Peer Review of the Office of the Comptroller and Auditor General

December 2008

1. Introduction

1.1 Peer reviews are common in the international auditing community. The review is an evaluation of the performance of an Audit Office, generally by members of one or more other Audit Offices. Because of the necessary independence of an Audit Office, there may be few mechanisms for oversight of its activities within its own jurisdiction. Review by its international peers is intended to compensate for that lack, without jeopardising the independence of the office subject to review.

1.2 Nearly all countries have an Audit Office – some official body or officer whose function it is to assist in holding the executive to account for its use of public funds. Office models vary. Common law jurisdictions, including the Republic of Ireland, the constituent countries of the United Kingdom, Australia and New Zealand, have an Auditor General. We drew on our knowledge of the various Audit Offices in those countries in carrying out this review.

1.3 Terms of reference

1.4 The then Comptroller and Auditor General[1] asked us to advise him on what his Office[2] needed to do to be an effective organisation. He set the following terms of reference:

'The Review will be a high level overview designed to assess

- the efficiency and effectiveness of the financial audits and value for money examinations conducted by the Office
- the management and governance of the Office
- the extent to which the Office delivers on its mandate.

1.5 The review team will make recommendations as it deems fit.'

1.6 The members of the review team are listed in Appendix 2.

1.7 Methodology

1.8 We carried out our review in Dublin in the second half of April 2008. We had earlier selected a range of people we wanted to interview and asked the Office to arrange appointments with them. All of those we nominated agreed to see us. We selected interviewees who could inform us about:

- the role of the Office in the Irish public sector, and its relationship with the civil service and other parts of the public sector;
- the role of the Office in relation to the Public Accounts Committee of the Dáil;
- the performance of the Office in carrying out financial audits;
- the performance of the Office in carrying out value for money examinations; and
- the governance and operations of the Office generally.

1 The Comptroller and Auditor General is referred to in the report as 'Auditor General'.
2 Office of the Comptroller and Auditor General, referred to in this report as 'the Office'.

1.9 Some of the people who spoke to us were able to inform us on two or more of these matters. A list of the people we interviewed is included in Appendix 2.

1.10 Prior to the review, we developed and sent to the Office questionnaires and requests for relevant documents on: independence, financial audit quality assurance, and the value for money audit work carried out by the Office.

1.11 The Office assembled a range of documents and information for us on those matters, as well as on the governance of the Office – including minutes of the meetings of the Audit Board, copies of reports and documents relevant to the Review (such as the 2006 Client Satisfaction Survey, the 2004 peer review of financial audit, and the 2007 financial audit monitoring report). They also provided for us contextual information on the departments of state we had selected for interview, and audit documents relating to the latest completed audits (financial and performance). The Office continued to produce documents for us during the course of the review.

1.12 **Format of report**

1.13 Our report comprises an Executive Summary (Section 2) and six other sections covering:

- The background to the operation of the Office;
- The independence of the Auditor General and of the Office;
- Governance and management;
- Financial audits;
- Value for money auditing;
- A comment on Output Statements.

1.14 It also includes two appendices:

- Our findings concerning the Auditor General's mandate and the legal status of the Office;
- Details of the membership of the review team, and of the persons we interviewed.

1.15 The Auditor General has responded to each of our recommendations. His response is included in the report, immediately following the relevant recommendation.

2 Executive summary

2.1 The Office is highly regarded in the public sector, and more widely. It has a strong reputation for independence. Like other parts of the civil service, the Office is focused on improvement and modernisation. It is clear to us that the Office has made significant improvements in its practices and processes in recent years.

2.2 We reviewed the Office's independence (essential for any auditor), its governance and its primary products: the financial and value for money audits. Our findings and comments on those matters are set out in this report, with a number of recommendations for improvements which the Office should make. (Those recommendations are listed in this summary for ease of reference.)

2.3 Our terms of reference sit under the more general request that we advise the Office what it needs to do to be an effective organisation. Our answers lie in the body of this report and, in particular, in our recommendations. For the purposes of summary, however, we see three aspects to the general request:

- How effective are the primary products of the Office – the financial and value for money audits, and the Auditor General's Annual Report to the Public Accounts Committee?
- How effective is the Office in its relations with its clients?
- How effective is the Office as part of the accountability system of the Irish public sector?

2.4 We think that the Office has made considerable improvements to its products, and we make recommendations regarding the continuing professionalisation of the Office and further improvements to its outputs that we think are important. However, we think that the effectiveness of its products is affected by its relations with its clients, and the position it occupies in the accountability system.

2.5 It is clear to us, from the interviews we conducted, that while the Office's reputation is sound, client expectations of it are both narrow and limited. The annual audit is regarded more as a 'necessary evil', than as a process which can add value to the client. Even when pressed, various interviewees could not see value for their own organisations in the audit process. There is a clear perception that the Office is focused on finding fault, a perception heightened by the nature of a Department's examination by the Public Accounts Committee.

2.6 The perceived focus on finding fault impacts on the relationship between auditor and client. Indeed, while we use the term 'client' throughout this report, clients do not generally regard themselves as clients, but as passive takers of the audit 'service'. Many say that the Auditor General's client is the Public Accounts Committee.

2.7 Clients complained to us that the Office would not offer suggestions for improvement, which both they and the Office think is precluded by the Auditor General's independence. We agree that there is, for any auditor, a balance between 'assessing' and 'assisting', but we do not think that an appropriate balance has been reached in the Irish system. We have come to the conclusion that the independence of the Auditor General and the Office, as it is perceived (or perhaps misinterpreted), is an impediment to the most effective and efficient relationship with the client.

2.8 The Office has an important role in the accountability of the Executive to Dáil Éirann. We are forced to conclude that it is not performing that role as well as it might – partly because of its own practices, but primarily because of limitations on the mandate of the Auditor General which we think are significant. They are:

- the Auditor General's lack of autonomy in resourcing the Office, flowing from the Office's being part of the civil service;
- his restricted mandate to carry out value for money audits – in particular, the very limited mandate to examine the effectiveness of public expenditure;
- the limited extent to which, and process by which, the Auditor General can report on the financial and value for money audits of entities other than departments;
- the absence of a follow-up mechanism for audit findings; and
- the limited extent to which the Auditor General can 'follow' public money into the hands of a recipient who is a non-government organisation.

2.9 We note too that the Auditor General's support of the accountability of the Executive to Dáil Éirann could be enhanced if he were to audit output statements delivered by departments.

2.10 In our view, the Auditor General could play a much more effective role in the accountability system if his Office were not part of the civil service and these other shortcomings were addressed. While these areas are matters for the Oireachtas, we have suggested several changes, concerning the status of the Office and the mandate of the Auditor General, which would put the Office on a footing more in line with Audit Offices in other common law jurisdictions. We think that the Office should explore those matters with the appropriate authorities.

2.11 We are conscious that the remedy for these matters is not within the direct control of the Auditor General. However, we note the comments of the then Auditor General in his foreword to the Office's Statement of Strategy for 2007–09:

> '… I believe that it is time to re-examine the role of the Office in the light of the many changes that have taken place in the public service since the role was last reviewed in 1992 – the more notable being in the areas of governance, performance reporting and customer service. The review preceded the enactment of the Comptroller and Auditor General (Amendment) Act 1993 under which we currently operate. I would see a new review examining the extent to which the Comptroller and Auditor General's current legislative mandate meets the public audit and accountability requirements of a modern democratic State. It could also take into account international developments in the areas of public and private sector audit.'

2.12 We endorse those comments, and hope that our review of the Office can contribute to such a re-examination.

2.13 Recommendations

<table>
<tr><th>Para. reference</th><th>Recommendations</th></tr>
<tr><td>4.17</td><td> We recommend that the Office takes a fresh look at the nature of the relationship that its financial auditors have with their clients. We believe that there is a need to encourage staff to work towards a position where audit is seen more as a force for good and where auditors, currently seen by clients as negative and adversarial, are more approachable and supportive. We recommend that the Office consider opportunities for publishing guides to ‘good practice’ on appropriate matters. </td></tr>
<tr><td>5.16</td><td> We recommend the following structure for the governance and management of the Office: The Comptroller and Auditor General should be responsible for the operations of the Office, but should delegate that responsibility to the Secretary and Director of Audit.
The Comptroller and Auditor General should establish an independent and non-executive advisory board.
The Audit Committee should be a committee of the board and comprise at least three of its members.
The Secretary and Director of Audit should chair a management board for the Office, comprising the Office’s Directors and Deputy Directors.</td></tr>
<tr><td>6.15</td><td> We recommend that the Office fundamentally review in 2009 the overall resources available for financial audit by examining the budgets for individual audits and having regard to the changes that have taken place and that are in prospect. We recommend that the review take account of: the additional work we suggest is needed to improve the quality of audits;
the initial training requirements of introducing the new Clarified International Auditing Standards in 2009; and
the scope for achieving further efficiency savings including those likely to be available in the medium term from the introduction of TeamMate.</td></tr>
<tr><td>6.16</td><td> We recommend that the Office take whatever steps are available to it in order to accelerate achieving the status of being fully professional. Ideally, this needs to be done within a time frame that is shorter than would be possible by natural wastage and retirement, but we recognise that it needs to be done having due regard to the interests of the staff of the Office who have served it well over the years. We recommend that the Office set itself a target of not having unqualified staff engaged on financial audit, other than trainees, by, say, 2011. Until complete professionalisation has been achieved, we recommend that the Office seeks to ensure that there is at least one professionally qualified member of staff involved in the management of each audit. </td></tr>
<tr><td>6.19</td><td>We recommend that, as long as the staff of the Office remain civil servants, the Office use to the maximum possible extent the flexibilities that it has so far negotiated in relation to staff recruitment. We further recommend that it seeks to negotiate additional flexibilities to enable it to require recruited audit staff to have professional accounting qualifications, and to match market pay and conditions for qualified staff, so that it can recruit and retain good quality staff who are professionally qualified.</td></tr>
<tr><td>6.21</td><td>We recommend that the preparation, quality review and issue of an up-to-date Office audit manual that covers all aspects of financial audit is given high priority. We consider that it is important that a comprehensive fully up to date audit manual is in place before the next cycle of audit planning commences.</td></tr>
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Para. reference	Recommendations
6.24	We recommend that all manager and directing grade staff should be reminded in writing of which accounts have been selected for 'hot' reviews and that those accounts should under no circumstances be submitted for certification in future before those reviews have taken place. We recommend that the operation of the 'hot' review procedures should be overseen by the Monitoring Director and the Audit Board advised immediately of any failure to apply it properly.
6.27	We recommend that all the staff of the Office engaged on financial audit be informed of the nature and scale of the deficiencies identified by the programme of 'cold' reviews and reminded of the importance that the Office attaches to these findings. We recommend that the results of the 2007 monitoring reviews are built into a programme of compulsory training for all staff engaged on financial audits and that a checklist of the issues identified is developed and made available to all staff managing and reviewing audits in the current annual cycle. We recommend that the Office consider giving the weaknesses identified, which were common to many audits, special emphasis in the audit manual currently being produced.
6.31	We recommend that all staff engaged on financial audit should be reminded again of their obligations in respect of ethical standards and that Senior Auditors and the Directorate should be charged with responsibility for ensuring that all aspects of ethical standards and requirements are fully met in future. We recommend that the Office institute a system requiring staff to declare interest in entities which are audited by the Auditor General, to assist in the identification of possible conflicts of interest and threats to independence. We recommend that the Office institute a system for the rotation of audit staff to avoid auditors remaining on an audit for longer than a set period of years.
7.15	We recommend that the Office clarify its criteria for selecting value for money topics and adopt a simple and transparent system for topic selection.
7.21	We recommend that the Office review its procedures for engagement with value for money clients, with particular emphasis on the level of seniority of engagement, on the planning and scoping of a study, as well as on the conduct of the study and the draft report.
7.27	We recommend that the Office review its value for money auditing methodology for consistency with International Auditing Standards, and make changes to the methodology where appropriate, particularly in relation to quality assurance.
7.31	We recommend that the Office seek both to increase the skills of value for money staff and to broaden the base of skills among those staff. We recommend that the Office strengthen its value for money audit team supervision.
8.5	We recommend that the Auditor General explore the possibility of assuming the role of auditing output statements.
Recommendations relating to Mandate (refer Appendix 1)	
5	We recommend that the Auditor General explore with the Minister for Finance the possibility of his Office being constituted as an independent Office outside the civil service. That office would employ its own staff who would no longer be civil servants. We observe that most Audit Offices enjoy this separate status in relation to staffing. We observe too that other Audit Offices have made such a transition without its proving to be a major hurdle.

Para. reference	Recommendations
8	We recommend that the Auditor General explore the possibility of proposing the extension of his statutory mandate to include examination of the effectiveness of the operations of an entity or activity funded by public money including the implementation of government policy.
12	We recommend that the Auditor General explore the possibility of proposing the extension of his statutory power to report to include the full range of reports on all of the public bodies subject to his audit. We recommend that the Auditor General propose the transfer to him of the responsibility for laying his reports before the Oireachtas.
17	We recommend that the Auditor General explore the possibility of proposing more formal mechanisms for the follow-up of his reports.
19	We recommend that the Auditor General explore the possibility of an extension to his ability under section 8(1)(b) of the Comptroller and Auditor General (Amendment) Act, 1993 to examine the books and records of a body receiving more than 50% of its funds from the State.

3 Background

3.1 The office of Comptroller and Auditor General is established by Article 33 of the Constitution. The Comptroller and Auditor General is ‘to control on behalf of the State all disbursements and to audit all accounts of moneys administered by or under the authority of the Oireachtas’. The Constitution also provides for the Comptroller and Auditor General to ‘report to Dáil Éirann at stated periods as determined by law’.

3.2 The Auditor General operates primarily under the Comptroller and Auditor General (Amendment) Act, 1993. The Act provides both for financial audits and, under section 9, for value for money studies.

3.3 The Comptroller and Auditor General is responsible for auditing over 350 public bodies. He also carries out a small but increasing number of value for money studies (nine reports in 2007).

3.4 The work of the Auditor General is carried out by the Office of the Comptroller and Auditor General, which is a department of the civil service. Section 6 of the Comptroller and Auditor General Act, 1923 gives the Auditor-General full power to make orders and rules for the conduct of the internal business of the Office. However, the Office is subject to the same budget process and the same provisions as to recruitment, appointment and remuneration as are other departments.

3.5 The level of staffing for the Office authorised by the Minister of Finance is 175, though at the time of our review in April 2008 staff numbers stood at 154. The funding for the Office for 2008 is estimated as €14.45 million.

3.6 The Office identifies three work programmes – financial auditing, reporting, and value for money examinations – and is organised accordingly, each of the three sections being led by a Director of Audit.

3.7 Statement of Strategy (2007–09)

3.8 The Office’s Statement of Strategy for 2007 to 2009 describes the Mission of the Auditor General as ‘to provide independent assurance that public money is properly managed and spent to good effect and to contribute to improvements in public administration’.

3.9 The Office sees its key challenge as shaping its services to anticipate and respond to Dáil Éirann’s and other stakeholders’ needs while continuing to build and maintain an efficient organisation. To meet that challenge, the Office identifies three strategic priorities:

- to deliver its services efficiently and effectively;
- to maximise the value of its work; and
- to ensure that it is equipped to meet current and future challenges.

4 Expectations of an Audit Office – independence

4.1 A fundamental principle of providing audit and assurance services is that an auditor must be independent of the entity being audited. The *Code of Ethics for Professional Accountants* issued by the International Federation of Accountants outlines the importance of auditors' not engaging in any activity that impairs or might impair the integrity, objectivity or the good reputation of the auditor and the accounting profession. Independence, which encompasses both independence of mind and independence in appearance, is outlined in detail in section 290 of the *Code of Ethics for Professional Accountants*.

4.2 Independence of a public sector auditor or audit institution is complicated by the institution itself being a part of the State. The relevant constitutional and legal provisions must therefore afford the auditor the necessary organisational and functional independence to carry out the role of holding the Executive to account.

4.3 We accept that the Auditor General and the management of the Office are confident that, in practice, the Auditor General and the Office are independent from the Executive. Further, we emphasise that we were left in no doubt that the Auditor General and the Office are generally perceived as independent by the public bodies they audit.

4.4 In 1977 the international auditing community[3] set out the fundamental requirements for independent government auditing. In 2007, they endorsed the 1977 Declaration, and identified eight core principles as essential for independence.[4] It is important to note that these principles describe the ideal. No Audit Office has been assessed as completely satisfying all eight principles:

1. an appropriate constitutional/legal framework;
2. independence of the Auditor General, including security of tenure and legal immunity in the discharge of duties;
3. a broad mandate and full discretion in discharge of functions;
4. unrestricted access to information;
5. the right and obligation to report on work;
6. freedom to decide on the content and timing of audit reports and to publish and disseminate them;
7. the existence of effective follow-up mechanisms on recommendations made by the Auditor General;
8. financial and managerial/administrative autonomy and the availability of appropriate human, material and monetary resources.

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3 The IXth Congress of the International Organisation of Supreme Audit Institutions (INTOSAI): Lima Declaration of Guidelines on Auditing Precepts

4 The XIXth Congress of the International Organisation of Supreme Audit Institutions: Mexico Declaration of Independence

4.5 We assessed the Office with reference to those principles. Our conclusions are set out in Appendix 1 of this report. In summary, there are in our view five areas in which the Office falls short of the INTOSAI standard, at least in theory, if not always in practice:

- the Auditor General's lack of autonomy in resourcing the Office, flowing from the Office's being part of the civil service;
- the Auditor General's restricted mandate to carry out value for money audits – in particular, the very limited mandate to examine the effectiveness of public expenditure;
- the extent to which, and process by which, the Auditor General can report on the financial and value for money audits of entities other than departments;
- the absence of a follow-up mechanism for audit findings; and
- the extent to which the Auditor General can 'follow' public money into the hands of a recipient which is a non-government organisation.

4.6 Relations with clients

4.7 While the Auditor General and the Office are generally perceived as independent, it appeared to us that that belief may not always be underpinned by a clear understanding of what auditor independence entails. Those we interviewed often volunteered the concept of independence in answer to a range of questions (sometimes to questions not necessarily connected with independence) – for example:

- some audited entities said that they believe they are not consulted on matters such as audit scope, because the Auditor General is independent;
- some audited entities consider that they cannot challenge 'process' issues such as timeliness, because the Auditor General is independent;
- some interviewees said that they do not expect the Auditor General to consult on his performance audit work programme because of his independence; and
- some interviewees, including members of the Office itself, believe that the Auditor General should not disseminate examples of 'best practice', or assist auditees to improve their practices, because it would conflict with his independence (and because it might duplicate the functions of the Executive.)

4.8 The question of relationship between the client and the Auditor General and/or the Office was of course a topic which most of our interviewees discussed. It is a topic which pervades many of the matters we cover in this report. However, we choose to consider the issue in the context of independence because interviewees consistently, it seemed to us, attributed difficulties in their relations with the Office to the Auditor General's independence. We have reflected a selection of such remarks in the previous paragraph.

4.9 There is, as we have noted, no question that the Auditor General and the Office as a whole are held in high regard throughout the public sector. The independence of the Auditor General and the Office is seen as essential and unchallenged. And we recognise that it is important for audit staff to maintain a distance from the audited entities in order to avoid the familiarity threat identified and discussed in ethical standards.

4.10 However, almost all of those we interviewed considered their entity's relationship with the staff of the Office on an audit to be adversarial – in some measure at least. They do not see the accountability and audit process as supportive of the management process. The annual audit is something to be 'got through' as painlessly as possible.

4.11 Clients often do not regard the staff of the Office as approachable, and they seek in some respects to keep their heads below the parapet for fear of causing themselves problems with the auditors. While they know that the Office has a wealth of experience and knowledge, they are reluctant to ask for advice lest it expose a problem to the auditor, which will then be reported publicly. We noted in a number of interviews a desire for the Office to share its knowledge of 'good practice'.

4.12 Moreover, clients perceived close links between the Office and the Public Accounts Committee which they thought encouraged the audit staff to be overly negative and critical in the opinions they formed. The Auditor General is (we understand) a witness when he appears before the Committee, but his sitting next to the Chair of the Committee appears to align him with the Committee. Disturbingly, one interviewee went so far as to suggest that the Auditor General was so much 'the PAC's man' that he risked losing his independence from the political process.

4.13 This issue was also identified in the client satisfaction survey undertaken for the Office by OCS Consulting in October 2006. OCS Consulting reported that audited entities were surprised that the Office regarded them as 'clients'. Clients saw the Public Accounts Committee as the Office's client; and themselves as merely the subject of a process. Examples of ways in which other Audit Offices have gone about improving relationships with their clients are described in Figure 4.1.

Figure 4.1 Examples of steps taken by other Audit Offices to develop client relationships

Many Audit Offices in other countries have relationship difficulties with their clients and have worked hard in recent years to develop a more positive relationship with those entities. They have taken action to encourage entities to see them as a force for good, as organisations that are happy to be consulted early about possible accounting issues that might arise down track in the audit process. They have stressed that audit is about the auditors trying to satisfy themselves that the accounts are right, rather than scoring points in a negative way by trying to prove the accounts to be wrong. They have stressed the value added in the audit process and that part of the function of Audit Offices is to help audited entities account for their transactions properly and efficiently.

There are various ways in which Audit Offices have sought to change the attitude of audited entities to their work and to emphasise the contribution that they can make. Some have embarked on secondment and exchange programmes where staff from the Audit Office go to work in the entity for a period and staff from the entity work in the Audit Office. Some Audit Offices have gone out of their way to find opportunities to speak at conferences, training sessions and the like run by the audited entities and have used those opportunities partly to stress the positive aspects of audit. Some run regular focus groups and workshops on topics of wide general interest and invite relevant people from audited entities to attend and participate. Some hold annual gatherings for Heads of Finance/agency chief accountants/Accounting Officers to discuss issues of common interest. Some Audit Offices do a mix of all of these things.

4.14 We know that the Office recognises this issue and has increased its participation in external events such as conferences in recent years. However, we conclude that there is considerable scope for more to be done to change the attitude of some of the staff, and of some of the audit clients, to the nature of the audit process.

4.15 Several of those we interviewed, unprompted, commented on ways in which the Office, or the Auditor General himself, might improve relations with the civil service or improve understanding of the Office. Suggestions included the Auditor General's attendance at the annual meeting of Secretaries-General to talk about his proposed work programme, his consulting major departments on issues they thought important for the Office to examine, and the possibility of publishing guides to 'good practice' jointly with the Department of Finance.

4.16 We note in particular the opportunity to form better relationships with entities' audit committees. We were surprised to hear from many of those we interviewed that the auditor rarely attended meetings of their audit committee. On the other hand, where there is a relationship between the auditor and audit committee, the interviewees saw it as beneficial. We suggest that, for all major clients, the auditor should appear before the audit committee at each of its meetings. At the least, the auditor should attend to discuss the audit plan, and the results of the annual audit. Similarly, we see benefit in the value for money auditor engaging with the client's audit committee at both the outset and the completion of the audit. We note that engagement with the client's audit committee is an obligation under International Auditing Standards (under which the Office operates – refer Section 6 below).

4.17 We recognise that such changes in attitude cannot be achieved overnight and that it will require work by all staff, but particularly at Senior Auditor and Directorate levels, progressively to influence hearts and minds.

Recommendations:

We recommend that the Office takes a fresh look at the nature of the relationship that its financial auditors have with their clients. We believe that there is a need to encourage staff to work towards a position where audit is seen more as a force for good and where auditors, currently seen by clients as negative and adversarial, are more approachable and supportive.

We recommend that the Office consider opportunities for publishing guides to 'good practice' on appropriate matters.

Auditor General's Response

Accepted.

The Office is very conscious of the need to develop its relationship with its clients. In 2006, we commissioned independent consultants to carry out a survey of the satisfaction of our clients with the level and nature of the service we provide them. This found that clients were generally satisfied with the quality of the service, but that there were ways in which the Office could add value through our work. We have been developing our approach to client relationships along the lines suggested above. We recognise that it will take time for client perceptions to respond.

We have identified audit committees as key stakeholders in the audit process and have worked to develop our relationships with them. Staff have been issued with detailed guidance on dealing with audit committees. Part of our 2007 Office conference dealt with communication with audit committees and managing client relations.

Also arising from the consultation process, we are committed to improving our relationship with clients by:

- *focusing more on opportunities for improvement*
- *increasing the focus on better practice within audit work.*

5 Governance and management

5.1 The Office of the Comptroller and Auditor General is a department of the Civil Service. It is headed by a Secretary and Director of Audit, who is the Accounting Officer for the department. The Office's strategy and operations are overseen by an 'Audit Board', comprising the Auditor General as chair, the Secretary and the other two Directors of Audit. The Board usually meets every two months, though when we carried out our review in April 2008, it appeared not to have met since December 2007.

5.2 The Office established an Audit Committee in 2004 to support the Accounting Officer, in the manner recommended by the Mullarkey Report. The Committee is non-executive and advisory only. It meets three or four times a year. The Committee appears to us to operate well, and to provide valuable external input for the Office. It is however the only formal external source of input to the Office.

5.3 We were told that the then Auditor General had some five or six years ago instituted an advisory board of five external and independent people, on a pilot basis. The board was intended to advise the Auditor General on the fulfilment of his mandate, and on improvements which the Office might make. It was to meet with the Auditor General and the Secretary every six months. However, the Board was disestablished when it did not prove of great assistance, perhaps, it was suggested to us, because of its lack of clear purpose and infrequent meetings. The Audit Committee now addresses some of the matters that board might have covered.

5.4 Several issues arise in addressing the question of appropriate governance and management structure for an Audit Office:

- The need to protect the independent constitutional position of the Auditor General;
- Given that independence, the extent to which the Auditor General should be separate from management of the operations of the Office;
- The desirability of an Audit Office being an exemplar of good practice, because of its role in giving assurance about, and commenting on, other entities;
- In accordance with accepted good practice, the desirability of separating as far as possible responsibility for governance and management – often difficult where an office is led by a single constitutional officer.

5.5 The current governance arrangements for the Office are perhaps understandable, because the Office is a department of the civil service. It would be inappropriate for the Auditor General, given his constitutional position and responsibility for reporting to the Oireachtas on aspects of the civil service, to have formal accountability for the operation of part of the civil service.

5.6 In practice though, the Auditor General chairs the Audit Board and works closely with the Office, and would have difficulty in discharging his constitutional role if he did not. On the other hand, the Secretary is accountable for the operation of the Office, yet the Auditor General has the greater authority. In short the current arrangements blur independence and lines of accountability, even if they might appear to work in practice. We were advised that they do work effectively, relying on pragmatism and close cooperation between the Auditor General and the Secretary.

5.7 We recognise the significant enhancements that have been put in place in the Office in recent years including the creation of an independent audit committee, the use of strategy and output statements, and the use of client surveys and external review processes to improve the working of the Office. These measures address many of the needs of a public service organisation seeking to employ best practice standards.

5.8 However, we believe that the Office should now embark on a further stage of upgrading its governance arrangements to help ensure that it remains fit for purpose and reflects best practice.

5.9 We have considered the constitutional and legal position of the Auditor General and the current thinking on public sector governance, as well as the Office's existing arrangements. We think that a governance and management system for the Office should both give formal responsibility for the Office to the Auditor General, and provide separation between governance and management functions.

5.10 We suggest elsewhere in this report that the Office explore the possibility of its ceasing to be part of the civil service. We envisage the Comptroller and Auditor General continuing to be an independent officer under the Constitution. The Auditor General would have responsibility for his constitutional duties, and for the Office, his means of carrying out those duties.

5.11 The Auditor General would delegate to the Secretary (perhaps renamed Director-General) full powers to run the Office. We suggest that the title 'Director-General' is less associated with the civil service, and would reflect the position's focus on management rather than policy.

5.12 We suggest, building on the successful introduction of an independent audit committee, the establishment of a formal advisory board, reporting to the Auditor General. The advisory board would, in a general sense, oversee the working of the Office. It would not, however, have any role in the constitutional work of the Auditor General, such as the control of public money, carrying out audits of public entities, or reporting the outcome of those audits to the Oireachtas.

5.13 We suggest that an advisory board might comprise perhaps five members, all independent and non-executive. The Auditor General and the Secretary/Director-General would attend its meetings. The advisory board would:

- receive the reports of the Secretary/Director-General on the operations of the Office;
- receive the reports of the Audit Committee;
- agree the Output and Strategy statements for the Office and recommend them to the Auditor General, who would be free to change them;
- request and receive periodic peer reviews, client surveys and quality audits of the office; and
- provide an annual report on the operation of the Office for the Auditor General, who would be responsible for publishing it.

5.14 An Audit Committee would comprise, say, three of the members of the advisory board, and would be a committee of the board. We suggest that, given the role of the proposed advisory board, it should have a more focused role than the present Audit Committee. The Audit Committee should meet with the external auditors annually in closed session without any executives. The Chairman of the Audit Committee would report to the advisory board after each meeting.

5.15 The members of the advisory board should serve a maximum of two three-year terms. However, this should be managed in the early stages to facilitate periodic rotations to preserve continuity while providing for an annual refreshing of skills (perhaps starting from the start of the second term of office one person would rotate off the Board annually).

5.16 We think too that a new management board should take the place of the Audit Board, to oversee the ongoing management of the Office. It should be chaired by the Secretary/Director-General and comprise the Directors, and perhaps the Deputy Directors. This Board should meet at least fortnightly, should have formal papers, agenda and minutes of meetings. It should be charged with proposing a Strategy Statement, an Output Statement (including an annual business plan), and an annual report of outputs. It should take all the decisions on the day-to-day management of the Office, and negotiate the work plan for the Office with the Auditor General.

Recommendation:

We recommend the following structure for the governance and management of the Office:

- ***The Comptroller and Auditor General should be responsible for the operations of the Office, but should delegate that responsibility to the Secretary and Director of Audit.***
- ***The Comptroller and Auditor General should establish an independent and non-executive advisory board.***
- ***The Audit Committee should be a committee of the board and comprise at least three of its members.***
- ***The Secretary and Director of Audit (perhaps renamed 'Director-General') should chair a management board for the Office, comprising the Office's Directors and Deputy Directors.***

Auditor General's Response

The broad thrust of the recommendation is accepted.

While any fundamental alteration to the status of the Office would require legislation, the Auditor General has power within the current framework created under Section 6 of the Controller and Auditor General Act, 1923 to establish the governance arrangements for the Office. By virtue of Article 33 of the Constitution, he is responsible for the audit operations of the Office.

The governance and management arrangements in the Office are in the process of being changed. The key elements of the revised governance and management structure are

- *a Management Board, consisting of the Directors and Deputy Directors of Audit and chaired by the Secretary and Director of Audit, has been established to co-ordinate the management and operation of the Office*

- *an Audit Board, chaired by the Auditor General and composed of the Auditor General and the Directors of Audit, is responsible for audit business, including receiving reports from the management board*
- *an Audit Committee, comprising four independent individuals, will operate under an agreed charter, reporting to and supporting the Secretary and Director of Audit in the exercise of his functions as Accounting Officer*
- *a consultative board will be established, which the Auditor General will consult in relation to audit policy.*

6 Financial audits

6.1 Background

6.2 The financial audit of the accounts of central government and state sponsored bodies is the core activity of the Office. Some 365 accounts were audited in 2007, a slight increase over the previous year. Financial audit employs around 74% of the staff resources available to the Office (86% if the staff in Corporate Services are discounted).

6.3 Recent changes and improvements

6.4 Over ten years ago the Office decided that it should become fully professional. Since that time, all new recruits to the audit grades have been required to gain a professional qualification, and failure to do so within seven years results in termination of their employment contracts as trainee auditors. A number of the staff engaged on financial audit have considerable experience of that work but are not professionally qualified.

6.5 In 2006 the Auditor General adopted international auditing standards (ISAs) for all financial statement work. These comprise International Auditing Standards (UK and Ireland) and the ethical standards ES1 to ES5 issued by the Auditing Standards Board, and the International Standard on Quality Control (UK and Ireland) 1 (referred to in this document as ISQC1) which introduced new and more demanding quality assurance procedures that have to be met in all respects if full compliance with international auditing standards is to be achieved. The move to full implementation of international auditing standards involved a significant investment in staff training and in implementing additional procedures.

6.6 The full application of ISQC1 in 2007 for the first time in particular represented a significant additional but essential resource commitment. It involved, for example, undertaking:

- up to 15 'hot' internal quality control reviews on selected high profile, large, complex or high risk accounts before the audit reports on them were issued;
- a programme of ten 'cold' look-back reviews designed to examine the standard of audit work managed by each of the Senior Auditors in the Office over a three-year cycle; and
- a cyclical review of the extent to which the ethical standards and expectations contained in legislative and civil service requirements as well as ES1 to ES5 have been consistently met by all staff engaged on financial audit.

6.7 In parallel with the introduction of international auditing standards and quality assurance arrangements, there were other considerable additional pressures on the resource of the Office in relation to financial audit in 2007:

- The Office implemented the TeamMate electronic working paper system to record the planning, execution and reporting of all financial audit work.

- The Office sought to advance the audit cycle in order to improve the timeliness of the accountability process. This involves progressively increasing the amount of interim audit work and speeding up the process of completing the final audit work. The aim is to bring forward to 31 July the certification of the Appropriation Accounts and the publication of the Auditor General's Annual Report by 2009.

6.8 All of these changes in relation to financial audit placed additional burdens on the staff of the Office who are allocated to the financial audit work. Moreover, they have taken place at a time when the Office was building up the pool of resources dedicated to undertaking value for money audits, and some staff have left financial audit work to join the value for money team. Also, we observe that the Office has been operating below its approved complement: at the time of our review there were 154 staff in post compared with an approved complement of 175 staff.

6.9 These resource pressures have in some measure been counter-balanced by three initiatives:

- It was decided that it should be possible to look to financial audit to make efficiency savings by reducing input costs by 5% over the period 2007 to 2009.
- While there was an initial investment in training and familiarisation in relation to introducing the TeamMate electronic working paper system, in the medium term this is expected to result in savings on the annual staffing of each of the audits.
- It was decided to contract out 1200 audit man days annually to the audit profession on the basis of two-year contracts extendable for a third year.

6.10 It was against this background of considerable change and significant net overall resource pressure that we sought to identify the quality of financial audit being achieved and the scope for further improvements. In order to do this we:

- reviewed the Office's response to an ISQC1 questionnaire that we developed and issued;
- examined a background note and a range of associated documents relating to financial audit that we requested;
- reviewed the Report of the Monitoring and Ethics Director to the Audit Board on the first year's operation of ISQC1, and interviewed her concerning that Report and other HR matters relating to financial audit;
- discussed with Secretaries-General of a selection of government departments and their staff their experiences of having their financial statements audited by the staff of the Auditor General; and
- reviewed in depth the key documents (such as the Engagement Letter, a copy of the accounts, the Audit Plan, the matters for Deputy Director attention on the outcome of the audit, the Management Letter, and so on) and interviewed the Senior Auditor on selected completed large audits.

6.11 **Our views**

6.12 It is very clear to us that the Office has worked hard over recent years to improve the quality of financial audit that it does, and much has been achieved. The Office recognises that there is more to be done and sees this as an on-going process in 2008 and 2009. We support that view. The comments set out in the following sections are offered as a contribution to the further work which the Office plans to undertake.

a) Staffing levels

6.13 It is clear that as a result of the factors set out in the introduction to this section, the staff engaged on financial audit are currently under significant pressure. Our impression is that on some audits they are stretched to the point where the quality of audit achieved could be at risk. Further pressure on resources, and the need for significant additional investment in training, will arise as a result of the current international programme of clarification of international auditing standards. This will produce a complete set of more demanding international auditing standards at the end of 2008 which the Office will need to implement. In our judgement it will be at least a further year before TeamMate and the ISQC1 arrangements have fully bedded in and any resource gains from them are achieved.

6.14 Our concern about the adequacy of the financial audit resource, in future, is reinforced by our understanding that no zero-based budget for financial audit work has been produced by the Office in recent years. Also, the prevailing practice seems to have been to seek to contain the budgets of individual audits at existing levels and to cope with change, increasing demands and additional procedures by expecting more of staff and trying to squeeze out efficiency savings.

6.15 We have recorded earlier in this report our views on the resourcing challenges for the Office which arise from its being a department of the civil service.

Recommendations:

We recommend that the Office fundamentally review in 2009 the overall resources available for financial audit by examining the budgets for individual audits and having regard to the changes that have taken place and that are in prospect.

We recommend that the review take account of:

- ***the additional work we suggest is needed to improve the quality of audits;***
- ***the initial training requirements of introducing the new Clarified International Auditing Standards in 2009; and***
- ***the scope for achieving further efficiency savings including those likely to be available in the medium term from the introduction of TeamMate.***

Auditor General's Response

Accepted.

b) Staffing professionalisation

6.16 We acknowledge that many of the staff who are not professionally qualified are very experienced and are doing a sound job. But in an Office which has set its sights on being fully professional it seems to us unacceptable that a large proportion of the managing and directing grades on financial audit are unqualified. Our understanding is that of the order of six of the 12 Deputy Directors and 20 of 40 Senior Auditors are not professionally qualified. As a consequence, they will not be fully trained in all the current demands of the accounting and auditing profession, will not be subject to a compulsory continuing professional training update programme, nor be bound by the ethical obligations that attach to being a member of a CCAB-I[5] body. However, we recognise that all the Office's training and audit systems are based on an implementation of ISA provisions by all staff.

Recommendations:

We recommend that the Office take whatever steps are available to it in order to accelerate achieving the status of being fully professional. Ideally, this needs to be done within a time frame that is shorter than would be possible by natural wastage and retirement, but we recognise that it needs to be done having due regard to the interests of the staff of the Office who have served it well over the years.

We recommend that the Office set itself a target of not having unqualified staff engaged on financial audit, other than trainees, by, say, 2011.

Until complete professionalisation has been achieved, we recommend that the Office seeks to ensure that there is at least one professionally qualified member of staff involved in the management of each audit.

Auditor General's Response

Accepted in part.

The Office has concentrated the assignment of professionally qualified staff in the financial audit area. Currently, all financial audit staff in the auditor grade and five of the six Deputy Directors of Audit are qualified accountants. Just over half of the Senior Auditors are qualified accountants.

We accept that it is desirable to complete the move to full professional status for financial audit staff in as short a time frame as possible and we will explore the possibilities of doing so but, as the report recognises, there are practical barriers to achieving this. In the meantime, we have recently reorganised reporting lines and have sought to ensure that there is at least one professionally qualified member of staff involved in the management of each audit.

c) Appointment procedures

6.17 The Office is a department of the civil service, and its staffing is determined in accordance with the centralised civil service system for appointment and remuneration. We discuss elsewhere in this report our view that the Auditor General's Office would be better located outside the civil service. We note in this context, however, that the system limits the Auditor General's ability to recruit, appoint and promote qualified accountants and auditors.

[5] Consultative Committee of Accountancy Bodies – Ireland is a forum of the four major accountancy bodies in the Republic of Ireland.

6.18 Recognising the nature of its work, the Office has been given some concessions, as compared with the civil service generally: it is permitted to grant two additional pay scale increments for passing professional examinations, and the Department of Finance has agreed to a more favourable arrangement for the replacement of staff who leave the Office under the decentralisation programme.

6.19 However, we understand that the Office is unable to specify an accounting qualification when recruiting from within the civil service because it already has unqualified people in such positions. We believe that such recruitment requirements are an impediment to the Office's pursuit of 'professionalisation' (see section b above).

Recommendation

We recommend that, as long as the staff of the Office remain civil servants, the Office use to the maximum possible extent the flexibilities that it has so far negotiated in relation to staff recruitment. We further recommend that it seeks to negotiate additional flexibilities to enable it to require recruited audit staff to have professional accounting qualifications, and to match market pay and conditions for qualified staff, so that it can recruit and retain good quality staff who are professionally qualified.

Auditor General's Response

Accepted.

The Office will review its resource requirement, taking account of obligations under International Auditing Standards in the area of financial audit and the need to attract and retain evaluation staff for its Value for money work.

d) Audit procedures and policies

6.20 Many of the changes to policies and procedures (such as the introduction of ISQC1) have been announced in ad hoc instructions to staff. But the Office does not have a comprehensive up-to-date financial audit manual.

6.21 We observe from the Annex to the Auditor General's Statement of Strategy 2007–2009 that one of the announced targets was to publish a revised Office audit manual by February 2008, but that project was not complete at the time of our review in April 2008, and the drafting work that had been undertaken had not been reviewed externally.

Recommendation:

We recommend that the preparation, quality review and issue of an up-to-date Office audit manual that covers all aspects of financial audit is given high priority. We consider that it is important that a comprehensive fully up to date audit manual is in place before the next cycle of audit planning commences.

Auditor General's Response

Accepted.

e) The operation of engagement quality control ('hot') reviews

6.22 The auditing profession views the annual programme of engagement quality control ('hot') reviews as of crucial importance to achieving high quality audits that avoid the risk of an inappropriate audit opinion being given. Where the head of an Audit Office identifies for such 'hot' review a list of audits which he judges to be high profile, large, complex or high risk it is important they are so reviewed.

6.23 We note that in the case of four of the 19 audits so identified in 2007 the audit opinion was signed without a 'hot' review taking place, thus exposing the Auditor General to the risk of giving an incorrect audit opinion.

6.24 In the light of these oversights we understand that an adjustment to the TeamMate electronic working paper system has been introduced to remind staff of the need for a 'hot' review when the account has been selected for one.

Recommendations:

We recommend that all manager and directing grade staff should be reminded in writing of which accounts have been selected for 'hot' reviews and that those accounts should under no circumstances be submitted for certification in future before those reviews have taken place.

We recommend that the operation of the 'hot' review procedures should be overseen by the Monitoring Director and the Audit Board advised immediately of any failure to apply it properly.

Auditor General's Response

Accepted. In the light of the report of the Monitoring Director on the operation of the 2007 'hot' reviews, the process was amended in March 2008. Now,

- *audit managers and directing staff are informed by email of which specific audits have been selected for 'hot' review*
- *an automatic alert has been built in to the electronic working papers system that requires the Deputy Director to check if a 'hot' review should be carried out.*

f) The results of the monitoring look-back ('cold') reviews

6.25 The programme of monitoring look-back ('cold') reviews undertaken in 2007, the first of its kind undertaken by the Office, served to identify some important weaknesses in the audit processes on the completed audits examined.

6.26 Deficiencies included weaknesses in audit planning, inadequate systems descriptions, inadequate identification of key controls, poor documentation, sampling weaknesses, incomplete or inadequate descriptions of issues identified in the course of audits etc. These deficiencies, which are listed in the Appendix to the 2007 Report of the Monitoring and Ethics Director, are core deficiencies that go to the heart of the audit process.

6.27 Our own limited review of completed audits served to confirm the existence of some of the weaknesses identified by the Office's monitoring arrangements. In particular, on one of the audits examined we were not persuaded that the audit had been properly planned and resourced or that the planning and risk assessment requirements set out in ISA 300 and (particularly) ISA 315 had been properly applied.

Recommendations:

We recommend that all the staff of the Office engaged on financial audit be informed of the nature and scale of the deficiencies identified by the programme of 'cold' reviews and reminded of the importance that the Office attaches to these findings.

We recommend that the results of the 2007 monitoring reviews are built into a programme of compulsory training for all staff engaged on financial audits and that a checklist of the issues identified is developed and made available to all staff managing and reviewing audits in the current annual cycle.

We recommend that the Office consider giving the weaknesses identified, which were common to many audits, special emphasis in the audit manual currently being produced.

Auditor General's Response

Accepted.

The 2007 monitoring of cold reviews identified deficiencies of the kind referred to by the Review Group, but it also concluded that overall the audits were undertaken in accordance with professional standards and regulatory and legal requirements. It commented that some of the audits reviewed were undertaken to a very high standard and review staff noted an overall improvement in the quality of working paper files as compared to the previous year (2006), which it attributed to the use of newly introduced electronic working papers.

The nature of the deficiencies were outlined to financial audit staff at the Office annual conference in November 2007 and, subsequently, training was organised in the areas where it was perceived the greater weaknesses arose.

We will continue to work to ensure that cold review findings are used to identify training needs and are followed up by staff managing and reviewing audits.

g) Maintaining strict adherence to ethical standards

6.28 We understand that all staff at deputy Director level and above produce annual ethics statements under public service regulations. In May 2007 senior audit staff received detailed briefing on the new quality assurance arrangements, including the application of ethical standards. All financial audit staff were provided with a copy of the new arrangements; and a second memo was sent to staff in November 2007 reminding them of the need to comply with procedures regarding ethical standards.

6.29 We note that the new requirements were implemented only slowly. We observe that out of a sample of around 37 (10%) audits reviewed by the Office's Monitoring Director in February 2008 under the new monitoring arrangements, in only 13 cases had the necessary ethical confirmations been completed. In many cases the confirmations were not completed until after the audit had been completed. And in only five of the 37 audits reviewed had the confirmations been completed by all members of the audit team.

6.30 Identifying and managing possible conflicts of interests and threats to independence are important in all audits but are of special importance in the public sector. We view it as very important that full compliance with ethical standards is seen in the Office as the norm and that it is seen as unacceptable for the documentation of compliance with such standards on the audit files to be disregarded.

6.31 We note too that the Office has no formal system for declaring and recording interests of staff members, so as to identify possible conflicts of interest and threats to independence. Nor does it have a formal policy for staff rotation designed to avoid the 'familiarity threat', as the ethical standards require. Systems with which we are familiar involve a six-monthly or annual declaration by each staff member of any interests which they or close family members have in entities which the Auditor General audits, and in other entities which do business with the Audit Office. That information is used in allocating staff to audits.

Recommendations:

We recommend that all staff engaged on financial audit should be reminded again of their obligations in respect of ethical standards and that Senior Auditors and the Directorate should be charged with responsibility for ensuring that all aspects of ethical standards and requirements are fully met in future.

We recommend that the Office institute a system requiring staff to declare interest in entities which are audited by the Auditor General, to assist in the identification of possible conflicts of interest and threats to independence.

We recommend that the Office institute a system for the rotation of audit staff to avoid auditors remaining on an audit for longer than a set period of years.

Auditor General's Response

Accepted.

All the staff of the Office are subject to the ethical and other requirements set out in the Civil Service Code of Standards and Behaviour (September 2004). In addition, as noted at 6.22 above, all staff at Deputy Director level and above submit annual ethics statements under public service regulations, and are required to declare any conflicts of interest that arise in the course of their work. In practice, staff are aware of the possibility of conflicts of interest and threats to independence. However, it is accepted that a formal system of declarations is appropriate.

Following the Monitoring Director's review of operation of the declarations process in the 2007 audit work, written reminders were issued to staff in May 2008 about the need to complete the prescribed ethical declarations. Compliance with the declaration requirement will be kept under review.

The scale of staff changes over the past number of years has meant that, in practice, most staff did not remain on an audit for an extended period. However, we will now adopt a formal policy on the rotation of staff.

7 Value for Money Auditing

7.1 Section 9 of the 1993 Act provides that the Auditor General may:

> ‘(1) …carry out such examinations as he considers appropriate for the purpose of ascertaining—
>
> (a) whether and to what extent the resources of the Department, person or fund—
> (i) have been used, and
> (ii) if acquired or disposed of by the Department, person or fund, have been so acquired or disposed of,
> economically and efficiently, and
>
> (b) whether any such disposal has been effected upon the most favourable terms reasonably obtainable.
>
> (2) Without prejudice to the generality of subsection (1), the systems, procedures and practices employed by the Department or person concerned or the manager of the fund concerned for the purpose of enabling the Department or person or the manager of the fund to evaluate the effectiveness of its or his operations may be examined by the Comptroller and Auditor General.
>
> (3) Without prejudice to the generality of subsections (1) and (2), the Comptroller and Auditor General may, in carrying out examinations under this section, make such comparisons, including comparisons of systems, procedures and practices, as he considers appropriate.
>
> (4) Where the Comptroller and Auditor General proposes to make any examination under this section, he may, at his discretion, seek the views of the committee of Dáil Éireann established under the Standing Orders of Dáil Éireann to examine and report to Dáil Éireann on the appropriation accounts.’

7.2 We record our views on the relatively restricted nature of that mandate in Appendix 1 of this report.

7.3 Resource

7.4 Value for money auditing is currently only a small part of the business of the Office. The Auditor General published nine such reports in 2007, compared with two in 2006, and four in 2005. The Statement of Strategy states an intention to increase the number of reports to 13 by 2009. At the time of our review, the Office employed 21 staff on value for money studies – three Deputy Directors, ten auditors and eight assistant and trainee auditors. The Directorate was overseen by a Director of Audit who spent half his time on that function.

7.5 Terms of reference

7.6 Our terms of reference in relation to value for money auditing asked us to assess, at a high level, ‘the efficiency and effectiveness of the … value for money examinations conducted by the Office’.

7.7 We selected two recent studies for particular consideration: concerning the Financial Regulator and the National Museum of Ireland. We spoke to representatives of each auditee, and to the lead auditor for each study. We also reviewed the Office's Manual on Reporting (April 2008 edition) which covers all the Auditor General's reporting outputs, and received general comments on the value for money output from other interviewees. Given the 'high level' nature of the assessment, we did not examine the files for the two studies. Nor have we analysed the two reports – we note that the Office has commissioned the Institute of Public Administration (in April 2008) to review the quality of seven value for money reports, including these.

7.8 Our focus was the efficiency of the examination process and the perceived effectiveness of the work carried out. The two studies selected proved to offer a contrast both in the conduct of the examination, and in the degree to which the client considered the study to be of value. At the time of our review, the Public Accounts Committee had not examined either report.

7.9 Several issues emerged from our consideration of the two studies and the Office's value for money practice which we think require attention.

7.10 We are conscious that the value for money practice is a developing area for the Office, and that considerable progress has been made already – for instance in the development of the Manual on Reporting, and in the number of audits carried out. We offer the following comments and recommendations with the intention that they assist the Office in further developing this area of practice.

7.11 Topic selection

7.12 Value for money auditing gives wider and richer information on aspects of the performance of a public body than the financial statement audit can. It is important therefore that the subjects selected for review are of value to the parliament and other stakeholders, and, above all, to the entity subject to the study. This is particularly so given the small number of studies the Office is resourced to carry out. We expected that the Office would have some system for establishing the relative merits of possible subjects, based on materiality and risk, financial or otherwise. We did not find such a system.

7.13 We asked the Office on what criteria it selected and prioritised topics for value for money examinations. We were told that possible topics arise from a combination of sources – annual financial audit work, the Auditor General's discussions with the Public Accounts Committee, public concern, information provided in confidence to the Office, and preliminary reviews carried out by the Office.

7.14 Such a wide range of considerations does not indicate to us that the Office has a coherent approach to the selection of value for money topics. We do not suggest a complex system for identifying and prioritising topics – that would not be justified for such a small number of studies. However, we believe that there should be a clear basis for selection – materiality and risk being the obvious criteria. Although these are included in the Office's list of considerations, it does not seem that they are primary or overriding concerns.

7.15 There will always be a wide range of topics which the Office could examine. It is important that it has an efficient and transparent means of selection, so that it can explain to its stakeholders, and to the client, why it is examining a particular topic (and why it may not be pursuing others). We note that, while they cooperated in the audit, neither of the value for money clients to whom we spoke knew why they had been selected for examination.

Recommendation:

We recommend that the Office clarify its criteria for selecting value for money topics and adopt a simple and transparent system for topic selection.

Auditor General's Response

Accepted.

The Office has clarified its criteria for evaluating potential reporting topics. Theses were set out in the Manual on reporting (April 2008). In summary, proposals for reports will be assessed in terms of:

- *The risk of underperformance or of loss of value for money in the area to be reported on;*
- *The potential of the examination to add value;*
- *The feasibility for the Office to carry out the examination efficiently and effectively.*

7.16 Engagement with the value for money client

7.17 The general focus of value for money auditing, while supporting the accountability of public entities, should be performance improvement. That is best achieved by auditor and client working with, rather than against, one another. It is essential that there be good engagement between auditor and client early in the preparatory stage of a study, as well as during the course of the examination and at the stage of a draft report. Good engagement is necessary for the smooth progress of the examination, and for the study to be of value, both in fact and perception, to the auditee and other stakeholders.

7.18 The examination team is unlikely to have much knowledge of the client entity prior to the audit (unless the study is a follow-up audit), and will need to obtain information from the client. The auditor should consult the client on matters including the timing of the examination, the issues to be addressed, the scope of the study, the criteria against which performance will be assessed, and the particular technical skills which the examination team might require.

7.19 Such engagement should take place at a senior level, on the part of both the Office and the client, although the day-to-day working relationship during the examination is likely to be between the examination team and the relevant members of staff of the client. The intention should be to establish a constructive and professional relationship, and a culture of 'no surprises'. There would also in our view be merit in the examination team engaging with the entity's audit committee.

7.20 Section 6.2 of the Manual on Reporting concerns 'client liaison'. However, it focuses largely on a formal exchange of information, and does not in our view adequately capture the need for a relationship with the audit client based on a mutual understanding of each other's purpose.

7.21 In practice, the quality of the relationship with the client in the two audits we reviewed was variable. In one case, the degree of engagement both in the scoping of the audit and in its conduct appeared to us to have been a burden to the client. In the other case, the engagement was insufficient, and at insufficient level of seniority. As a direct consequence, it seemed to us, there was never in that case a common understanding between auditor and client as to the nature and scope of the audit.

Recommendation:

We recommend that the Office review its procedures for engagement with value for money clients, with particular emphasis on the level of seniority of engagement, on the planning and scoping of a study, as well as on the conduct of the study and the draft report.

Auditor General's Response

Accepted.

The Office's procedure for engagement with value for money clients envisages meetings at Deputy Director of Audit level (on the part of the Office) and at Assistant Secretary, or equivalent, level (for the client) to discuss the scope, evaluation framework and plan for the examination. Clearance of the report is also usually dealt with at that level. Liaison on day-to-day operational matters is done at project leader level with a liaison person nominated by the head of the client body. We will review the extent to which this model is applied in practice.

7.22 Methodology

7.23 The Manual on Reporting sets out the Office's general systems, procedures and practices for value for money studies. We noted three points concerning the methodology which we wish to record, in addition to the matter of engagement with the client discussed above.

7.24 The first is the engagement of expert advice by the audit team. Value for money auditors are likely to be generalists. Many public entities will have quite specialised functions – the studies we considered each concerned such a body. The involvement of an expert should increase the efficiency of the examination process, and strengthen the client's confidence in the value of the study.

7.25 The Manual on Reporting provides for ad hoc Advisory Boards, comprising independent experts in the client entity's field (section 6.4), and allows that individual members of the Board might act as special advisors to the examination team. However, the Manual provides no guidance on when to establish such a Board. No Boards were established, or other expert advice obtained, in either of the studies we considered. In our view, those studies would have benefited greatly from the use of experts.

7.26 Secondly, the Manual does not give guidance on handling a change of scope of a value for money study. From time to time, new matters will arise in the course of a study which ought reasonably to be brought within scope. That was the case in one of the two studies we looked at. Changing, and particularly increasing, the scope of a study requires careful consideration and engagement with the client. In our view, the Manual could usefully provide guidance for examination teams in such circumstances.

7.27 Lastly, the Manual states that the standards and guidelines 'take account' of the INTOSAI *Implementation Guidelines for Performance Auditing* (July 2004) and of the INTOSAI Auditing Standards. We understand however that the value for money methodology has not been made compliant with International Auditing Standards. We see merit in the application of those Standards to the value for money audits, particularly the more comprehensive quality assurance processes which the Standards contain.

Recommendation:

We recommend that the Office review its value for money auditing methodology for consistency with International Auditing Standards, and make changes to the methodology where appropriate, particularly in relation to quality assurance.

Auditor General's Response

Accepted in part.

The Office's manual on reporting, which covers value for money examination methodology, was developed based on the INTOSAI standards for performance audits. The extent to which International Auditing Standards contain additional standards of relevance to value for money appears limited.

A process of quality assurance in relation to value for money examination reports was piloted in April 2008, looking at eight recent reports. This 'cold review' process found that the reports published were generally of a high standard, and made some recommendations in relation to how report material could be presented to increase their effectiveness. The Office manual on reporting is being amended to reflect the recommendations, and a 'cold review' process will be put in place on a rolling basis.

7.28 Staff skills

7.29 The Value for Money Directorate has 21 staff, some long-serving in that Directorate, some who were financial auditors and have moved within the Office as it increased its value for money work, and some who are relatively new to the Office and the Directorate.

7.30 Our impression is of a team that is still developing in its abilities. Value for money auditing requires people with good analytical skills, and the ability to write the reports. Not all staff in the Directorate have both sets of skills. While a degree of compensation is possible, we think that the Office should seek both to increase the skills of value for money staff and to broaden the base of skills among those staff.

7.31 It was not clear to us that value for money auditors were always adequately supervised – due in part to shortages of staff, and also to more senior staff with supervisory responsibilities being themselves engaged on audits. This view relates to the two value for money studies which we considered, and emerged from our interviews of staff and clients concerned in those studies.

Recommendation:

We recommend that the Office seek both to increase the skills of value for money staff and to broaden the base of skills among those staff.

We recommend that the Office strengthen its value for money audit team supervision.

Auditor General's Response

Accepted in part.

The Office is building its capacity to carry out reporting work in a number of ways. Staff with skills and qualifications appropriate to reporting work (but not with accounting qualifications) have been recruited directly into the reporting area. Over a number of years, staff with a financial audit background have been selected through internal competition and sponsored in education programmes in subjects highly relevant to reporting work, up to Master's level. We recognise that this kind of capacity building is a long-term process, and are committed to maintaining our efforts in these respects.

We do not accept that staff are not adequately supervised. There is generally a high level of engagement of management level staff in all stages of reporting work.

8 Output statements

8.1 We include for the sake of completeness, a comment on the possible audit of output statements.

8.2 A department's output statement gives details of the services which the department will produce during the forthcoming year. Output statements are an important development in the accountability of public sector entities, because they focus on the delivery of services. Service delivery is the reason for existence of most public sector entities.

8.3 We note, however, that there is as yet no reporting against output statements at year end of outputs actually delivered, and consequently no audit of that information.

8.4 We believe that there is a role for the Auditor General in auditing departments' outputs. His audit of outputs, and reporting to the Oireachtas, would enhance Oireachtas scrutiny of the Executive.

8.5 We do not suggest that the audit of performance information is a role undertaken by all Audit Offices. However, as different jurisdictions increasingly require public sector entities to report performance information, so the practice of auditing those reports is growing. We acknowledge the resource implications for the Auditor General of such a proposal, but we think it of sufficient importance to merit consideration.

Recommendation:

We recommend that the Auditor General explore the possibility of assuming the role of auditing output statements.

Auditor General Response

The Constitution stipulates that the Auditor General's reporting mandate is determined by law. Consequently, this recommendation is a matter of policy for Government.

This suggestion will be brought to the attention of the Minister for Finance.

Appendix 1

Independence

1. We set out below the conclusions we reached in reviewing the Office against the INTOSAI principles set out in paragraph 4.4 above. There are in our view five areas in which the Office falls short of the INTOSAI standard, at least in theory, if not always in practice:

   - the Auditor General's lack of autonomy in resourcing the Office, flowing from the Office's being part of the civil service;
   - the Auditor General's restricted mandate to carry out value for money audits – in particular, the very limited mandate to examine the effectiveness of public expenditure;
   - the extent to which, and process by which, the Auditor General can report on the financial and value for money audits of entities other than departments;
   - the absence of a follow-up mechanism for audit findings; and
   - the extent to which the Auditor General can 'follow' public money into the hands of a recipient which is a non-government organisation.

Resourcing

2. The INTOSAI principle is that an Auditor General should have available 'necessary and reasonable human, material and monetary resources', and 'the Executive should not control or direct the access to these resources'. Instead, the legislature should be responsible for ensuring that an Auditor General has the proper resources to carry out his mandate.

3. The position of the Auditor General is established by the Constitution, but the Office is a department of the civil service. Funding and staffing are determined as they are for other civil service departments. The Minister of Finance sets the permitted staffing complement for the Office. The Minister also determines the civil service centralised system for appointment and remuneration to which the Office is subject. Funding of the Office follows the normal budget process for departments of state.

4. We saw no evidence that the Office had failed to obtain any approval it had sought from the Minister of Finance to increase its staffing complement. Nor is there any evidence that the Minister or Department of Finance have ever opposed any application for funding.

5. However, the application of civil service appointment and remuneration provisions, in our view, comes into conflict with the Auditor General's independence. It limits his ability to recruit, appoint and promote qualified accountants and auditors, so that a significant aspect of the Auditor General's operation is under the control or influence of the Executive. That limitation has practical effect, as discussed in Part 6c) above.

   Recommendation:

   We recommend that the Auditor General explore with the Minister for Finance the possibility of his Office being constituted as an independent Office outside the civil service. That office would employ its own staff who would no longer be civil servants. We observe that most Audit Offices enjoy this separate status in relation to staffing. We observe too that other Audit Offices have made such a transition without its proving to be a major hurdle.

Mandate – value for money auditing

6. The INTOSAI principle requires that an Auditor General have 'a sufficiently broad mandate and full discretion' in the discharge of his functions. That mandate should include the power to audit the 'economy, efficiency, and effectiveness of government or public entities' operations'.

7. The Auditor General's 'value for money' mandate is set out in section 9 of the Comptroller and Auditor General (Amendment) Act, 1993, and is quoted above in Section 7.1 of this report. In essence, while the Auditor General can audit the economy and efficiency of an entity's operations, he may not review effectiveness. His 'effectiveness mandate' is limited to examining 'the systems, procedures and practices employed by the [entity] for the purpose of enabling the [entity] to evaluate the effectiveness of its … operations'.

8. The powers of the Comptroller and Auditor General are a matter for the parliament to determine. However, we are sufficiently concerned by the matter to offer the following observations:

   - An Auditor General should not audit, or comment on, the merits of government policy – that is the preserve of a government.
   - However, it is common for other Audit Offices to have the mandate to audit the effectiveness of the operations of a public entity, including the implementation of government policy – that is, given the policy, has it been implemented efficiently and effectively, in accordance with its own terms?
   - The terms of reference for the Public Accounts Committee appear to be broader than the Auditor General's mandate: the Committee is to refrain from 'enquiring into the merits of a policy or policies of the Government or a member of the Government or the merits of the objectives of such policies'. However, the Committee will receive from the Auditor General only reports on effectiveness evaluation systems. It seems to us unlikely therefore that the Committee is able to use the full breadth of its own terms of reference.
   - We are not aware of any other provision in the Irish system for the independent review of effectiveness.

   Recommendation:

   We recommend that the Auditor General explore the possibility of proposing the extension of his statutory mandate to include examination of the effectiveness of the operations of an entity or activity funded by public money including the implementation of government policy.

Reporting – semi-state bodies

9. The INTOSAI principles include an Auditor General's 'right and obligation to report on their work'.

10. The Auditor General's ability to report is set out in section 11 of the Comptroller and Auditor General (Amendment) Act, 1993. The right to report on his audits of semi-state bodies is limited. He is empowered by section 11(2)(a)(ii) to prepare a special report only on 'any general matters arising in relation to audits, inspections or examinations' of those entities. He cannot therefore report on a specific matter relating to a particular body, but rather on themes or common issues arising in those audits.

11. We were surprised at the lack of attention paid to semi-state bodies in the accountability cycle, given the significant role played by many semi-state bodies in the disbursement of public funds. Large semi-state organizations experience limited scrutiny by the Oireachtas compared with that experienced by smaller departments of state.

12. We note that section 11 provides for the Auditor General's reports to be laid before the Oireachtas by the relevant Minister, rather than by the Auditor General. Reports on financial audits must be tabled as soon as possible, but value for money reports, and any general reports concerning the audits of semi-state bodies, may be laid before the Dáil within three months. Thus the Minister rather than the Auditor General determines the timing of publication.

Recommendations:

We recommend that the Auditor General explore the possibility of proposing the extension of his statutory power to report to include the full range of reports on all of the public bodies subject to his audit.

We recommend that the Auditor General propose the transfer to him of the responsibility for laying his reports before the Oireachtas.

Follow-up mechanisms

13. INTOSAI considers that an Auditor General's independence is enhanced by 'the existence of effective follow-up mechanisms on recommendations made by the Auditor General'.

14. Those mechanisms could be formal, such as a statutory requirement that an entity account for actions taken in response to an Audit Office's recommendations, or informal, such as select committees in practice requiring entities to account, or the Audit Office itself undertaking follow-up audits.

15. The Office undertakes a few follow-up audits, and where a department is concerned, it can report to the Public Accounts Committee in the Auditor General's Annual Report.

16. The Annual Report is the Auditor General's main product. It is his report to the Public Accounts Committee on his findings during the audits of Departments' financial statements in the previous year. In effect, it forms the Committee's work programme for the forthcoming year. There is a formal report and response communication process between the Committee and the Minister for Finance in place in relation to the Annual Report and its examination by the Committee. The Committee's report is laid before the Dáil, but the House does not debate it.

17. While the role of the parliament of course falls outside our terms of reference, we note the limited engagement of the Oireachtas in following up on the findings and recommendations of the Auditor General and the Public Accounts Committee.

Recommendation

We recommend that the Auditor General explore the possibility of proposing more formal mechanisms for the follow-up of his reports.

Mandate – following the money

18. A broad mandate should also include the power to audit the 'use of public monies, resources, or assets, by a recipient or beneficiary regardless of its legal nature'.

19. The Auditor General is able, under section 8 of the Comptroller and Auditor General (Amendment) Act, 1993, to inspect the books and records of any body for a financial year in which moneys received directly from the State amount to 50% or more of that body's gross receipts for that year. However, the inspection can be made only for the year in which the funds are received, and not for a year in which they are spent, if that year is a later year (unless that year is also one in which more than 50% of the body's gross receipts come from the State).

Recommendation

We recommend that the Auditor General explore the possibility of an extension to his ability under section 8(1)(b) of the Comptroller and Auditor General (Amendment) Act, 1993 to examine the books and records of a body receiving more than 50% of its funds from the State.

Auditor-General's Response

The proposals outlined in this Appendix would all entail amending legislation. This is ultimately a matter of policy for the Government.

These suggestions will be brought to the attention of the Minister for Finance.

Appendix 2

Review team:

The review team comprised:

Ms Phillippa Smith	Deputy Controller and Auditor-General for New Zealand
Mr Lew Hughes	Member of the UK Auditing Practices Board and former Assistant Auditor General, UK National Audit Office
Mr Andrew Clarke	Chartered Accountant and former managing partner Horwath Bastow Charleton
Mr Paul Haran	Principal of the College of Business and Law, UCD and former Secretary General of the Department of Trade and Employment

Interviewees:

The Team interviewed the following external stakeholders:

Bernard Allen TD	Chairman of the Committee of Public Accounts
Brendan Kenneally	Vice Chairman of the Committee of Public Accounts
Dermot McCarthy	Secretary General to the Government
Kieran Coughlan	Clerk of Dáil Éireann
Dermot Quigley	Chairman of the OCAG Audit Committee
Kevin Sheehan	Deloitte (OCAG external auditor)
David Doyle	Secretary General, Department of Finance
Sean Gorman	Secretary General, Department of Enterprise, Trade and Employment
Ciaran Connelly	Secretary General, Department of Finance Public Service Management and Development
Donal McNally	2nd Secretary General, Policy Unit, Department of Finance
Brigid McManus	Secretary General, Department of Education and Science
Prof Brendan Drumm	Chief Executive Office, Health Service Executive
Patrick Neary	Chief Executive, Financial Regulator
Dr Patrick Wallace	Director, National Museum
Hugh O'Connor	OCS Consulting (Client Satisfaction Survey)

In addition to discussions with John Purcell (the Auditor General at the time of the Review), the Team interviewed the following senior staff of the Office:

John Buckley	Secretary and Director of Audit
Gerry Smyth	Director of Audit (Health, Education and Semi-states)
Fergus Glavey	Director of Audit (Government Departments)
Maureen Mulligan	Deputy Director, Corporate Services

The Team also interviewed members of the staff of the Office who were responsible for particular financial audits and performance audit.