



B.28

Parliamentary paper

# Annual Report 2011/12

Office of the Auditor-General  
PO Box 3928, Wellington 6140

Telephone: (04) 917 1500  
Facsimile: (04) 917 1549

Email: [reports@oag.govt.nz](mailto:reports@oag.govt.nz)  
Website: [www.oag.govt.nz](http://www.oag.govt.nz)

# Annual Report 2011/12

Presented to the House of  
Representatives as required by  
section 37 of the Public  
Audit Act 2001.

September 2012

ISSN 1179-8963 (print)  
ISSN 1179-8971 (online)



# Contents

Auditor-General's overview	5
Part 1 – About us	9
Our purpose	10
Our assessment of achieving our outcomes	11
Strategic risks and risk management	18
Report of the Audit and Risk Committee	21
Part 2 – Our output classes, performance measures, and targets (including <i>Statement of service performance</i> )	23
Output class: Audit and assurance services	24
Output class: Supporting accountability to Parliament	39
Output class: Performance audits and inquiries	46
Part 3 – Organisational health and capability	59
Part 4 – Financial statements	70
Appendices	
1 – Entities audited under section 19 of the Public Audit Act 2001	107
2 – Independent review of audit allocation and fee setting and monitoring report	109
3 – List of our major reports completed in 2011/12	115
4 – Senior management	117
5 – Directory of offices	119
Figures	
1 – Our operating model	11
2 – Outcomes framework	12
3 – New Zealand's ranking in the Worldwide Governance Indicators, 2008 to 2011	13
4 – Kiwis Count Survey results in 2008 and 2010: Public servants do a good job	14
5 – New Zealand's score on the Transparency International Corruption Perceptions Index, 2008 to 2011	14
6 – Percentage of unmodified audit opinions and audits completed on time	15
7 – Integrity and Conduct Survey results in 2007 and 2010: State service agencies that promote their standards of integrity and conduct	16
8 – Integrity and Conduct Survey results in 2007 and 2010: State servants' observation and reporting of misconduct	17
9 – Kiwis Count Survey results in 2008 and 2010: Most recent public service experience was an example of good value for tax dollars spent	18
10 – Our strategic risks and risk management	19
11 – Our work contributing to effective and efficient public service delivery	24
12 – Analysis of movements in audit fees	28
13 – Summary of impacts and outputs for Audit and assurance services	29
14 – Grades for management control environment (MCE), 2008/09, 2009/10, and 2010/11	30
15 – Grades for financial information systems and controls (FISC), 2008/09, 2009/10, and 2010/11	31
16 – Grades for service performance information and associated systems and controls (SPIASC), 2008/09, 2009/10, and 2010/11	31
17 – Percentage of audited financial reports that contain modified audit opinions	32
18 – Percentage of management report recommendations accepted by public entities	33
19 – Percentage of audited financial reports issued on time	34

20 – Percentage of outstanding audit reports at 30 June because of our inaction	35
21 – Percentage of management reports issued within six weeks	35
22 – Percentage of clients satisfied with the quality of audit work	37
23 – Percentage of auditors achieving a grade of satisfactory or better from quality assurance reviews	38
24 – Financial performance of output class: Audit and assurance services	38
25 – Summary of impact and outputs for Supporting accountability to Parliament	42
26 – Percentage of select committee members who confirmed that our advice assists them in Estimate of Appropriations and financial review examinations	43
27 – Percentage of other stakeholders who rated our advice as 4 or better on a scale of 1 to 5 for relevance and usefulness	43
28 – Percentage of select committee members who rated our advice as 4 or better on a scale of 1 to 5 for quality and usefulness	44
29 – Percentage of reports and advice given to select committees and Ministers at least two days before an examination, unless otherwise agreed	45
30 – Financial performance of output class: Supporting accountability to Parliament	46
31 – Work in progress from our 2011/12 Annual Plan	49
32 – Number and type of inquiries completed	50
33 – Summary of impacts and outputs for Performance audits and inquiries	52
34 – Completed reports on matters arising from performance audits and other studies, and inquiries	53
35 – Percentage of select committee, local government, and other stakeholders who rate the quality and usefulness of our performance audit reports as 4 or better on a scale of 1 to 5	54
36 – Percentage of findings on routine inquiries reported to the relevant parties within three months	55
37 – Percentage of findings on significant inquiries reported to the relevant parties within six months	55
38 – Number of findings on major inquiries reported to the relevant parties within 12 months	56
39 – Percentage of enquiries under the Local Authorities (Members' Interests) Act 1968 completed within 30 working days	38
40 – Financial performance of output class: Performance audits and inquiries	58
41 – Staff profile	61
42 – Summary of measures and standards for organisational health and capability	65
43 – Staff engagement survey scores	66
44 – Average number of years that staff have been employed by the Office	66
45 – Annual turnover of staff	67
46 – Percentage of audit staff passing NZICA accreditation examinations	68
47 – Ratings for expertise of Audit New Zealand staff	69

## Auditor-General's overview



The past year has been tough for many countries and people around the world, and tougher for some than others. New Zealanders have shown determination in facing our own challenges, while keeping an eye on the uncertain and often volatile environment overseas. Collectively, the public sector has responded to the clear need to focus on the effective and efficient use of scarce resources.

Many changes were made or initiated in the public sector during 2011/12, and there will be more to come as the face of our public sector continues to change. The reality is that change will be ongoing, and with it comes the opportunity to improve the way things are done, as well as the services provided to our fellow New Zealanders.

My Office has made adjustments to our own practices to ensure that we keep pace with changes – such as amalgamations of government agencies and setting of new accounting standards – and to be in a position to provide clarity about auditing matters, and give support and advice where appropriate.

### Highlights for 2011/12

My staff and contracted audit service providers performed strongly throughout the year, given the amount and effect of change on top of an ambitious reporting programme focused on public entities' use of their resources. In spite of these challenges, our results show that our work is having the impact we seek. Among our achievements and successful new initiatives during 2011/12, highlights were:

### Reports and advice

Our published reports addressed issues of importance, with the public giving particular attention to the reports on freshwater quality, Māori housing, and the Crown's retail deposit guarantee scheme. We also successfully introduced separate reports for the health and education sectors.

We used the results of our major survey about fraud in the public sector to encourage conversations about fraud. We reported publicly and shared the survey

results with our auditors and public entities in a way that encouraged them to be alert and to feel comfortable about raising questions about fraud. Again, I acknowledge the integrity and efforts of our public sector to keep fraud at bay.

Our work plays an important part in supporting accountability to Parliament, and our stakeholders' feedback confirms my Office is continuing to perform at a high level. The sector knowledge and relationship management skills of my staff are particularly valued.

### Auditing and inquiry work

We received numerous requests to carry out inquiries on a range of issues, and decided that five of these warranted major inquiries – a significant number for our Office to carry out at one time. Since the financial year end, we have completed two of the five major inquiries, and made considerable progress on the other three. We also audited the long-term plans (LTPs) of all local authorities for the 10 years from 2012 to 2022, with the exception of the Christchurch City Council, which obtained a one-year extension of time because of the earthquakes. These audits provide assurance to communities that the main long-term planning issues have been highlighted, and that the supporting information is reasonable for decision-making, community participation, and future accountability. No one is debating the necessity of long-term planning in local government, but its future form is being subjected to scrutiny that I think is warranted.

For the first time, we included an emphasis-of-matter paragraph in our audit opinion on the Financial Statements of the Government because of uncertainty about the financial effect of the Canterbury earthquakes. We also carried out the first full-year financial audit and the LTP audit of the new Auckland Council.

It was important that we maintained the quality of our auditing work in a rapidly changing public sector environment during 2011/12. We were able to do this and to maintain good stakeholder relationships throughout the year. We also made a solid contribution to a number of reforms led by others – notably, the External Reporting Board's new suite of accounting standards.

### Communications

During 2011/12, we began several new communications initiatives to expand our ability to reach target audiences and engage more widely about our work. In July 2011, we launched a website for school students and teachers to profile the role of the Auditor-General in our system of government, and to provide New Zealand-focused resources based on case studies of our work. We introduced Facebook and Twitter accounts, and initiated a successful online forum to bring together a group



of public entities to share information and good practice about accountability and reporting performance.

### **Our international contribution**

In my role as the current Secretary-General of the Pacific Association of Supreme Audit Institutions (PASAI), we began our five-year funding agreement with the Ministry of Foreign Affairs and Trade, which has enabled my Office to provide more support to the PASAI secretariat, and colleagues in the Pacific.

### **Preparation for 2012/13 and beyond**

During 2011/12, we carried out extensive consultation on our proposed 2012/13 work programme and began work on a new Office Strategy for 2013-17.

I am proud of our achievements and how we have managed the challenges of 2011/12. I thank all my staff and audit service providers for their ongoing commitment and hard work, and look forward to an invigorating year as we focus on our theme for 2012/13: *Our future needs – is the public sector ready?*

A handwritten signature in black ink, appearing to read 'Lyn Provost', with a stylized, cursive script.

Lyn Provost  
Controller and Auditor-General

28 September 2012



Part 1  
**About us**

## Our purpose

The Controller and Auditor-General (the Auditor-General) carries out audits, performance audits, and inquiries, and reports to Parliament and the public to improve the performance of, and the public's trust in, the public sector.

### The Auditor-General's role

The Auditor-General is an Officer of Parliament who carries out her role independent of executive government and Parliament, but is accountable to Parliament for the public resources she uses to do the job.

By law, the Auditor-General is the auditor of all public entities in New Zealand – a total of almost 4000 public entities, such as government departments, central agencies, Crown entities, schools, and State-owned enterprises.

All public entities are accountable for their use of public resources and powers. It is the Auditor-General's job to give Parliament and the public independent assurance about how public entities are operating and accounting for their performance.

The role also includes auditing local authorities, which are accountable to the public for the activities they fund with locally raised revenue. As well as annual audits, the Auditor-General audits local authorities' long-term plans, which are prepared every three years.

### The organisation

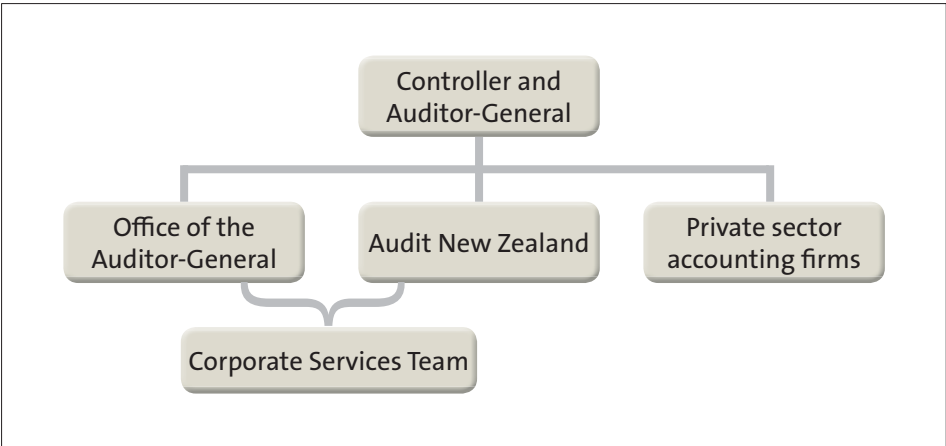
The work of the Auditor-General is carried out by about 350 staff in two business units – the Office of the Auditor-General (OAG) and Audit New Zealand, supported by a shared team of corporate services staff – and by auditors contracted from about 50 private sector accounting firms.

The OAG carries out strategic planning, sets policy and standards, appoints auditors and oversees their performance, carries out performance audits, provides reports and advice to Parliament, and carries out inquiries and other special studies.

Audit New Zealand is the larger of the two business units. It carries out annual audits allocated by the Auditor-General and operates from seven locations around the country. It also provides other assurance services to public entities within the Auditor-General's mandate and in keeping with the Auditor-General's auditing standard on the independence of auditors.

Figure 1 shows how all these parts fit together in our operating model.

**Figure 1**  
Our operating model



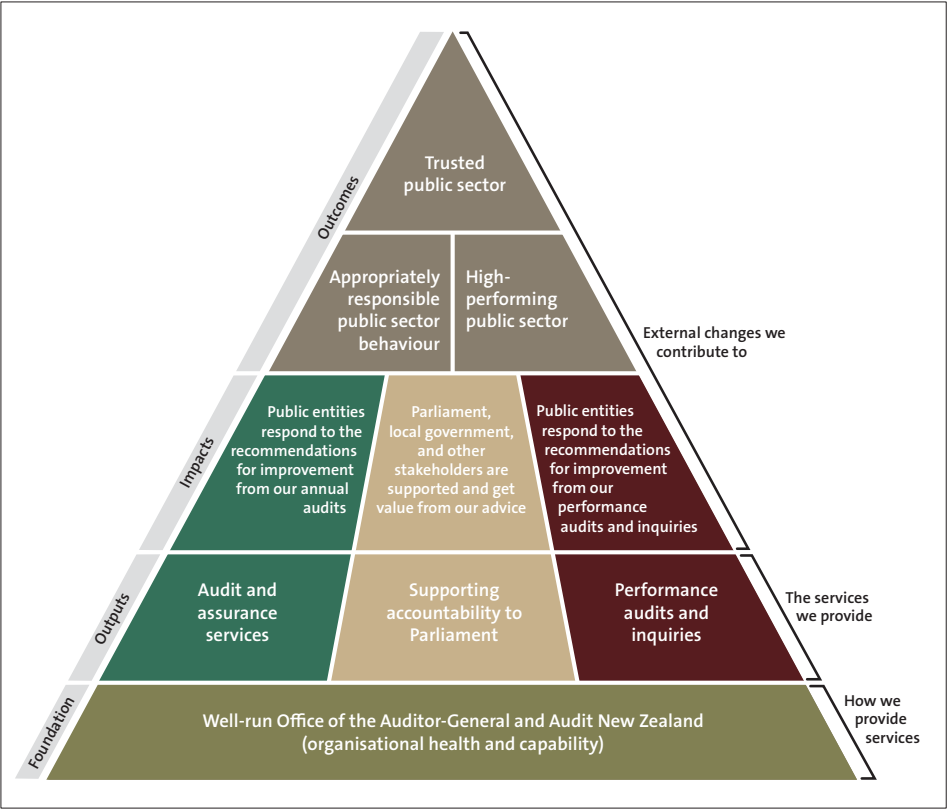
Our outcomes framework diagram in Figure 2 summarises the outcomes we are seeking, the impacts we aim to make, and the outputs we deliver. It also shows that our work is underpinned by our organisational health and capability, which is achieved through a well-run OAG and Audit New Zealand.

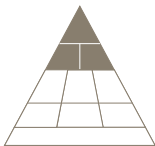
**Our assessment of achieving our outcomes**

Our overall assessment is that our outcomes were maintained or improved with:

- New Zealand maintaining its ranking in or above the 90th percentile of the Worldwide Governance Indicators in 2011;
- New Zealand’s 2011 Transparency International Corruption Perceptions Index score being 9.5 out of 10, which ranked New Zealand first in the world; and
- Maintained or improved results being shown in other measures as set out in the following pages.

Figure 2  
Outcomes framework



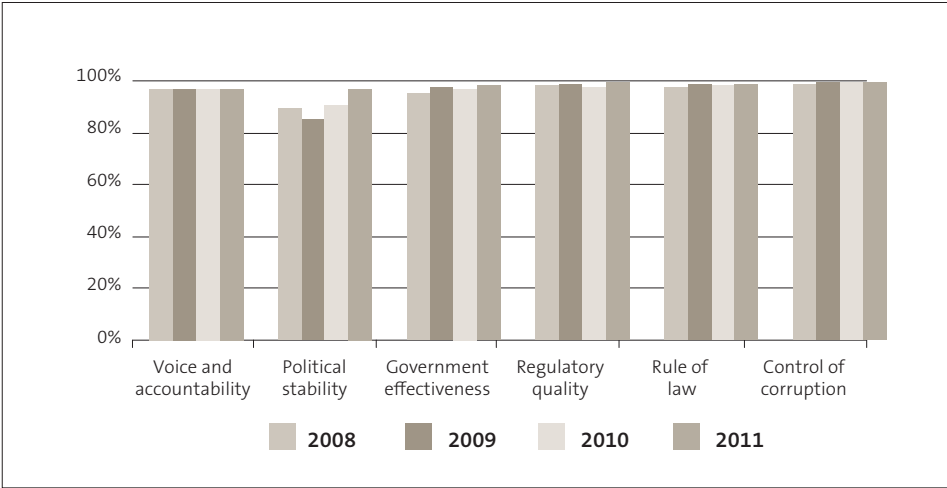


Outcome: Trusted public sector

**Measure:** New Zealand is ranked in or above the 90th percentile of the Worldwide Governance Indicators.

**Result: Achieved.** New Zealand maintained its ranking in 2011, with all Worldwide Governance Indicators above the 90th percentile.

Figure 3  
New Zealand’s ranking in the Worldwide Governance Indicators, 2008 to 2011

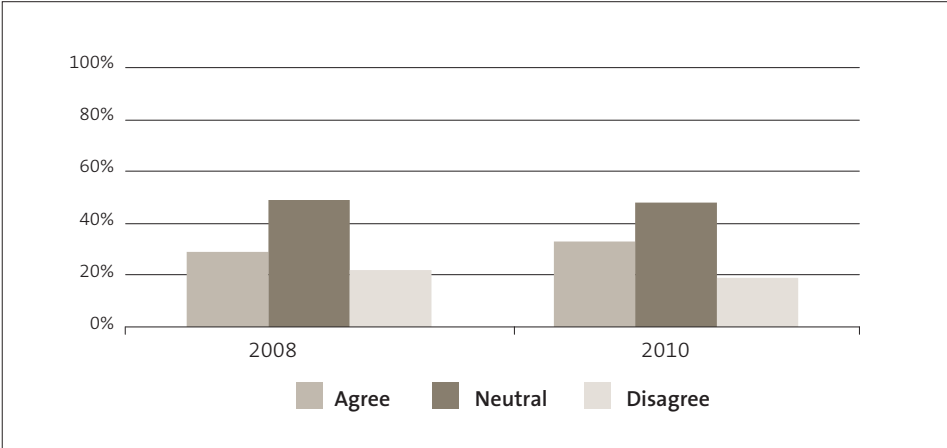


**Measure:** The State Services Commission’s biannual Kiwis Count Survey\* shows that the public’s confidence that public servants do a good job is improved (or at least maintained).

**Result: Achieved.** The most recent results available (2010) showed that the public’s confidence that public servants do a good job has improved.

\* Changes to Kiwis Count Survey methodology mean that 2012 results for this measure are not yet available.

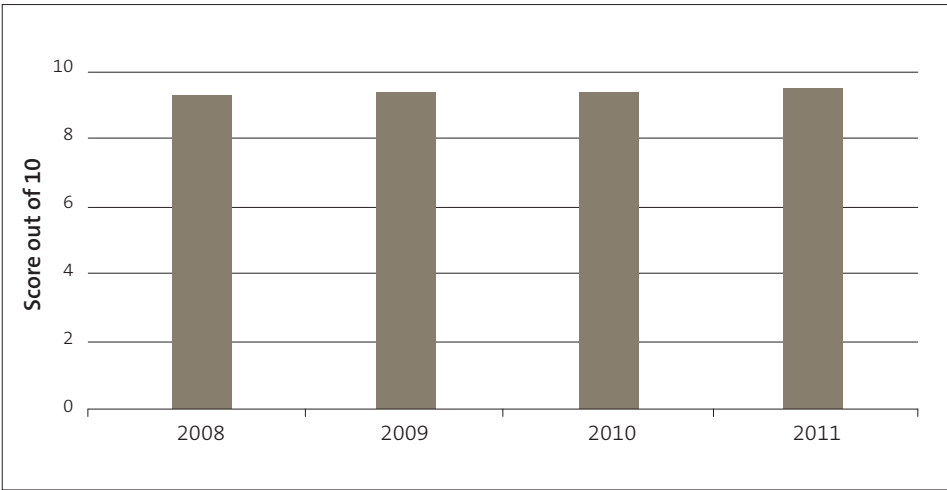
**Figure 4**  
Kiwis Count Survey results in 2008 and 2010: Public servants do a good job



**Measure:** New Zealand’s score on the Transparency International Corruption Perceptions Index is improved (or at least maintained).

**Result: Achieved.** New Zealand’s Transparency International Corruption Perceptions Index score was maintained in 2011.

**Figure 5**  
New Zealand’s score on the Transparency International Corruption Perceptions Index, 2008 to 2011





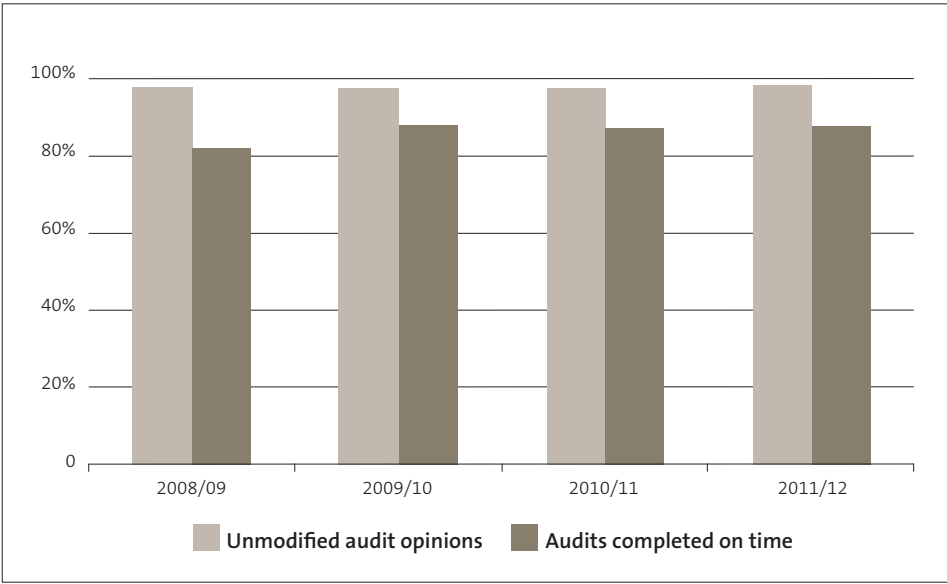
Outcome: Appropriately responsible public sector behaviour

**Measure:** Public entities’ financial reports fairly reflect their actual performance and are publicly available on time.

**Comment:** Responsible public entities provide public audited financial reports that are on time and fairly reflect their performance. Audits that are completed on time provide an indicator that public entities are well managed and meeting their reporting responsibilities. An unmodified audit opinion is an indicator that public entities are reporting appropriately and in accordance with standards.

**Result: Achieved.** 2011/12 results showed 98% of audit opinions were unmodified and 88% of audits were completed on time (percentages are rounded to nearest whole number).

**Figure 6**  
Percentage of unmodified audit opinions and audits completed on time



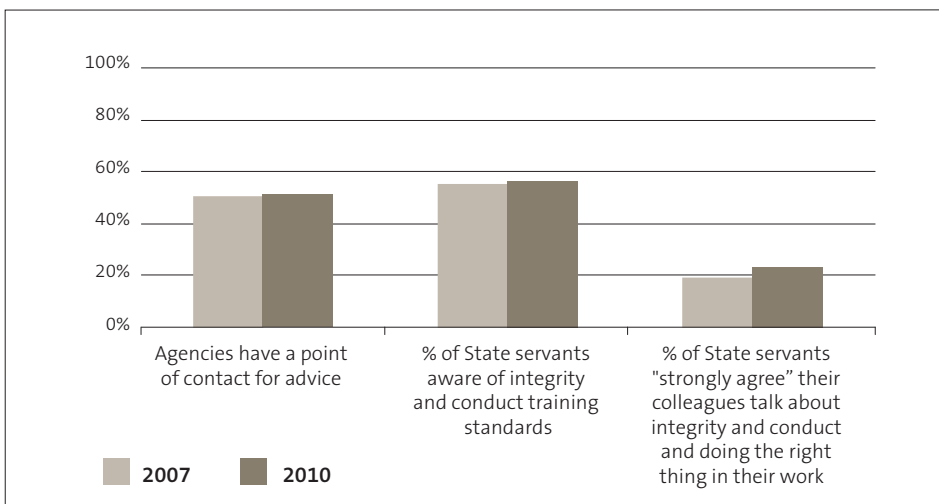
**Measure:** The State Services Commission's Integrity and Conduct Survey\* shows improved (or at least maintained) rates of State servants who reported that State service agencies promote their standards of integrity and conduct.

**Result: Achieved.** The most recent results available (2010) show improved rates of State servants who reported that State service agencies promote their standards of integrity and conduct.

\*This survey is held every three years, and results are published in calendar years.

**Figure 7**

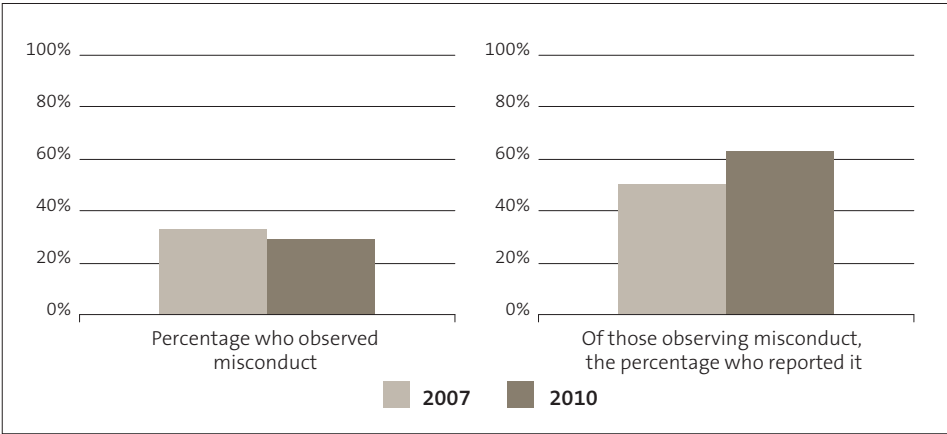
**Integrity and Conduct Survey results in 2007 and 2010: State service agencies that promote their standards of integrity and conduct**



**Measure:** The State Services Commission's Integrity and Conduct Survey shows improved (or at least maintained) rates of State servants who reported that, where they observed misconduct breaches in the past year, they reported it.

**Result: Achieved.** The most recent results available (2010) show improved rates of State servants who reported that, where they observed misconduct breaches in the past year, they reported it.

**Figure 8**  
Integrity and Conduct Survey results in 2007 and 2010: State servants’ observation and reporting of misconduct



Outcome: High-performing public sector

**Measure:** The State Services Commission’s biannual Kiwis Count Survey shows improved (or at least maintained) rates of public satisfaction with:

- their most recent public service experience; and
- public services experienced in the last year compared with non-government agencies.

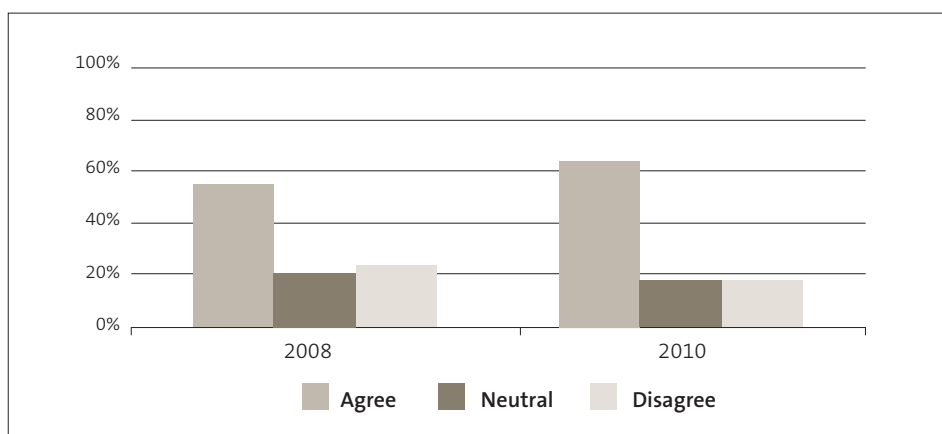
**Results:** Methodology changes in the Kiwis Count Survey between 2008 and 2012 mean that the results are not directly comparable. However, August 2012 results confirmed that the overall quality of service delivery had improved since 2009 with 27 services out of 42 improving, and 12 of those services showing significant improvements. No data was available on respondents’ ratings of experiences with public services with non-government agencies.

**Measure:** The State Services Commission's biannual Kiwis Count Survey shows improved (or at least maintained) rates of respondents reporting that their most recent public service experience was an example of good value for tax dollars spent.

**Result: Achieved.** The most recent results available (2010) show improved rates of respondents reporting that their most recent public service experience was an example of good value for tax dollars spent.

**Figure 9**

**Kiwis Count Survey results in 2008 and 2010: Most recent public service experience was an example of good value for tax dollars spent**



## Strategic risks and risk management

The Auditor-General faces four ongoing strategic risks. These risks are primarily managed through processes that support the work we do, as shown in Figure 10.

Throughout the 2011/12 year, the Office continued its focus on managing risks, particularly strategic risks. The leadership team discusses these quarterly, including assessing any environmental or internal changes that may affect the Office's position. The Audit and Risk Committee receives a report quarterly and provides additional insight and advice to the Office regarding the strategic risks. The Committee's own report for 2011/12 is on pages 21-22.

**Figure 10**  
Our strategic risks and risk management

Risk	Management
1. <b>Loss of independence</b> – independence underpins the value of the Auditor-General's work and reporting. Losing that independence in fact or appearance, whether by failure on the part of the Auditor-General, her staff, or her appointed auditors to act independently or otherwise, would undermine trust in our organisation.	<p>We manage this risk by applying the Auditor-General's independence standards. The Auditor-General sets a high standard for independence for her employees and the auditors she appoints to carry out audits on her behalf. Monitoring the independence standards, including for the two statutory officers and all employees, is carried out through a system that includes regular declarations of interest and, where necessary, implementing measures to mitigate conflicts of interest.</p> <p>Senior managers in the Office monitor and regularly assess any factors that may threaten auditor independence. We are satisfied that the Office has appropriate plans to reduce the effect of these factors to an acceptable level.</p>
2. <b>Audit failure</b> – the risk that we issue an incorrect audit opinion with material effect or a report that is significantly wrong in nature or process.	<p>The Auditor-General adheres to professional auditing standards, including implementing and complying with the revised quality control standards from the New Zealand Institute of Chartered Accountants and the External Reporting Board, supplemented by the Auditor-General's auditing standards to address public sector matters not covered by general auditing standards.</p> <p>We monitor adherence to auditing standards through external quality assurance regimes (such as participating in New Zealand Institute of Chartered Accountants' practice reviews and, from time to time, international peer reviews). Our internal quality control procedures include carrying out quality assurance reviews of all our appointed auditors and our Office products on a risk basis and to ensure reviews of all auditors and products over a three-year period.</p> <p>Before performance audits are presented to Parliament, a process of external report clearance and internal substantiation and review is observed.</p>
3. <b>Loss of capability</b> – the risk that we are unable to retain, recruit, or access people with the technical and other skills our audit work requires.	<p>We carry out ongoing training and development of our staff and our appointed auditors and their staff on matters necessary for audit work. We provide management programmes, leadership development initiatives, and professional development programmes for our own staff.</p>

4. **Loss of reputation** – the risk that we lose reputation or credibility that affects our ability to maintain effective relationships with stakeholders. This could arise either because of failings in one of the three risk areas listed above or because of external expectations and perceptions about the role of the Office or its findings on any particular matter that has been the subject of audit scrutiny. The Auditor-General’s discretionary mandate is broad, and it is inevitable that we will not meet all expectations.

Managing this risk requires the exercise of judgement about where to focus our audit effort and how best to report while also achieving the greatest likelihood of public sector improvement. There are a number of ways this risk is managed in our day-to-day work:

- the Office’s Combined Leadership Team meets on a regular basis to discuss issues and feedback from key stakeholders and public entities on our audit work;
- senior staff liaise with public entities and key stakeholders;
- we carry out regular stakeholder and client feedback surveys; and
- we monitor the media to identify where the Office could communicate more effectively about its role and the results of its audit work.

## Report of the Audit and Risk Committee for the year to 30 June 2012

### Members:

John Hagen MBA, MCom, FCA, *Investigating accountant*, Chairman (to 23 March 2012)

Fred Hutchings BBS, FCA, *Director*, Chairman (from 20 June 2012)

Kerry Prendergast MBA, NZRN, NZRM, CNZM, *Director*

Phillippa Smith BA, LLB, MPP, *Deputy Controller and Auditor-General*

Neil Walter MA, CNZM, *Director* (to December 2011)

The Audit and Risk Committee is an independent committee established by and reporting directly to the Auditor-General. The Committee was established in 2003 to oversee:

- risk management and internal control;
- audit functions (internal and external) for the Office;
- financial and other external reporting;
- the governance framework and processes; and
- compliance with legislation, policies and procedures.

The Committee has no management functions.

During the past year, the Committee:

- met on three occasions to fulfil its duties and responsibilities;
- received briefings from the Auditor-General and other senior managers on key business activities of the Office, as a basis for ensuring that risks facing the Office are being appropriately addressed;
- oversaw the Office's continuing review of its risk management framework and the procedures underpinning the framework;
- discussed with the external auditors their findings from their audit work;
- monitored the implementation of recommendations made by the external auditor;
- oversaw the internal auditor's development and implementation of an audit programme;

- received and considered the report on the internal audit of the payroll system; and
- reviewed the annual report and annual financial statements of the Office prior to their approval by the Auditor-General, having particular regard to the accounting policies adopted, major judgemental areas, and compliance with legislation and relevant standards.

The Committee has reported to the Auditor-General on the above and other matters it has seen fit to do so. There are no outstanding or unresolved concerns that the Committee has brought to the attention of the Auditor-General.

Fred Hutchings  
Chairman  
Audit and Risk Committee

14 September 2012



## Part 2

Our output classes, performance measures, and targets (including *Statement of service performance*)

## Introduction

### Achievement of our work programme

In our Annual Plan 2011/12, our work programme was set out in four main parts. Our achievements in three of those parts (annual audits; performance audits, inquiries, and other studies; and our contribution to the international auditing community and development of accounting and auditing standards) are set out in the output class performance information that follows on pages 24–58.

The fourth part was work we undertook in response to the challenge to the public sector of delivering effective and efficient public services in a fiscally constrained environment, and was carried out across our output classes as shown in Figure 11.

**Figure 11**

**Our work contributing to effective and efficient public service delivery**

We carried out work to	The work we did
Raise awareness of <b>risks that can arise from change</b> and how to manage them	<ul style="list-style-type: none"> <li>We prepared discussion papers on public-private partnerships and on financial management within government.</li> <li>We extensively reported the results of our survey of fraud in the public sector.</li> </ul>
Encourage better use of information to <b>support good decision-making</b>	<ul style="list-style-type: none"> <li>We reported our observations about the state of public entities' performance information and contributed these to the Treasury's work to review the Public Finance Act 1989.</li> </ul>
Provide <b>insight into local government</b>	<ul style="list-style-type: none"> <li>We prepared a report on improving the usefulness of annual reports in local government and reported on planning to meet the forecast demand for drinking water in Auckland.</li> </ul>
Provide <b>good analysis and reporting of information about the transport sector</b>	<ul style="list-style-type: none"> <li>We prepared an overview of our work in the transport sector and reported on the New Zealand Transport Agency's delivery of maintenance and renewal work on the state highway.</li> </ul>

Our published reports can be found on our website: [www.oag.govt.nz](http://www.oag.govt.nz). A list of the major reports completed during the year is included in Appendix 3.

## Output class: Audit and assurance services

The main purpose of an annual audit is to provide independent assurance about the fair disclosure of the financial information – and, in many instances, performance information – within annual reports. We also use our annual audits to gather information and knowledge about public entities to assist us in advising Parliament and other stakeholders, and to help determine our other work.

Public entities responding to their statutory public reporting obligations and to findings resulting from audits is fundamental to trust in the public sector. The approach of public entities to public reporting and their responses to audit recommendations help demonstrate their commitment to effective, efficient, and accountable service delivery.

In 2011/12, annual audits and other assurance services accounted for 88% of our total expenditure. The major portion of this output class relates to annual audits of public entities that are required by statute to be carried out.

### Key processes supporting annual audits

#### **Appointing auditors and monitoring audit fees**

The Auditor-General appoints auditors to carry out the annual audits of public entities. These auditors are appointed from a group that includes Audit New Zealand and private sector accounting firms. Most audits are allocated directly to an auditor, but from time to time an auditor is appointed to carry out an audit after a competitive tender.

We monitor audit fees to ensure that fees are fair to the public entities and also provide a fair return to the auditors for the work required by them to meet the Auditor-General's auditing standards.

During 2011/12, the Auditor-General appointed or reappointed auditors (except where a change of auditor was made within the same audit service provider) to conduct audits of 26 schools and 436 other public entities and their subsidiaries.

#### **Setting the Auditor-General's auditing standards**

Section 23 of the Public Audit Act 2001 requires the auditing standards of the Auditor-General to be published, by way of a report to the House of Representatives, "at least once every 3 years". *The Auditor-General's Auditing Standards* were most recently published in March 2011. These standards are available on our website ([www.oag.govt.nz](http://www.oag.govt.nz)).

No significant changes were made to the standards during 2011/12. We plan to amend the standards in 2012/13 to align them with the External Reporting Board standards. Responsibility for setting assurance standards transferred from the New Zealand Institute of Chartered Accountants to the External Reporting Board on 1 July 2011. We do not expect this alignment will result in any significant changes to the Auditor-General's auditing standards.

### **Maintaining auditor independence**

High independence standards are set for both the Auditor-General's employees and appointed auditors from private sector accounting firms. Compliance is monitored regularly, and any threats to auditor independence identified during the year were subject to mitigation actions that the Auditor-General considered appropriate to either eliminate the threats or reduce them to an acceptable level.

### **Quality assurance**

We carry out quality assurance reviews of appointed auditors to ensure that they have complied with the Auditor-General's auditing standards. We aim to review the performance of each of our appointed auditors at least once every three years. There are five levels of quality assurance rating: "excellent", "very good", "good", "satisfactory", and "re-review".

We also carry out reviews of each firm's quality control systems that are designed to provide assurance about the organisational factors that affect audit quality. We aim to complete these reviews at least once every three years in conjunction with our quality assurance reviews of appointed auditors.

## **Our performance in 2011/12**

We are generally pleased with results for **the impact** of our annual audits and other audits and assurance services this year. We note:

- a high percentage (88%) of audited financial statements being completed within statutory deadlines despite the disruption caused by the earthquakes, to both public entities and auditors alike;
- a low percentage (1.8%) of modified audit opinions being maintained;
- a high percentage (74%) of acceptance by public entities of our recommendations for improvement being maintained, with a small increase compared with the previous year (72%); and
- a high percentage of "good" or "very good" grades assigned to public entities' systems and controls being maintained for management control environment (93%) and financial information (94%), and an improving percentage for service performance information systems and controls (53% compared with 32% in the previous year).

The results for **carrying out** annual audits and other audits and assurance services show a less positive picture. We note:

- an increase in the number of audits in arrears (from 319 at 30 June 2011 to 348 at 30 June 2012), reflecting the 2011/12 year in which the audits of all local authorities' LTPs were carried out, creating resourcing pressures particularly for Audit New Zealand;
- a significant increase in the percentage of audit arrears being due to inaction on our part (42% compared with 20% in 2010/11), reflecting the resourcing issues noted above;
- a slight reduction in the timeliness of issuing management reports to public entities (93% compared with 94% in 2010/11) following the completion of our audits, against an ambitious target of 100%;
- a reduction in the level of client satisfaction as expressed by a sample of public entities, following a record high in 2010/11; the overall level of client satisfaction (83%) maintains a generally positive long-term trend;
- a reduction in the percentage of appointed auditors receiving a quality assurance grade of "satisfactory" or better (92% compared with 100% in 2010/11); and
- confirmation from an independent review that our processes for auditor appointments and audit fee monitoring have been carried out with due probity and objectivity.

### **2011/12 key developments**

During 2011/12, we continued:

- Supporting the change in standard-setting responsibility and approach of the new suite of public benefit entity accounting standards developed by the External Reporting Board (XRB);
- Supporting the work in phasing in the Auditor-General's revised auditing standard on reporting service performance information; and
- Our work on auditor regulation, now that all auditors of issuers are subject to regulation by the Financial Markets Authority (FMA). To protect the independence of the Auditor-General, audits of issuers carried out under the Public Audit Act 2001 are not subject to the new regulations. However, the Auditor-General intends to implement processes that are equivalent to (or as satisfactory as) the new regulations, including inviting the FMA to carry out quality reviews of issuer audits carried out on behalf of the Auditor-General.

### Independent review of audit allocation and fee setting and monitoring

- Our independent reviewer concluded that the processes by which we allocate audits in the public sector and set fees in the financial year to 30 June 2012 were carried out with due probity and objectivity. The full report is set out in Appendix 2.
- We completed a comprehensive review of audit allocation among the Auditor-General's audit service providers, including Audit New Zealand. Some audits have been reallocated among audit service providers during 2011/12, and further changes will be made as necessary to maintain alignment with the allocation model's key principles.

### Audit fees

- Fees were again affected by entity-specific issues in 2011/12. Some pressure on average charge-out rates resulted from auditors using a more senior team mix coupled with the return of some salary-driven pressure in the market for accountants and auditors.
- Figure 12 summarises the movements in audit fees from 2009/10 to 2011/12 based on the agreed audit fees at the time. It shows fee movement by sector and the effect of movements in audit hours and average hourly cost of carrying out audits.

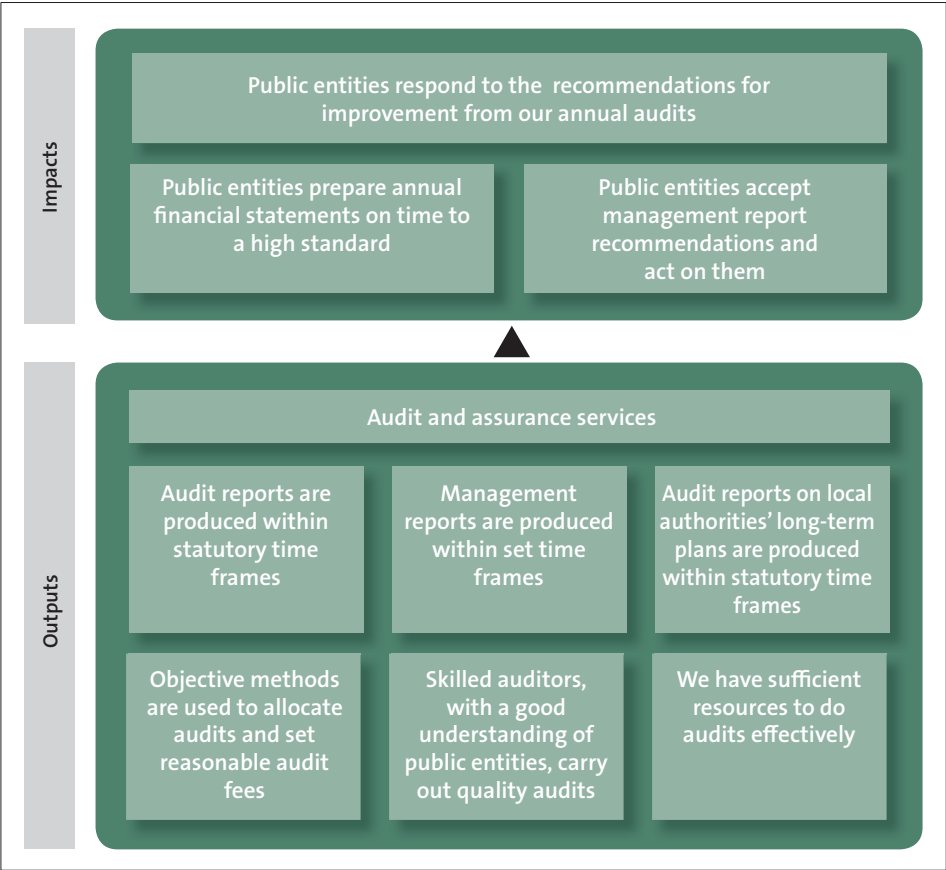
**Figure 12**

### Analysis of movements in audit fees

	2009/10 to 2010/11				2010/11 to 2011/12			
	Number of entities	Increase in total fee	Due to hours	Due to charge-out rate	Number of entities	Increase in total fee	Due to hours	Due to charge-out rate
Central government	350	4.2%	2.7%	1.5%	367	3.7%	2.4%	1.3%
Local government	370	3.2%	1.6%	1.6%	379	1.0%	0.2%	0.8%
Schools	2438	4.2%	1.0%	3.2%	2447	4.1%	0.6%	3.5%
<b>Total</b>	<b>3158</b>	<b>3.9%</b>	<b>2.0%</b>	<b>1.9%</b>	<b>3193</b>	<b>2.9%</b>	<b>1.4%</b>	<b>1.5%</b>



**Figure 13**  
Summary of impacts and outputs for Audit and assurance services



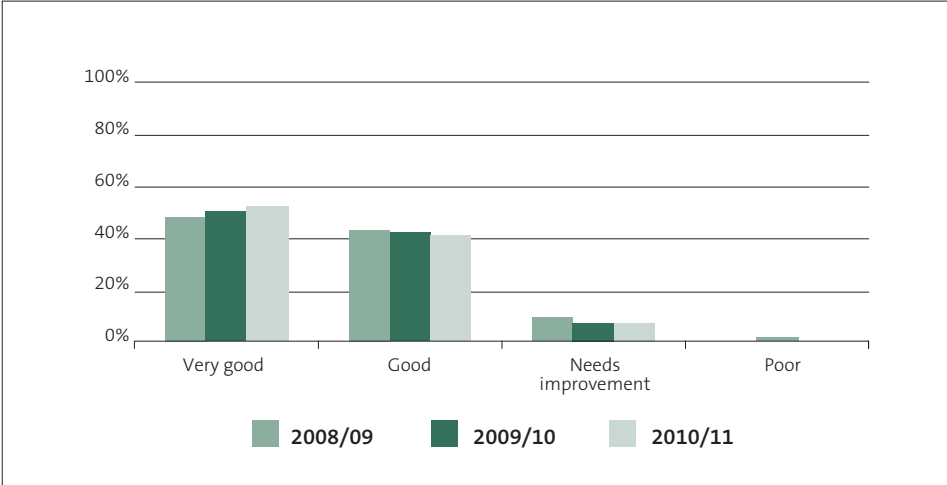
Impact: Public entities respond to the recommendations for improvement from our annual audits

**Measure:** Central government entities’ management control environment (MCE), financial information systems and controls (FISC), and service performance information and associated systems and controls (SPIASC) are improved (or at least maintained), measured against the previous two years.

**Comment:** We aim to contribute to improved financial and service performance reporting and improved performance management in public entities. We report our observations to entities on their MCE, FISC, and SPIASC, and assign grades accordingly: Very good, Good, Needs improvement, or Poor. Movements in the grades provide an indication of whether entities are accepting and responding to our recommendations, and improving their performance. 2011/12 results will not be available until November 2012.

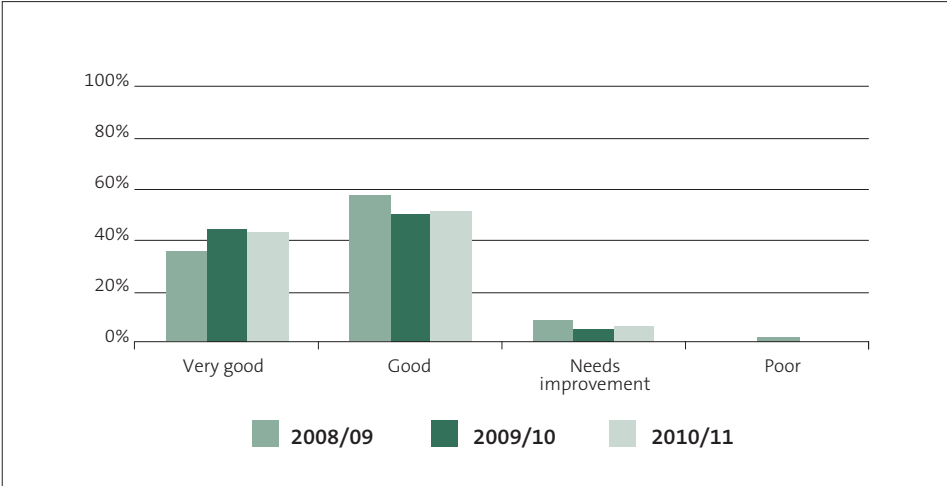
**Result: Achieved.** MCE, FISC, and SPIASC results (2010/11) show that, overall, these grades showed slight improvement measured against the previous two years.

Figure 14  
Grades for management control environment (MCE), 2008/09, 2009/10, and 2010/11

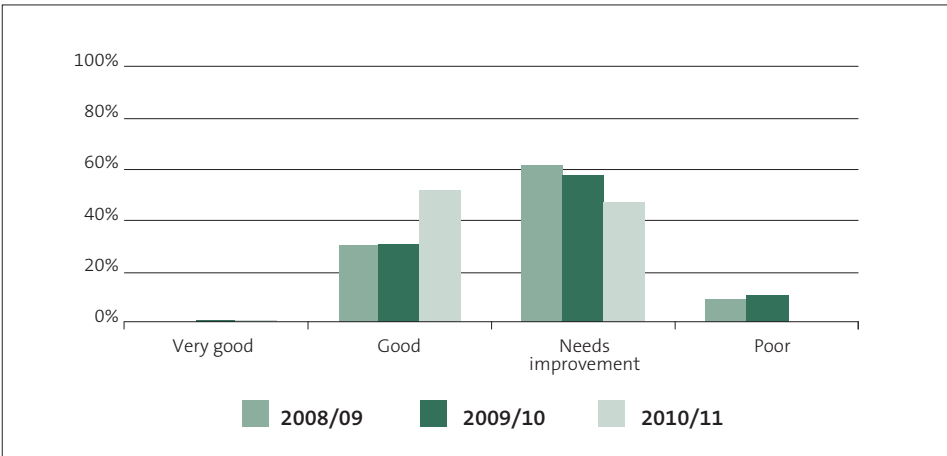




**Figure 15**  
Grades for financial information systems and controls (FISC), 2008/09, 2009/10, and 2010/11



**Figure 16**  
Grades for service performance information and associated systems and controls (SPIASC), 2008/09, 2009/10, and 2010/11



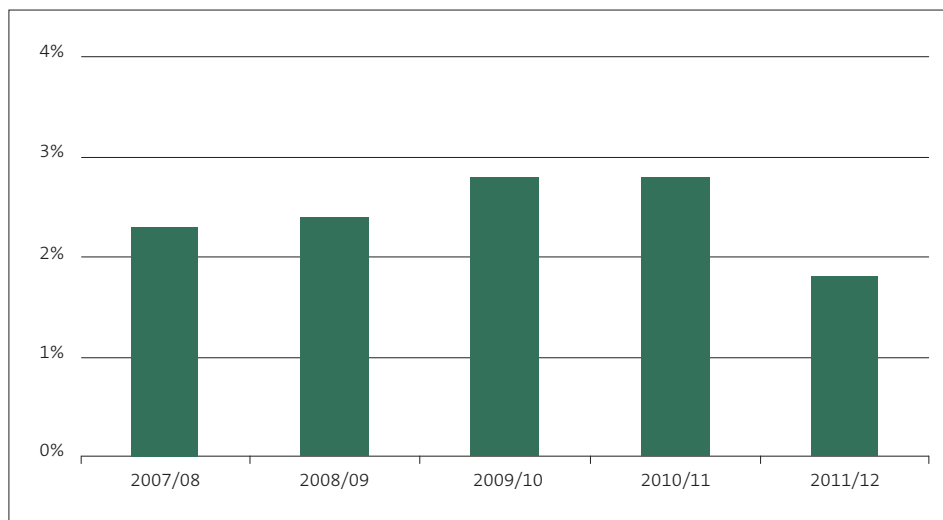
### Impact: Public entities prepare annual financial statements on time to a high standard

**Measure:** The percentage of public entities' audited financial reports containing modified audit opinions is reduced (or at least maintained), measured against the previous two years.

**Result: Achieved.** The percentage of public entities' audited financial reports containing modified audit opinions was reduced measured against the previous two years with an actual result of 1.8%.

**Figure 17**

Percentage of audited financial reports that contain modified audit opinions



Impact: Public entities accept management report recommendations and act on them

**Measure:** Public entities’ acceptance of audit service providers’ management report recommendations is improved (or at least maintained), measured against the previous two years.

**Comment:** For the year ended 30 June 2012, a sample of 40 entities with audit fees greater than \$50,000 were assessed against this performance measure. Before 2011, this was only assessed against a sample of Audit New Zealand’s management report recommendations.

**Result: Partially achieved.** The percentage of management report recommendations accepted by public entities was improved measured against the previous year’s results. Actual results: Accepted 74%, Rejected 8%, Noted or not responded to 18%.

Figure 18  
Percentage of management report recommendations accepted by public entities



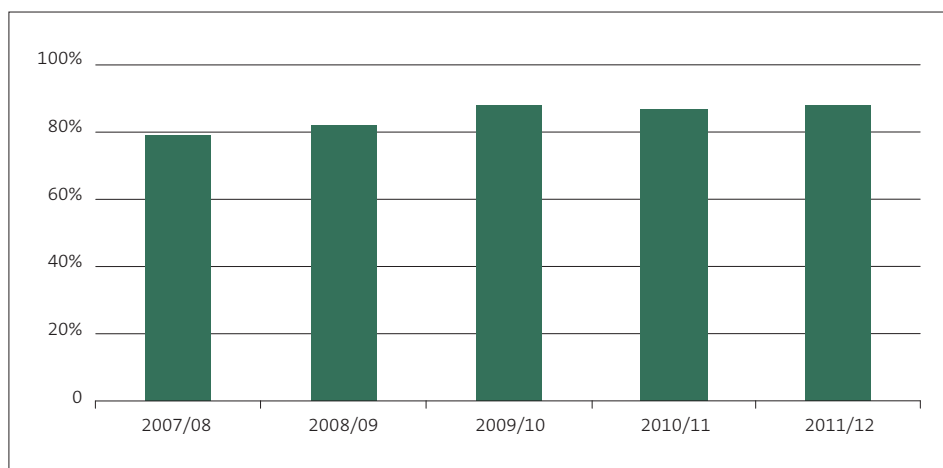
### Output: Audit reports are produced within statutory time frames

**Measure:** The percentage of public entities' audited financial reports issued within the statutory time frame is improved (or at least maintained), measured against the previous two years.

**Result: Achieved.** The percentage of public entities' audited financial reports issued within the statutory time frame was maintained with an actual result of 88%.

**Figure 19**

Percentage of audited financial reports issued on time

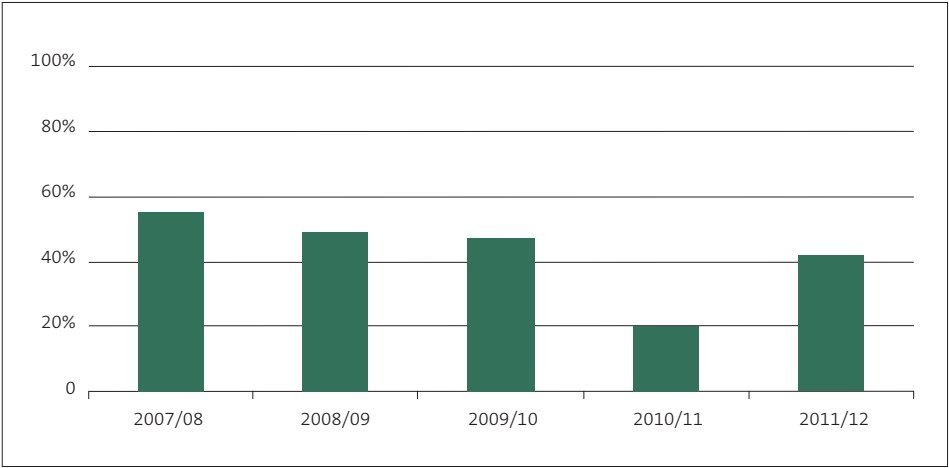


**Measure:** Less than 30% of the outstanding audit reports at 30 June are because of inaction on our part.

**Result: Not achieved.** The percentage of outstanding audit reports at 30 June because of inaction on our part was 42%.

**Comment:** Total arrears at 30 June 2012: 348, compared with 319 at 30 June 2011.

**Figure 20**  
Percentage of outstanding audit reports at 30 June because of our inaction

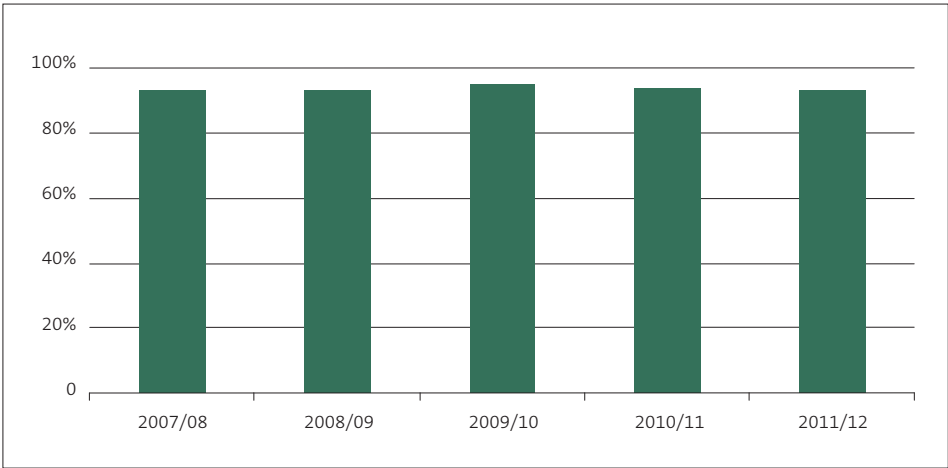


Output: Management reports are produced within set time frames

**Measure:** All management reports are issued within six weeks of issuing the audit report.

**Result: Not achieved.** 93% of management reports were issued within six weeks of issuing the audit report.

**Figure 21**  
Percentage of management reports issued within six weeks



### Output: Audit reports on local authorities' long-term plans are produced within statutory time frames

**Measure:** No outstanding long-term plan (LTP) audit opinions at 30 June of the year in which LTPs are to be adopted by local authorities are because of inaction on our part.

**Result: Achieved.** No outstanding LTP audit opinions at 30 June because of inaction on our part.

**Comment:** LTP audits are carried out on a three-yearly basis, and this year we report on our involvement in the 2012-22 LTP audits.

For the 2012-22 LTPs, 94% of local authorities adopted their final LTP within the statutory deadline. Christchurch City Council obtained a one-year extension of time because of the Canterbury earthquakes, and, of the remaining four local authorities that completed their responsibilities after 30 June, all have now adopted their final LTPs. The work was intensive, particularly from February to June 2012. It dominated the workload of our audit service providers, and was a factor in some deteriorating performance in our annual audit commitments during that period.

**Measure:** All LTP management reports are issued within six weeks of issuing the LTP audit opinion.

**Result: Not achieved.** 82% of management reports were issued within six weeks of issuing the LTP audit opinion.

### Output: Objective methods are used to allocate audits and set reasonable audit fees

**Measure:** An annual independent review of our processes confirms the probity and objectivity of the methods and systems we use to allocate and tender audits, and monitor the reasonableness of audit fees.

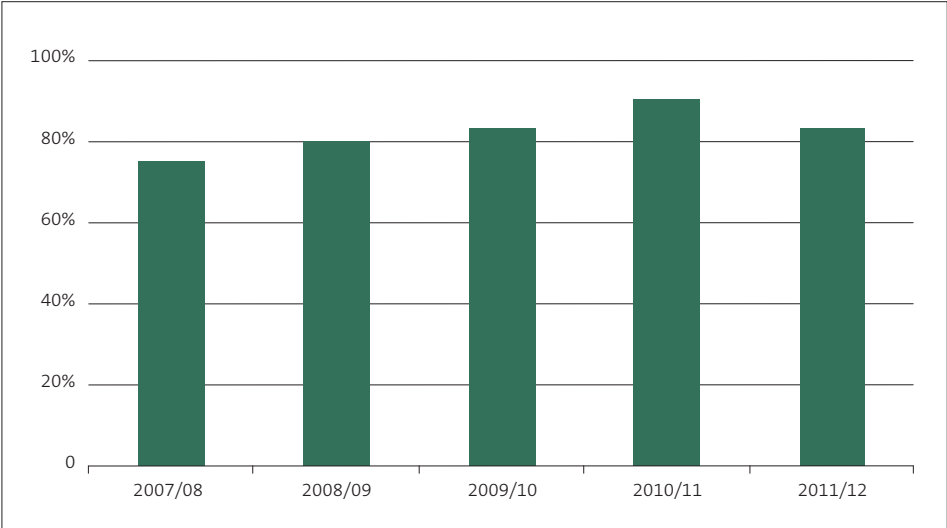
**Result: Achieved.** The 2011/12 review confirmed that we achieved this measure. See Appendix 2.

Output: Skilled auditors, with a good understanding of public entities, carry out quality audits

**Measure:** Client satisfaction survey results show that, overall, 75% of respondents are satisfied with the quality of audit work (including the expertise of staff and the quality of the public entity’s relationship with their audit service provider).

**Result: Achieved.** Overall, 83% of respondents were satisfied with the quality of audit work.

Figure 22  
Percentage of clients satisfied with the quality of audit work



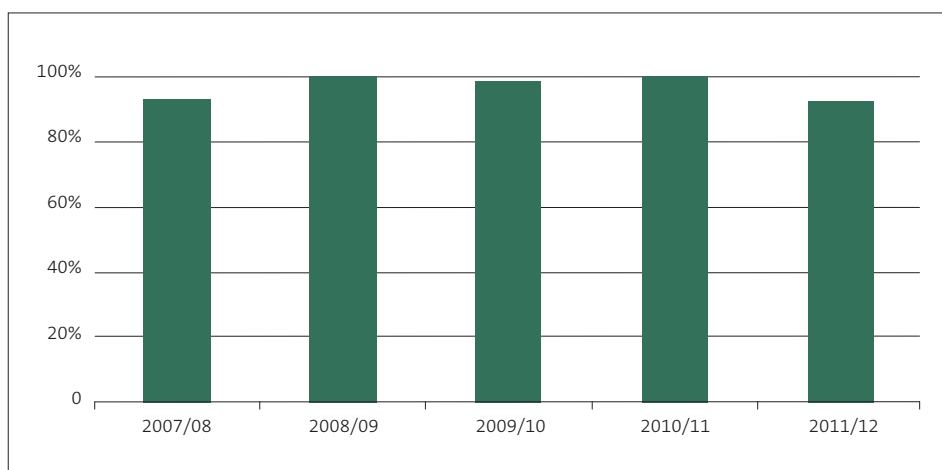
**Measure:** Quality assurance reviews for all appointed auditors are completed during a three-year period. Of the auditors reviewed in any given year, 100% achieve a grade of “satisfactory” or better.

**Comment:** This measure also appeared in the Organisational Health and Capability section of our *Annual Plan 2011/12*. It was removed from that section to avoid unnecessary duplication of results.

**Result: Not achieved.** 92% of auditors achieved a grade of “satisfactory” or better.

**Figure 23**

Percentage of auditors achieving a grade of satisfactory or better from quality assurance reviews



### Output: We have sufficient resources to do audits effectively

**Measure:** The Officers of Parliament Committee accepts any significant proposals for an appropriation increase in audit fees and expenses.

**Result:** No significant proposal was made in 2011/12 for an increase in appropriation for audit fees and expenses.

**Figure 24**

Financial performance of output class: Audit and assurance services

	2011/12 Actual \$000	2011/12 Supp. Estimates \$000	2010/11 Actual \$000	2009/10 Actual \$000
<b>Income</b>				
Crown	150	150	150	150
Other	71,644	70,485	65,194	63,939
<b>Expenditure</b>	(70,729)	(70,635)	(65,043)	(62,736)
<b>Surplus/(Deficit)</b>	<b>1,065</b>	<b>0</b>	<b>301</b>	<b>1,353</b>



## Output class: Supporting accountability to Parliament

This output class includes two outputs:

- Services to Parliament – providing advice and assistance to select committees and other stakeholders; and
- Controller function – carrying out the Controller function.

### Services to Parliament

We provide advice and assistance to Parliament through:

- reports and advice to select committees to assist their financial reviews of government departments and Offices of Parliament, State-owned enterprises, and some Crown entities;
- reports and advice to select committees to assist their examination of the Estimates of Appropriations;
- reports to responsible Ministers on the results of the annual audits; and
- reporting to Parliament and other stakeholders on matters arising from our annual audits.

### Contributing to the international auditing community

In 2011/12, the OAG hosted a range of international delegations providing opportunities to exchange information and build networks internationally. We were pleased to assist colleagues from the State Audit Offices of India and Vietnam, the Board of Audit and Inspection of Korea, and the Australian National Audit Office, as well as visitors from the Malaysian Accountant General, the Chief Information Commissioner, India, and representatives from Ministries of the Republic of Korea.

We continued to support the promotion of transparent, accountable, effective and efficient use of public sector resources in the Pacific through our role as the current Secretary-General of the Pacific Association of Supreme Audit Institutions (PASAI), and the Auditor-General's representation of the PASAI region on the governing board of the International Organisation of Supreme Audit Institutions (INTOSAI). 2011/12 was the first year of our five-year funding agreement with the Ministry of Foreign Affairs and Trade, which has enabled our Office to provide significantly more support and expertise in the Pacific.

We are members of various committees of INTOSAI, including the Professional Standards Steering Committee. This year, we were involved in chairing two working groups tasked with developing guidance for supreme audit institutions. One of these working groups is developing a new INTOSAI standard on the value and benefits of Supreme Audits Institutions (SAIs) which sets out ways that SAIs can add value through carrying out their own work.

### **The Controller function**

The Controller function of the Controller and Auditor-General provides independent assurance to Parliament that the expenses and capital expenditure of government departments and Offices of Parliament have been incurred for purposes that are lawful and within the scope, amount, and period of the appropriation or other authority.

The OAG and appointed auditors carry out standard procedures to give effect to the Controller function in keeping with the Auditor-General's auditing standards and a Memorandum of Understanding with the Treasury. This involves reviewing monthly reports provided by the Treasury, and advising the Treasury of any issues arising and the action to be taken.

Each year, we report to Parliament on the significant issues arising from the operation of the Controller function.

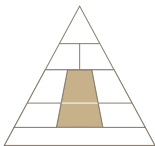
### **Our performance in 2011/12**

Our results for this output class show that our work continues to play an important part in supporting accountability to Parliament. This is pleasing, given the continuing high demand for advice to select committees: in 2011/12 we provided advice in support of 95 financial reviews and 47 Estimates examinations (90 and 53 in 2010/11).

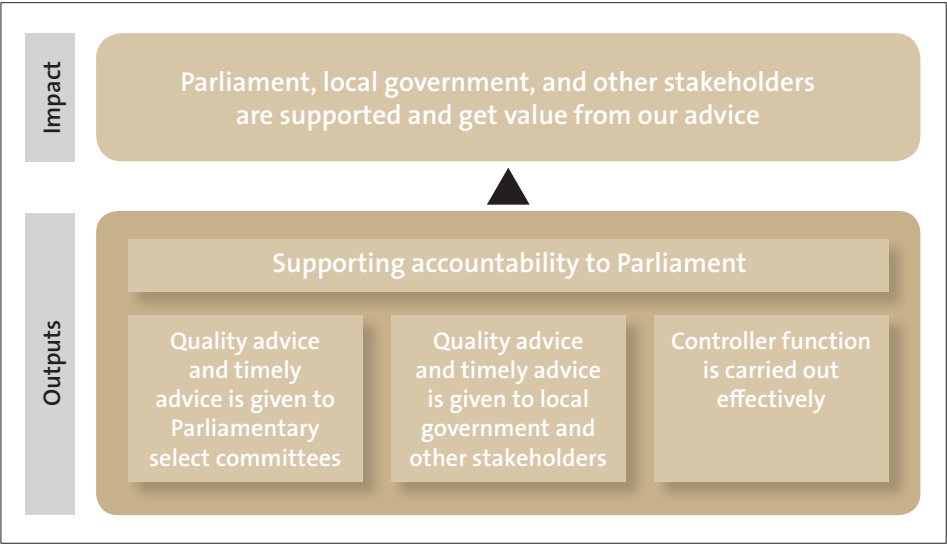
Our stakeholder feedback confirms that the Office is continuing to perform at a high level, with stakeholders valuing the professional and impartial advice and guidance that they receive from us. Our feedback from select committee chairs indicates that the sector knowledge and relationship management skills of our staff are highly valued.

Select committee members continue to value the quality and usefulness of our advice – 89% of members surveyed agree that the Office’s advice assists in their Estimates of Appropriation and financial review examinations, up from 86% in the previous year. The percentage of members who rate the quality of our advice as 4 or better on a scale of 1 to 5 has increased from 86% to 100%. The percentage of members who rate the usefulness of that advice against the same scale has decreased from 86% to 78%. We saw an increase in the rating of other stakeholders for the relevance and usefulness of our advice on a scale of 1 to 5 from 75% to 80%. The small number of stakeholders we survey does lead to significant shifts in percentage terms from year to year.

Our stakeholders told us that they would like us to engage more systematically with them, and to provide more information about the Office’s broader and longer-term plan of work, including our expectations and priorities. This feedback aligns with our work on developing a more strategic approach to our work programme planning. We are continuing with initiatives to take more of a sector approach to our work and reporting, and we will produce new sector-specific reports in 2012/13.



**Figure 25**  
Summary of impact and outputs for Supporting accountability to Parliament

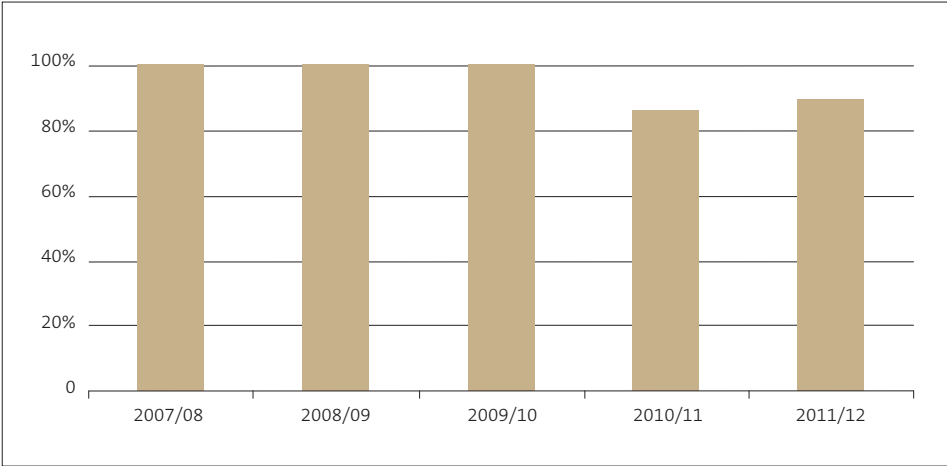


**Impact:** Parliament, local government, and other stakeholders are supported and get value from our advice

**Measure:** At least 85% of select committee members confirm that our advice assists them in Estimates of Appropriation and financial review examinations.

**Result: Achieved.** 89% of select committee members confirmed that our advice assists them in Estimates of Appropriation and financial review examinations.

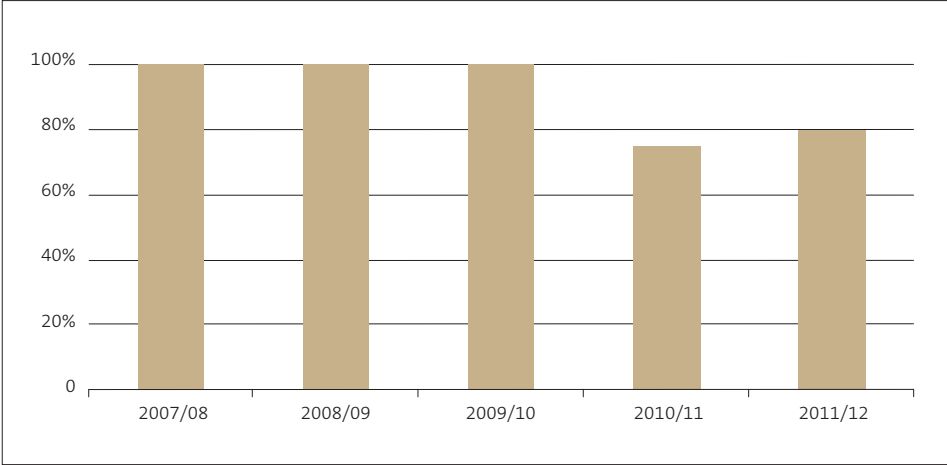
**Figure 26**  
Percentage of select committee members who confirmed that our advice assists them in Estimates of Appropriations and financial review examinations



**Measure:** At least 85% of other stakeholders we survey rate the advice they receive from us as 4 or better on a scale of 1 to 5 for relevance and usefulness.

**Result: Not achieved.** 80% of other stakeholders we survey rate the advice they receive from us as 4 or better on a scale of 1 to 5 for relevance and usefulness.

**Figure 27**  
Percentage of other stakeholders who rated our advice as 4 or better on a scale of 1 to 5 for relevance and usefulness



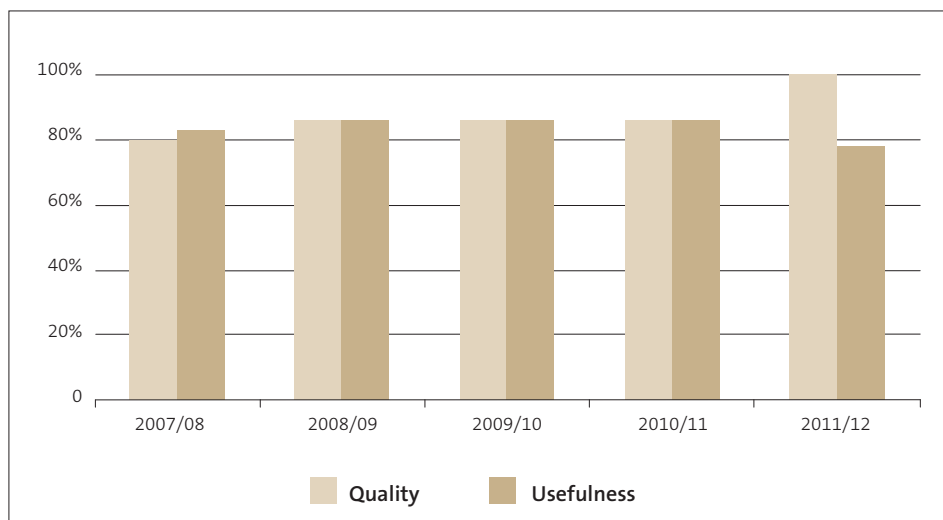
### Output: Quality advice and timely advice is given to Parliamentary select committees, local government and other stakeholders

**Measure:** At least 85% of select committee members we survey rate the advice they receive from us as 4 or better on a scale of 1 to 5 for quality and usefulness.

**Result: Partially achieved.** 100% of select committee members rated the advice they receive from us as 4 or better for quality, and 78% rated the advice they receive from us as 4 or better for usefulness.

**Figure 28**

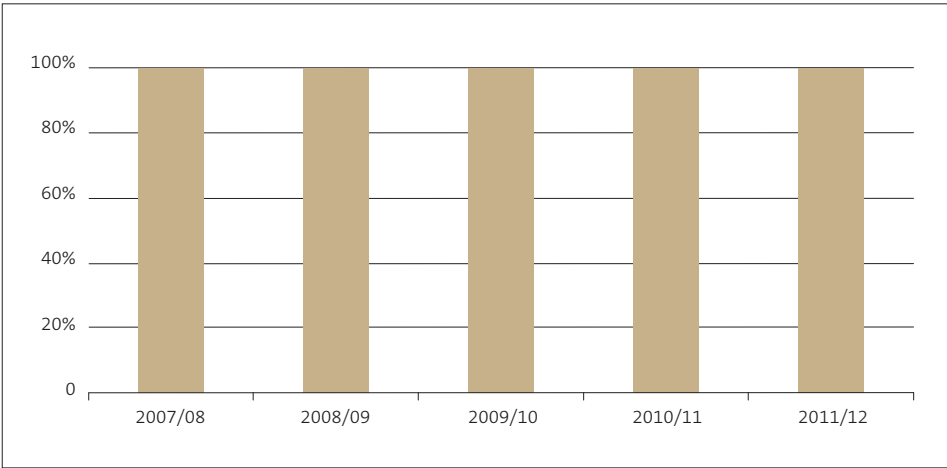
Percentage of select committee members who rated our advice as 4 or better on a scale of 1 to 5 for quality and usefulness



**Measure:** Reports and advice are given to select committees and Ministers at least two days before an examination, unless otherwise agreed.

**Result: Achieved.** 100% of reports and advice were given to select committees and Ministers at least two days before examination.

**Figure 29**  
Percentage of reports and advice given to select committees and Ministers at least two days before an examination, unless otherwise agreed



**Measure:** An internal quality assurance review of a sample of financial review, Estimates of Appropriations, and Ministerial reports confirms that they meet relevant standards and procedures, including that reports are consistent in their framework and approach, and are peer-reviewed in draft.

**Comment:** A review is carried out at least once every three years. The nature, extent, and frequency of those reviews are based on risk.

**Result:** No review was considered necessary in 2011/12. A review carried out in 2010/11 confirmed that the appropriate systems were in place and operated effectively.

Output: Controller function is carried out effectively

**Measure:** Internal quality assurance is carried out to gain assurance that our policies, procedures, and standards for the Controller function have been applied appropriately.

**Comment:** A review is carried out at least once every three years. The nature, extent, and frequency of those reviews are based on risk.

**Result: Achieved.** An internal quality assurance review in June 2012 confirmed that our policies, procedures, and standards for the Controller function were applied appropriately.

**Measure:** Monthly statements provided by the Treasury are reviewed for the period September to June inclusive. Advice of issues arising and action to be taken is provided to the Treasury and appointed auditors within five working days of receipt of the statement.

**Result: Achieved.** All monthly procedures were followed and agreed time frames achieved.

**Figure 30**  
Financial performance of output class: Supporting accountability to Parliament

	2011/12 Actual \$000	2011/12 Supp. Estimates \$000	2010/11 Actual \$000	2009/10 Actual \$000
Income				
Crown	2,760	2,760	2,460	2,460
Other	174	245	0	0
Expenditure	(3,047)	(3,005)	(2,442)	(2,342)
Surplus/(Deficit)	(113)	0	18	118

### Output class: Performance audits and inquiries

The Public Audit Act 2001 allows the Auditor-General to carry out performance audits and to inquire into a public entity’s use of its resources. Our performance audit and inquiries work allows the Auditor-General to consider and provide advice about matters in greater depth than is possible within the statutory scope of an annual audit.

**Performance audits** are significant and in-depth audits covering issues of effectiveness and efficiency. The issues examined by performance audits are independently selected by the Auditor-General. We plan our work programme carefully, to provide Parliament with assurance about an appropriate range of specific issues or programmes, and how well these are managed by the relevant public entity or entities.

By contrast, our **inquiries** work largely reacts to issues of current public concern. We usually receive 200 to 300 requests for inquiries annually, spanning a wide range of concerns about central and local government entities. Most are dealt with through routine correspondence, but each year there are some that require significant work. If there is general public interest in an inquiry, we will usually publicly report the results. The Auditor-General also administers the Local



Authorities (Members' Interests) Act 1968, which regulates pecuniary interest questions in the local government sector. Each year, we usually receive 50 to 100 requests under that Act.

We also do **other studies** that result in published reports and good practice guidance on topical issues of public sector accountability and performance.

Through our performance audits, inquiries, and other studies, we seek to identify good or emerging practices, raise any concerns, and recommend ways that a public entity can perform better, as appropriate. Our reports have benefits for the audited entities and for the wider public sector, and our work encourages:

- beneficial changes and good practice in the performance of public entities;
- development of better methods to evaluate aspects of public sector management; and
- increased understanding of an audited entity, of the wider environment in which public entities operate, and/or of public sector management.

## Our performance in 2011/12

### Reports on performance audits, other studies, and major inquiries

In 2011/12, we completed a range of reports on matters arising from performance audits, other studies, and major inquiries. These reports are listed in Appendix 3, and copies are available on our website ([www.oag.govt.nz](http://www.oag.govt.nz)).

Our published reports encourage ongoing high performance and performance improvement across the public sector. They highlight complexities to be managed, factors underpinning good decision-making and success, and make recommendations for improvement, where appropriate.

### Quality and usefulness of our reports

Each year, we seek the views of a small sample of select committee members and other stakeholders on the quality and usefulness of our published performance audit reports. This year we are pleased that 93% of stakeholders surveyed highly rated the **quality** of our performance audits, with our target being 85%. We were disappointed that the proportion of stakeholders highly rating the **usefulness** of performance audit reports has dropped in the last two years, falling to 62% this year, well below our 85% target. In 2012/13, our intention is to better understand the decrease in usefulness rating, and to consistently meet or exceed our 85% target for quality and usefulness in the future.

Each year, two of our performance audit reports are independently reviewed. Reviewers rate the reports on a scale from 1 (low quality) to 5 (top quality) against a set of review criteria, and also give an overall rating. Our reports were rated highly for quality (just less than 4), and common strengths such as strong overviews putting across key messages, and well-formulated, appropriate, and realistic recommendations were noted. Our 2012 report ratings are however slightly lower than for previous years' reports, and we are committed to improving the quality of our reports by addressing the improvement areas identified.

### **Progress in acting on our recommendations**

We regularly report on the progress public entities have made in acting on our performance audit reports' recommendations. Our May 2012 report on *Public entities' progress in implementing the Auditor-General's recommendations 2012* showed that good progress had been made in implementing most recommendations. Slow progress in some areas reflected changes in policy direction, unforeseen difficulties in implementing new technology or lack of co-ordination, planning and information sharing between agencies.

We were also pleased that public entities not directly involved in our audits had used the reports' lessons and recommendations. Many city and district councils, for example, were using our audit framework to assess and strengthen how they forecast demand for drinking water.

Our inquiries' work has contributed to positive change, helping people understand what public entities are doing by providing an independent and detailed description of what has happened, assurance over the proper use of public resources, and highlighting areas where change is needed. We were very pleased, for example, that many concerns raised in our report, *How the Department of Internal Affairs manages spending that could give personal benefit to Ministers* (December 2010), were addressed in the development of the Members of Parliament (Remuneration and Services) Bill, introduced in October 2011. We have also monitored the Department's implementation of significant administrative improvements.

### Progress with completion of our 2011/12 Annual Plan

Figure 31 lists work from our 2011/12 Annual Plan that has been completed since 30 June 2012, or will be completed in 2012/13.

#### Figure 31

##### Work in progress from our 2011/12 Annual Plan

1	Response of the New Zealand Police to the Commission of Inquiry into Police Conduct: Third monitoring report (to be presented to the House of Representatives in October 2012)
2	Road safety: Enforcement efforts to reduce drink-driving
3	Effectiveness of arrangements to check the standard of rest homes services: Follow-up report (presented to the House of Representatives on 18 September 2012)
4	Biosecurity: Preparedness for, and response to, incursions from unwanted organisms
5	Protecting and maintaining our biodiversity and natural ecosystems
6	Education for Māori: Context for our proposed audit work until 2017 (presented to the House of Representatives on 14 August 2012)
7	Further work to meet the statutory requirement that the Auditor-General review the service performance of Auckland Council and its council controlled organisations.

Work deferred from our 2011/12 Annual Plan, including an audit of a specific defence acquisition project and/or an audit of the defence acquisition process, and School Governance: How well school boards of trustees plan and review for student achievement, will be considered as potential topics for future work programmes.

### The relevance and usefulness of our work programme

Our 2012/13 work programme is focused on the question: *Our future needs – is the public sector ready?* We chose this theme as a result of extensive consultation carried out in 2011/12. We consulted with Parliament and other stakeholders, receiving support for our theme and helpful advice that assisted us to clarify the scope of some of our proposed specific performance audits and other studies.

### Inquiries

During 2011/12 we received 227 new requests for inquiries and 54 requests on Local Authorities (Members' Interests) Act matters. We had carried forward a total of 17 requests from the previous year, and ended this year carrying forward 33 requests. In terms of workflow, we usually have about 20 inquiry matters open at any point in time.

**Figure 32**  
Number and type of inquiries completed

Inquiry type	2011/12	2010/11	2009/10	2008/09	2007/08
Major	2	3	5	2	0
Significant	4	10	16	11	11
Routine	204	144	182	99	115
No inquiry	2	41	66	142	116
LAMIA*	54	91	80	53	110
Total	266	289	349	307	354

\* Local Authorities (Members' Interests) Act 1968.

Our inquiries function enables us to react to issues of current public concern, and is inevitably reactive. In publishing terms, 2011/12 appeared relatively quiet. We did not produce any inquiry reports that warranted tabling in Parliament and published only two inquiry reports on our website:

- *Inquiry into the use of parliamentary travel entitlements by Mr and Mrs Wong* (September 2011); and
- *Inquiry into how Christchurch City Council managed conflicts of interest when it made decisions about insurance cover* (April 2012).

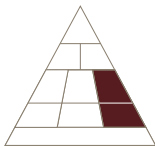
However, the year was still busy. We dealt with a large number of routine matters that required careful work, and we also had several significant matters “open” in our system for an extended period of time while we monitored steps that were being taken elsewhere on the various issues.

The last few months of 2011/12 were marked by a large number of high profile requests to inquire into matters of public concern. By the end of the year we had announced four new major inquiries, and we were close to completing one other major inquiry. We were also considering an unusually high number of requests on other matters of significant public interest. The level of public interest in our inquiry work is prompting us to review how we interact with the media on matters of current public interest.

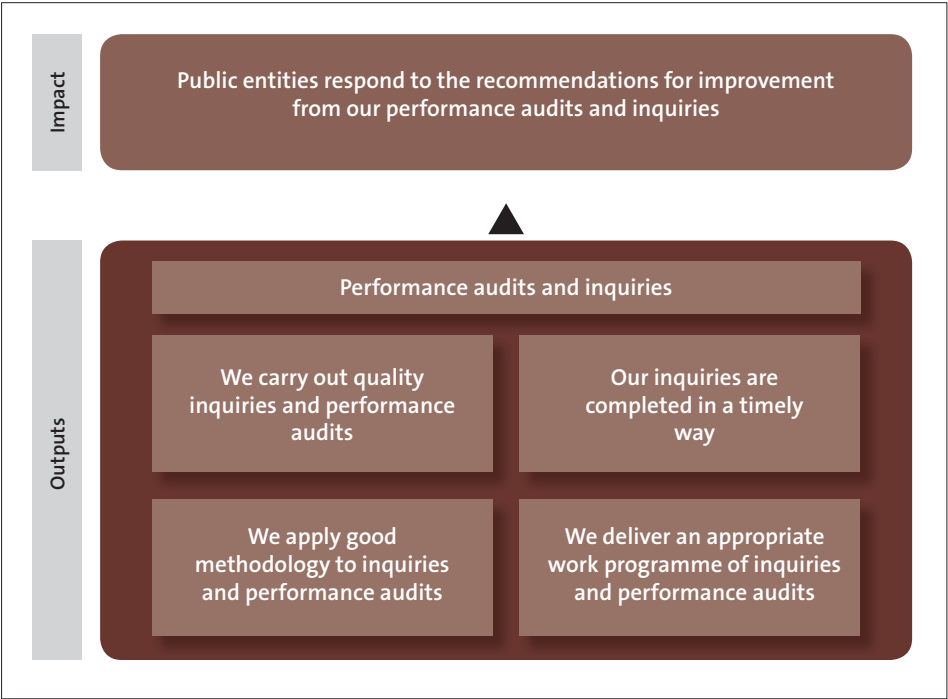
Matters resulting in “no inquiry” have dropped to two this year. This change shows the results of the work carried out in the last year to provide better public information on our inquiries work, to help people understand what issues we can and cannot look at, and to improve our basic processes for receiving and managing requests efficiently. We now have more effective systems for ensuring that we focus our effort on matters that are appropriate.

**The Local Authorities (Members' Interests) Act 1968**

We responded to requests on 54 matters relating to this Act in 2011/12. No particular issues warrant comment this year. We provided a comprehensive submission to the Department of Internal Affairs in response to its discussion paper on options for reform of the Act, but the review does not appear to have progressed further.



**Figure 33**  
Summary of impacts and outputs for Performance audits and inquiries



**Impact:** Public entities respond to the recommendations for improvement from our performance audits and inquiries

**Measure:** Entities accept or respond to the recommendations made in the reports on our performance audits.

**Comment:** Each year, we review how entities have responded to a selection of our reports and present the results to Parliament in our annual follow-up report.

**Result: Achieved.** In May 2012, we reported to Parliament on how well public entities had acted on the recommendations that we made in six performance audit reports published in 2009 and 2010. Our report *Public entities' progress in implementing the Auditor-General's recommendations 2012* showed good progress had been made in implementing most recommendations.

**Measure:** Entities take action in response to concerns identified in inquiry reports, as assessed by follow-up on a sample of sensitive and major inquiries carried out in the previous year.

**Results: Achieved.** In 2011/12, we followed up on three major inquiry reports. In two cases, our recommendations provided the basis for major change programmes that have progressed well over the last year. In one case, our recommendations were accepted in principle and the issues were incorporated into broader work on organisational change.

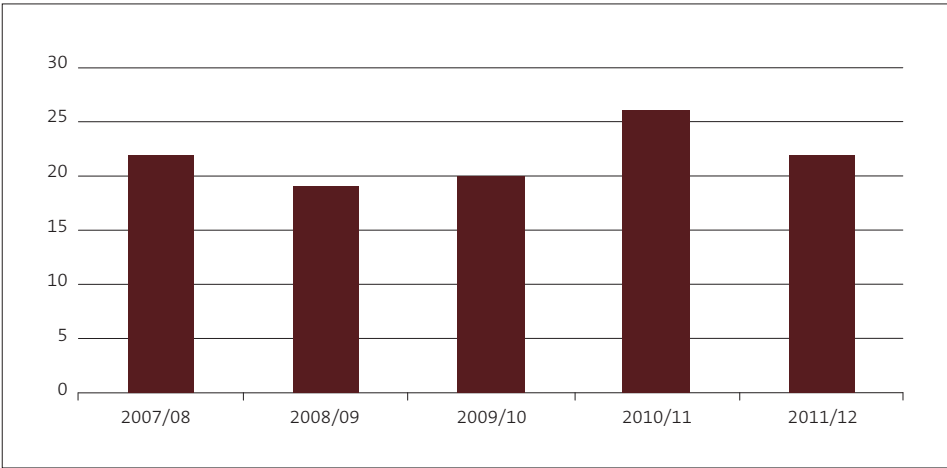
In 2010/11, we followed up on three inquiries. In all cases, the entities accepted our comments and took action to address the concerns.

Output: We carry out quality inquiries and performance audits

**Measure:** We complete 19 to 21 reports on matters arising from performance audits and other studies, and inquiries.

**Result: Achieved.** We completed 22 reports on matters arising from performance audits and other studies, and inquiries (see Appendix 3).

**Figure 34**  
Completed reports on matters arising from performance audits and other studies, and inquiries



**Measure:** Independent reviews of two performance audit reports confirm the quality of our reports.

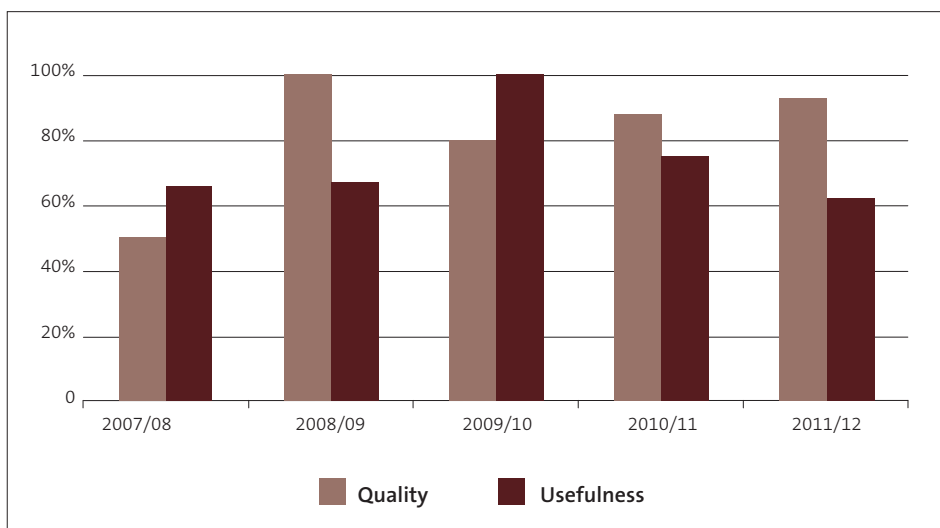
**Results: Achieved.** Overall review results confirmed the quality of reports and provided feedback on areas for improvement.

**Measure:** At least 85% of the stakeholders that we seek feedback from rate our performance audit reports (relevant to their sector or interest) as 4 or better on a scale of 1 to 5 for quality and usefulness.

**Result: Partially achieved.** 93% of our stakeholders rated our performance audit reports as 4 or better for quality. 62% rated our performance audit reports as 4 or better for usefulness.

**Figure 35**

Percentage of select committee, local government, and other stakeholders who rated on a scale of 1 to 5 the quality and usefulness of our performance audit reports as 4 or better



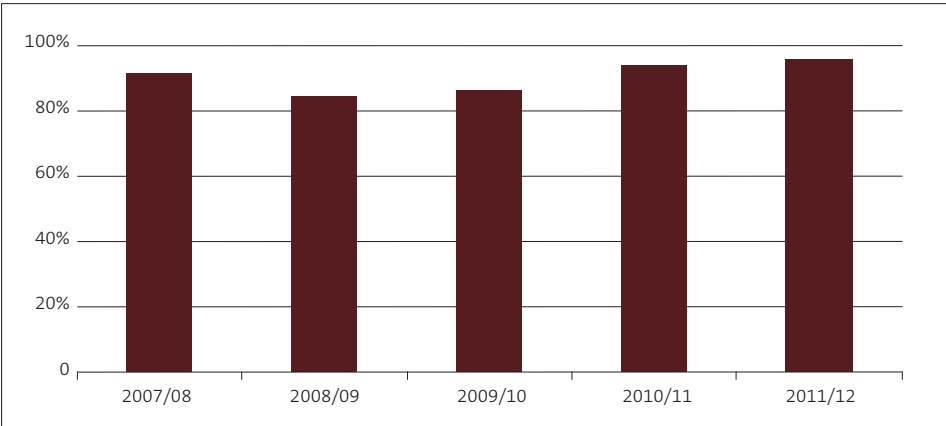


Output: Our inquiries are completed in a timely way

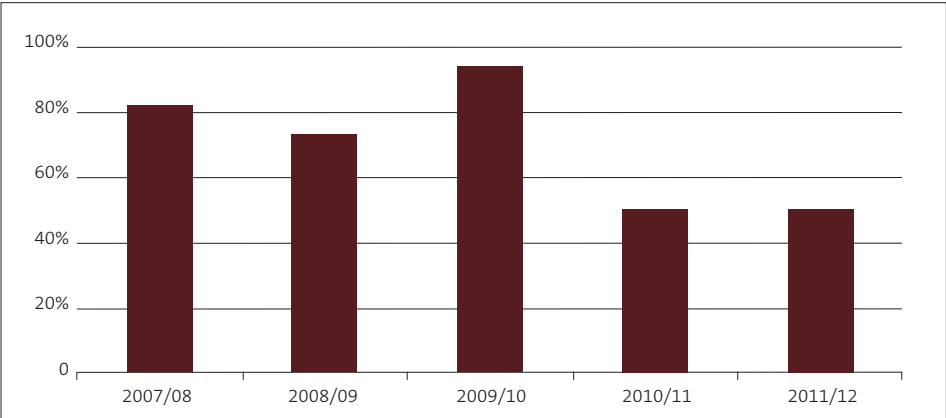
**Measure:** 80% of our findings on inquiries are reported to the relevant parties within three months for routine inquiries, six months for significant inquiries and 12 months for major inquiries.

**Result: Partially achieved.** 96% of findings reported within three months for routine inquiries, 50% of findings reported within six months for significant inquiries, and 100% of findings reported within 12 months for major inquiries.

**Figure 36**  
Percentage of findings on routine inquiries reported to the relevant parties within three months



**Figure 37**  
Percentage of findings on significant inquiries reported to the relevant parties within six months



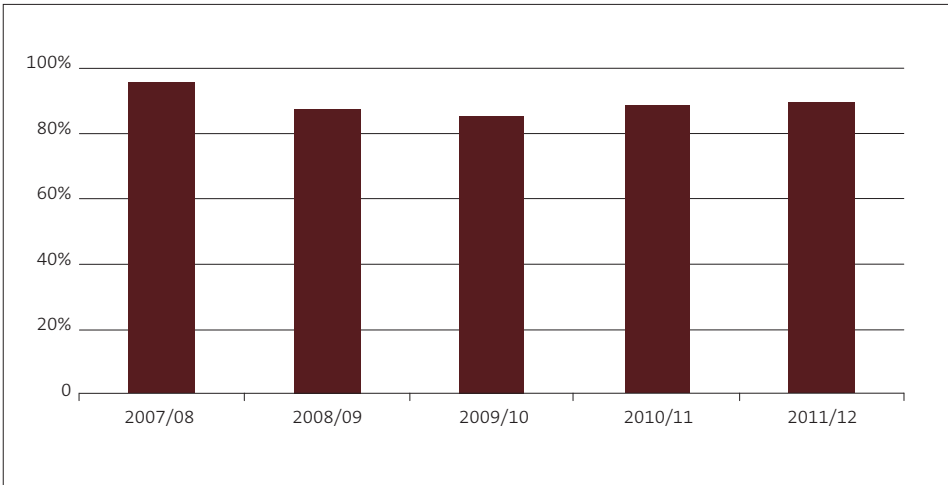
**Figure X**  
Number of findings on major inquiries reported to the relevant parties within 12 months

Year	Completed major inquiries	Reported within 12 months
2012	1	1
2011	3	1
2010	5	4
2009	2	Both reported within 13 months

**Measure:** We complete 80% of enquiries under the Local Authorities (Members’ Interests) Act 1968 within 30 working days.

**Result: Achieved.** 89% of LAMIA enquiries completed within 30 working days (48 out of total of 54).

**Figure 39**  
Percentage of enquiries under the Local Authorities (Members’ Interests) Act 1968 completed within 30 working days



## Output: We apply good methodology to inquiries and performance audits

**Measure:** Our performance audit methodology reflects good practice for carrying out such audits, as assessed every second year by the Australian National Audit Office.

**Results:** The next Australian National Audit Office peer review of our methodology and reports will be conducted in late 2012 or early 2013. There was no review in 2011/12.

2010/11 – The Australian National Audit Office (ANAO) reviewed two performance audits and found that they met most of the review criteria and were generally conducted in keeping with key OAG processes and practices.  
2008/09 – The ANAO reviewed two performance audits and confirmed areas in which the quality of our reports is strong and noted areas for us to improve.

**Measure:** Internal quality assurance reviews on selected performance audit reports confirm that reports are prepared in keeping with the performance audit methodology.

**Comment:** A review is carried out at least once every three years. The nature, extent, and frequency of the reviews are based on risk.

**Results:** No review was considered necessary in 2011/12.

A 2010/11 internal review confirmed that appropriate systems and controls are in place and that reports are prepared in keeping with the performance audit methodology.

**Measure:** Responses to requests for inquiries and our administering of the Local Authorities (Members' Interests) Act 1968 requests are in keeping with relevant policies, procedures, and standards, as confirmed by internal quality assurance review.

**Comment:** A review is carried out at least once every three years. The nature, extent, and frequency of the reviews are based on risk.

**Results:** No internal quality assurance review was considered necessary in 2011/12. 2010/11 – Reviews were completed for both the general inquiries and LAMIA enquiries systems, and confirmed that responses to requests were provided in keeping with relevant policies, procedures, and standards.

### Output: We deliver an appropriate work programme of performance audits

**Measure:** Select committees and other stakeholders are satisfied with the proposed work programme of performance audits (as indicated by feedback on our draft annual work programme.)

**Results:** Achieved. 2012 – Feedback received from select committees and other stakeholders mainly supported our proposed work programme, and enabled us to clarify the proposed scope of some specific pieces of work.

2011 – Feedback received from select committees and other stakeholders mainly supported our proposals and approach, with a specific suggestion that in future years we look at the performance of the New Zealand Police in road safety enforcement. 2007 to 2010 – Feedback received from select committees and other stakeholders mainly supported our proposals and approach.

**Figure 40**

Financial performance of output class: Performance audits and inquiries

	2011/12 Actual \$000	2011/12 Supp. Estimates \$000	2010/11 Actual \$000	2009/10 Actual \$000
<b>Income</b>				
Crown	6,287	6,287	6,587	6,587
Other	0	0	0	0
Expenditure	(5,790)	(6,287)	(5,991)	(6,044)
<b>Surplus/(Deficit)</b>	<b>497</b>	<b>0</b>	<b>596</b>	<b>543</b>

Part 3

## Organisational health and capability

We need a strong foundation of skilled people working together in a well-run organisation to ensure that we can achieve our outcomes, impacts, and outputs.

### Our people

We will continue to recruit a number of new staff each year. Some of these will be experienced professionals – replacing those who have left us – but we also hire a number of accounting graduates. We expect to see our staff develop both their vocational and leadership expertise, strengthening their contribution to the Office and the public sector. We will continue our focus on each individual's needs in developing skills identified in our competency frameworks, on our leadership development programmes, and on improving the level of engagement of our people (as measured by our annual staff engagement survey).

Historically, our highest area of staff attrition is in recently qualified accountants. The global and local economic downturn resulted in a reduced turnover of staff in 2009/10. However, as expected, attrition since then has returned to pre-recession levels.

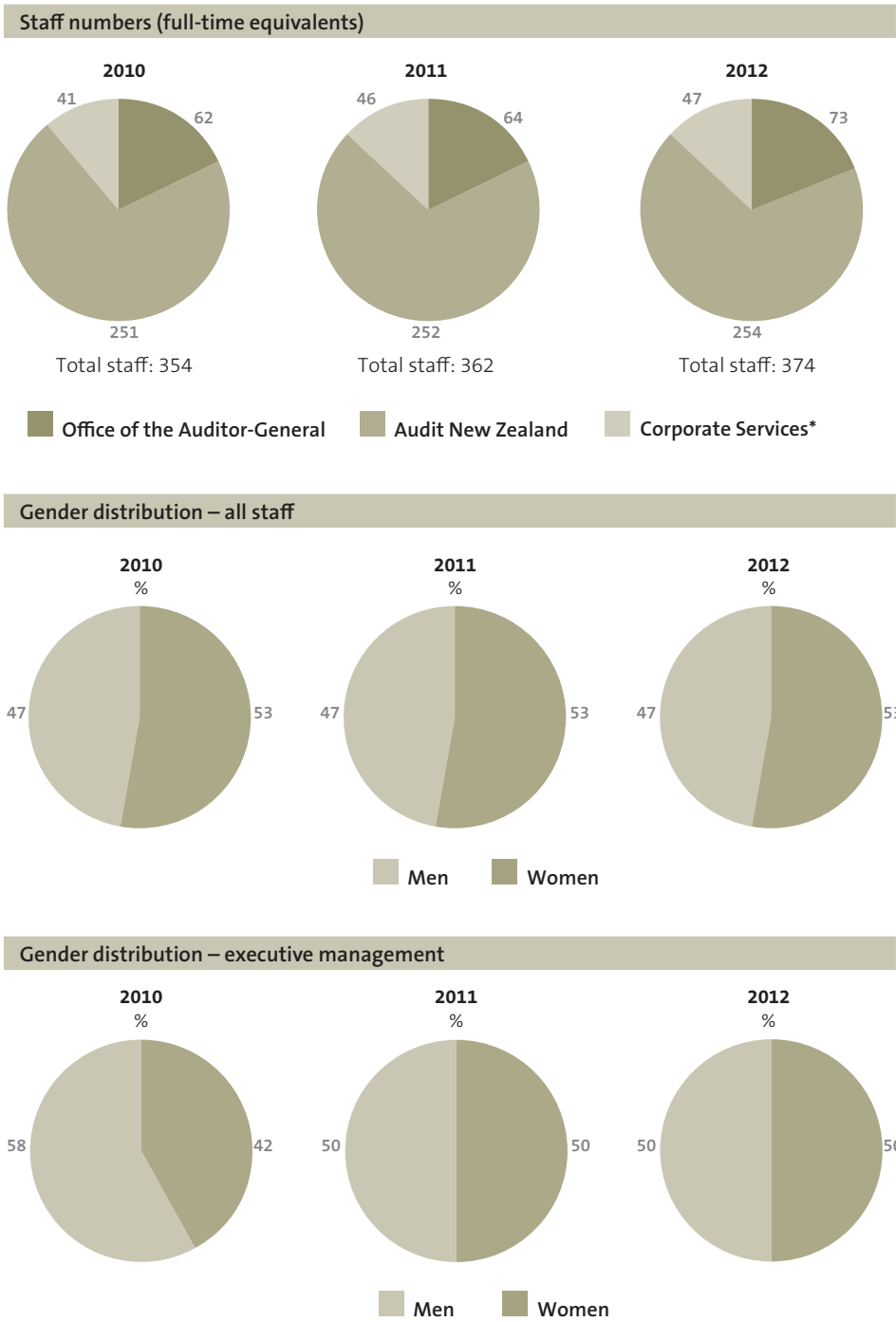
### Equal employment opportunities

The Office's equal employment opportunities programme is embedded in our recruitment and employment policies. Our recruitment programme aims to attract and appoint the best people, who have the appropriate skills, values, and attributes to meet the Office's needs, objectives, and strategic direction. We recruit in a manner that provides equal employment opportunity to Māori, women, ethnic or minority groups, and people with disabilities.

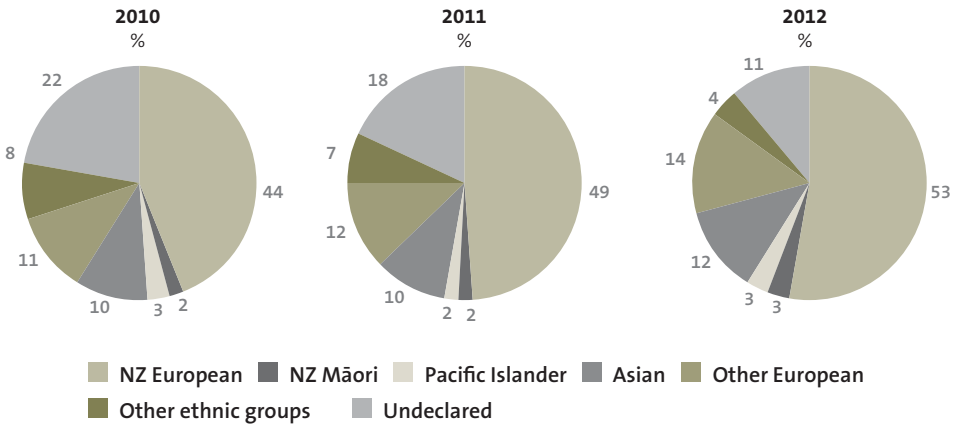
Recruitment and employment decisions and practices (such as feedback from exit interviews) are monitored to confirm application of policies. Managers are made aware of, and given support to fulfil, our good employer obligations through specific programmes, courses, and one-on-one coaching.

Our staff profile in Figure 41 shows staff numbers and staff diversity from 2010 to 2012. Increases in staff numbers in both the Office of the Auditor-General and Corporate Services over this period have resulted from the increased demand for specialist support roles and pressure on core business activities.

Figure 41  
Staff profile



Ethnicity distribution



Functional distribution



\*Corporate Services function is shared between the OAG and Audit New Zealand.



## Our performance in 2011/12

### Business practices

In 2011/12, we carried out an effectiveness and efficiency self-assessment of some of our corporate functions. The “Better Administrative and Support Services” (BASS) benchmark results indicate that our corporate costs are slightly less than the average in the BASS cohort, and that our effectiveness – as measured by BASS’s Management Practice Indicators – is broadly consistent with the cohort.

### Facilities

This year, we made very good progress on addressing our long-term property needs in Wellington and Auckland. Although we are pursuing some options, we have not yet found a satisfactory solution for our Christchurch staff.

The Office received additional capital funds in 2011/12 to fit out replacement premises for our staff in Wellington, allowing us to consolidate all Wellington staff into one location. We subsequently entered into an agreement to lease space at a fully refurbished 100 Molesworth Street. At the end of the 2011/12 year, the refurbishment is well advanced and we expect to complete the relocation of all staff by the end of the 2012/13 year.

At the end of 2011/12, the lease on our Auckland premises expired. Following an extensive procurement process, we entered into a lease for newly refurbished premises, and staff were successfully relocated in July 2012.

Since the Canterbury earthquakes, our Christchurch staff have been working from temporary premises. Although these premises meet basic requirements, the effectiveness and efficiency of our people has been affected. We have been searching unsuccessfully for replacement premises over the 2011/12 year, and we are hopeful that we will locate appropriate premises in the 2012/13 year.

### Information systems

We rely on information technology to do our work. To ensure an effective, efficient, and customer-focused service, our audit staff working in the field use specialist auditing and remote access and communications tools which presents us with significant logistical issues. This year we developed further enhancements to one of the most important tools we use to help manage these logistical issues – the Audit Status Database (ASD), which we built in-house. It contains our authoritative source information about the almost 4000 public entities we audit, and also includes information about auditors, audits, and audit contracts.

In 2011/12, we selected a partner to work with us on implementing an Enterprise Content Management system (ECM) that allows the collection, storing, analysis, sharing, reuse, and reporting of the information the Auditor-General and her staff and Appointed Auditors collect during the course of their work. We recognise the significant value this information and insight could bring to improving the performance of the public sector, and we are keen to make the collection, analysis, and use of this information and insight as effective and efficient as we can.

In 2011/12, we also initiated projects to upgrade our end-user desktop environment including the audit support tool used by our auditors, and enhanced the functionality of our audit tracking systems.

#### **Audit New Zealand**

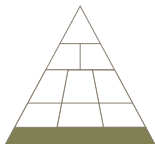
Our audit staff have consistently performed well in the New Zealand Institute of Chartered Accountants (NZICA) accreditation examinations. This year a very pleasing 97% pass rate was achieved by staff who sat these examinations, ensuring that we again met our 95% target.

Our targets for client survey results were not maintained this year, and showed some small decreases in ratings. We are committed to improving these results and ensuring that our clients are confident that we understand their business and operating context.

This year's results for the New Zealand Institute of Chartered Accountants (NZICA) practice review of Audit New Zealand were pleasing. The NZICA review considered that Audit New Zealand has:

- nationwide audit and assurance methodology;
- quality assurance procedures;
- quality control programmes; and
- procedures that comply with NZICA's professional, ethical, quality control standards and the Auditor-General's auditing standards.

Participation in the practice review is voluntary for Audit New Zealand because its NZICA members employed by the Auditor-General do not offer accounting services to the public.



**Figure 42**  
Summary of measures and standards for organisational health and capability



Staff are engaged and satisfied

**Measure:** Improve (or at least maintain) the engagement and satisfaction of our staff measured against the previous two years.

**Comment:** The Office’s staff engagement survey is based on responses to statements on a 5-point scale, with “1” being the lowest score and “5” being the highest.

**Result: Partially achieved.** Our survey results saw slight improvements in overall engagement (3.84) and teamwork (3.72). We maintained results in overall satisfaction (3.63), basic needs met ( 3.93), management support (3.65), and growth (4.04).

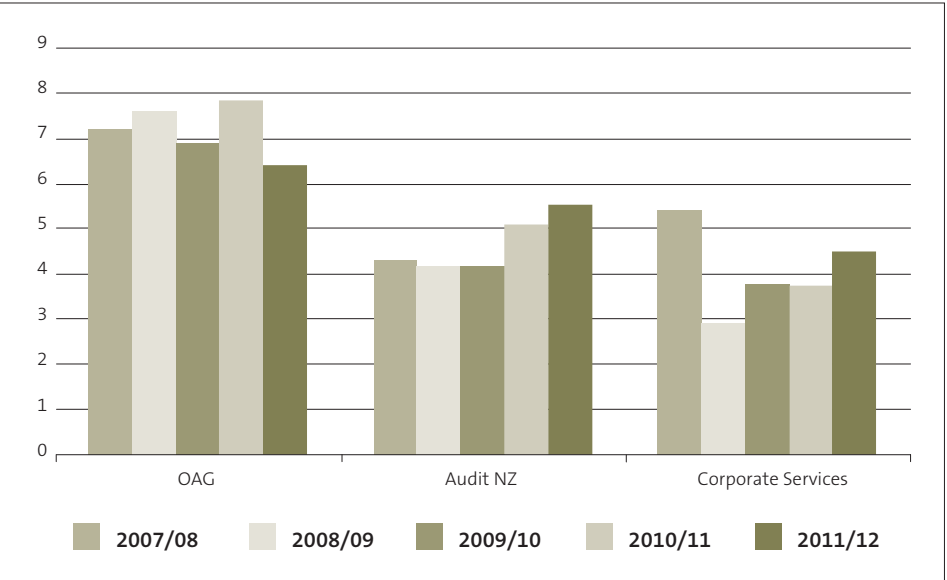
Figure 43  
Staff engagement survey scores



**Measure:** Improve (or at least maintain) the average years of experience of our staff measured against the previous two years.

**Result:** **Achieved** for Audit New Zealand (5.5 years) and Corporate Services (4.5 years). **Not achieved** for OAG (6.4 years).

Figure 44  
Average number of years that staff have been employed by the Office

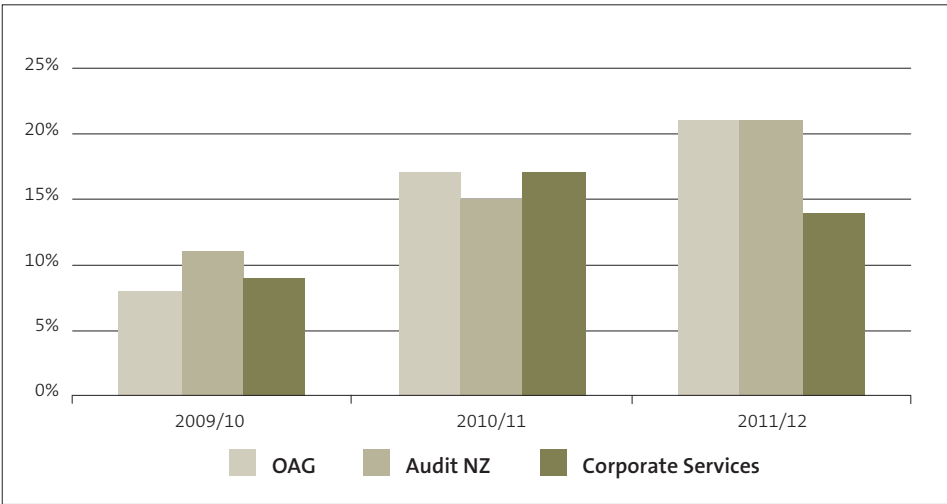


**Measure:** Staff turnover – no target set.

**Comment:** We have previously reported turnover information in the staff profile section. However, we consider that a more appropriate place is here, under Staff are engaged and satisfied. Turnover is influenced by the New Zealand economy, and by the worldwide demand for qualified auditors. Following the global financial crisis, our turnover dropped to 10%, but in the last two years it has returned to more normal levels. Overall we are comfortable with a turnover of up to 20%, but would prefer no more than 15%.

**Result:** Staff turnover results: OAG 21%, Audit NZ 21%, Corporate Services 14%.

**Figure 45**  
Annual turnover of staff



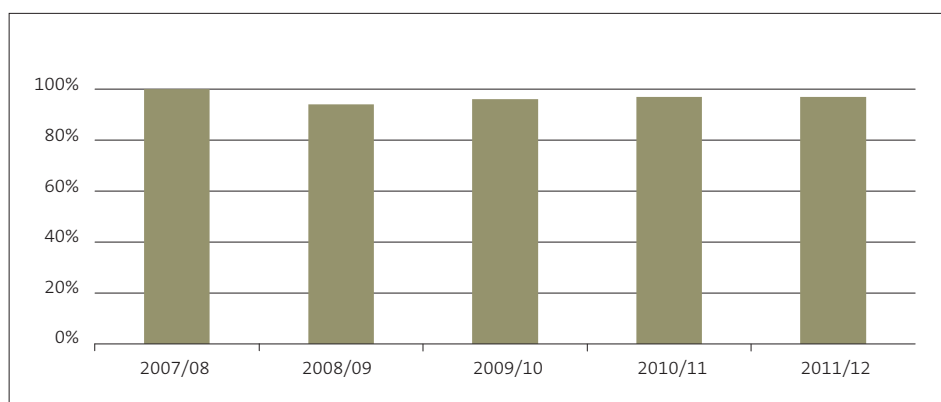
## Audit staff have high levels of expertise

**Measure:** Achieve a pass rate of staff undertaking accreditation examinations of not less than 95%.

**Result: Achieved.** 97% pass rate for staff sitting accreditation examinations.

**Figure 46**

Percentage of audit staff passing NZICA accreditation examinations

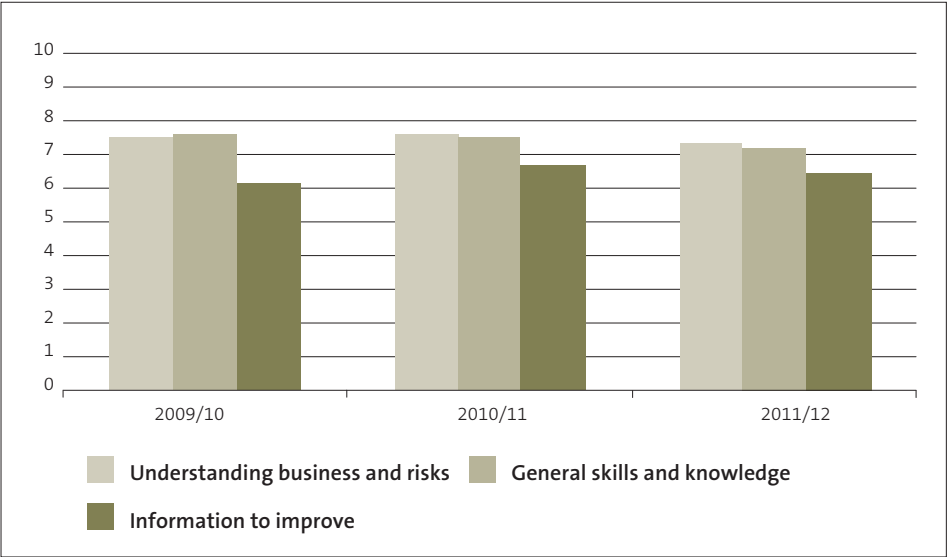


**Measure:** Client survey feedback shows that auditors' knowledge of entities' business and operating context is improving, and that auditors are investing in work to understand that context. Our clients give us improved (or at least maintained) ratings (on a scale of 0 to 10) compared with the previous two years for their auditors':

- understanding of the client's business and the risks that clients face;
- general skills and knowledge required to conduct their audit; and
- provision of information to help clients identify and promote improvement in their operations.

**Result: Not achieved.** Our clients' ratings were not maintained. Understand business and risks 7.3, General skills and knowledge 7.2, Information to improve 6.4.

**Figure 47**  
Ratings for expertise of Audit New Zealand staff



**Audit staff have high levels of expertise: Auditing performance information**

**Measure:** Our quality assurance reviews of our audit and assurance work confirms that auditors are carrying out the requirements of AG-4 (Revised).

**Comment:** AG-4 (Revised) is the Auditor-General’s revised auditing standard on auditing non-financial performance information.

**Results: Achieved.** Quality assurance reviews of our audit and assurance work confirmed that auditors are carrying out the requirements of AG-4 (Revised).

**Comment:** The reviews have identified some areas where the audit of this information could be improved in future.

Part 4

**Financial statements**



## Contents

Audit report	72
Statement of responsibility	75
Statement of comprehensive income	76
Statement of changes in taxpayers' funds (equity)	77
Statement of financial position	78
Statement of cash flows	79
Statement of commitments	80
Statement of contingent liabilities and contingent assets	81
Statement of output expenses, other expenses, and capital expenditure against appropriations	82
Statement of unappropriated expenditure	83
Statement of trust money	83
Notes to the financial statements	84

# Audit report



## INDEPENDENT AUDITOR'S REPORT

### TO THE READERS OF THE CONTROLLER AND AUDITOR-GENERAL'S FINANCIAL STATEMENTS AND NON-FINANCIAL PERFORMANCE INFORMATION FOR THE YEAR ENDED 30 JUNE 2012

We have been appointed by the House of Representatives to carry out the audit of the financial statements and non-financial information included in the annual report of the Controller and Auditor-General for the year ended 30 June 2012.

We have audited:

- the financial statements of the Controller and Auditor-General on pages 76 to 105, that comprise the statement of financial position, statement of commitments, statement of contingent liabilities and contingent assets as at 30 June 2012, the statement of comprehensive income, statement of changes in taxpayers' funds (equity), statement of cash flows, statement of output expenses, other expenses and capital expenditure against appropriations, statement of unappropriated expenditure, and statement of trust money for the year ended on that date and the notes to the financial statements that include accounting policies and other explanatory information; and
- the non-financial performance information of the Controller and Auditor-General that comprises the statement of service performance on pages 24 to 58.

#### Opinion

In our opinion:

- the financial statements of the Controller and Auditor-General on pages 76 to 105:
  - comply with generally accepted accounting practice in New Zealand;
  - fairly reflect the Controller and Auditor-General's:
    - financial position as at 30 June 2012;
    - financial performance and cash flows for the year ended on that date;
    - output expenses, other expenses and capital expenditure against each appropriation administered by the Controller and Auditor-General and each class of outputs included in each output expense appropriation for the year ended 30 June 2012; and
    - unappropriated expenditure for the year ended 30 June 2012; and
  - fairly reflect the trust money administered by the Controller and Auditor-General.
- the non-financial performance information of the Controller and Auditor-General on pages 24 to 58:
  - complies with generally accepted accounting practice in New Zealand; and
  - fairly reflects the Controller and Auditor-General's service performance and outcomes for the year ended 30 June 2012, including for each class of outputs:
    - the service performance compared with the forecasts in the forecast statement of service performance at the start of the financial year; and
    - the revenue earned and output expenses incurred as compared with the forecasts in the forecast statement of service performance at the start of the financial year.

The audit was completed on 28 September 2012. This is the date at which our opinion is expressed.

audit and assurance services CST NEXIA AUDIT visit us at [www.cstnexus.co.nz](http://www.cstnexus.co.nz)

Level 3, CST Nexia Centre, 22 Amersham Way, PO Box 76 261 Manukau City New Zealand. Tel 0-9 262 2595 Fax 0-9 262 2606 Email: [team@cstnexus.co.nz](mailto:team@cstnexus.co.nz)

CST NEXIA AUDIT is a member of Nexia International, a worldwide network of independent accounting and consulting firms.





The basis of our opinion is explained below. In addition, we outline the responsibilities of the Controller and Auditor-General and our responsibilities, and explain our independence.

#### **Basis of Opinion**

We carried out the audit in accordance with International Standards on Auditing (New Zealand), and we applied the Auditor-General's Auditing Standard 4 (Revised) – *The Audit of Service Performance Reports* that is also applied to the audit of non-financial performance information in many other public sector entities in New Zealand. Those standards require that we comply with ethical requirements and plan and carry out our audit to obtain reasonable assurance about whether the financial statements and the non-financial performance information are free from material misstatement.

Material misstatements are differences or omissions of amounts and disclosures that would affect a reader's overall understanding of the financial statements and non-financial performance information. If we had found material misstatements that were not corrected, we would have referred to them in our opinion.

An audit involves carrying out procedures to obtain audit evidence about the amounts and disclosures in the financial statements and the non-financial performance information. The procedures selected depend on our judgement, including our assessment of risks of material misstatement of the financial statements and the non-financial performance information, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Controller and Auditor-General's preparation of the financial statements and the non-financial performance information that fairly reflect the matters to which they relate. We consider internal control in order to design audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the Controller and Auditor-General's internal control.

An audit also involves evaluating:

- the appropriateness of accounting policies used and whether they have been consistently applied;
- the reasonableness of the significant accounting estimates and judgements made by the Controller and Auditor-General;
- the appropriateness of the reported non-financial performance information within the Controller and Auditor-General's framework for reporting performance;
- the adequacy of all disclosures in the financial statements and the non-financial performance information; and
- the overall presentation of the financial statements and the non-financial performance information.

We did not examine every transaction, nor do we guarantee complete accuracy of the financial statements and the non-financial performance information. We have obtained all the information and explanations we have required and we believe we have obtained sufficient and appropriate audit evidence to provide a basis for our audit opinion.



### **Responsibilities of the Controller and Auditor-General**

The Controller and Auditor-General is responsible for preparing financial statements and non-financial performance information that:

- comply with generally accepted accounting practice in New Zealand;
- fairly reflect the Controller and Auditor-General's financial position, financial performance, cash flows, output expenses, other expenses and capital expenditure against each appropriation and unappropriated expenditure;
- fairly reflect the trust money administered by the Controller and Auditor-General; and
- fairly reflect the Controller and Auditor-General's service performance and outcomes.

The Controller and Auditor-General is also responsible for such internal control as is determined necessary to enable the preparation of financial statements and non-financial performance information that are free from material misstatement, whether due to fraud or error.

The Controller and Auditor-General's responsibility arises from sections 45A, 45B, and 45F of the Public Finance Act 1989.

### **Responsibilities of the Auditor**

We are responsible for expressing an independent opinion on the financial statements and the non-financial performance information and reporting that opinion to you based on our audit. Our responsibility arises from section 38 of the Public Audit Act 2001 and sections 45D and 45F of the Public Finance Act 1989.

### **Independence**

When carrying out the audit, we followed the independence requirements of the New Zealand Institute of Chartered Accountants.

We carry out some audits of public entities on behalf of the Controller and Auditor-General. The amount of work we carry out on behalf of the Controller and Auditor-General is no more than the amount of work we did prior to our appointment as auditor of the Controller and Auditor-General. Other than the audit of the Controller and Auditor-General and the audits we carry out on behalf of the Controller and Auditor-General, we have no relationship with or interests in the Controller and Auditor-General.

*CST Nexia Audit*

**CST Nexia Audit  
Chartered Accountants  
Manukau City, New Zealand**

## Statement of responsibility

In terms of the Public Finance Act 1989 and the Public Audit Act 2001, the Controller and Auditor-General is responsible for the accuracy and judgements used in the preparation of the financial statements, and for establishing and maintaining systems of internal control designed to provide ongoing assurance of the integrity and reliability of financial reporting.

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

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

In my opinion, the information set out in the statement of service performance, the financial statements, and attached notes to those statements (on pages 24–58 and 76–105) fairly reflects our service performance, financial activities, and cash flows for the year ended 30 June 2012, and our financial position as at that date.

Signed:



Lyn Provost  
Controller and Auditor-General  
28 September 2012

Countersigned:



Maria Viviers  
Chief Financial Officer  
28 September 2012

## Statement of comprehensive income for the year ended 30 June 2012

This statement reports the income and expenditure relating to all outputs (goods and services) produced by the Office. Supporting statements showing the income and expenditure of each output class are on pages 38, 46, and 58.

Explanations of significant variances against the main Estimates are detailed in Note 20.

Actual 2011 \$000		Notes	Actual 2012 \$000	Supp. Estimates 2012 \$000	Main Estimates 2012 \$000
<b>Income</b>					
10,000	Crown funding	2	10,045	10,045	10,000
64,958	Audit fee revenue	3	71,433	70,840	71,851
212	Other income		329	0	0
25	Gain on sale of plant and equipment		56	40	0
<b>75,195</b>	<b>Total income</b>		<b>81,863</b>	<b>80,925</b>	<b>81,851</b>
<b>Expenditure</b>					
34,744	Personnel costs	4	37,660	37,378	37,568
38,407	Other operating costs	5	41,546	42,324	42,943
867	Depreciation and amortisation expense	9, 10	886	901	1,071
261	Capital charge	6	322	322	269
<b>74,279</b>	<b>Total expenditure</b>		<b>80,414</b>	<b>80,925</b>	<b>81,851</b>
<b>916</b>	<b>Net surplus/(deficit)</b>		<b>1,449</b>	<b>0</b>	<b>0</b>
0	Other comprehensive income		0	0	0
<b>916</b>	<b>Total comprehensive income</b>		<b>1,449</b>	<b>0</b>	<b>0</b>

The accompanying notes form part of these financial statements.



# Statement of changes in taxpayers' funds (equity)

## for the year ended 30 June 2012

Actual 2011 \$000		Notes	Actual 2012 \$000	Supp. Estimates 2012 \$000	Main Estimates 2012 \$000
3,521	Taxpayers' funds brought forward at 1 July		4,021	4,021	4,021
916	Total comprehensive income		1,449	0	0
(916)	Repayment of surplus to the Crown	12	(1,449)	0	0
500	Capital contribution		0	0	2,200
<b>4,021</b>	<b>Taxpayers' funds at 30 June</b>		<b>4,021</b>	<b>4,021</b>	<b>6,221</b>

The accompanying notes form part of these financial statements.

# Statement of financial position

## as at 30 June 2012

This statement reports total assets and liabilities. The difference between the total assets and total liabilities is called taxpayers' funds.

Explanations of significant variances against the main Estimates are detailed in Note 20.

Actual 2011 \$000		Notes	Actual 2012 \$000	Supp. Estimates 2012 \$000	Main Estimates 2012 \$000
	<b>Current assets</b>				
4,283	Cash and cash equivalents		5,479	2,942	4,379
255	Prepayments		841	180	185
1,886	Work in progress		1,207	2,000	2,200
6,003	Debtors and other receivables	8	6,752	6,267	5,601
12,427	<i>Total current assets</i>		14,279	11,389	12,365
	<b>Non-current assets</b>				
1,304	Property, Plant and equipment	9	1,593	1,407	1,646
810	Intangible assets	10	659	886	1,280
2,114	<i>Total non-current assets</i>		2,252	2,293	2,926
<b>14,541</b>	<b>Total assets</b>		<b>16,531</b>	<b>13,682</b>	<b>15,291</b>
	<b>Current liabilities</b>				
5,047	Creditors and other payables	11	5,442	5,161	4,783
916	Repayment of surplus	12	1,449	0	0
0	Provisions	13	209	0	0
3,971	Employee entitlements	14	4,842	3,915	3,707
9,934	<i>Total current liabilities</i>		11,942	9,076	8,490
	<b>Non-current liabilities</b>				
586	Employee entitlements	14	568	585	580
586	<i>Total non-current liabilities</i>		568	585	580
<b>10,520</b>	<b>Total liabilities</b>		<b>12,510</b>	<b>9,661</b>	<b>9,070</b>
<b>4,021</b>	<b>Net assets</b>		<b>4,021</b>	<b>4,021</b>	<b>6,221</b>
	<b>Taxpayers' funds</b>				
4,021	General funds		4,021	4,021	6,221
<b>4,021</b>	<b>Total taxpayers' funds</b>		<b>4,021</b>	<b>4,021</b>	<b>6,221</b>

The accompanying notes form part of these financial statements.



## Statement of cash flows for the year ended 30 June 2012

This statement summarises the cash movements in and out of the Office during the year. It takes no account of money owed to the Office or owing by the Office, and therefore differs from the statement of comprehensive income.

Actual 2011 \$000		Notes	Actual 2012 \$000	Supp. Estimates 2012 \$000	Main Estimates 2012 \$000
<b>Cash flows from operating activities</b>					
10,000	Receipts from the Crown		10,045	10,045	10,000
37,310	Receipts from public entities*		42,821	41,961	43,015
(5,412)	Payments to suppliers *		(6,991)	(9,583)	(10,043)
(34,381)	Payments to employees		(36,616)	(37,268)	(37,459)
(4,891)	Net GST paid**		(5,851)	(4,178)	(4,205)
(269)	Capital charge paid		(322)	(322)	(269)
<b>2,357</b>	<i>Net cash flow from operating activities</i>	15	<b>3,086</b>	<b>655</b>	<b>1,039</b>
<b>Cash flows from investing activities</b>					
83	Receipts from sale of plant and equipment		172	72	92
(777)	Purchase of plant and equipment		(948)	(722)	(950)
(75)	Purchase of intangible assets		(198)	(430)	(850)
<b>(769)</b>	<i>Net cash flow from (used in) investing activities</i>		<b>(974)</b>	<b>(1,080)</b>	<b>(1,708)</b>
<b>Cash flows from financing activities</b>					
(2,014)	Surplus repayment to the Crown		(916)	(916)	0
500	Capital contribution		0	0	2,200
<b>(1,514)</b>	<i>Net cash flow from (used in) financing activities</i>		<b>(916)</b>	<b>(916)</b>	<b>2,200</b>
74	Total net increase (decrease) in cash held		1,196	(1,341)	1,531
4,209	Cash at the beginning of the year		4,283	4,283	2,848
<b>4,283</b>	<b>Cash at the end of the year</b>		<b>5,479</b>	<b>2,942</b>	<b>4,379</b>

\* The statement of cash flows does not include the contracted audit service provider audit fee revenue or expenditure, as these do not involve any cash transactions with the Office.

\*\* The GST component of operating activities reflects the net GST paid to and received from the Inland Revenue Department. GST has been presented on a net basis, as the gross amounts do not provide meaningful information for financial statement purposes.

The accompanying notes form part of these financial statements.

## Statement of commitments

### as at 30 June 2012

This statement records expenditure to which the Office is contractually committed at 30 June 2012.

#### Non-cancellable operating lease commitments

The Office leases property, plant, and equipment in the normal course of its business. The majority of these leases are for premises, which have a non-cancellable leasing period ranging from three to nine years.

The Office's non-cancellable operating leases have varying terms, escalation clauses, and renewal rights. There are no restrictions placed on the Office by any of its leasing arrangements.

#### Capital commitments

Capital commitments are the aggregate amount of capital expenditure contracted or authorised for the acquisition of property, plant, and equipment that have not been paid for or not recognised as a liability as balance date.

Actual 2011 \$000		Actual 2012 \$000
	<b>Non-cancellable operating lease commitments</b>	
1,662	Not later than one year	1,785
1,081	Later than one year and not later than five years	7,180
0	Later than five years	6,614
2,743	<i>Total non-cancellable operating lease commitments</i>	15,579
	<b>Capital commitments</b>	
0	Contractual	2,165
0	Authorised but not yet contracted	642
0	<i>Total capital commitments</i>	2,807
<b>2,743</b>	<b>Total commitments</b>	<b>18,386</b>

The accompanying notes form part of these financial statements.

# Statement of contingent liabilities and contingent assets

## as at 30 June 2012

81

This statement discloses situations that existed at 30 June 2012, the ultimate outcome of which is uncertain and will be confirmed only on the occurrence of one or more future events after the date of approval of the financial statements.

**Contingent liabilities**

The Office did not have any contingent liabilities as at 30 June 2012 (nil as at 30 June 2011).

**Contingent assets**

There were no contingent assets as at 30 June 2012 (nil as at 30 June 2011).

The accompanying notes form part of these financial statements.

# Statement of output expenses, other expenses, and capital expenditure against appropriations

## for the year ended 30 June 2012

This statement reports actual expenses incurred against each appropriation administered by the Office.

Actual 2011 \$000	Vote Audit	Actual 2012 \$000	Supp. Estimates 2012 \$000
	<b>Appropriations for output expenses</b>		
	<i>Multi-class output appropriations</i>		
	Statutory Auditor Function		
2,442	Supporting accountability to Parliament	3,047	3,005
5,991	Performance audits and inquiries	5,790	6,287
8,433	Total statutory auditor function	8,837	9,292
	<i>Annual and other appropriations</i>		
150	Audit and assurance services	150	150
64,893	Provision of audit and assurance services (revenue-dependent appropriation) <sup>1</sup>	70,579	70,485
73,476	Total appropriations for output expenses	79,566	79,927
	<b>Other expenses to be incurred by the Office</b>		
803	Remuneration of the Auditor-General and Deputy Auditor-General <sup>2</sup>	848	848
852	Capital expenditure	1,153	1,152
<b>75,131</b>	<b>Total</b>	<b>81,567</b>	<b>81,927</b>

- 1 Revenue-dependent appropriation – Provision of audit and assurance services. In 2011/12, the Office earned \$71.433 million from audit and assurance services – refer Note 3. The Office is permitted to incur expenditure up to the amount of revenue earned for this appropriation.

- 2 Costs incurred pursuant to clause 5 of Schedule 3 of the Public Audit Act 2001.

The accompanying notes form part of these financial statements.

## Statement of unappropriated expenditure for the year ended 30 June 2012

The Office incurred no unappropriated expenditure during the year ended 30 June 2012 (nil for the year ended 30 June 2011).

## Statement of trust money for the year ended 30 June 2012

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

Until June 2010, the Office carried out the financial transactions on behalf of PASAI, recorded in a trust account.

PASAI now operates through an incorporated society, with the financial records managed by the Secretariat. During the 2010/11 financial year, trust account balances were transferred to the Secretariat and the trust accounts were closed.

All trust money transactions were recorded on a cash basis. None of the transactions associated with the PASAI trust account are recorded in the statement of comprehensive income or the statement of financial position.

Actual 2011 \$000		Actual 2012 \$000
10	Opening balance at 1 July	0
0	Receipts	0
(10)	Payments	0
0	Closing balance at 30 June	0

The accompanying notes form part of these financial statements.

# Notes to the financial statements

## for the year ended 30 June 2012

### Note 1: Statement of accounting policies

#### Reporting entity

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

The Controller and Auditor-General's activities include work carried out by the Office of the Auditor-General (OAG) and Audit New Zealand (referred to collectively as "the Office"), and contracted audit service providers. The Office has designated itself as a public benefit entity for the purposes of New Zealand equivalents to International Financial Reporting Standards (NZ IFRS).

In addition, the Office has reported on trust money that it administers.

The financial statements of the Office are for the year ended 30 June 2012. The financial statements were authorised for issue by the Controller and Auditor-General on 28 September 2012.

#### Basis of preparation

The financial statements of the Controller and Auditor-General have been prepared in accordance with sections 45A, 45B, and 45F of the Public Finance Act 1989, which include the requirement to comply with New Zealand generally accepted accounting practice (NZ GAAP), and Treasury Instructions.

These financial statements have been prepared in accordance with New Zealand generally accepted accounting practice (NZ GAAP). They comply with NZ IFRS and other applicable Financial Reporting Standards, as appropriate for a public benefit entity.

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

The financial statements have been prepared on a historical cost basis. The financial statements are presented in New Zealand dollars, and all values are rounded to the nearest thousand dollars (\$000). The functional currency of the Office is New Zealand dollars.

There have been no changes in accounting policies during the financial year.

*Standards, amendments, and interpretations issued that are not yet effective and have not been adopted early*

Standards, amendments and interpretations issued but not yet effective that have not been adopted early, and which are relevant to the Office include:

- NZ IFRS 9 Financial Instruments will eventually replace NZ IAS 39 Financial Instruments: Recognition and Measurement. NZ IAS 39 is being replaced through the following three main phases: Phase 1 Classification and Measurement, Phase 2 Impairment Methodology, and Phase 3 Hedge Accounting. Phase 1 has been completed and has been published in the new financial instrument standard NZ IFRS 9. NZ IFRS 9 uses a single approach to determine whether a financial asset is measured at amortised cost or fair value, replacing the many different rules in NZ IAS 39. The approach in NZ IFRS 9 is based on how an entity manages its financial assets (its business model) and the contractual cash flow characteristics of the financial assets. The financial liability requirements are the same as those of NZ IAS 39, except for when an entity elects to designate a financial liability at fair value through the surplus or deficit. The new standard is required to be adopted for the year ended 30 June 2016. However, as a new Accounting Standards Framework will apply before this date, there is no certainty when an equivalent standard to NZ IFRS 9 will be applied by public benefit entities.

The Minister of Commerce has approved a new Accounting Standards Framework (incorporating a Tier Strategy) developed by the External Reporting Board (XRB). Under this Accounting Standards Framework, the Office is classified as a Tier 1 reporting entity and will be required to apply full Public Benefit Entity Accounting Standards (PAS). These standards are being developed by the XRB based on current International Public Sector Accounting Standards. The effective date for the new standards for public sector entities is expected to be for reporting periods beginning on or after 1 July 2014. This means the Office expects to transition to the new standards in preparing its 30 June 2015 financial statements. As the PAS are still under development, the Office is unable to assess the implications of the new Accounting Standards Framework at this time.

Due to the change in the Accounting Standards Framework for public benefit entities, it is expected that all new NZ IFRS and amendments to existing NZ IFRS will not be applicable to public benefit entities. Therefore, the XRB has effectively frozen the financial reporting requirements for public benefit entities up until the new Accounting Standards Framework is effective. Accordingly, no disclosure has been made about new or amended NZ IFRS that exclude public benefit entities from their scope.

## Accounting policies

### Income

Income is measured at the fair value of the consideration received. Income is derived mainly from the Crown for outputs provided to Parliament, from fees for the audit of public entities' financial statements, and from fees for other assurance work carried out by Audit New Zealand at the request of public entities.

#### *Crown funding*

Revenue earned from the supply of outputs to the Crown is recognised as revenue when earned.

#### *Fee revenue generated by the Office for audits and other assurance work*

Fee revenue is recognised when earned, by reference to the stage of completion of audit and other assurance work, if the outcome can be estimated reliably. Revenue accrues as the audit activity progresses by reference to the value of work performed, and as direct expenses that can be recovered are incurred. If the outcome of an audit cannot be estimated reliably, revenue is recognised only to the extent of the direct costs incurred in respect of the work performed. If there are significant uncertainties regarding recovery, or if recovery is contingent on events outside our control, no revenue is recognised.

#### *Fee revenue generated by contracted audit service providers for audits*

Fee revenue generated by contracted audit service providers for audits of public entities is also recognised as the work progresses, based on advice from the contracted audit service providers. Contracted audit service providers invoice and collect audit fees directly from public entities.

#### *Interest*

Interest revenue is recognised using the effective interest method.

### Expenditure

#### *Expenses of audit service providers*

Fees for audits of public entities carried out by contracted audit service providers are recognised as the work progresses, based on advice from the contracted audit service providers. Contracted audit service providers invoice and collect audit fees directly from public entities.

#### *Leases*

An operating lease is a lease that does not transfer substantially all the risks and rewards incidental to ownership of an asset. Lease payments under an operating



lease are recognised as an expense on a straight-line basis over the lease term. All leases entered into by the Office are operating leases.

#### *Foreign currency transactions*

Foreign currency transactions (including those for which forward foreign exchange contracts are held) are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the surplus or deficit.

#### *Capital Charge*

The capital charge is recognised as an expense in the period to which the charge relates.

### **Financial instruments**

Financial assets and financial liabilities are initially measured at fair value plus transaction costs, unless they are carried at fair value through profit or loss, in which case the transaction costs are recognised in the surplus or deficit.

### **Cash and cash equivalents**

Cash includes cash on hand and funds on deposit with banks and is measured at its face value.

### **Work in progress**

Work in progress is stated at estimated realisable value, after providing for non-recoverable amounts. Work in progress represents unbilled revenue.

### **Debtors and other receivables**

Debtors and other receivables are initially measured at fair value and, where appropriate, subsequently measured at amortised cost using the effective interest rate, less impairment changes.

Impairment of a receivable is established when there is objective evidence that the Office will not be able to collect amounts due according to the original terms of the receivable. Significant financial difficulties of the debtor, probability that the debtor will enter into bankruptcy, and default in payments are considered indicators that the debt is impaired. The amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted using the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the surplus or deficit.

**Property, plant and equipment**

Property, plant and equipment consists of furniture and fittings, leasehold improvements, office equipment, IT hardware, and motor vehicles. Property, plant and equipment is shown at cost, less accumulated depreciation and impairment losses.

*Additions*

Individual assets, or group of assets, are capitalised if their cost is greater than \$1,000.

The cost of an item of property, plant and equipment is recognised as an asset if, and only if, it is probable that future economic benefits or service potential associated with the item will flow to the Office and the cost of the item can be measured reliably.

In most instances, an item of property, plant and equipment is recognised at its cost. Where an asset is acquired at no cost, or for a nominal cost, it is recognised at fair value as at the date of acquisition.

*Disposals*

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount of the asset. Gains and losses on disposals are included in the surplus or deficit.

*Subsequent costs*

Costs incurred subsequent to initial acquisition are capitalised only when it is probable that future economic benefits or service potential associated with the item will flow to the Office and the cost of the item can be measured reliably.

The costs of day-to-day servicing of property, plant and equipment are recognised in the surplus or deficit as they are incurred.

*Depreciation*

Depreciation is provided on a straight-line basis on all property, plant and equipment, at rates that will write off the cost less estimated residual values of the property, plant and equipment over their useful lives. The useful lives and associated depreciation rates of major classes of assets have been estimated as follows:

Furniture and fittings	4 years (25%)
Office equipment	2.5 - 5 years (20% - 40%)
IT hardware	2.5 - 5 years (20% - 40%)
Motor vehicles	3-4 years (25% - 33%).

Leasehold improvements are depreciated over the unexpired period of the lease or the estimated remaining useful lives of the improvements, whichever is the shorter.

The residual value and useful life of an asset is reviewed, and adjusted if applicable, at each balance date.

### **Intangible assets**

#### *Software acquisition and development*

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Costs associated with maintaining computer software are recognised as an expense when incurred.

Costs that are directly associated with the development of software for internal use by the Office are recognised as an intangible asset. Direct costs include the software development and employee costs.

Staff training costs are recognised as an expense when incurred.

#### *Amortisation*

The carrying value of an intangible asset with a finite life is amortised on a straight-line basis over its useful life. Amortisation begins when the asset is available for use and ceases at the date that the asset is derecognised. The amortisation charge for each period is recognised in the surplus or deficit.

The useful life and associated amortisation rate of computer software is estimated at between 2.5 and 5 years (20% - 40%).

### **Impairment of non-financial assets**

Property, plant and equipment and intangible assets that have a finite useful life are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable through either continued use or disposal. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

Value in use is depreciated replacement cost for an asset where the future economic benefits or service potential of the asset are not primarily dependent on the asset's ability to generate net cash inflows and where the Office would, if deprived of the asset, replace its remaining future economic benefits or service potential.

If an asset's carrying amount exceeds its recoverable amount, the asset is impaired and the carrying amount is written down to the recoverable amount. The impairment loss is recognised in the surplus or deficit. Any reversal of an impairment loss is also recognised in the surplus or deficit.

**Creditors and other payables**

Creditors and other payables are initially measured at fair value and, where appropriate, subsequently measured at amortised cost using the effective interest method.

**Income in advance**

Income in advance is recognised where amounts billed are in excess of the amounts recognised as revenue.

**Employee entitlements***Short-term employee entitlements*

Employee entitlements that the Office expects to be settled within 12 months of balance date are measured at nominal values based on accrued entitlements at current rates of pay.

These include salaries and wages accrued up to balance date, annual leave and time off in lieu earned but not yet taken at balance date, retiring and long service leave entitlements expected to be settled within 12 months, and sick leave.

The Office recognises a liability for sick leave to the extent that future absences are expected to be greater than the sick leave entitlements earned in the future. The amount is calculated based on the unused sick leave entitlements that can be carried forward at balance date, to the extent that the Office anticipates those unused entitlements will be used by staff to cover those future absences.

The Office recognises a liability and an expense for bonuses where it is contractually obliged to pay them, or where there is a past practice that has created a constructive obligation.

*Long-term employee entitlements*

Entitlements that are payable beyond 12 months, such as long service leave and retiring leave, have been calculated on an actuarial basis. The calculations are based on:

- likely future entitlements based on years of service, years to entitlement, the likelihood that staff will reach the point of entitlement, and contractual entitlements information; and
- the present value of the estimated future cash flows.

*Presentation of employee entitlements*

Sick leave, annual leave, time off in lieu of overtime worked and vested long service leave are classified as a current liability. Non-vested long service leave and retiring/resigning leave expected to be settled within 12 months of balance date are classified as a current liability. All other employee entitlements are classified as a non-current liability.

**Superannuation schemes**

Obligations for contributions to the Auditor-General's Retirement Savings Plan, KiwiSaver, and the Government Superannuation Fund are accounted for as defined contribution plans, and are recognised as an expense in the surplus or deficit as incurred.

**Provisions**

A provision is recognised for future expenditure of uncertain amount or timing when there is a present obligation (either legal or constructive) as a result of a past event, it is probable that an outflow of future economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Provisions are not recognised for future operating losses.

**Taxpayers' funds**

Taxpayers' funds is the Crown's investment in the Office, and is measured as the difference between total assets and total liabilities.

**Commitments**

Expenses yet to be incurred on non-cancellable contracts that have been entered into on or before balance date are disclosed as commitments to the extent that there are equally unperformed obligations.

Cancellable commitments that have penalty or exit costs explicit in the agreement on exercising that option to cancel are included in the statement of commitments at the value of that penalty or exit cost.

**Goods and Services Tax**

All items in the financial statements, including appropriation statements, are stated exclusive of Goods and Services Tax (GST), except for receivables and payables in the statement of financial position, which are stated on a GST-inclusive basis.

Where GST is not recoverable as input tax, it is recognised as part of the related asset or expense. The net amount of GST recoverable from, or payable to, the Inland Revenue Department (IRD) is included as part of receivables or payables in

the statement of financial position. The net GST paid to or received from the IRD, including the GST relating to investing and financing activities, is classified as an operating cash flow in the statement of cash flows.

Commitments and contingencies are disclosed exclusive of GST.

### **Income tax**

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

### **Main Estimates and Supplementary Estimates**

The Main Estimates figures are those included in the Office's annual plan for the year ended 30 June 2012. In addition, the financial statements also present updated figures from the Supplementary Estimates. The Main estimates and Supplementary estimates figures have been prepared in accordance with NZ GAAP, using accounting policies that are consistent with those adopted in preparing these financial statements.

### **Output cost allocation**

The Office has determined the cost of outputs using allocations as outlined below.

*Direct costs* are those costs directly attributable to a single output.

Direct costs that can readily be identified with a single output are assigned directly to the relevant output class. For example, the cost of audits carried out by contracted audit service providers is charged directly to output class: Provision of audit and assurance services.

*Indirect costs* are those costs that cannot be identified in an economically feasible manner with a specific output. These costs include: corporate services costs; variable costs such as travel; and operating overheads such as property costs, depreciation, and capital charges.

Indirect costs are allocated according to the time charged to a particular activity.

There have been no changes in cost allocation policies since the date of the last audited financial statements.

### **Judgements and estimations**

The preparation of these financial statements requires judgements, estimations, and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

*Audit fee revenue and work in progress*

Assessing the value of audit fee revenue and associated work in progress or income in advance for engagements open at balance date is the most significant area where such judgements, estimations, and assumptions are made. This involves estimating the stage of completion of each engagement based on the value of work completed at balance date and the expected work to complete the engagement. A different assessment of the outcome on an engagement may result in a different value being determined for revenue and also a different carrying value being determined for work in progress.

*Depreciation and amortisation*

Determining the amortisation rates for intangible assets and depreciation rates for physical assets requires judgement as to the likely period of use of the assets. Different assessments of useful lives would result in different values being determined for depreciation or amortisation costs, accumulated depreciation or amortisation, and net book values.

*Retirement and long service leave*

An analysis of the exposure in relation to estimates and uncertainties surrounding retirement and long service leave liabilities is disclosed in note 14.

**Note 2: Crown funding**

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

**Note 3: Audit fee revenue**

Actual 2011 \$000		Actual 2012 \$000
37,486	Fee revenue generated by the Office for audit and assurance services	41,952
27,472	Fee revenue generated by contracted audit service providers for audits of public entities*	29,481
<b>64,958</b>	<b>Total audit fee revenue and other income</b>	<b>71,433</b>

\* Revenue generated by contracted audit service providers does not involve any cash transactions with the Office.

## Note 4: Personnel costs

Actual 2011 \$000		Actual 2012 \$000
33,203	Salaries and wages	35,468
339	Other employee-related costs	299
1,000	Employer contributions to defined contribution plans	1,040
202	Increase/(decrease) in employee entitlements	853
<b>34,744</b>	<b>Total personnel costs</b>	<b>37,660</b>

Employer contributions to defined contribution plans include contributions to the Auditor-General's retirement savings plan, KiwiSaver, and the Government Superannuation Fund.

## Note 5: Other operating costs

Actual 2011 \$000		Actual 2012 \$000
(54)	(Decrease)/Increase in provision for impairment of receivables	(14)
85	Fees to CST Nexia for the audit of the Office's financial statements	88
5	Fees to CST Nexia for other assurance services provided to the Office	30
1,924	Operating lease payments	1,988
138	Fees for audits of public entities carried out by CST Nexia*	123
27,334	Fees for audits of public entities carried out by other contracted audit service providers*	29,358
79	Net loss on disposal	6
8,896	Other expenses	9,967
<b>38,407</b>	<b>Total operating costs</b>	<b>41,546</b>

\* Expenditure relating to audits carried out by contracted audit service providers does not involve any cash transactions with the Office.

## Note 6: Capital charge

The Office pays a capital charge to the Crown on its taxpayers' funds as at 31 May and 30 November each year. The capital charge rate is determined by the Treasury, and for the year ended 30 June 2012 was 8% (2011 – 7.5%).



## Note 7: Overdraft facility

The Office has the use of an overdraft facility to manage its seasonal cash flows during the second half of the financial year. The overdraft limit is \$500,000, and interest is charged on the daily balance at Westpac Banking Corporation's Prime Lending Rate.

During this financial year, no funds were drawn down under the facility (and none were drawn down in 2010/11).

## Note 8: Debtors and other receivables

Actual 2011 \$000		Actual 2012 \$000
6,195	Debtors	6,782
(192)	Less provision for impairment of receivables	(178)
6,003	<i>Net debtors</i>	6,604
0	Other receivables	148
<b>6,003</b>	<b>Total debtors and other receivables</b>	<b>6,752</b>
	<b>Represented by:</b>	
6,003	Current	6,752
0	Non-current	0
<b>6,003</b>	<b>Total</b>	<b>6,752</b>

The carrying value of debtors and other receivables approximates their fair value.

As at 30 June 2012 and 2011, all overdue receivables have been assessed for impairment and appropriate provisions applied, as detailed below:

	2011			2012		
	Gross \$000	Impair- ment \$000	Net \$000	Gross \$000	Impair- ment \$000	Net \$000
Not past due	3,838		3,838	5,537		5,537
Past due 1-30 days	1,814		1,814	733		733
Past due 31-60 days	111		111	162		162
Past due 61-90 days	90		90	0		0
Past due >90 days	342	(192)	150	350	(178)	172
<b>Carrying amount</b>	<b>6,195</b>	<b>(192)</b>	<b>6,003</b>	<b>6,782</b>	<b>(178)</b>	<b>6,604</b>

The impairment provision has been calculated based on expected losses for the Office's pool of debtors. Expected losses have been determined based on an analysis of the Office's losses in previous periods and review of specific debtors.

Movements in the provision for impairment of receivables are as follows:

Actual 2011 \$000		Actual 2012 \$000
246	Balance at 1 July	192
(54)	Decrease in provisions made during the year	(14)
0	Receivables written off during the year	0
<b>192</b>	<b>Balance at 30 June</b>	<b>178</b>

## Note 9: Plant and equipment

	Furniture and fittings \$000	Office equipment \$000	Leasehold improve- ments \$000	IT hardware \$000	Motor vehicles \$000	Total \$000
<b>Cost</b>						
Balance at 1 July 2010	2,570	239	0	2,451	1,304	6,564
Additions	4	43	0	333	396	776
Disposals	(407)	(10)	0	(419)	(364)	(1,200)
Balance at 30 June 2011	2,167	272	0	2,365	1,336	6,140
Additions	2	1	282	303	367	955
Asset Reclassification		500		(500)		0
Disposals	(65)	(31)	0	(467)	(442)	(1,005)
Balance at 30 June 2012	2,104	742	282	1,701	1,261	6,090
<b>Accumulated depreciation and impairment losses</b>						
Balance at 1 July 2010	2,430	208	0	2,112	587	5,337
Depreciation expense	78	19	0	261	205	563
Elimination on disposal	(396)	(11)	0	(419)	(238)	(1,064)
Balance at 30 June 2011	2,112	216	0	1,954	554	4,836
Depreciation expense	39	25	0	257	223	544
Asset reclassification*		500		(500)		0
Elimination on disposal	(62)	(31)	0	(467)	(323)	(883)
Balance at 30 June 2012	2,089	710	0	1,244	454	4,497
<b>Carrying amounts</b>						
Balance at 1 July 2010	140	31	0	339	717	1,227
Balance at 30 June 2011	55	56	0	411	782	1,304
<b>Balance at 30 June 2012</b>	<b>15</b>	<b>32</b>	<b>282</b>	<b>457</b>	<b>807</b>	<b>1,593</b>

\* The Office has reviewed its asset classification and, as a result, has transferred a number of assets from computer hardware to office equipment in order to more fairly reflect the nature of those assets.

**Work in progress**

The total amount of leasehold improvements in the course of construction is \$282,433 (2011 – nil).

**Note 10: Intangible assets**

	Acquired software \$000	Internally generated software \$000	Total \$000
<b>Cost</b>			
Balance at 1 July 2010	3,134	120	3,254
Additions	76	0	76
Disposals	0	0	0
Balance at 30 June 2011	3,210	120	3,330
Additions	198	0	198
Disposals	(237)	0	(237)
Balance at 30 June 2012	3,171	120	3,291
<b>Accumulated amortisation and impairment losses</b>			
Balance at 1 July 2010	2,176	40	2,216
Amortisation expense	280	24	304
Disposals	0	0	0
Balance at 30 June 2011	2,456	64	2,520
Amortisation expense	318	24	342
Disposals	(230)	0	(230)
Balance at 30 June 2012	2,544	88	2,632
<b>Carrying amounts</b>			
At 1 July 2010	958	80	1,038
At 30 June 2011	754	56	810
At 30 June 2012	627	32	659

There are no restrictions over the title of the Office's intangible assets. No intangible assets are pledged as security for liabilities.

## Note 11: Creditors and other payables

Actual 2011 \$000		Actual 2012 \$000
1,932	Creditors	1,386
2,154	Income in advance	2,751
430	Accrued expenses	672
531	GST payable	633
<b>5,047</b>	<b>Total creditors and other payables</b>	<b>5,442</b>

Creditors and other payables are non-interest-bearing, and are normally settled on 30-day terms. The carrying value of creditors and other payables therefore approximates their fair value.

## Note 12: Surplus payment due to the Crown

The Office is not permitted to retain operating surpluses under the Public Finance Act 1989. Thus, the surplus for the year of \$1,449,567 is repayable to the Crown, and is due to be paid by 31 October 2012.

Actual 2011 \$000		Actual 2012 \$000
916	Surplus current year	1,449
2,014	Surplus brought forward	916
(2,014)	Payment to the Crown	(916)
<b>916</b>	<b>Total provision for payment to the Crown</b>	<b>1,449</b>

## Note 13: Provisions

Actual 2011 \$000		Actual 2012 \$000
0	Onerous contracts	59
0	Lease make good	150
<b>0</b>	<b>Total provisions</b>	<b>209</b>

	Onerous contracts \$000	Lease make good \$000	Total \$000
Balance at 1 July 2011	0	0	0
Additional provisions made	59	150	209
Amounts used	0	0	0
<b>Balance at 30 June 2012</b>	<b>59</b>	<b>150</b>	<b>209</b>

### Onerous contracts

The provision for onerous contracts arises from a non-cancellable lease where the unavoidable costs of meeting the lease contract exceed the economic benefits to be received from it. The Office expects to vacate its Audit NZ Wellington premises at the beginning of June 2013, when the OAG and Audit NZ Wellington offices will move into one location. The current Audit NZ Wellington office lease expires on 30 June 2013.

### Lease make good

In respect of one of its leased premises, the Office is required at the expiry of the lease term to make good any damage caused to the premises.

## Note 14: Employee entitlements

Actual 2011 \$000		Actual 2012 \$000
	<b>Current employee entitlements comprise:</b>	
1,493	Salary and other accruals	2,073
2,114	Annual leave	2,262
102	Long service leave	99
94	Time off in lieu of overtime worked	152
91	Retirement leave	150
77	Sick leave	106
3,971	<i>Total current portion</i>	4,842
	<b>Non-current employee entitlements comprise:</b>	
19	Long service leave	0
567	Retirement leave	568
586	<i>Total non-current portion</i>	568
<b>4,557</b>	<b>Total employee entitlements</b>	<b>5,410</b>

The measurement of the retirement and long service leave obligations depend on a number of factors that are determined on an actuarial basis using a number of assumptions. Two key assumptions used in calculating this liability include the discount rate and the salary inflation factor. Any changes in these assumptions will affect the carrying amount of the liability.

The discount rate is based on NZ Government bond data at 30 June 2012. The salary inflation factor has been determined after considering historical salary inflation patterns and after obtaining advice from an independent actuary.

If the discount rate were to differ by 1% from the Office's estimates, with all other factors held constant, the carrying amount of the liability would be an estimated \$39,960 higher/lower.

If the salary inflation factor were to differ by 1% from the Office's estimates, with all other factors held constant, the carrying amount of the liability would be an estimated \$57,079 higher/lower.

### **Note 15: Reconciliation of surplus to net cash flow from operating activities**

This reconciliation discloses the non-cash adjustments applied to the surplus reported in the statement of comprehensive income on page 76, to arrive at the net cash flow from operating activities disclosed in the statement of cash flows on page 79.

Actual 2011 \$000		Actual 2012 \$000
916	<b>Surplus</b>	1,449
	<b>Non-cash items</b>	
867	Depreciation and amortisation	886
867	<i>Total non-cash Items</i>	886
	<b>Working capital movements</b>	
(77)	(Increase)/decrease in prepayments	(586)
(499)	(Increase)/decrease in debtors and other receivables	(749)
239	(Increase)/decrease in work in progress	679
656	(Decrease)/increase in payables	395
0	(Decrease)/increase in provisions	209
180	(Decrease)/increase in employee entitlements	871
499	<i>Total net working capital movements</i>	819
	<b>Investing activity items</b>	
53	Loss/(profit) on sale of plant and equipment	(50)
0	Loss/(profit) on sale of intangible assets	0
53	<i>Total net investing activity items</i>	(50)
	<b>Other items</b>	
22	Increase/(decrease) in non-current employee entitlements	(18)
22	<i>Total other items</i>	(18)
2,357	<b>Net cash flow from operating activities</b>	3,086

## Note 16: Related party transactions

All related party transactions have been entered into on an arms' length basis.

The Office is a wholly-owned entity of the Crown. The Government is a major source of revenue for the Office.

### Significant transactions with government-related entities

The Office has received funding from the Crown of \$10.045 million (2011– \$10 million) to provide performance audits, inquiries, advice to parliament and audits of small entities for the year ended 30 June 2012.

### Collectively, but not individually significant transactions with government-related entities

In conducting its activities, the Office is required to pay various taxes and levies (such as GST, FBT, PAYE, and ACC levies) to the Crown and entities related to the Crown. The payment of these taxes and levies, other than income tax, is based on the standard terms and conditions that apply to all tax and levy payers. The Office is exempt from paying income tax.

The Office also purchases goods and services from entities controlled, significantly influenced, or jointly controlled by the Crown. Purchases from these government-related entities for the year ended 30 June 2012 totalled \$1.981 million (2011 \$2.124 million). These purchases included air travel from Air New Zealand, office rental from State Services Commission, capital charge from The Treasury, and postal services from New Zealand Post.

During the year, there were transactions between the Office and close family members of key management personnel, as follows:

- Some close family members of key management personnel were employed by the Office. The terms and conditions of their appointment were no more favourable than the Office would have adopted if there were no relationship to key management personnel.
- Close family members of a member of key management personnel were directors in a company that provided services to the Office under a contract that was entered into prior to the appointment of the member. The cost of the services purchased was \$4,370 (2011 – \$9,852) and there was nil outstanding at balance date (2011 – \$8,165).

#### Key management personnel compensation

Actual 2011 \$000		Actual 2012 \$000
3,201	Salaries and other short-term employee benefits	3,348
0	Post-employment benefits	0
0	Other long-term benefits	0
0	Termination benefits	0
<b>3,201</b>		<b>3,348</b>

Key management personnel include the Auditor-General, the Deputy Auditor-General, and the ten members of the OAG and Audit New Zealand Leadership Teams.

#### Note 17: Financial instrument risks

The Office's financial instruments are limited to cash and cash equivalents, debtors and other receivables, and creditors and other payables. These activities expose the Office to low levels of financial instrument risks, including market risk, credit risk, and liquidity risk.



**Market risk***Currency risk*

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The Office incurs a small portion of operating expenditure in foreign currency, and risk is minimised through prompt settlement. Recognised liabilities that are payable in a foreign currency were nil at balance date (2011 – \$313,000).

*Interest rate risk*

Interest rate risk is the risk that the fair value of a financial instrument will fluctuate, or the cash flows from a financial instrument will fluctuate, due to changes in market interest rates.

The Office has no interest-bearing financial instruments and, accordingly, has no exposure to interest rate risk.

**Credit risk**

Credit risk is the risk that a third party will default on its obligation to the Office, causing the Office to incur a loss.

In the normal course of the Office's business, credit risk arises from debtors and other receivables and deposits with banks.

The Office is permitted to deposit funds only with Westpac, a registered bank with high credit ratings. For its other financial instruments, the Office does not have significant concentrations of credit risk.

The Office's maximum credit exposure for each class of financial instrument is represented by the total carrying amount of cash and cash equivalents, and net debtors and other receivables (see Note 8).

There is no collateral held as security against these financial instruments, including those instruments that are overdue or impaired.

**Liquidity risk**

Liquidity risk is the risk that the Office will encounter difficulty raising liquid funds to meet commitments as they fall due.

In meeting its liquidity requirements, the Office closely monitors its forecast cash requirements with expected debtor receipts and cash drawdowns from the New Zealand Debt Management Office. The Office maintains a target level of available cash to meet liquidity requirements.

The Office's financial liabilities are outlined in Note 11: Creditors and other payables. These are all due to be settled within two months.

## Note 18: Categories of financial instruments

The carrying amounts of financial instruments in each of the NZ IAS 39 categories are as follows:

Actual 2011 \$000		Actual 2012 \$000
	<b>Loans and receivables</b>	
4,283	Cash and cash equivalents	5,479
6,003	Debtors and other receivables (Note 8)	6,752
<b>10,286</b>	<b>Total loans and receivables</b>	<b>12,231</b>
	<b>Financial liabilities measured at amortised cost</b>	
5,047	Creditors and other payables (Note 11)	5,442
<b>5,047</b>	<b>Total creditors and other payables</b>	<b>5,442</b>

## Note 19: Management of taxpayers' funds (equity)

The Office's taxpayers' funds (equity) comprise general funds and is represented by net assets.

The Office manages its revenues, expenses, assets, liabilities, and general financial dealings prudently to achieve the goals and objectives for which it has been established. The Office's equity is largely managed as a by-product of managing income, expenses, assets, liabilities, and compliance with the Government Budget processes and Treasury Instructions.

## Note 20: Explanation of major variances against budget

Explanations for major variances from the Office's forecast figures in our *Annual Plan 2011/12* are as follows:

### Statement of comprehensive income

Operating costs were lower than forecast, mainly due to the overall efficiencies arising from a high volume audit year. The forecast reflects the revenue dependent appropriation.

Depreciation and amortisation expense was lower than forecast as capital expenditure on intangible assets did not occur as planned.

### Statement of changes in taxpayers' funds

In 2011, Parliament approved a capital contribution of \$2.2 million to fund the fitout of the Office's Wellington premises, and this was reflected in the main estimates for 2011/12. However, the fitout will now take place in 2012/13.

**Statement of financial position**

Current assets are higher than forecast, which is mainly due to a higher cash balance arising from the operating surplus for the year. Debtors and other receivables are also higher than forecast and work in progress lower than forecast due to the timing of audit fee invoicing.

Current liabilities are higher than forecast, which is attributable to the provision for repayment of surplus to the Crown and higher payables due to the timing of payments at the end of the financial year.

**Note 21: Office accommodation statistics**

The following statistics are provided in accordance with directives issued by the Government to chief executives in 1991 on the management of departmental accommodation.

Actual 2011		Actual 2012
6037m <sup>2</sup>	Area	6207m <sup>2</sup>
367	Number of staff (FTE)	374
16.4m <sup>2</sup>	Space allocation per person	17m <sup>2</sup>
\$1,908,955	Total costs of leased office accommodation	\$1,961,746
\$5,202	Rent costs per person	\$5,241
\$266	Utility costs per person	\$255
0	Vacant accommodation	0



## Appendix 1

# Entities audited under section 19 of the Public Audit Act 2001

Section 37(2)(c) of the Public Audit Act 2001 (the Act) requires us to include in the annual report a list of entities audited by the Auditor-General under an arrangement in accordance with section 19 of the Act.

At 30 June 2012, arrangements had been entered into for audits of the following entities:

- Unipol Recreation Limited
- Māori Education Trust
- Literacy Aotearoa
- Tokelau International Trust Fund
- NZ Sports Foundation Charitable Trust
- Greytown District Trust Lands Trust
- TLab Limited
- AUT/Millennium Ownership Trust
- Antarctic Institute: Andriil Joint Venture.



## Appendix 2

# Independent review of audit allocation and fee setting and monitoring report

109

From SIR DAVID GASCOIGNE

PO Box 2793  
Wellington  
New Zealand

Tel: +64 4 498 5120  
Mobile: +64 274 405 405  
e-mail: david.gascoigne@xtra.co.nz

14 August 2012

Mrs Lyn Provost  
Controller and Auditor-General  
PO Box 3928  
WELLINGTON

Dear Mrs Provost,

### ANNUAL REPORT OF THE INDEPENDENT REVIEWER OF AUDIT ALLOCATION PROCESSES

1. You have retained me as an independent reviewer of the basis upon which auditors are appointed to act on your behalf, and the basis upon which appropriate levels of audit fees are determined.
2. This is my report on those processes for the financial year ended 30 June 2012. I confirm that I am independent of the Office of the Auditor-General (OAG), Audit New Zealand and all private sector audit firms.
3. My instructions require me to evaluate the processes involved and to report upon the probity and objectivity with which they are implemented. No limitation has been placed upon the manner in which I carry out my assignment. I have been free to inspect both paper and computer based files, documents and correspondence as I wished.
4. There are three distinct types of allocation process:
  - (a) an allocation made by the Auditor-General of an auditor for a given entity, in accordance with "the audit allocation model";
  - (b) an appointment of an auditor for a given entity, following a contestable tender; and
  - (c) a re-appointment for a further term of an appointed auditor's contract to audit a particular entity.
5. **Allocations:** In the past financial year, the Auditor-General appointed auditors for 58 new entities. That number includes 15 schools or school-related entities. Apart from schools, these new entities include, for example, newly established Crown entities, new subsidiaries of existing entities, new entities resulting from mergers. The "audit allocation model" under which those appointments were made has been the principal method of allocation since 2003. There is an established and now well-publicised set of criteria for those appointments (see paragraphs 6 and 7 below). There has been no evident dissatisfaction expressed by those entities either with the method or with the terms of any of the appointments effected during the year.
6. In the last year's report (paragraphs 22 to 24) I described the work then underway to review – and to improve – the audit allocation model. The purpose of the work was to revise the underlying principles of the model, with a view to making the process more efficient and more responsive to changing circumstances. The restated principles were to be clearly enunciated, but were also to be capable of some flexibility in their operation.

7. There was widespread consultation during the course of the review. The revised model is now being applied progressively, sector by sector. In my view, the process has been well handled, and seems to have been well received by those affected.
8. **Contestable Tenders:** No appointments were made by means of this process during the past year. The process still remains available, in particular circumstances, but the increasing sophistication and practicality of the audit allocation model mean that the use of contestable tenders is likely to occur only occasionally. A contestable tender process for the appointment of an auditor would most likely be used only for a large entity with a commercial focus. The Auditor-General does, nonetheless, contemplate that the use of this process may be useful in some other circumstances.
9. **Re-appointments: generally:** Leaving aside the position as to auditors for schools (see the following paragraph 10), existing auditors were re-appointed during the financial year to audit 385 public entities and their subsidiaries for a further term. In addition, in 8 instances a change was effected, with a different auditor being appointed in place of an existing one. The circumstances leading to these latter appointments involved auditor independence and auditor/entity relationship issues. Again, in the case of all 393 appointments covered by this paragraph 10, a careful process has been followed. There have been no unresolved issues arising from the method or the terms of appointment.
10. **Reappointments: schools:** Every three years a major exercise takes place involving the appointment or re-appointment of auditors for approximately 2,440 schools. (The approximation arises from the fact that the numbers are not static.) That exercise was last carried out in 2009. It is being undertaken again in 2012, in respect of the three year period beginning on 1 January 2012. It is a large and detailed exercise, but it is proceeding satisfactorily.
11. Apart from that exercise, for the OAG's financial year ended 30 June 2012, the main activity in relation to the appointment of auditors for schools has been where a new school has been established, or a private school has become integrated. In that regard, appointments of auditors have been made for 15 new or integrated schools or school-related entities (see paragraph 5).
12. In addition, the auditors of 11 schools were changed during the past contract period to 31 December 2011 – 9 of them because the existing appointed auditor was unable to carry out the audit so that a new one needed to be appointed, and 2 for other reasons.
13. Again, there was no evident dissatisfaction with the processes described in the two preceding paragraphs.
14. **Issues about fees:** During the course of the past year, a number of entities raised questions or made complaints about the level of increase in audit fees or, occasionally, about auditor performance. Some of these have been informal in nature (and have been readily and promptly resolved). Others have been more formal in nature (with well articulated letters expressing the grounds for an entity's concern).
15. The basis for these claims about fees is, generally, that in difficult financial times, when an entity's revenue is constrained, it is neither appropriate nor fair that an audit fee should remain at a high level. There is sometimes a perception held by an entity that an alternative auditor could do the task for less than the current fee.
16. The OAG has a detailed data-base which has become both sophisticated and precise. It provides an analysis of audit fees for all public entities. The contributing components (hours and rates, levels of experience) of the fees for all types and sizes of entities, year by year, individually and sector by sector, may be compared and contrasted. In particular,



3

the movement in hourly rates and in time expended on an audit, or a range of audits, can be accurately identified.

17. The OAG uses this material, constructively, to help respond to enquiries or complaints received. The response is usually given by the OAG direct to the entity, though sometimes the auditor responds, using the data supplied by the OAG. In either case, the data which is relevant to a particular entity is recorded in an explanatory letter, along with a description of the various factors lying behind the cost increases.
18. In a small number of cases, it is apparent that the actions of the entity itself have contributed to the increase in fees. For example, in some cases the materials that will require audit are poorly presented, incomplete, contradictory or have several iterations. Those factors tend to result in an increase in the auditor's time, with a consequent increase in fees.
19. In the great majority of cases, the detailed explanation given to entities by the OAG (or, in some cases, by an auditor using data supplied by the OAG) has led to a resolution, or to a withdrawal of the complaint, or to no further action being taken by the entity. In the year under review I inspected the records in respect of 16 entities which had expressed concern about the level of fees or auditor performance. In all those cases a resolution has either been achieved or is clearly foreshadowed. In other words, as at 30 June 2012, there were no instances of significant and continuing contention.
20. My review of the materials for the financial year to 30 June 2012 has again shown that where, occasionally, there is some dissatisfaction expressed by entities or auditors, it tends to centre upon two particular issues.
21. The first is related to auditor performance or auditor/entity relationship. This arises very infrequently, but when it does, it has consistently been resolved. The resolution occasionally entails a well-considered change in the appointed auditor. I have seen nothing untoward in this regard.
22. The second relates to the level of fees – either initially or upon a subsequent claim for increase. Viewed broadly, the role of the Auditor-General, acting through the OAG, is to ensure that audit fees are fair and reasonable. The OAG provides detailed information, when needed, with a view to assisting the entity and the auditor to come to an accord about this. As a former Auditor-General has said, it is important that an audit fee is struck, in each case, that gives the entity, the Auditor-General and Parliament “confidence that an audit may be conducted to the standards required of public sector entities and provides a fair return (but no more than that) to the auditor to do the job that all expect.” Overall, my view is that that objective has been substantially achieved during the past year.
23. **Auckland Council: residual issues:** In my report for the previous year, I commented upon the timely and comprehensive planning leading up to the amalgamation of Councils and Council Controlled Organisations that took place in Auckland in October 2010.
24. Viewed broadly, from an auditing perspective the transitions have gone well. Some of the systems, especially those involving some smaller entities, have not come together as readily as had been hoped. There is still some rationalisation – and thus efficiencies and savings – yet to be achieved. The OAG is seeking to have these aspects finalised. Overall, however, a very large and complex process of change in audit structures and processes is being achieved satisfactorily.
25. **Christchurch earthquakes:** The calamitous events in Christchurch have given rise to many new issues. The financial impact on the city has been severe. And this has created a need for speedy, practical responses. But prudence and a sense of responsibility must also be maintained.

26. The efforts of the OAG, the auditing community generally, and the public entities – all of which have had to adapt quickly - have been commendable. I have inspected the files of the more significant entities affected. These include: Christchurch City Council, Canterbury Earthquake Recovery Authority; The Earthquake Commission, Christchurch Earthquake Appeal Trust, Christchurch Stadium Trust, AML Insurance Ltd, Southern Response Earthquake Services Ltd, and others.
27. I have noticed a common effort to be cooperative and practical in matters relating to audit and control. In many cases, the greatly increased volumes of work and uncertainty do justify some increase in fees. Generally, there has been give and take on both sides. (In one case, an auditor volunteered to continue on a pro bono basis.) There are still many issues to be worked through and resolved. (For example: how to manage donations and to ensure they are applied for the purposes for which they were given.) But I believe that, with the goodwill that is evident, solutions in all likelihood will be found and agreed.
28. **Other issues:** I have observed a number of other issues that have evolved during the past year. They include:
  - (a) **Fees publication:** In my report last year I mentioned the work that was being done, consultatively, on developing a new paper entitled "Appointing public sector auditors and setting audit fees." That paper has now been completed and has been made widely available. I consider that it sets out the principles and processes fairly, clearly and concisely. It should help public entities and auditors alike to engage more effectively in the processes overseen by the Auditor-General;
  - (b) **Regulatory issues:** I have noted that the OAG has taken or is taking steps to ensure compliance with existing, new or pending requirements, such as:
    - (i) International Standards of Auditing provisions as to the change and rotation of auditors;
    - (ii) Financial Markets Authority and NZ Institute of Chartered Accountants requirements as to the licensing of auditors;
    - (iii) The Maori Trust Boards Amendment Act 2011 has the effect of making Maori Trust Boards directly responsible to their beneficiaries, with the consequence that they will now fall outside the Auditor-General's statutory audit mandate. Transitional arrangements are being evolved, in anticipation of the change.
  - (c) **Limited liability companies:** The Public Audit Act does not allow the Auditor-General to contract with limited liability companies for the conduct of audits of public entities. Contracts must be with either individual auditors, or with partnerships comprising individuals. It was found recently that there were three instances where auditors had sought to introduce limited liability companies they had set up into the contractual arrangements. That has been stopped and processes have been put in place to avoid any recurrence;
  - (d) **Large mergers:** The recent merger of Ministries which resulted in the formation of the Ministry of Business Innovation and Enterprise has been effected and audit arrangements satisfactorily concluded. This merger was not as complex as the one involving Auckland Council, but the issues that arose were much the same. The work which the OAG had done in relation to the Auckland merger proved valuable in this regard;
  - (e) **Foreign jurisdiction entities:** The Auditor-General and the OAG have clarified the position about audit arrangements for overseas subsidiaries of New Zealand

5

based public entities. The position that has been reached is that the Public Audit Act does not give the Auditor-General any mandate over entities established outside New Zealand. The practical outcome is that appointed auditors of New Zealand entities are required to take steps to gather sufficient information on overseas subsidiaries to be able to provide an audit opinion on consolidated group accounts. I have considered the process by which that conclusion was reached. I consider it to be correct in principle and practical in its outcome.

29. **Conclusions:** I now state my overall conclusions. These follow from what I have said in the preceding paragraphs of this letter. My conclusions are:
- (a) On the basis of the written material I have seen and the explanations I have been given by OAG personnel, I consider that the processes adopted by the Auditor-General and by the OAG in relation to the allocation and appointment of auditors for audits falling within the Auditor-General's mandate, during the financial year to 30 June 2012, have been appropriate for their purpose, and have been applied in a way which is fair and responsible, having regard to the respective interests of the parties concerned;
  - (b) That observation applies both to the way in which auditors have been appointed or re-appointed, and to the way in which questions as to the appropriateness of a proposed audit fee have been dealt with;
  - (c) In cases where issues have been raised by entities as to fee levels or as to auditor performance, those issues have been, or are being, dealt with fairly and professionally;
  - (d) Other issues which I have examined (such as those referred to in paragraphs 23 to 28) which touch upon the Auditor-General's mandate and the operations of the OAG have, in my view, been evolved reasonably and responsibly.
30. Taking everything into account, my conclusion is that the processes by which audits in the public sector have been allocated and fees have been set, in the financial year to 30 June 2012, have been carried out with due probity and objectivity.

Yours sincerely



Sir David Gascoigne, KNZM, CBE



## Appendix 3

# List of our major reports completed in 2011/12

### Performance audits

New Zealand Customs Service: Providing assurance about revenue (published 5/7/11)

Home-based support services for older people (published 12/7/11)

Planning to meet the forecast demand for drinking water in Auckland (letter published 17/8/11)

Government planning and support for housing on Māori land (published 6/9/11)

New Zealand Transport Agency: Delivering maintenance and renewal work on the state highway network (published 27/9/11)

Managing freshwater quality: Challenges for regional councils (published 27/9/11)

The Treasury: Implementing and managing the Crown Retail Deposit Guarantee Scheme (published 4/10/11)

Transpower New Zealand Limited: Managing risks to transmission assets (published 4/10/11)

Report on Defence major projects report (published 15/11/11)

New Zealand Blood Service: Managing the safety and supply of blood products (published 14/2/12)

Public entities' progress in implementing the Auditor-General's recommendations 2012 (published 3/5/12)

New Zealand Qualifications Authority: Assuring the consistency and quality of internal assessment for NCEA (published 31/5/12)

Institutional arrangements for training, registering, and appraising teachers (published 12/6/12)

Realising benefits from six public sector technology projects (published 27/6/12)

### Inquiries

Inquiry into the use of parliamentary travel entitlements by Mr and Mrs Wong (published 5/9/11)

Inquiry into how Christchurch City Council managed conflicts of interest when it made decisions about insurance cover (published 19/4/12)

### Other reports and studies

Local government: Improving the usefulness of annual reports (published 27/9/11)

Managing the implications of public private partnerships (published 17/11/11)

Severance payments: A guide for the public sector (published 20/3/12)

Summary of our fraud survey results - individual volumes for nine different sectors (last volume published 1/6/12):

- Summary of our fraud survey results for government departments
- Summary of our fraud survey results for local authorities
- Summary of our fraud survey results for district health boards
- Summary of our fraud survey results for tertiary education institutions
- Summary of our fraud survey results (for Crown research institutes, Autonomous Crown entities, Crown agents or companies, Independent Crown entities, and Central government – other)
- Summary of our fraud survey results for schools
- Summary of our fraud survey results for local government entities
- Summary of our fraud survey results for State-owned enterprises
- Summary of our fraud survey results for licensing and community trusts

Fraud awareness, prevention, and detection in the public sector (published 19/6/12)

Reviewing financial management in central government (published 28/6/12)

Appointing public sector auditors and setting audit fees (published 10/8/11)

The Emissions Trading Scheme – summary information for public entities and auditors (published 25/8/11)

Overview of the Auditor-General's work in the transport sector (published 5/4/12)

District Health Boards: Quality annual reports (published 25/6/12)

**Reports on matters arising out of the performance and exercise of the Auditor-General's functions, duties, and powers (under section 20 of the Public Audit Act 2001)**

Central government: Results of the 2010/11 audits (Volume 1) (published 21/12/11)

Education sector: Results of the 2010/11 audits (published 21/12/11)

Health sector: Results of the 2010/11 audits (published 6/3/12)

Central government: Results of the 2010/11 audits (Volume 2) (published 7/3/12)

Local government: Results of the 2010/11 audits (published 5/4/12)

Note. The first 22 reports are funded from Output class: Performance audits and inquiries. See page 53 for measure and results.

## Appendix 4

# Senior management

Controller and Auditor-General

Lyn Provost

Deputy Controller and Auditor-General

Phillippa Smith

### **OAG Leadership Team**

Assistant Auditor-General, Accounting and Auditing Policy

Greg Schollum

Assistant Auditor-General, Corporate Services

Peter Grant

Assistant Auditor-General, Legal

Nicola White

Assistant Auditor-General, Local Government

Bruce Robertson

Assistant Auditor-General, Parliamentary Group

Gareth Ellis

Assistant Auditor-General, Performance Audit Group

Mike Scott

Assistant Auditor-General, Research and Development

Ann Webster

### **Audit New Zealand Executive Leadership Team**

Executive Director, Audit New Zealand

Stephen Walker

General Manager, Operations

Bethia Gibson

General Manager, Professional Practices

Chong Lim

Assistant Auditor-General, Corporate Services

Peter Grant





## Appendix 5

# Directory of offices

### Office of the Auditor-General

Level 1, 100 Molesworth Street  
PO Box 3928  
Wellington 6140  
Telephone: (04) 917 1500  
Fax: (04) 917 1549  
Website: [www.oag.govt.nz](http://www.oag.govt.nz)

### Audit New Zealand

#### National Office

Level 8, St Paul's Square  
45 Pipitea Street  
PO Box 99  
Wellington 6140  
Telephone: (04) 496 3099  
or 0508 283 486 (0508 AUDIT NZ)  
Fax: (04) 496 3095  
Website: [www.auditnz.govt.nz](http://www.auditnz.govt.nz)

#### Auckland

Level 6, 280 Queen Street  
PO Box 1165  
Auckland 1140  
Telephone: 0508 283 486 (0508  
AUDIT NZ)  
Fax: (09) 366 0215

#### Hamilton

17 Clifton Road  
PO Box 256  
Hamilton 3240  
Telephone: 0508 283 486 (0508  
AUDIT NZ)  
Fax: (07) 838 0508

### Tauranga

745 Cameron Road  
PO Box 621  
Tauranga 3140  
Telephone: 0508 283 486  
(0508 AUDIT NZ)  
Fax: (07) 577 9321

### Palmerston North

49 Victoria Avenue  
PO Box 149  
Palmerston North 4440  
Telephone: 0508 283 486  
(0508 AUDIT NZ)  
Fax: (06) 356 7794

### Wellington

Level 8, St Paul's Square  
45 Pipitea Street  
PO Box 99  
Wellington 6140  
Telephone: (04) 496 3099  
or 0508 283 486 (0508 AUDIT NZ)  
Fax: (04) 496 3195

### Christchurch

Unit 4B, 337 Harewood Road  
Bishopdale  
PO Box 2  
Christchurch 8140  
Telephone: 0508 283 486  
(0508 AUDIT NZ)  
Fax: (03) 359 4128

### Dunedin

Level 1, 399 Moray Place  
PO Box 232  
Dunedin 9054  
Telephone: 0508 283 486  
(0508 AUDIT NZ)  
Fax: (03) 479 0447



# Publications by the Auditor-General

Other publications issued by the Auditor-General recently have been:

- Roles, responsibilities, and funding of public entities after the Canterbury earthquakes
- Effectiveness of arrangements to check the standard of services provided by rest homes: Follow-up audit
- Inquiry into aspects of ACC's Board-level governance
- Education for Māori: Context for our proposed audit work until 2017
- How the Far North District Council has administered rates and charges due from Mayor Wayne Brown's company, Waahi Paraone Limited
- Reviewing financial management in central government
- Realising benefits from six public sector technology projects
- Annual Plan 2012/13
- District health boards: Quality annual reports
- Fraud awareness, prevention, and detection in the public sector
- Institutional arrangements for training, registering, and appraising teachers
- New Zealand Qualifications Authority: Assuring the consistency and quality of internal assessment for NCEA
- Statement of Intent 2012–2015
- Public entities' progress in implementing the Auditor-General's recommendations 2012
- Inquiry into how Christchurch City Council managed conflicts of interest when it made decisions about insurance cover
- Overview of the Auditor-General's work in the transport sector
- Local government: Results of the 2010/11 audits

## Website

All these reports, and many of our earlier reports, are available in HTML and PDF format on our website – [www.oag.govt.nz](http://www.oag.govt.nz). Most of them can also be obtained in hard copy on request – [reports@oag.govt.nz](mailto:reports@oag.govt.nz).

## Notification of new reports

We offer facilities on our website for people to be notified when new reports and public statements are added to the website. The home page has links to our RSS feed, Twitter account, Facebook page, and email subscribers service.

## Sustainable publishing

The Office of the Auditor-General has a policy of sustainable publishing practices. This report is printed on environmentally responsible paper stocks manufactured under the environmental management system standard AS/NZS ISO 14001:2004 using Elemental Chlorine Free (ECF) pulp sourced from sustainable well-managed forests. Processes for manufacture include use of vegetable-based inks and water-based sealants, with disposal and/or recycling of waste materials according to best business practices.

Office of the Auditor-General  
PO Box 3928, Wellington 6140

Telephone: (04) 917 1500  
Facsimile: (04) 917 1549

Email: [reports@oag.govt.nz](mailto:reports@oag.govt.nz)  
Website: [www.oag.govt.nz](http://www.oag.govt.nz)