available. The coverage encompassed aspects of : payroll, travel and entertainment, accounts payable, billing, accounts receivable, closing the books/financial reporting, budgeting, fixed asset accounting and taxation.

These activities are performed by all organisations (albeit to different degrees) and, consequently, direct comparisons would be possible. Benchmarking of the finance function was conducted across the three elements of time, cost and quality.

Recognising the conceptual and logistic difficulties in conducting benchmarking studies, the ANAO decided to conduct the complete pilot phase of the project using a commercial database and questionnaire. The main objectives of the pilot phase were to:

- judge the level of interest for the study amongst Commonwealth agencies;
- test the relevance of the purchased data collection instrument to the APS context;
- test the finance function model (including the extent to which specific activities are performed in the APS);
- develop a methodology for data collection, including critical checks on data validity; and
- test and, if necessary, modify the content and/or presentation of the benchmarking report.

The ANAO tested the market for benchmarking databases and collection instruments in Australia, New Zealand, the United States of America and the United Kingdom. Australian Federal Government agencies were approached directly and invited to participate in the pilot phase of the benchmarking study. Participation was made voluntary in this phase. The positive response rate was approximately 60 per cent with support for the project growing with the project's progress. Those who refrained from participation indicated that either they knew they had problems with the operations of the finance function in their organisation (and did not want a report on it) or they did not have the necessary resources to complete a questionnaire. Nine organisations participated in the pilot phase. The sample was constructed so as to highlight any possible difficulties in the study.

- The project's outputs and benefits

Recognising the different needs of our two primary clients; Parliament and the agencies, the ANAO intends to produce two types of report. As a participant in the benchmarking study, an agency will receive a customised benchmarking report. The report will compare the agency's performance against that of other Commonwealth agencies as well as that of the private sector. The results of this report will be distributed only to the agency concerned.

The ANAO will also produce for Parliament a "global" benchmarking report. This report will include common findings across all the benchmarked agencies. The findings will not be attributed to any organisation except where best practice is identified. The purpose of identifying agencies with best practice is to facilitate sharing of the knowledge with the broader APS community. This report will contain an overview of observed best practices from both the public and private sectors.

The agencies participating in the study indicated to the ANAO that they perceived a number of benefits from the exercise. Some intended to use the results to measure/assess the performance of their finance function. They

were either unsure about how to conduct the process or the cost of gaining access to external data was considered to be too high. Some were undertaking process re-engineering of their finance function and wanted a quantifiable measure of their improvement. Others were convinced that their financial practices were very good and wanted some independent measure of their success. The ANAO was in position to provide the necessary independent viewpoint.

Agencies were obviously favourably disposed as there was no direct cost for them in participating and obtaining reports. Nevertheless, it was recognised that the approach taken by the ANAO of forming a strategic alliance with an external provider was a very cost-effective way of obtaining external data. The ability of the ANAO to produce two types of comparison (with the private sector and separately within the Commonwealth) was seen as adding value to the reports. One agency was so convinced that its financial practices were of a high standard that it specifically requested comparison with the private sector and not necessarily with other Commonwealth agencies.

- Benefits to the ANAO

The quantitative benchmarks obtained during the study will form the basis of an Australian Government database designed and maintained by our Business Assurance Service Group. It is intended that the database and further benchmarking studies will be used strategically to identify areas of concern, which may be subject to further Financial Control and Administration audits, and/or which may warrant a separate Better Practice Guide. Financial statement auditors may also use the database when planning an audit as the information contained in it provides indications of error and significance rates. The database also provides an indication of performance against other similar agencies. The qualitative data may be used for future Better Practice Guides. However, the decision to continue the current study past its pilot phase has not yet been made, pending the pilot phase evaluation.

Within our own office, the Business Assurance Services group has been able to provide information on relevant benchmarks and better practices to a number of financial and performance auditors for other audit activity with beneficial results. This initiative has strengthened the commitment to the development of an integrated database for general use across the Office.

- Agency support for the project

The support for the project amongst Commonwealth agencies grew as the project progressed. One participant decided to benchmark all 25 divisions of the agency (instead of the originally planned single division). Another, which was not originally included, specifically requested to be part of the study. Several participants also indicated that they were interested in forming a

benchmarking forum, facilitated by the ANAO, to share experiences in approaches taken to financial management. Many agencies informed us that they would endeavour to keep a record of the information necessary for the project in anticipation of their future participation in any benchmarking of the finance function study.

In summary, the project has the potential to provide substantial improvement in the financial practices of Commonwealth agencies and to facilitate sharing of identified best practices among them. It also has the potential to provide a more strategic focus for future auditing services provided by the ANAO which would greatly assist in our future business planning. As such, it will also provide a more robust basis for providing assurance to the Parliament and its Committees on a fundamental area of their concern to ensure proper accounting, and accountability, for public resources.

Privatisation and financial statement auditing

Privatisation, whether by trade sale or public share offer, has always impacted on the financial statement business of Auditors-General through our participation, for example, in the activities associated with the due diligence program, which ensures the accuracy and completeness of information provided to prospective purchasers. Information disclosed to potential purchasers typically includes financial performance data for a five year period and the most recent audited financial statements, which also emphasises the importance of comprehensive and sound financial statement auditing practices.

The underlying objective of a financial statement audit is generally understood to be to express an opinion on the fairness of the information reported in the financial statements. However, for the public sector auditor, the financial statement audit typically extends beyond the minimum work necessary to substantiate financial statement disclosure. If the Auditor-General is to truly add value and provide appropriate assurance, it is important that the public sector financial statement audit recognise and report matters which, although not directly related to the financial statements or supporting systems, impact on the efficient, effective and ethical use of public resources. Not the least of such concerns is fraud but Parliamentary Members have also shown interest in failures to adhere to guidelines for purchasing and use of government credit cards.

In the longer term, privatisation also impacts directly on the public sector audit practice because it often reduces the nature and extent of the Auditor-General's mandate. In my case, the *Auditor-General Act 1997* and *Commonwealth Authorities and Companies Act 1997* provide that my financial statement audit mandate includes wholly-owned Australian federal government companies or companies in which the government has a controlling interest. As a result, the full sale, or sale of a controlling interest, in

a Government Business Enterprise (GBE) will invariably reduce the number and nature of those entities subject to a financial statement audit by my Office. The problem that creates for many Auditors-General is a diminution of opportunities to maintain particular knowledge, understanding and even skills of audit staff which can impact adversely on both their retention and recruitment, as I noted earlier. A particular challenge is created where there are only one or two entities involved in the area, for example, telecommunications, but any loss of a sizeable GBE, such as the Commonwealth Bank and QANTAS Airways, can have an adverse impact on skills maintenance which can be more pervasive in its implications not only for other audits but also for the effectiveness of the Office.

Privatisation and performance (or value for money) auditing

Asset sales invariably represent a significant and financially material government activity. The United Kingdom Treasury has noted that a range of legislative, commercial and propriety issues arise when a public sector business or service is privatised.⁴² From our perspective, it is worth noting that Auditors-General have wider responsibilities in these areas than the traditional private sector auditor. Our New Zealand colleagues have previously observed that, in order to provide assurance to the Parliament, and the community, that the privatisation process has been successful, post sale audit activities need to consider:

- *satisfying public information requirements about the sale. For example information about the nature of the tendering process or the terms of sale may not always be known to the public. In these circumstances the reporting of such information by the Supreme Audit Institution (SAI) goes some way toward meeting that need for information by the general public;*
- *ascertaining and reporting whether the maximum value for money was achieved on sale;*
- *ascertaining and reporting whether the sale achieved the objectives set preceding the sale. For example, some governments offer the sale of commercial activities carried out in the public sector as a way of redeeming public debt or improving the efficiency of delivery of social services such as public health. The SAI might consider whether it is appropriate to provide public comment on whether that objective has been met; and*
- *assessing whether any regulatory requirements accompanying the sale have been met on an ongoing basis.⁴³*

The assurance provided by such audit activities plays an important role in enhancing accountability for the stewardship of the sale process and confirming whether post-sale performance is meeting the objectives set by government.

Australia has an ongoing program of asset sales at the federal level of government. My Office has undertaken a program of performance audits to examine the extent to which government sale objectives have been achieved: the effectiveness of the management of the sale; and the ongoing risk exposure. To ensure their effectiveness, my privatisation audits (such as the audits of the Telstra (our major public sector communications supplier) share offer⁴⁴, the leasehold sales of Federal airports⁴⁵, and third tranche sale of the Commonwealth Bank⁴⁶) are undertaken by a team of experienced officers who understand the commercial nature of the transactions and the overlaying public accountability issues. In addition, we engage appropriately qualified professionals to provide specific technical, including commercial, advice.

A key issue in these performance audits has been the role of financial, legal and other private sector advisers to the sale process. In Australia, the privatisation process itself is now subject to extensive outsourcing, often under multi-million dollar advisory contracts. This places considerable emphasis on contract management and balancing commercial interests with the overlaying public accountability required of the public service. One of the key outcomes from our privatisation audits has been the identification of opportunities for significant improvement to the process of tendering and managing these advisory contracts, the adoption of which have led to improved overall value for money and project management quality in subsequent sales. In short, the emphasis is on identifying better practice to add value to public administration as a major audit objective.

Asset sales in Australia are invariably conducted by way of public share offers or trade sales. Although there are similarities in some of the administrative processes associated with the management of public share offers and trade sales, there are also stark differences which need to be considered when planning and undertaking audits of such sales. Because of the time pressures, commerciality of these sales and public interest issues, ANAO audits have all been ex-post. Opportunities were available to undertake probity audits of the sales processes but there were potential conflicts of interest as well as resourcing issues which inhibited our participation.

By virtue of their scale, sensitivity and complexity, audits of public share offers are quite challenging undertakings. Furthermore, the scale of such offers particularly emphasises the importance of sound administrative practices because small deficiencies can have significant adverse financial implications. As mentioned, my Office has examined the two largest public share offers conducted in Australia, namely the sale of one-third of the shares in Telstra Corporation and the third tranche sale of shares in the Commonwealth Bank which raised proceeds of A\$5.15 billion and A\$14.24 billion respectively. These reports have examined the key factors that affect the success of any public share offer, such as:

- the level and structure of fees paid to stockbrokers and advisers as these fees significantly influence the motivation for these firms to act in the vendor's interest. While fees need to be high enough to motivate them to sell shares, it is important that the entity oversighting the sale should take advantage of the competitive broking market by considering the level of fees sought by individual brokers when deciding on the composition of the selling syndicate for the offer. It is equally important that the division of fees and commissions between the fixed component shared among the selling syndicate and the 'competitive' component paid according to which broker secured the order for shares provides an incentive for all brokers to actively market and sell shares,⁴⁷ and that fees and commissions only be paid for services provided. For example, underwriting fees should only be paid on shares that are actually underwritten;
- the 'price discovery' process which is important to achieving value for money in initial public offers. In Australia, the final offer price is established by a 'bookbuilding process' whereby investors submit bids in advance of the pricing of the share offer and, on the basis of this information, shares are allocated to qualifying bidders. In secondary offers, a market price already exists for the shares being sold and this makes the process of establishing the issue price less complex. However, in an initial public offer, the bookbuild performs a more important price discovery role and it is important that the bookbuild allocation criteria, and any indicative price ranges specified by the vendor, encourage and reward bidders who indicate their price elasticity of demand for shares; and
- the logistics of the settlement process are important if the vendor is to receive the full proceeds from the share sale in a timely manner. This requires comprehensive settlement procedures to be developed and advised to successful bidders, ongoing monitoring and reconciliation of relevant bank accounts, and the implementation of effective settlement default procedures.

The accountability aspects of such elements of the sales process are outside the experience of most public servants and are not well understood by private sector participants. There is an ongoing learning process for all concerned, not least by the auditors concerned. [In relation to the latter, the document produced by the INTOSAI Privatisation Working Group in 1998 entitled 'Guidance on Best Practice for the Audit of Privatisations'](#)⁴⁸ will be of considerable ongoing assistance to audit offices.

It has been pleasing to observe that these trade sale audits have had a real impact on the way sales are being conducted. For example, Federal airports in Australia have been sold in two tranches and each tranche has been audited. An aspect of my Office's approach to auditing the second tranche sale was to

examine action taken in response to recommendations made in the audit report on the first tranche sale. We found that all eleven recommendations in our 1998 report were implemented by agencies, even though not all had been fully agreed to by the agency responsible for Federal asset sales. The improved processes resulting from implementation of these recommendations supported an effective overall outcome for the Phase 2 sales. This outcome was also due to the greater understanding of the accountability requirements by private sector contractors who not only addressed audit comments but also initiated related discussions with the auditors concerned.

I also note the positive response to the ANAO's report on the audit of the 1997 sale of one-third of Telstra. In seeking passage of the sale legislation for the sale of a further 16.6 per cent of Telstra, the Government announced that the issues raised in the report on the one-third sale would be taken into account. (join paragraphs) Of note, is that the related prospectus indicated that fees to be paid to advisers and brokers could be significantly below those paid in the first sale, as was recommended by the audit. We also understand that the audit has led to process improvements and the recovery of funds in relation to contractual payments earlier questioned by the ANAO. This latter point illustrates the important 'compliance' or 'control assurance' role that performance audit can play, and this is something we are giving increasing emphasis in all our performance audit activities.

Implications for Public Audit Institutions

The lessons learned in this section are that Public Audit Institutions, in order to remain relevant and viable, have to ensure that they:

- have *tested* and *proven* management frameworks which are capable of sustaining and reinforcing a high level of performance in an often volatile environment. We are working in a *knowledge* industry in which our effectiveness and relevance is a direct function of our capacity to foster organisational and individual learning and professional development (in its broadest possible sense). Although creativity is not a quality which the person on the street might naturally associate with the label 'auditor', it is essential that we foster creativity, encourage continuous learning and promote the adoption of new technologies where appropriate. We should be testing concepts, tools and practices in advance of their broader application instead of playing 'catch up';
- are positioned at the *leading edge* of developments in private and public sector administration, management and business processes. While audit is almost always retrospective, or *ex post*, in nature, it is nevertheless essential that we remain forward looking. As a knowledge-based organisation, we are well positioned to forge mutually beneficial strategic relationships with professional bodies, academic institutions and research organisations – not just in the traditional areas of accounting and audit – but also in the social science disciplines, commerce and law from which emanates much of the academic literature about current trends. We need to position ourselves as opinion leaders on issues of probity, governance and accountability. If we expect public sector organisations to act on our recommendations, we need to ensure that the Audit Office '*brand*' is recognised as having value. One way to confer value on our products is to be recognised as being knowledgeable, informed, current and credible; and
- know their *market*. By this I mean that Public Audit Institutions need to be capable of delivering the audit products their various stakeholders want for their perceived purposes (while of course maintaining audit independence and adherence to their statutory responsibilities). My audits of privatisation are a case in point. Similarly, government contracting is an area where there is a growing demand for audit activity. Outside of the academic literature, our reports are possibly the only publicly available source of independent, appropriately evidenced and '*non-journalistic*' information about the conduct of privatisation and/or contracting initiatives. This gives us a significant market advantage for this type of product, which is no cause for any complacency. A clear imperative is to ensure that our reports and products are accessible and useful as well as well targeted and appropriately marketed.

Of course, audit reports are not the only vehicle for delivering our product (the activities largely being audit analysis and opinion). We are in the business of guiding, as well as changing, administrative behaviour. Therefore we need to understand and determine how behavioural change can best be brought about. There is strong anecdotal evidence that our most notable and valued contributions have resulted from the adoption of recommendations about better practices. As well, there are clear indications that the audit process itself acts as the catalyst for improved performance not just the report prepared (recognising, of course, that without the prospect of a public report, there may be less discipline, pressure and/or incentive for behavioural change).

It seems reasonable to conclude that there is a variety of ways in which the audit function can have a demonstrable impact on public sector management practices. Public Audit Institutions increasingly have an educative function, although it may not be articulated as such in our legislation or mission statements. At the end of the day, although the publication of audit reports provides a measure of productivity and performance, the outcome we aim to achieve – our core business if you will – is *not* simply the production of reports.

Our core business is achieving *behavioural change* consistent with the tenets of effective, efficient, ethical and accountable management reflecting the ready adoption of accepted better practice. This can be achieved through a range of means, including regular meetings and other associations with public sector management and private sector providers, shared partnerships and other involvement with professional bodies and major accounting/auditing firms, audit reports, better practice guides, involvement in training, conducting workshops and/or participation in relevant conferences. Success will come, as Mr Le Marechal (quoted earlier) indicated to me, if we can attract a sizeable core of truly excellent people. This will occur if we are seen to be excellent organisations providing high quality services to government and the Parliament, representing citizens.⁴⁹

ENSURING EFFECTIVE AUDIT PERFORMANCE

In the preceding section of this paper, I concluded with the observation that Public Audit Institutions are knowledge-based organisations often concerned with the promotion of behavioural change. We are in the position of helping to shape expectations, assessing performance against such expectations and promoting behaviours and practices which are consistent with those expectations. Our outputs, therefore, have normative features (insofar as we are involved in the business of standard setting); are educative (in that we are concerned to market and promote the adoption of better practices); and are

evaluative (because we are concerned with the effective implementation of better practices).

These considerations suggest that the performance of Public Audit Institutions (in terms of the achievement of identified outcomes) has to be tested on several levels. First, we need to be able to demonstrate that the administrative and business practices we are advocating are soundly based and founded on sound and reliable research. This is particularly important in view of the potential for reputational risk. Our credibility with our stakeholders (Parliamentarians and Legislators, auditees and the community) depends on our being seen to have relevant expertise. Second, we need to be able to demonstrate that we have *made a difference*. If we accept that we can make a significant impact on behavioural change (which is essentially an educative function), we need to be prepared to show that *positive* behaviour change has occurred as a direct consequence of the way in which we exercised our audit function. Third, we need to be prepared to be tested in relation to the quality, robustness, relevance and professionalism of our analysis, including the professional conduct of auditors, the application of relevant knowledge, an understanding of the public sector environment and the appropriateness of audit tools.

Using information technology for strategic advantage

There has been a continuing and dynamic growth in the use of information technology and telecommunications to assist in public program delivery. For example, the use of Internet facilities has increased considerably across the APS. This brings into sharp focus a range of access, security, privacy, storage and retrieval issues relating to the data held by the public sector. We are also witnessing the greater use of decision support systems which should ensure greater consistency and equity of treatment as well as allowing greater individual attention to be given to more complex cases. Such systems require sound quality assurance review mechanisms to promote confidence and credibility of stakeholders, including clients.

The ANAO's Business Plan for the next three years identifies the following major challenges for each of the key result areas in our Corporate Plan:

- as a specialist public sector audit practice, we must add value above that potentially available from other providers;
- there will be an ongoing emphasis on enhancing our current services and investing in new audit methodology, product development and differentiation;
- providing a work environment that encourages strong personal commitment, performance and innovation; and

- strengthening a business culture which includes a strong focus on the skills, abilities and commitment of staff and on quality products and services relevant to contemporary public administration.

Information technology (IT) in its broadest sense is having a fundamental impact on the business of government. It is therefore essential that Public Audit Institutions recognise this fact and respond accordingly. IT is a means to an end and can greatly facilitate the usefulness of information in all its various forms. The quality and usefulness of information are pre-conditions of good decision-making. The information available to any organisation has to be recognised as one of its major assets. The proper management of this resource can provide the organisation with a significant strategic advantage not least when it is in the service business which covers the majority of government activities.

Public sector auditors need to keep abreast of the availability of IT tools which include survey software, database packages for data analysis, and data interrogation systems, in order to continuously improve the quality and efficiency of their audits. They also need to explore ways in which they can contribute to the development of new IT systems, as well as identifying cost-effective ways of reviewing IT systems on an ongoing basis. Public Audit Institutions need to consider having in place an Information Technology Strategy addressing requirements for state of the art hardware and integrated audit technology software products that will best meet public sector auditing requirements and responsibilities. As the ANAO has found in respect of its financial statement audits, the solutions offered by the private sector may often be appropriate for the purpose. As well, there is the excellent work being performed by the INTOSAI EDP Audit Standards Committee including wide-ranging workshops and production of courseware materials.

The main challenges facing both internal and external auditors in relation to information technology include developing methodologies and computerised tools to keep pace with changes occurring in data management and communication; and maximising the benefits of IT to improve audit quality and increase productivity. As with all managers, we need to have the necessary expertise and understanding of our business to develop appropriate IT strategies and oversight their implementation.

The impact of technology on accountability and risk management

The use of IT is having considerable impact on agency accountability and risk management, both positively and negatively. We recognise that there are risks inherent in the management of IT systems themselves, particularly relating to the security of agency data in a contestable or outsourced service delivery environment where we do not have direct access and control.

The past decade has seen a radical transformation take place in the role of IT within organisations worldwide, not to mention the impact it has had on individuals' lives. I know that my staff derive enormous benefit from the information about management and audit practice in Australia and elsewhere which they increasingly obtain from the Internet. However, the increased ability to capture and store information has a downside. Put plainly, organisations and individuals are significantly challenged in their capacity to effectively access, interpret, manage, apply and disseminate the volume, diversity and often uncertain origin of information enabled by IT (and the Internet in particular).

An example of the use of IT systems as 'enabling technology' that provides quality information to assist in decision-making can be seen in the growing use of rulebase decision systems (or expert systems) to administer complex legislative and policy material. While the widespread adoption of rulebase systems to support administrative decision-making has been foreshadowed for some years, the relatively recent adoption of such systems by Australian federal Government agencies indicates that they will be increasingly used to support, control and improve administrative decision-making based on legislative and/or policy rules.

A recent paper on this topic, presented to the Institute of Public Administration Australia⁵⁰, identifies the opportunities and risks associated with the use of 'rulebased' systems. There is a need to balance both in order to make the most effective use of this technology. Opportunities include improvements in the quality, accuracy and consistency of decisions and administrative processes, and hence improved client service. Such opportunities may be realised as a result of managing, reducing and removing different risks from aspects of the decision-making process by providing staff with access to information relevant to their decisions. The risks involved relate to the complex IT development processes needed as well as the lead times involved in system development, the potential for a loss of staff skills and knowledge of policy over time and an over-reliance on IT systems to produce the right answer every time.

Importantly, the authors assert that such systems cannot be introduced in isolation and should be accompanied by a broader redesign of the decision-making process and environment, including changes to service delivery arrangements, work structures and practices, staff skill sets and quality control practices. This type of technology does not replace the need for judgement or skills on the part of staff. However, it does provide a new model for decision-making based on a risk management perspective.

The greater level of access to data has also brought with it security issues, such as unauthorised access and entry of virus infected programs, which have raised the risks to agencies' computing environments and which are being addressed through so-called 'firewalls' (which are basically software

protection) or through physical separation. Data encryption systems have been, and continue to be, developed to provide a degree of assurance to managers and users. Initiatives have been taken to implement some kind of public key encryption arrangement for general protection and assurance.

The move to electronic commerce and the greater use of the Internet for business purposes, will also put increasing pressure on management of our information systems and systems controls. My office has recently undertaken an audit of the use of electronic commerce or business in Australian federal government agencies⁵¹. The audit was conducted largely through a survey of agencies on their use of technologies such as the Internet to conduct business and their expectations of what will be their position in 2001.

Delivery of Government services on the Internet has the potential to:

- give access to a wide range of government services to a large group of the population, including those in remote areas of Australia;
- give access to government services and information 24 hours a day and seven days a week;
- allow the public to navigate to the government information source without the need for prior knowledge of where to look; and
- be a relatively inexpensive form of service delivery compared with other arrangements such as face to face and call centre interaction.

Commensurate with the potential for improved service and reduction in costs is the increased risk in the following areas:

- the security of information transferred over the Internet;
- the privacy of information on individual or business; and
- the ability to authenticate the user requesting government services or financial assistance.

Recent ANAO financial statement audits have identified several emerging issues regarding the security and internal control mechanisms of IT systems in public sector agencies. IT supports various entity programs and can be integral to the validity, completeness and accuracy of financial statements. Consequently, the audit of IT systems and processes is fundamental to forming an opinion on the adequacy of proper accounts and records that support entities' financial statements. The 1997-98 financial statements identified several IT control issues, including:

- system access rights found to be excessive or unauthorised;
- inadequate review and approval of users' access to systems;

- an external service provider having unlimited access which was not monitored; and
- inadequate review, approval and testing of changes to applications.⁵²

Similar issues were identified for the 1998-99 statements.⁵³

The need to focus on effective systems controls is further highlighted by a recent report of the Australian Institute of Criminology which indicates that the increased usage of information technology will lead to a major rise in white collar crime against governments.⁵⁴ Allied to this concern are warnings about growth in the use of E-Mail not just in terms of adequate systems controls to prevent compromising network performance and the efficient conduct of functions or business but also the possibility of litigation where communications are not subject to executive review but could involve liability for the organisation.⁵⁵

With the increased involvement of the private sector in the provision of public services, the security of agency data is a critical issue. Contracts negotiated between public service agencies and their private sector providers must include provisions which acknowledge Australian federal government IT security requirements. In addition to the technical issues associated with the protection of the data held by government agencies from unauthorised access or improper use, there are also issues associated with the security of, for example, personal information held by government agencies which falls within the scope of the Privacy Act. A watchful citizenry will want to be certain that agencies and their contractors cannot evade their obligations under such legislation.

The ANAO is seeking to bring the issue of IT controls and security to the attention of all public sector agencies and our first step in this process was the production of a better practice guide (released in October 1998) in relation to security and control for the SAP R/3 system.⁵⁶ SAP R/3 is the most widely-used financial management information system in the APS today with over thirty Australian federal government entities currently using it. The areas covered by the guide include the amount of time and investment necessary for effective implementation of the system to minimise the risk of future security problems. While the guide deals specifically with SAP R/3, generic risk management controls are discussed which can be applied to other financial management information systems.

Internet use and implications for audit

Use of the Internet has grown enormously in recent years. Several Australian Federal Government agencies, that currently use private or proprietary government networks for electronic service delivery, are considering using the Internet as an alternative. Government service delivery through the Internet presents both significant opportunities and challenges in the delivery

of on-line services. Depending on the level of sophistication of the application, the Internet allows government agencies to publish information, interact with clients in the exchange of information, and/or transact business electronically. For most agencies, the Internet has the potential to:

- improve public access to a wide range of government services, especially by people who live in regional and remote areas;
- provide access to certain government services 24 hours a day, seven days a week;
- reduce the cost of delivery of some government services; and
- improve the quality of certain government services.

In 1997, the Australian Government outlined new measures designed to enhance prospects of growth and strengthen Australian industries' capacity by, among other things, helping to ensure that business, the community and all tiers of government maximised opportunities to add to and benefit from the global information age. These measures included a plan to establish the Australian Federal Government as a leading-edge user of technology, including establishing a Government Information Centre and committing to all appropriate services being Internet-deliverable by 2001. Internet services were to complement - not replace - existing written, telephone, fax and counter services, and to greatly improve the quality, user-friendliness and consistency of those services.

Ideally, agency planning for Internet use should include planning for monitoring, review and performance evaluation of agency outputs and outcomes. Effective planning would enable agencies to begin to monitor the effectiveness and efficiency of such use from the outset. Agencies' review of reliance on the Internet for program delivery is also warranted because Internet service delivery is not necessarily of higher quality than alternatives, particularly at this stage of the Internet's development. The ANAO survey, referred to earlier, showed that agencies have adopted a wide range of measures involving use of the Internet. Promoting a set of common measures that agencies use to assess the success or otherwise of their efforts would facilitate further understanding of Internet service delivery from a whole-of-government perspective with benefits for all agencies.

In addition to examining the impact of Internet use on agency performance, it is essential that consideration be given to the implications of its use for privacy and audit. The agencies surveyed by the ANAO expected that information about their contracts with the private or community sectors would remain as commercial-in-confidence. Individuals' concerns were expressed about the broader concept of an individual's rights to influence the way personal information was collected and used. A key provision of the Privacy Amendment (Private Sector) Bill, expected to be introduced in the

first sitting of Parliament this year, is new 'National Privacy Principles for the Fair Handling of Personal Information'. These Principles set standards about how business should collect, secure, store, use and disclose personal information. The Bill makes a distinction between 'personal' and 'sensitive' information. The latter includes information on a person's religious and political beliefs and health where the private sector is more strictly limited in its collection and handling. This legislation could have a marked impact on that sector's involvement in the delivery of public services.⁵⁷

Where there is Internet service delivery, financial and other kinds of losses and damage can be suffered by agencies' clients through agencies publishing incorrect or misleading information on their Websites. This may be a result of ignorance, negligence, abuse or deliberate sabotage, and lead to legal liabilities for the agency. In other words, the delivery of services via the Internet introduces new risks and exposure that can result in a legal liability for government. Well-designed security and privacy policies can minimise risks and liabilities while informing agencies' clients of important aspects of the services they can expect to receive. The ANAO considers that, where they have not done so already, agencies should develop policies and operational strategies for the security of their Websites together with policies and strategies regarding information related to individuals or organisations available from the site.

Government agencies need to come to terms quickly with the potential applications of Public Key Infrastructure (PKI) technologies to encrypt, decrypt and verify data. In public key technologies, each user of the system has two keys, a public key and a private key which can be used to ensure the privacy, authentication, non-repudiation and integrity of information contained in messages. PKI is of importance to all agencies wishing to embark on initiatives that do more than just disseminate information. It is a core enabler. Key issues addressed by PKI are:

- each person communicating electronically needs to ensure that the recipient is who he or she thinks it is, so that one cannot later deny being the sender of a particular electronic message or transaction. This ability to rebut a party's denial of sending a message is called non-repudiation; and
- the ability to encrypt data transmissions over an open or public network (such as is used by the Internet), so that those transmissions can be read only by the intended recipient.

GATEKEEPER is the Commonwealth Government's strategy for implementing a government PKI.⁵⁸ An important element of on-line transactions with the Commonwealth is the ABN-DSC (Australian Business Number – Digital signature certificate) which will be used to verify electronic signatures.

There are many challenges for auditors inherent in the proliferation of electronic information and communication systems. Technological innovation has conditioned users to expect virtually instantaneous communications and – by extension – instantaneous decisions and results. While it clearly has provided benefits, technology has also presented new risks not only for an organisation's control environment but its also for its knowledge base and the skills composition of its workforce. Of specific interest to auditors has been the recent Auditing Guidance Statement (AGS 1050) on 'Audit Issues Relation to the Electronic Presentation of Financial Reports'.⁵⁹ The AGS identifies specific matters which may be addressed by the auditor with management to reduce the risk that the audit report on an entity's financial report is inappropriately associated with unaudited information on the entity's web site.⁶⁰

We have, at the moment, a three tiered communications hierarchy with hardcopy documentation (traditional paper file based records) still at the top in many, if not most agencies, followed by electronic or digitally based information (using virtual office systems or *groupware*, electronic diaries or data and e-mail archives) and verbal communications (which may or may not be supported by notes, diary entries, tape recordings or other evidentiary material). A focus on results requires a capacity to make decisions and act quickly but, hopefully, not at the expense of due consideration in a robust risk management environment (culture) and lacking accountability for those decisions and actions.

There appears to be an increasing tendency for policy and administrative decisions to be communicated and confirmed through E-mail communications. This is a function of our changing expectations about the speed of communications, a growing emphasis on timely management of the 'political' dimensions of policy, and the appropriation by the public sector of a 'commercial paradigm' in which 'deals are done' (which is given added impetus by the involvement of private sector 'partners' in various aspects of government operations). Nevertheless, as better practice private sector firms demonstrate, good record-keeping is an integral part of a sound control environment and subject to a regularly reviewed risk management strategy which is integral to their required outcomes.

The increasing use of E-mail poses significant challenges in terms of our traditional evidentiary standards (which traditionally hinge on paper-based records) and the skills base of our auditors. A separate, but just as important, issue is the inappropriate use of E-mail. We are already confronting situations in which traditional forms of documentary evidence are not available. Technological change has resulted in a degree of 'de-skilling' in traditional public sector audit practice but a commensurate 're-skilling' in decision-making systems. Auditors are already confronting situations in which they are having to make links in the chain of decision-making in organisations which no longer keep paper records, or having to discover

audit trails in electronic records, desk top office systems or archival data tapes.

The problem is that we do not have the range of skills necessary to do the job and we need a strategy to overcome this deficiency. Essentially, auditors now need to possess a level of forensic IT skills they have not traditionally had to have at the Federal level. To these forensic skills they also need to add evidentiary standards appropriate to these forms of information – in other words, how does the auditor establish whether communication has occurred and obtain assurance about the records they have found?

Perhaps we need to look to the example of our colleagues in the areas of prudential assurance or criminal investigations who are continually refining investigatory methodologies to keep pace with offences such as insider trading, corporate fraud or misuse of drugs. If we go down this path, we may have to consider whether there is need to harmonise more closely evidentiary standards for audit with those of the criminal or civil justice systems in our respective jurisdictions. For the moment it might be that the technology is evolving far more rapidly than governments can respond with legislative or statutory controls. This is of particular concern for the management of Commonwealth records by National Archives of Australia.

Finally, we will need to address the Pandora's Box represented by the boundary between the official and the personal communications. Electronic records – especially E-mail records – are likely to contain both official records and personal communications. Any position taken on personal communications on official systems should have regard to the organisation's internal communications policy as well as of any applicable legislative framework. In any event, it would seem prudent for an auditor to consult early with the organisation's management to determine an appropriate protocol for extracting required electronic records which not only protects the auditor's right to access such records but also provides protection against unnecessary infringement on personal records and personal privacy.

The Triple Bottom Line

Within the foreseeable future we can expect to see an emergence and consolidation of new modalities of accountability. One example is the so-called *Triple Bottom Line*. A recent article suggested that the current socio-legal construction of accountability in the business world – and I would include government operations in this category – is on the threshold of a major paradigm shift⁶¹. Public and other stakeholder expectations in an increasingly globalised business and communications environment will, according to the article's author and other proponents of the Triple Bottom Line (TBL), provide the drivers for a shift away from traditional *input-output* based model of accountability towards a focus on *economic prosperity, environmental quality and social justice*.⁶²

TBL goes beyond the current orthodox focus on financial performance (in the narrow sense of profit and loss), the utilisation of inputs and the disposition of outputs, and probity (expressed as conformance with applicable law and the minimisation of liability) to also take into account the environmental and social consequences of business activity. In part, this view is supported by the passage of various 'right-to-know' legislation. As well, new corporate governance rules are challenging the traditional non-disclosure or low-disclosure policies of companies and is consequently giving rise to new expectations and standards of transparency. One could speculate about the effects of the greater spread of shareholding generally and the impact of large size Management and Superannuation Funds, particularly when their holdings are sufficient to gain a seat or seats on Corporate Boards.

TBL reporting could lead to changes to the manner in which public and private sector organisations report performance and discharge their accountability to their stakeholders. The concept of sustainability requires new definitions of performance and the re-articulation of organisational goals. In the private sector, this would involve some balancing of environmental and social considerations against profitability. The bottom line for the public sector is often diffuse with a range of sometimes apparently conflicting objectives and, consequently, balances have to be struck at points in time and over time. An important aspect for both sectors is management of reputation, which is an all-pervasive issue for performance assessment. It is essential for a sustainable future particularly where the general community is placing some value on corporations' meeting broader 'social' goals.

The public sector may be inherently better positioned for the application of TBL given the focus on *outcomes* as a primary measure of performance in the absence of any profit concept to assess results. Even publicly owned commercial operations may be amenable to TBL given the prevalence of community service obligations in their charters. Much of the Australian public sector (Federal, State and local) requires agencies and their suppliers to demonstrate conformity to industrial, affirmative action, privacy and environmental legislation and associated other socially oriented practices in their Annual Reports.

The extent of conformity to these expectations is a logical line of investigation and report by audit as part of any review of performance. While Supreme Audit Institutions in a number of countries have developed specific environmental audits and related audit approaches and techniques, such as New Zealand, Canada and the Netherlands, the ANAO has tended to address such issues in its performance audit reports. Nevertheless, the guidance material provided by the INTOSAI Working Group on Environmental Auditing is proving to be of considerable benefit to SAIs embarking on such audits.

TBL, or sustainability reporting, requires less reliance on output indicators and an increased focus on calculating the externalities associated with a business or activity. In particular, TBL seeks to overcome the limitations of traditional financial accounting, such as:

- a restricted focus on the interests of stakeholders with a financial interest in the entity;
- adoption of the 'entity' assumption according to which transactions or events which do not directly impact the entity are ignored for accounting purposes;
- expenses are defined so as to exclude the recognition of impacts on resources not controlled by the entity (such as the environment); and
- recording only those items which can be measured with reasonable accuracy (whereas, many environmental or social externalities may not be capable of accurate valuation).⁶³

Key barriers to the adoption of TBL reporting include the lack of standard methodologies; the lack of appropriate skills, knowledge and/or experience and the difficulties of identifying social and environmental costs and the valuation of liabilities. TBL can only proceed from a strong interdisciplinary base. In addition to the traditional accounting, statistical, management science and, more recently, an ethical skills base which characterises much of audit, TBL requires the skills of environmental and social scientists, engineers and technologists, which are often found in performance or value-for-money auditing.

Above all, we are being urged to move beyond the '*black boxes*' of sustainability auditing, reporting and accounting to give practical meaning to TBL concepts.⁶⁴ While the areas of economic or shareholder value are well developed and understood, indicators of environmental or social value-added remain to be comprehensively developed. Indicators of corporate environmental performance might include:

- *materials use*: quantities and types of materials used. This indicator tracks resource inputs, distinguishing their composition and source;
- *energy consumption*: quantities and types of energy use or generation. This indicator, the energy analogue to materials use, also differentiates between types;
- *non-product output*: quantities and types of waste created before recycling, treatment or disposal. This indicator distinguishes production efficiency from end-of-pipe pollution control; and
- *pollutant releases*: quantities and types of pollutants released to air, water

and land. This indicator includes toxic chemicals, as well as greenhouse gases, solid wastes, and other pollutants.⁶⁵

Basic elements of corporate social performance might include:

- *employment practices*: The provision of a safe working environment; financial and job security; freedom from discrimination on race, gender, colour or creed; and opportunity for professional development;
- *community relations*: The contribution of a company to community development, including: job creation; taxes paid/tax breaks received; philanthropy; and employee volunteerism;
- *ethical sourcing*: Engagement in fair trading practices with suppliers, distributors and partners; ensuring that suppliers do not use child or forced labour; provision of safe working conditions and fair wages; and
- *social impact of product*: The contribution of products and services to social welfare, equity, and the meeting of basic human needs, such as food, shelter, water and health care.⁶⁶

This is clearly a 'greenfield' area for research and development as far as audit is concerned. I note that a recently released standard from the Institute of Social and Ethical Accountability in London (AA1000) incorporates an auditing standard through which organisations can provide assurance to stakeholders as to the quality of their social and ethical accounting, auditing and reporting.⁶⁷ The trans-border and global issues inherent in TBL suggest that the development of appropriate methodologies and indicators would benefit enormously from international input.

One outcome of last December's World Trade Organisation (WTO) meeting in Seattle was a significant north-south divergence in priorities and perspectives between the industrialised and post-industrial countries and those that are the less developed and industrialising. The potential exists for audit to contribute to constructive dialogue and rapprochement on such issues and approaches. However, any progress may well largely depend on a more knowledgeable and demanding community expressing its preferences in the Ballot Box and/or share market. Nevertheless, the issues involved are central to democratic governance and its administrative framework in which public audit has to play a useful, including a leadership, role in accountability for performance, as I noted at the outset of this paper.

Continuous Process Auditing

Another paradigm shift to be confronted by public auditors involves the possible/likely shift to real time continuous assurance about financial and non-financial information. A set of yearly financial statements accompanied by an annual audit report may not be regarded as sufficient in the future.

Continuous audit approaches are now being adopted and can be expected to mature further over the next decade. Continuous auditing, accompanied by continuous reporting, does, and will increasingly, require auditors to place greater emphasis on delivering additional value from audit through analysis and interpretation of organisational performance. In part, it may also overcome a criticism about the timeliness of audits and, consequently, their usefulness. The change marks a not too subtle shift in the role of auditor from that of a provider of assurance to one of a business adviser⁶⁸ and raises issues about the maintenance of the independent role of auditors.

The Auditor-General for British Columbia, Canada has referred to 'modern' government organisations as being 'values driven' – meaning an increased emphasis, as a result of public demand, on qualitative matters such as standards of conduct, sustainability in the use of public resources and environmental stewardship.⁶⁹ He has outlined a number of implications arising from the shift to a values-driven public sector which warrant repeating here in this context:

'With less focus on traditional controls and more attention given to the values and ethical climate of each government organisation, the auditor will need to learn how to assess such values and ethical climate. Issues such as leadership, communication, and employee consensus will become, as or more, important than traditional controls such as division of duties and proper signing authorities, etc.'

The audit community will have to become far more skilled than it now is in assessing performance measures and results and, in particular, outcomes. Our capacity to assess key performance indicators is as yet somewhat basic, and we have no conceptual framework for assessing the validity and completeness of such indicators. We also have yet to develop skills for assessing attribution problems -that is, who should be held responsible for performance achievements.

Auditors should become aware of the importance of government organisations possessing the necessary capacity to transform themselves into learning organisations, and have the criteria to be able to assess those organisations, as well as the skills to measure performance against those criteria.

The auditor should acquire skills in customer survey work, either doing it directly, or assessing the success of an agency's efforts to publicly measure and report on its performance. The auditor should also be able to assess service quality, and the extent of client/customer focus within the organisation.

Auditors will need to have outstanding information technology skills. Also, auditors will have to be prepared to give real-time opinions, rather than the periodic paper-based opinions provided at present. This will call

*for continuous auditing, and the ability to assess system changes and risks in shortened time periods.'*⁷⁰

The last observation is particularly relevant to the issue of continuous process auditing, or CPA, which I would now like to discuss in more detail.

The questions we have posed about audit independence and the challenges posed by technological innovations converge in the context of CPA, which can be defined as:

*'a methodology that enables independent auditors to provide written assurance on a subject matter using a series of auditors' reports issued simultaneously with, or a short period of time after, the occurrence of events underlying the subject matter.'*⁷¹

CPA is intended to provide:

*'an integrated diagnostic view of an online real-time system and to monitor the system in order to provide early warning of system problems (i.e. control weaknesses) and to insure the financial integrity of the system.'*⁷²

CPA requires the implementation of data management systems which support the continuous monitoring analysis of data flowing using a set of auditor defined rules. Any exceptions to these rules will call the auditor's attention to any deterioration or anomalies in the system. Continuous process auditing allows constant analysis and review which allows the auditor to improve the focus and scope of the audit.

Computer networking makes it possible for stakeholders' analysts to connect to certain parts of an organisation's information system and monitor performance on a day-to-day basis. This technology might result in greater disclosure – including greater voluntary disclosure – and may have a profound impact on approaches to corporate governance.⁷³ At this time, the issues for the private sector about increased disclosure would be quite different to those operating in the public sector, where impacts are largely about political performance, rather than profitability or increased share value, as in the former sector.

The Internet enables external auditors to remotely conduct some degree of continuous auditing. Although auditees may be resistant to the continuous exposure represented by CPA, continuous auditing *is very likely to increase compliance and reduce incidences of "creative accounting" or incidents of negligence in performing controls.*⁷⁴ The real contribution of CPA may be realised when most information exists only in electronic form (such as in a paperless airline reservation system⁷⁵). Auditors can use software to detect auditor-specified exception items from among all transactions processed. It is likely that controls would need to be implemented to prevent unauthorised modification

to the embedded audit module. Possible controls would include the use of suitable passwords to restrict access to source codes and procedures to ensure the organisation's compliance with application software maintenance procedures.⁷⁶

As with other data, Internet-enabled external continuous audit involves significant security issues and the need to apply appropriate controls to prevent unauthorised access to confidential data.⁷⁷ Apart from controls on electronic access, it would also be necessary to consider the security issues inherent in the use of external consultants to perform various aspects of CPA where the consultants have access to confidential information which might have a commercial value or other potential conflict of interests.

A research report prepared by a study group of the Canadian Institute of Chartered Accountants, reached the following conclusions in relation to the development and application of CPA which, despite their length, are considered important enough in this context to quote fully here as follows:

'1. Continuous audits are viable, provided certain, interrelated conditions are met.

- The short time frames for reporting would result in the need for a high degree of automation of the processes entities use to capture, manipulate and store data and to report information related to the subject matter being audited. Consistent with this requirement, the data underlying the subject matter would need to be precisely defined in terms of their components and the desired quantitative and qualitative relationships of those components.*
- The automated processes would need to be highly reliable in producing information about a subject matter soon after the occurrence of events underlying that subject matter. Increased emphasis on the use of automated preventive controls would be essential. Also, automated "alarm triggers" would be used to provide timely reports on anomalies and errors detected by controls and on possible control failures.*
- Highly automated audit procedures would need to be implemented to provide most of the required audit evidence. The audit tools would be integrated, to varying degrees, with the entity's systems and controls. Often, there would be a need for internal auditors to be involved in setting up the audit process. Automated procedures would be supplemented from time to time with procedures requiring the personal presence of auditors.*
- The auditors need to be quickly informed of the results of automated procedures, particularly when the process has identified anomalies or errors requiring follow-up procedures to be performed personally by audit personnel. The automated audit process would therefore need to include efficient electronic communication links, with appropriate security features, between an entity's site and that of the auditors.*

- *Auditors' reports would need to be produced automatically and be safeguarded against unauthorised changes. Such reports could include short interval reports (e.g., reports issued daily, weekly), "evergreen reports" (i.e., reports that are always available to users and dated as at the time of user access) and "reports on demand" (i.e., reports that are available when specifically requested by a user and dated as at the time of request).*
 - *Auditors would have to be technically proficient enough to handle the circumstances of the engagement. In most cases, that would require a high level of expertise in various aspects of information technology. The auditors would also require a sound grasp of the subject matter being audited.*
2. *Research by academics, experimentation by practitioners and guidance from standard setters are all necessary to help continuous audit services evolve. Examples of significant issues to be addressed include:*
- *Can auditors obtain reliable audit evidence when it may not be practicable to readily access external sources or wait for subsequent events to occur?*
 - *How can the automated audit process appropriately and rapidly determine the nature, timing and extent of continuous substantive procedures when control risk levels fluctuate? Should substantive procedures be required when control risk is assessed as very low?*
 - *How would the nature of the subject matter of the audit and the need to report continuously affect the way auditors determine materiality guidelines and desired level of audit risk?*
 - *How can auditors most effectively use sophisticated automated audit tools and techniques that are currently not much used in traditional financial statement audits?*
 - *Could the objectivity of external auditors be significantly impaired when automated audit tools are embedded in the entity's systems?*
 - *How can the knowledge, expertise and work of internal auditors be used most effectively in setting up a continuous audit process?*
3. *Demand for more reliable, relevant and timely decision-making information is likely to create a need for continuous audits, but the auditing profession needs to position itself to respond appropriately to the marketplace.*
- *Empirical research is needed to identify specific circumstances where two conditions exist simultaneously: (i) continuous information is vital to decision making and (ii) users perceive that a continuous audit by an objective party would improve the reliability of the information and, thereby, significantly enhance their decision-making process.*

- *Auditors must change their mindset to embrace a continuous reporting environment and then acquire the requisite technical skills and knowledge of subject matter to meet the demands of this environment.*⁷⁸

CPA is significantly different from an annual financial statement audit in that:

- auditors' reports are issued at short intervals (for example, daily or weekly) or made available immediately;
- reports could take the form of an "evergreen report" that is available whenever a user accesses a web site;
- reports would contain audited information, with the auditor's report dated as at the time of user access; and
- reports could take the form of a "report on demand," which is similar to the 'evergreen' report but available only if specifically requested by the user.⁷⁹

Unlike the traditional financial statement audit, a CPA could focus on any type of information relevant to organisational decision-making, such as the authenticity, integrity and non-repudiation of electronic commerce transactions, the effective operation of controls over a publicly accessible database, and various non-financial measures of an organisation's performance.⁸⁰

In applying CPA, a number of significant technical hurdles would need to be overcome. Unlike an annual financial statement audit, where evidence is often obtained well after the occurrence of underlying events, in a continuous audit environment little time would elapse between the occurrence of events and transactions and the process of obtaining audit evidence and reporting on related information. There would be much less time to investigate and deal with any anomalies detected and, the time required for the resolution of frequent anomalies could delay reports, thereby diminishing the usefulness of continuous auditing.⁸¹

Overcoming these technical hurdles requires that certain conditions need to be met as follows:

- First, the information to be audited would have to be generated by reliable systems. In a continuous reporting auditing environment, key controls should be preventive controls, or automated detective controls that operate soon after transactions are initially processed. To ensure simultaneous updating of all components of the information, various systems and sub-systems would have to be integrated by networking and sharing of common data.

- Second, the continuous audit process needs to be highly automated. Auditors are becoming more familiar with the use of automated audit tools and, depending on the subject matter being audited, the tools now used on many financial statement audits could also be used for continuous audits. Audit tools have to be more integrated with an organisation's systems because they have to be applied more frequently and their initiation would have to be automatic rather than manual (perhaps at pre-specified times or with the occurrence of an event such as the use of a particular module in the organisation's system). Immediate reporting engagements would require the use of audit tools that are highly integrated with the entity's systems and operate frequently or perhaps continuously.
- Third, there is a need for effective links between the auditor's systems and the audited organisation's system to enable fast, accurate and secure communication of audit instructions and results. The auditor could, for example, be directly linked to the auditee's wide area network.
- Fourth, accurate and understandable auditors' reports have to be made available on a timely basis. The continuous information related auditors' report could, for example, be posted to a web site so that they are readily accessible by users. The auditee would have to implement, and the auditors would have to test, controls over automated process for updating the formation and the auditors' report.
- Fifth, auditors need to have the proficiency to undertake CPA. This includes not only a sound grasp of subject matter being audited (which may be non-financial) but a high level of information technology skills. However, since no one auditor can be expected to have in-depth knowledge of all aspects of a subject or of various types of computerised systems, a continuous audit team may have to obtain the required expertise from external consultants.⁸²

According to the author of the foregoing comments, who is a senior manager in the Canadian Institute of Chartered Accountants Auditing Standards department:

*'To establish the conditions for effective continuous auditing, auditors must change their mindset and invest the required energy, knowledge and technical resources. While it might be an exaggeration to say that the auditing profession is in a fight for survival, there is no doubt that the old model of annual financial statement audits is becoming less relevant. Auditing can, however add more value to an entity if the service timely enough to meet the needs of decision-makers. Continuous auditing seems to be the route to go.'*⁸³

Similar points were made in a later article by Professor Michael Groomer who was an adviser to the CICA/ASCPA joint study group on continuous auditing.⁸⁴ In particular, he reiterates the significant technical hurdles

involved as well as the time pressures associated with, for example, the processes needed to obtain audit evidence and to generate an audit report. Not surprisingly, Professor Groomer stresses that continuous audit must be a win-win process with both top management and audit seeing a positive outcome. Whether public audit is, or is not, pro-active in encouraging a move to continuous auditing, it must at least be ready to engage with organisations that regard such auditing as a means of 'providing timely attestation for decision-makers'.⁸⁵

IT competency and audit

It almost goes without saying that, if Public Audit Institutions are to successfully address the technical, management, behavioural and legal issues inherent in the application of information technologies in the public services, they will have to have suitable leading edge skills. Information technology is continually evolving. Moreover, it evolves so rapidly these days, with the shelf-life of IT products (both software and hardware) being so relatively short, that it becomes a daunting task simply to keep up. This is an area which requires specialist skills and we need to consider how best to identify, secure, apply and continuously develop those skills in order to keep them current and available.

It is probably fair to say that IT knowledge and capability has probably had most impact on financial statement and allied IT audit practices. However, I am also conscious of the emerging pressures that performance audit practice is confronting with some technological advances. In particular, performance auditors who have traditionally worked with paper-based, hard copy records, are increasingly encountering organisations which are '*paper-less*'. Although the *paperless office* has been touted for years and, until now has largely failed to materialise (in fact, it is probably fair to say that IT has caused an explosion in the use of paper) its time may well be coming and we will need the protocols, tools and knowledge to deal effectively with it.

Fundamentally, we will have to make decisions about how to source these skills. This boils down to questions '*build or buy?*' or '*build **and** buy?*'. We need to ask the strategic question as to whether the short term expediency of externally sourcing IT expertise (as it applies to the conduct of audit activities) is outweighed by the medium to longer term loss of strategic market advantage. If audit offices are effectively reduced to being purchasers or brokers of third party audit expertise can pressure for direct sourcing of these services from the market by auditees be all that far behind? I feel strongly, therefore, that although external sourcing of IT expertise is necessary at least in the short term, we also need to carefully examine options that result in knowledge transfer to Public Audit Institutions and the appropriate skilling of their personnel which could come with strategic partnerships with other audit practices, both public and private.

Globalisation and the contestability of audit services

The foregoing discussion leads to what is possibly the most important issue confronting Public Audit Institutions today, that is, the extent of privatisation and its impact on core business and our ability to recruit/retain skilled personnel. I take some comfort from a reversal of an earlier government decision to virtually privatise the Victorian State Auditor-General's Office where there was an apparent up-swell of public and political support for the restoration and protection of a fully independent and appropriately resourced public audit function.⁸⁶ However, it would be too simplistic to assume, in the current transitional public sector environment, that public auditors would be insulated from the pressures of contestability. Nevertheless, this would have consequential implications for audit independence and ability to perform associated statutory responsibilities.

In particular, we must be aware of, and develop strategies for dealing with, any competitive pressures emanating from the large multi-national accounting and management consultancy firms. Public audit practices are, in the larger scheme of things, relatively small organisations. We do not enjoy a global pool of financial, human or informational resources. We do not have the same capacity to generate funding, differentially price products, acquire knowledge, manage inputs, reward performance or deploy capital or personnel. If it is not already the case, it is realistic to expect that the participation by the multi-nationals in various facets of government business world wide is likely to lead to an almost unassailable capture of knowledge and expertise at least in significant areas of that business. As well, the greater degree of convergence between the public and private sectors limits the comparative advantage of detailed knowledge and understanding by Public Audit Institutions of the nature and operations of governance.

As I noted earlier, we are basically in the knowledge business. Although we enjoy, for the moment, a statutory monopoly on the provision of audit opinions about the activities of public sector organisations, the mode of production (meaning the resources utilised by the Auditor-General to form his or her opinion) enjoys no such protection. We are, like small business, coming face to face with a global market marked by freer trade and competition with firms that enjoy scale economies far in excess of anything we can hope to achieve ourselves. For the present, ours is a niche business – although it must be said that it is a niche which is already attracting the interest of the private sector, in part because Auditors-General are outsourcing at least their non-core audit activities as I am doing. Indeed this has allowed the ANAO to form strategic partnerships with particular multi-national organisations that have facilitated access to particular skills and world-wide data bases.

In industry, competition for government business has led smaller firms to form consortia in order to compete with larger players. They become, in

effect, a '*virtual*' corporation. Although the market remains to be fully convinced of their viability and contribution, it should be possible for consortia comprised of smaller, complementary but independent entities to approximate the market power of a larger unified entity. In some ways, this model provides a signpost for Public Audit Institutions.

While it is unlikely – for statutory and political reasons – that we will ever form consortia to collectively 'bid' for work (and this is not to say that there is no scope for joint or at least contemporaneous audits) we *can* act corporately and cooperatively in the areas of knowledge and skills transfer, information technology and research and development without any adverse impact on our individual independence. In marketing terms, this is about taking advantage of natural synergies between Public Audit Institutions to make our small organisations look like bigger ones by providing *depth* in relation to our business critical resource (*knowledge*) through our relations with like organisations elsewhere in our own countries and across the world.

The Australian Government has determined that there is considerable scope for the privatisation and outsourcing of government services and activities. Undoubtedly, one of the most significant developments in APS reform has been the requirement to test the market with a view to determining the most efficient and effective method of service delivery. Competitive Tendering and Contracting (CTC)⁸⁷ is resulting in greater contracting-out of what has been regarded as traditional core, as well as non-core, government services which in turn is creating new risks for public administration which need to be managed properly, in particular by Chief Executive Officers and Boards who are statutorily accountable for the efficient, effective and ethical use of their resources.

With increased pressure upon APS agencies to become contestable, more and more agencies are electing to use contractors. APS agencies tend to outsource internal audit more extensively than organisations outside the APS. The results of a survey of Australian federal government agencies undertaken by the ANAO in 1997 indicated that 60 percent of all agencies surveyed, which included most of the larger APS agencies, used contractors (mainly from the large multi-national accounting firms) to undertake some or all of their internal audit work and 58 per cent of APS agencies contracted-out their IT audit functions⁸⁸. One concern is that the decision to contract accounting firms/auditors should not be seen as also outsourcing financial oversight and reporting responsibilities, in particular where the outsourcing is quite narrowly focussed, say, on financial statement preparation, or on ad hoc systems control assurance assignments as the only areas of apparent financial concern. As with all outsourcing in the public sector, the accountability for results remains with the agency/entity managers.

Contestability of Internal Audit

Contestability applies just as much to the internal audit function as it does to any other operational activity. In-house internal audit functions will only survive if they are contestable in the emerging public sector environment. By that I mean the in-house staff must have comparable skills and provide a comparable product at a competitive price with the latter being only one element of CTC action. In becoming contestable and adopting best practice, internal audit operations are being totally restructured, downsized and often given the added burden of managing contractors. The nature and extent of such change does not do much for the confidence and trust of management. It appears that many internal audit areas are still in the transitional phase, attempting to justify their continuing existence based on their detailed knowledge and understanding of the agency's operations and systems.

In my view, internal audit staff (both in-house and contractors) need to have a sound appreciation of the current and proposed public sector reforms, as I indicated earlier, particularly in the area of financial management and administration. Executive management would like to think that personnel engaged in the internal audit function have a real commitment to, and ownership of, the organisation's objectives, values and code of conduct. I would also like to see a commitment to public service and a well developed sense, and understanding, of public accountability by private sector providers. However, we need to be well aware of the limitations of any outsourcing contract particularly those of a 'discrete' nature where the major obligations of each party are clearly specified in the contract.

Why are APS managers and CEOs looking to outside experts to provide them with assurance on the reliability and adequacy of their operating systems and controls, and to assist them in improving their operational performance? Why aren't they using their agencies' in-house staff? I suggest that many CEOs are looking outside their agencies for assurance because they judge that external consultants, particularly from the large accounting firms, have a broader range of experience and expertise on which to benchmark their findings, recommendations and advice. This judgement may also reflect a view that the service is cheaper as well as concerns about the increasing complexity of their own environment and desire for assurance where they are more personally responsible for the accountability framework and agency performance. Unfortunately, it may also reflect a perceived gap in the professional capability of in-house and outsourced internal audit services which is often a self-fulfilling truth as management has often progressively downgraded the function over recent years with the increasing pressure on resources as a result of smaller budgets.

Any decision by management on outsourcing should be made on a realistic assessment of value for money given the risks and responsibilities involved. This assessment will vary with the circumstances of each agency and the trade-offs individual managements are prepared to consider, particularly in their control environments and within their broader accountability

responsibilities to the Parliament or Legislature. It is important that such assessments are made within the ambit of their corporate governance arrangements so that the full implications are reviewed but not in any partial sense where the consequences are only discovered later in some accountability failure, impacting adversely on the whole agency and its reputation.

As with the external audit function the necessary skill sets and knowledge requirements for internal audit staff are varied and complex and rarely reside wholly within one individual or even a small number of people. This can be a major factor impinging on the effectiveness of small internal audit sections typically found in the smaller agencies. A particular problem is to attract suitable candidates at the levels necessary to be credible both to potential recruits and to those with whom they would be working. As well, there is the difficulty of maintaining professional expertise with little or no peer contact.

Nevertheless there may well be compelling reasons for simply complementing an in-house capability with the required external skills and capacity. I am particularly sympathetic to the situation confronting management in determining viable arrangements in small agencies. There is clearly a 'critical mass' problem which impacts adversely on the recruitment and retention of the requisite in-house professional skills. This is also of concern to external audit who are dependent on the professionalism and contribution of internal audit. I could also add Audit Committees which are in virtual partnership with internal and external audit as an important element of corporate governance.

Whither the ANAO

The Office of the Auditor-General and the Australian National Audit Office are established by the *Auditor-General Act 1997*. Under the Act, the Auditor-General is an 'Independent Officer of the Parliament'. That description reflects the concern to emphasise the total independence of the Auditor-General. The Act also includes a number of fundamental elements which are aimed at safeguarding that independence and preventing inappropriate influence being exerted on the Auditor-General by either the Executive or the Parliament. They are mainly reflected in the following provisions:

- the Auditor-General cannot be directed by anyone in relation to the performance of his/her functions;
- the Auditor-General is appointed by the Governor-General following approval by the JCPAA;
- he/she is appointed for a period of ten years and can only be dismissed by a resolution of both Houses of the Australian Federal Parliament;

- availability of powers of access to information relating to the performance of an audit function; and
- guaranteed availability of funds appropriated by Parliament for ANAO operations.

The importance of the independence of the Auditor-General is encapsulated in the following comment by the tenth Auditor-General for Australia, Mr Keith Brigden AO:

*'Audit independence and audit effectiveness can amount to much the same thing. If an auditor does not enjoy independence from the bodies subject to audit it will only be a matter of time before some measure of control by auditees becomes apparent. When that happens, the effectiveness of the audit process will inevitably suffer. In practical terms, impairment of the auditor's independence is synonymous with impairment of audit effectiveness.'*⁸⁹

However, while I and my Office enjoy a high degree of functional independence, that certainly does not mean I operate without reference to the Executive and the Parliament. Nor does it mean I have an 'open cheque book' for resources.

My Office is funded through budget appropriations and, like any other entity that is budget funded, we are expected to ensure that value for money is achieved for each taxpayer dollar spent. Indeed, under the *Financial Management and Accountability Act 1997*, I and the heads of other Australian federal government agencies subject to the Act, are required to promote the efficient, effective and ethical use of the Australian federal government resources for which we are responsible (section 44).

The ANAO's budget and resources are determined in consultation with the Joint Committee for Public Accounts and Audit (JCPAA) which has the responsibility to examine the draft budget estimates of the Office and to make recommendations to the Parliament and the Prime Minister on those estimates. Through this process, which does not involve the Executive Government, independent judgements are made as to whether the ANAO is adequately funded to meet its statutory obligations. While ultimately it is the Executive's prerogative to decide the level of funds earmarked for the ANAO in the Appropriation Bills that are presented for Parliamentary approval, clearly, any proposed funding which departed in any significant way from that recommended by the JCPAA, would be likely to be questioned by the Parliament.

While the ANAO must remain independent of the bodies it audits, the Office is, nevertheless, a part of the public sector as a statutory body. Consequently, we have a responsibility to contribute to the overall performance and development of the public sector. For our products to remain credible and

relevant, we also need to demonstrate we are meeting the challenges of the changing public sector environment and, within our capacity, are contributing to the implementation of the Government's reform agenda. Over a number of years, we have placed increased emphasis on ensuring that our services are contestable; outsourcing non-core business functions where the private sector can provide better value for money; and ensuring commitment to the processes of benchmarking, quality assurance, peer review and continuous improvement.

The capacity to monitor performance is a prerequisite to being able to improve performance and we have expended a good deal of effort on developing our performance monitoring framework. We measure the quality and impact of our products through a range of quantitative and qualitative measures, including surveys of Parliamentarians and our audit clients. Our audits are regularly subjected to formal quality assurance review processes and we conduct peer review and benchmarking activities with State Audit Offices and relevant private sector organisations. We do not see our independence as meaning we are under no obligation to be accountable for the use of our resources.

Our capacity to deliver quality auditing services is also enhanced through maintaining strong relationships with our public sector peer groups in Australia and overseas and with the various professional accounting and auditing bodies. We have close links with several national and international auditing organisations through which we assist with the development of auditing standards, professional practices and exchanges of experience. The ANAO also works closely with major accounting firms and professional accounting bodies to set and maintain professional and ethical standards internally, the importance of which I underlined earlier. Outsourcing of selected activities and the contracting-in of specialist expertise to assist on particular audits have also provided us with opportunities to extend and develop our knowledge and skill base.

The foregoing indicates that, in managing ourselves, we are continually looking to the future and the medium to long term issues and challenges that face auditing and the ANAO, and consequently developing strategies to successfully meet those issues and challenges. A major strategy is to create and maintain the breadth, and particularly the depth, of public sector knowledge and skills, complemented by outside expertise and information systems, that will be capable of delivering the required outputs and outcomes efficiently, effectively and ethically. In essence, we want to ensure that our comparative advantage as a public sector auditor is demonstrated through our performance and valued by *all* our stakeholders.

The contemporary trend has been towards the notion of continuous auditing discussed earlier. In the past, auditing has been a largely retrospective activity where opinions and advice produced after the event have met

fundamental assurance obligations to Parliament but have not necessarily contributed markedly to improving public sector performance. Rather, auditors have often told managers what they should have done in hindsight. However, as public administration has changed, auditing has had to take a more pro-active approach to ensure audit services are timely and relevant and can also make 'real-time' contributions to enhancing public administration.

In recent times, our approach has been to add value wherever possible by working closely with entities to identify and solve problems now, not later, by making constructive recommendations for change and by promoting and disseminating better management practice. The latter is often based on our knowledge and experience of the whole of government including access to better private sector practice often through the databases of one or more of the Big Four accounting firms. Advances in information technology and the widespread availability of different information sources mean we cannot be complacent about our audit products and services, particularly about how we deliver them to our audit clients, notably the Parliament.

The following extracts from a recent speech the Auditor-General of Western Australia, provide some useful insights into the future of auditing and its role in assisting managers to improve entity performance:

'... I believe we are starting to see the audit deliverable as more than just the opinion on the financial statements, controls and performance indicators of an entity. We are expanding our view of the deliverable to that set of continuous communications that exploit all the knowledge we have gained during the audit.

... Of all the professions, auditors are in the best position to be able to assist managers and executives in interpreting and analysing performance information. Our work is such that it requires a good grasp of the entire range of activities and operations of an entity and ensures we maintain a level of professional scepticism and a critical eye for facts and details. In short our level of knowledge is often on a par with the most senior executives in the organisation, but with the added advantage of objectivity and independence.

*It is important that we exploit this position in a positive way and take a proactive interest in assisting managers to improve the agency's performance. An agency's ability to be seen as a going concern in the future will depend on how well it manages its performance. Why shouldn't the auditor also ensure their own audit business is a 'going concern' by acting now to advise and assist managers on how to use performance information to their best advantage?'*⁹⁰

I consider that my Office is well down the track in terms of the framework described above. The management challenge for us is to keep moving

forward and to continue to look over the horizon in order to maintain our comparative advantage and be indispensable.

CONCLUDING REMARKS

It is now time to close the circle. Of course, it can never be completely closed because we cannot accurately predict the turn of events. We can, however, reliably extrapolate from immediate past and present events to speculate about possible future directions. In order to know where we are going, we have to come to terms with where we have been. We know, for instance that we have been through a period of significant and sustained change. If we think about it, we become aware that change has been rather more episodic than gradual. Regardless of that, to the extent that we have been concerned with the 'here and now', it is easy to lose sight of the fact that change is ongoing. It is basic human nature to assume a 'steady state' even though dispassionate analysis demonstrates that our expectations, behaviours, assumptions and priorities are constantly shifting.

To the extent that, as organisations or individuals, we often act on the basis of assumptions about a steady state, we are demonstrating a failure to adapt. Such failure accentuates the risk to survival. Adaptation is about learning and responding, about minimising mistakes and not repeating them when they occur. We *are* in the knowledge business where a competitive edge is conferred by our ability to learn as well as to adapt and apply our knowledge in a useful way. Fostering and promoting the learning capabilities of our organisations, and the individuals who work in them is an essential and irreducible adaptive strategy to carry into the new millennium.

We – as Public Audit Institutions – are as much a part of a dynamic social, political and economic environment as any other statutory or public body. We are not shielded from change or the forces that impel change. Being aware of, and having in place the analytical tools to monitor and project trends in our business environment will assist us to gain and hold a competitive edge. Because we live in a world in which ideas, technologies, resources and practices can be readily transmitted from one part of the globe to another, our challenge will be to take care to monitor globally as carefully as we monitor our immediate environment. Parochialism not only offers no protection from globalisation, it actually poses a significant threat to survival or at least to credibility and confidence in the institution.

The best way to defend our statutory mandate and our independence is to continue to demonstrate how well we perform – both in terms of what we produce and how we produce it. Managing our performance will be critical in demonstrating our continuing relevance. We need to define our business carefully and strive towards excellence in those areas where we consider we

have a comparative advantage. This may mean working within reduced or declining resources (in real and absolute terms) without compromising quality. This can be achieved if we apply ourselves creatively to the design of our industrial, administrative, intellectual and technological systems and organisational structures, both internally and externally, in active partnerships both with our peers and with the profession of which we are a part. Such partnerships should take advantage of the INTOSAI framework and work of its various committees and working parties.

There is a future for public audit because the private and public sectors are different and will remain so despite the apparent convergence taking place as part of public sector reform. [The essential differences are clearly articulated by Professor Richard Mulgan of the Australian National University as follows:](#)

*'The private sector has no equivalent of parliament as an institution of public accountability nor are private sector companies subject to continuous public scrutiny from a political opposition competing for public support as an alternative management team.'*⁹¹

[The public audit](#) task is to do what we can do individually and collectively to ensure that we continue, and reinforce, the traditions of audit independence; provide credible assurance to the Parliament and its Committees in particular, of the ethical, efficient and effective use of public resources; and add value to public administration that is recognised by all our stakeholders who, in turn, have a commensurate commitment to public audit. In particular, we have to affirm and reinforce public service values and the ethical conduct that underpins them. Both our independence and public service values are a source of significant comparative advantage in the provision of public audit services.

The focus of public sector reform is on results but it also matters how those results are achieved. A major challenge for the public sector in the future, including for Audit as I have suggested, is performance management. If we are successful in achieving a credible, trusted performance management framework, we will earn the confidence and support of all our stakeholders, including those who work, and want to work, in the public sector. From an accountability viewpoint, which is also a major on-going audit concern, the following observation by the Comptroller General of the United States is apposite:

*'Performance management ensures accountability because it generates valid and reliable data on program impact on the allocation of resources and on the economy, efficiency, effectiveness and integrity with which the government's finances are run.'*⁹²

This discussion paper has attempted to identify how Public Audit Institutions can contribute to such an outcome while providing the necessary assurance of

public sector achievements in these respects. There is no doubt that such assurance will depend importantly on the quality of our services and reports which in turn will depend on the commitment, skills and professionalism of our staff. As the Public Audit Forum in the United Kingdom has observed:

*'Public audit plays an essential role in maintaining confidence in the stewardship of public funds and in those to whom the responsibility of stewardship is entrusted. Public auditors are, of course, themselves accountable for their performance and are duty bound to undertake their work in a professional, objective and cost-effective manner and with due regard to the needs of the organisations they audit.'*⁹³

In particular, we have to earn the confidence and respect of our main stakeholder, the Parliament, which, in turn, is the guardian of our independence and our ability to contribute to the improving performance and accountability of the public sector. While we must continue to provide assurance of the ethical, efficient and effective use of public resources, we should also aim to add value to public administration in all our audit activity. Therefore the overriding emphasis of our work should be on quality, timeliness, continuous improvement and achieving value for money outcomes.

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ACAG consists of the Auditors-General of all audit jurisdictions within Australia, New Zealand, Fiji and Papua New Guinea. Associate membership is available to any other interested jurisdiction. A Convenor is appointed from among the members to oversee the work of the group.

The objectives of ACAG are to foster and promote the development of public sector auditing in the Australasian region through:

- developing and promulgating authoritative pronouncements as to the nature, scope, independence and role of Auditors-General in the Australasian context;
- promoting educational activities to contribute to the efficiency and effectiveness of Audit Offices' performance;
- contributing to the development of mutually beneficial methodologies for, and approaches to, the discharge of audit mandates;
- promoting cooperation in the conduct of audits;

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- promoting the development of a professional quality assurance peer review program for participating offices;
 - contributing to enhancement of parliamentary liaison functions across jurisdictions, particularly with the Australasian Council of Public Accounts Committees; and
 - identifying and promulgating, where appropriate, the collective opinion of Auditors-General on draft accounting and auditing standards and other relevant issues.

The members of ACAG meet twice each year to endorse a program of tasks. In addition, meetings may be held for Audit Office staff on common issues: an annual senior officers' conference at which each Office presents a paper on a topic of common interest, and occasional meetings of senior managers to discuss developments in common key areas such as performance audit methodology. Tasks routinely undertaken by ACAG include coordinating Offices' comments on exposure drafts of Auditing Standards, sharing information on the adoption of new software or audit methodology, conducting peer reviews of the work of Offices, and sharing other information such as approaches to corporate governance, staff management and office structures.

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