

## Relevant strategic objectives

### Reports and advice

Being authoritative and relevant

### Parliament

Being highly regarded by Parliament

Here is an overview of our achievements, challenges and future steps for our Financial Audit business unit.

### Our challenge in the year ahead

- We did not achieve our target of 100 per cent for the performance measure 'External/peer reviews finding no material departures from professional and regulatory standards' (page 14).
- Our average index score for financial audit process decreased by 4 per cent, from 77 per cent in 2014–15 to 73 per cent in 2015–16, with some agencies concerned about the timeliness of the audit program, the continuity of audit staff, and responsiveness to agency needs (page 71).

### Next steps

- We will increase our focus on people within the financial audit business unit, particularly around learning and development, reward and recognition, and succession planning (page 72).
- We will change our model for delivery of financial audits, particularly around the extent to which we rely on audit service providers for high-risk, material and/or strategic financial audits (page 72).
- We will continue to enhance our Audit Snapshot reports to Parliament (page 72).
- We will rebase all of our financial audit budgets as part of a cyclical review process (page 72).



## Achievements

- Following the issue of a disclaimer of audit opinion on its 2014–15 financial report, the Department of Education & Training (DET) undertook a major remedial work program working in close consultation with our office (page 71).
- We issued the Auditor-General's review report on the 2016–17 Estimated Financial Statements of the state on 22 April 2016, earlier than in the previous year (page 71).
- We issued 98 per cent of our audit opinions within the statutory deadlines, right on target, despite encountering client delays, several contentious and complex matters, and changes arising from the 2015 machinery-of-government changes (page 14).
- We tabled seven reports on the results of financial audits in Parliament, and a report on financial systems information technology controls (page 68).
- 43 of the 44 recommendations we made were accepted (page 20).
- We issued 539 audit opinions on the financial statements of agencies, and 108 audit opinions on the performance statements of agencies (page 14).

## What we do

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Our financial audit program delivers a number of assurance services for a range of agencies.

As part of Output Group 1, our financial audit program delivers reports to Parliament on the results of financial audits and on the Annual Financial Report of the State of Victoria.

As part of Output Group 2, our financial audit program delivers audit opinions on financial statements and performance statements of public sector agencies, an opinion on the Annual Financial Report of the State of Victoria and a review report on the estimated financial statements of the State of Victoria.

Eight financial audit reports (including one Information Systems Audit report) listed in our Annual Plan 2015–16 were tabled, as listed below. There were no changes to the proposed program of tabled reports during the year.

<p><b>October 2015</b></p> <p><i>Financial Systems Controls Report: Information Technology 2014–15</i></p> <p><b>November 2015</b></p> <p><i>Local Government: 2014–15 Audit Snapshot</i></p> <p><i>Auditor-General's Report on the Annual Financial Report of the State of Victoria, 2014–15</i></p> <p><i>Public Hospitals: 2014–15 Audit Snapshot</i></p>	<p><b>December 2016</b></p> <p><i>Water Entities: 2014–15 Audit Snapshot</i></p> <p><i>Portfolio Departments and Associated Entities: 2014–15 Audit Snapshot</i></p> <p><b>May 2016</b></p> <p><i>Universities: 2015 Audit Snapshot</i></p> <p><i>Technical and Further Education Institutes: 2015 Audit Snapshot</i></p>
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## How we do it

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The objective of each of our annual financial audits is to express an 'audit opinion' as to whether the financial report (or other statement as applicable) presents fairly, in all material respects, the financial position and the financial performance of the audited agency, in accordance with applicable Australian Accounting Standards and the relevant legislative financial reporting requirements. When undertaking a financial audit, the *Audit Act 1994* requires the Auditor-General to also consider the issues of waste, probity, and the prudent use of public resources.

Our financial audits apply a risk-based audit methodology to ensure that they are performed in accordance with the Australian Auditing Standards and relevant professional and legislative requirements. Each year, our financial auditors review key internal controls over the financial systems of each government agency to assess the risk of material misstatements in the financial report. They also test aspects of controls or activities in detail, to draw out and report on systemic or sector-specific issues.

### Selection of areas of audit focus

'Areas of focus' are selected for specific review as part of our financial audits, such as governance, probity, fraud, financial prudence and noncompliance. The selected areas of focus are identified in our annual plan, and can result in related commentary being included in our reports to Parliament on the results of financial audits.

## Delivering our audits

### Resourcing

Our financial audits are conducted by our staff, or with the assistance of externally engaged firms. All financial audits conducted with the assistance of external firms known as audit service providers (ASPs) are subject to project management and quality assurance by our staff, and all audit opinions are issued by the Auditor-General.

The mix of resources we use to deliver our financial audit program changes over time based on multiple factors. In 2015–16, approximately 33 per cent of our audits were undertaken by our staff, with the remaining 67 per cent undertaken with the assistance of ASPs, as shown in Figure 23.

[Figure 23] Audits conducted in 2015–16, by materiality, risk and sourcing model

Materiality and audit risk	In-house (number)	Audit service provider assisted (number)	Total (number)
<b>Material entity audits</b>			
High risk	10	4	14
Moderate risk	17	15	32
Low risk	0	1	1
<b>Total material entity audits</b>	<b>27</b>	<b>20</b>	<b>47</b>
<b>Non-material entities</b>			
High risk	3	12	15
Moderate risk	56	130	186
Low risk	100	208	308
<b>Total non-material entity audits</b>	<b>159</b>	<b>350</b>	<b>509</b>
<b>Total audits</b>	<b>186</b>	<b>370</b>	<b>556</b>

Note: Based on data as at 30 June 2016.

The criteria we use to determine the resourcing of financial audits includes:

- **Materiality**  
Considerations of materiality also includes material agencies, which are those whose revenue, expenses, assets and/or liabilities are significant to the State of Victoria's annual financial report.
- **Risk profile**  
An agency's risk profile also includes audit risk. This is the risk that an inappropriate audit opinion is issued on a financial report.
- **Strategic value of the agency**  
An agency's strategic value is assessed in terms of its strategic importance to the state or relevant sector as a whole. For example, this includes the significance of its role in the state's budget strategy, as set out in the State Budget Papers.

### Risk-based financial audit methodology

To ensure that our financial audits are performed in accordance with the Australian Auditing Standards and relevant professional and legislative requirements, our financial audit methodology is integrated into our electronic audit toolset, Integrated Public Sector Audit Methodology, which was developed with the Queensland Audit Office, and is in use in four other Australian jurisdictions.

### **Methodology for reviewing the estimated financial statements**

Our review of the state's estimated financial statements uses the principles in ASAE 3450 Assurance Engagements involving Corporate Fundraising, and/or Prospective Financial Information.

### **Technical Issues Committee**

Our Technical Issues Committee provides advice and recommendations to the Auditor-General on proposed modifications to financial audit opinions, the appropriate policy or guidance that we should adopt in relation to significant financial reporting and auditing issues, and issues affecting our legislative mandate.

The committee comprises the Assistant Auditor-General, Standards and Quality, the Assistant Auditor-General, Financial Audit, the Standards and Quality Director, the relevant Financial Audit Sector Director responsible for the audits under consideration, and an independent Financial Audit Sector Director.

### **Technical Panel**

Our Technical Panel was established in June 2015 to inform and discuss the following matters with the Auditor-General and Deputy Auditor-General/Chief Executive Officer:

- current accounting and auditing technical issues
- current developments and emerging issues in the accounting and auditing technical profession, and our office's responses to these matters
- current and planned activities to address technical issues, including audit quality reviews and training
- current and planned activities of the ACAG Financial Reporting and Auditing Committee and other relevant professional bodies, including the status of responses to standard-setting bodies.

Our Technical Panel generally meets every month, and provides a forum to capture feedback from the Auditor-General and Deputy Auditor-General on the above matters.

### **Challenge Committee**

Our Challenge Committee reviews the progress and completion of financial audit parliamentary reports at key points in their development to ensure their quality, accuracy, logic and rigour. The committee then determines if the approach and the report are of a sufficiently high standard to progress to the next phase, or for documentation to be issued to relevant agencies.

#### *Debrief process*

At the end of every financial audit parliamentary report, we conduct an audit debrief process to identify positives and areas for improvement, which are considered in future activities. Each audit debrief is given careful consideration by our Challenge Committee.

### **Quality assurance**

To seek assurance that our audits meet professional and VAGO quality standards, our audits are reviewed by external or peer reviewers both in relation to the robustness of the audit process, and the quality of the final audit report. See page 49 for further information.

## Feedback from audited agencies

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Every second year we survey chief financial officers, and ask about the value they obtain from their financial audits.

In 2015–16, the average indexed rating for questions about audit value was 76 index points, which was consistent with the results for 2013–14 survey. Feedback from most financial audit clients was positive about the value of the audit, and in particular, many clients indicated that the audit provided assurance and confidence in relation to the financial processes of their organisation

We also survey the chief financial officers about the financial audit process and financial audit reporting to identify areas for improvement. While the average index score for financial audit reporting to agencies was consistent with the previous survey, the average index score for financial audit process decreased from 77 per cent to 73 per cent, 4 per cent lower than the last time the survey was run in 2013–14. While professionalism and skills of staff continue to score well, some agencies were concerned about the timeliness of the audit program, the continuity of audit staff, and responsiveness to agency needs. We discussed feedback received with our agency contacts where relevant, in part to clarify that feedback, and any action we may take in response as appropriate.

### Extracts from agencies responses to our post-audit surveys

“ We value VAGO’s observations on our financial statements—they raise issues that we sometimes overlook.

“ Recommendations are well received and respected within our organisation.

## Key developments in 2015–16

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### Contentious and complex matters

In 2015–16, we encountered several contentious and complex matters during a financial reporting cycle that had been influenced by the 2015 machinery-of-government changes. This resulted in a disclaimer of audit opinion on the 2014–15 financial report of the Department of Education & Training (DET).

Pleasingly, we note that DET has undertaken a major program of work throughout 2015–16 to systematically address the matters raised by our audit. This has included a revaluation of all land and buildings, a review and cleanse of asset records and a new assurance regime over school based transactions has been developed and is being implemented. This program of work has been assigned a very high priority by DET.

Our review of the State of Victoria’s 2016–17 Estimated Financial Statements was completed over a week earlier than in the previous year. This is a substantial achievement, given that the already tight deadlines for this review had been further tightened and some contentious matters were considered as part of that review. This led to the Auditor-General issuing an emphasis-of-matter paragraph.

### Financial audit re-orientation

The re-orientation of our financial audit business unit undertaken in 2015–16 included a review of the model for the delivery of audits, which considered the optimal resourcing model for the conduct of financial audits—that is, using internal resources or undertaking audits with the assistance of ASPs. This project will result in the delivery of a larger proportion of higher-risk, material and/or strategic financial audits using internal resources, and will benefit our office in several ways, including increasing control and oversight and consistency of approach to the more significant audits, reducing risk and increasing assurance.

In addition, we successfully managed the implementation of our new ASP panel arrangements.

## Looking forward

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### Targeted audit program

We plan to table seven financial audit snapshot reports and one information technology financial systems controls report in 2016–17. We expect to issue 555 audit opinions on financial statements and 111 audit opinions on performance statements.

### Innovation and continual improvement

We are committed to continual improvement in our financial audit practice and have identified the following three areas of focus for 2016–17.

#### **People**

Our focus will particularly be on learning and development (including developing and rolling out the financial audit training curriculum), reward and recognition, and succession planning.

#### **Product**

We will continue to enhance our financial audit reports to Parliament, including how we develop focus areas and analyse financial sustainability. We will continue to change our model for delivering financial audits, particularly the extent to which we rely on ASPs for high-risk, material and/or strategic financial audits. Also, we will implement an updated audit sampling methodology to enhance our audit approach to tests of details. We will further consider introducing enhanced audit reports (opinions), as envisaged under the Auditing and Assurance Standards Board Enhanced Audit Reporting framework.

#### **Process**

We will review how we supervise our ASPs.

In addition, we will rebase all of our financial audit budgets as part of a cyclical review process.