

**Office of the Auditor General of Canada**

**Report on a Review of the  
Performance Audit Practice**

Practice Reviews Conducted in the 2010–11 Fiscal Year

**May 2011**

**Practice Review and Internal Audit**

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## Introduction

- 1.** The Office of the Auditor General conducts independent audits that provide objective information, advice, and assurance to Parliament, territorial legislatures, and Canadians. The Office has several product lines, including performance audits, annual audits, and special examinations.
- 2.** Performance audits examine, against established criteria, whether government programs are being managed with due regard for economy, efficiency, and environmental impact, and whether measures are in place to determine their effectiveness. The subject of the audit can be a government entity or activity (business line), a sectoral activity, or a government-wide functional area.
- 3.** The Practice Review and Internal Audit team conducted practice reviews of selected performance audits reported between March and December 2010. This work was done in accordance with the monitoring section of The Canadian Institute of Chartered Accountants (CICA) Handbook—Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements (CSQC–1). It was also done in accordance with the Office’s 2010–11 Practice Review and Internal Audit Plan, which was recommended by the Audit Committee and approved by the Auditor General. The plan is based on systematic monitoring of the work of all audit principals in the Office on a cyclical basis.
- 4.** To meet CICA standards, the Office establishes policies and procedures for its work. These are outlined in an audit manual, various other audit tools, and a quality management system for each product line (which ensures that quality is built into the audit process). These guide auditors through a set of required steps to ensure that the audits are conducted according to professional standards and Office policies. There is a product leader at the assistant auditor general level for the performance audit product line, whose primary function is to provide leadership and oversight for the product line and to contribute to the quality of the individual audits.
- 5.** This report summarizes the major observations related to the practice reviews of the selected performance audits.

## Overview

### Objective

6. The objective of practice reviews is to provide the Auditor General with assurance that
- performance audits comply with professional standards and applicable legislative and regulatory requirements,
  - the quality management system (QMS) is effectively implemented, and
  - audit reports are supported and appropriate.

### Scope and methodology

7. We conducted practice reviews of six performance audits over the reporting period—two audits tabled in April 2010, two tabled in October 2010, and two tabled in December 2010.
8. Our reviews included an examination of electronic (TeamMate) and paper audit files. We examined audit files related to the planning, examination, and reporting of the audits. We interviewed audit team members, quality reviewers, and other internal specialists, as appropriate.

### Quality management system elements and process controls reviewed

9. The Performance Audit Quality Management System is summarized in Appendix A. We focused our work on the selected elements and key process controls that we considered key or high risk (Appendix B).
10. We also looked at how the quality reviewers carried out their responsibilities. Quality reviewers are management-level employees of the Office who are appointed to provide an objective evaluation, before the auditor's report is issued, of the significant judgments that the audit team made and the conclusions that it reached in formulating the audit opinion. The quality reviewer is an important element of the Office's quality control system and is involved in selected individual audits from initial planning decisions to the closing of the audit file.

## Rating system

11. We applied one of the following ratings to each selected QMS element of the individual performance audits under review:

- **Compliance.** Office policy requirements and applicable auditing standards were met; minor improvements might be possible.
- **Compliance but needs improvement.** Improvements are necessary in some area(s) to fully comply with Office policies and/or auditing professional standards.
- **Non-compliance.** Major deficiencies exist; there is non-compliance with Office policies and/or auditing professional standards.

12. After completing each practice review, we concluded on whether the audit conclusion was supported and appropriate.

13. This report highlights the procedures performed, the conclusions drawn, the deficiencies found, and the actions taken to resolve these deficiencies.

## Results of the Reviews

### Compliance with the quality management system and process controls

14. Overall, we found that, in five of the six files reviewed, the audit conclusions were supported and appropriate. In the other file, we concluded that, for one line of enquiry, the audit conclusion was too broadly stated given the actual work performed. There was not sufficient and appropriate evidence to support some observations and conclusions in the report related to that line of enquiry. Management subsequently required the audit team to add documentation to the audit file, and provide their rationale for the audit conclusion reached. The Practice Review Team did a follow-up review of this file, and found that the audit team had done so.

15. One of the six audit files was fully compliant with the elements reviewed (one was also fully compliant in the 2009–10 fiscal year). Another three files reviewed were compliant in all areas of the quality management system (QMS) except one area: independence (three files were compliant in 2009–10). The remaining two files needed improvement in the application of at least two elements of the QMS. Overall, the results are comparable to 2009–10.

16. In the practice reviews we conducted in prior years, we noted a number of instances where the QMS was not applied consistently and rigorously, or where its design needed improvement. As a result, the Office made

it a strategic priority to update and strengthen the design and implementation of the QMS. Given the nature and the extent of our findings, and given that audits were under way at the time of our review, we did not expect all findings to be fully addressed in the 2009–10 fiscal year.

**17.** We noted that the Office has undertaken initiatives, such as major updates of the audit manual, a review and update of the professional development curriculum, and the development of an action plan to address the recommendations made in practice review and peer review reports from the prior years.

**18.** We also noted that workshops have been held to share best practices and reinforce Office policies and expectations; the TeamMate audit tool has been updated; and, during training, emphasis was placed on observations from prior reports.

**19.** In our opinion, these actions contributed to the improvements we noted over the past two fiscal years.

**20.** When the audit engagements we reviewed showed areas where practices could be improved, the opportunities for improvement were discussed with the responsible principals and assistant auditors general, who agreed with the suggestions. The suggestions for improvement do not apply to all the performance audits reviewed.

## **Notable improvements**

**21.** In the files we reviewed this year, two areas showed significant improvement over previous years: the extent of review of audit work by more experienced members of the audit team and the use of audit programs.

### **Extent of review**

**22.** Assurance standards require that audit files be reviewed and that more experienced team members review the work of less experienced ones. This helps determine, among other things, whether teams have obtained sufficient and appropriate evidence to support the audit report and that adequate supervision and review is carried out throughout the audit.

**23.** In four of the six files reviewed, senior management was appropriately involved and provided timely review. Among other things, there was evidence of senior managers providing direction to audit teams and actively participating in key meetings and decisions at the planning and reporting phases of the audits.

**24.** Overall, working papers were reviewed on a timely basis, and the documentation on file demonstrated the extent to which the conducted and completed audit work was reviewed. However, in two of the six files,



we again observed in the 2010–11 fiscal year that some working papers were both prepared and reviewed by the same person. This practice stopped in March 2010 when the Office issued a practice advisory requiring a separate preparer and reviewer for performance audit working papers. The TeamMate electronic audit documentation tool also no longer allows the same person to perform both tasks.

### **Use of audit programs**

**25.** Office methodology and assurance standards require that audit procedures be developed to guide auditors in conducting their audit work. In the files we reviewed, we noted progress compared with last year when we had reported absent and incomplete audit programs outlining procedures to be conducted, or an absence of a summary of findings and conclusions on work performed. We found that in one file, audit programs were developed but not completed or linked to the audit work. In that file, the audit team was required to document how the work performed supported the audit observations.

### **Opportunities for improvements**

**26.** The observations in this section of the report and the recommendations at the end represent opportunities for improvement across performance audit practice, based on the findings most commonly identified in the individual practice reviews.

#### **Documentation of the audit file**

**27.** Teams are improving their use of TeamMate. Files are structured in a logical way to provide for ready access to the audit evidence. We continue to see an overall improvement in the structure of the audit files. Updates to the audit documentation tool and training provided throughout the year contributed to better file structures.

**28.** Five of the six files contained working papers supporting the work performed and sufficient evidence for the conclusions.

**29.** In one file, the team made extensive use of encrypted emails in conducting their work. These emails were stored in TeamMate; however, once archived, the emails are no longer accessible. Consequently, key elements of the audit substantiation are no longer accessible. However, the audit team had retained copies of emails elsewhere and was subsequently able to restore them and adjust the audit file.

**30.** TeamMate protocol and the internal Electronic Document Management Policy specify that encrypted emails should not be kept in the TeamMate electronic documentation tool. The Office has since reminded staff that the practice of saving encrypted emails in TeamMate should be discontinued.

Further guidance should be sent to audit teams to advise and explain how to store such information in audit files.

### **Period covered by the audit**

**31.** Assurance standards require that the period covered by the audit be disclosed in audit reports. In three of the six files, we noted that the period covered by the audit could have been better defined. In some cases, the period indicated was very broad—up to many years—and it was sometimes unclear if the situation described in the report extended back to the beginning of the period covered by the audit.

**32.** We also noted that the Entity Plan Summary, Audit Logic Matrix, and other related planning documents often did not specify the period under audit, nor did the audit program. Clarifying the period covered by the audit and the impact on the required audit work would benefit auditors in carrying out their work.

### **Change in scope of work, audit criteria, or audit objectives**

**33.** In three of the six files reviewed, we noted that changes were made to the audit objective or audit criteria. Some of those changes occurred well into the examination or reporting phases. We could not find evidence that the audit entities were formally advised of the changes, as required by Office methodology. In all three cases, the quality reviewers had not been informed of the change in the scope, criteria, and objectives on a timely basis. In two of the three cases, there was no evidence that the responsible assistant auditor general had approved the decision in a timely manner.

**34.** Moreover, in two of the three files, we could not determine if the audit team had assessed the impact of changes in the criteria or audit objective on the work to be carried out to conclude on the audit. In one case, significant changes were made to the planned work during examination, but there was not sufficient evidence that the audit team had assessed the impact of these changes on their ability to conclude on the audit objective. In this case, management subsequently required the audit team to add documentation to the audit file and provide the rationale for the audit conclusion reached. On the other file, the audit team was able to demonstrate that the change in scope of work did not impact their ability to conclude on the objective.

### **Departures from the quality management system**

**35.** The Office has developed a quality management system (QMS) that identifies a number of quality control steps to ensure that performance audits comply with Office policies. These steps apply to all performance audits and involve a number of required templates and consultations.

**36.** In one of the six files reviewed, we noted several departures from the QMS. Discussions on these departures were held with the product leader,

and documentation was on file outlining the departures and their rationale. However, the documentation was not completed in a timely manner, and was completed without seeking the product leader's disposition. There were no departures from professional standards.

**37.** In September 2010, the Office issued a practice advisory allowing audit teams to tailor the Office's quality controls based on audit risks for individual performance audits. More specifically, when departures from the QMS are recommended, the responsible practitioner needs to document the risk assessment and rationale for recommending departures from the QMS and have them approved by the responsible assistant auditor general. The product leader is responsible for reviewing the recommendation and proposing changes to the recommendation, if applicable. This process was not applicable at the time of the audit.

### **Quality reviewer**

**38.** As noted in prior years, quality review is an important element of quality assurance within the Office. For the files we looked at this year, we again noted improvement in the timeliness of the reviews, in comments provided to audit teams, and in the team's action on the comments. We also noted that in two of the files we looked at, the quality reviewers had knowledge of the program area audited and were able to provide more in-depth comments on the direction of the audit and audit findings.

**39.** However, the nature and extent of the quality reviewers' work still vary from one file to another. In one case, the quality reviewer did not sufficiently challenge the audit team, review working papers, and ensure that changes in scope and decisions were appropriately documented. In another case, the timing and nature of the work performed by the quality reviewer was not adequately documented.

**40.** We noted that when quality reviewers used a draft performance audit checklist, the nature, timing, and extent of the work they performed complied with the QMS and related audit standards. This checklist has been in draft status for more than three years.

**41.** In our view, it is important that the Office finalize the performance audit checklist for quality reviewers by incorporating the related review procedures and expectations in the methodology and related audit tools.

### **Independence**

**42.** Assurance standards require that auditors be independent of the entity they are auditing. Accordingly, threats to independence—and the safeguards used to reduce such threats to an acceptable level—must be assessed and documented. The Office has specific policies and procedures designed to prevent independence infractions. Notably, all those involved in the audit work

are required to complete a declaration of independence form for each assurance engagement they are assigned to.

**43.** In our previous 2009 and 2010 summary reports, we noted that not all those involved in the audit work had confirmed their independence and completed the form. In five of the six files reviewed this year, this was again the case. At the time the audits began, Office policy did not require all individuals advising the audit team in the conduct of its audit to complete a declaration of independence form.

**44.** A revised practice advisory was issued in December 2009 clarifying that all those involved in reviewing the audit work or advising the audit team members (for example, quality reviewers, internal advisors, advisory committee members, and internal specialists) were expected to assess, document, and address threats to independence at the beginning of every assurance engagement by completing an independence form.

**45.** We found that, in most cases, assessment of independence was not done for internal advisors, such as the specialists, the performance audit practice team, members of the audit logic matrix committee, and product leaders, or for the external advisors.

**46.** To mitigate risks, independence should be assessed for all of those involved in reviewing the audit work or advising the audit team; otherwise any lack or perceived lack of independence might impair the credibility of audit work, observations, and recommendations

## Conclusion and Recommendation

**47.** For five of the six performance audits that we reviewed, the auditor's report was supported and appropriate. In the other file, we concluded that for one line of enquiry, the audit conclusion was too broadly stated given the actual work performed. There was not sufficient and appropriate evidence to support some observations and conclusions in the report related to that line of enquiry. Management subsequently required the audit team to add documentation to the audit file and provide their rationale for the audit conclusion reached. The Practice Review Team did a follow-up review of this file, and found that the audit team had done so. We also conclude that, for the elements of the quality management system that we reviewed, there are opportunities for improvement in how they are implemented.

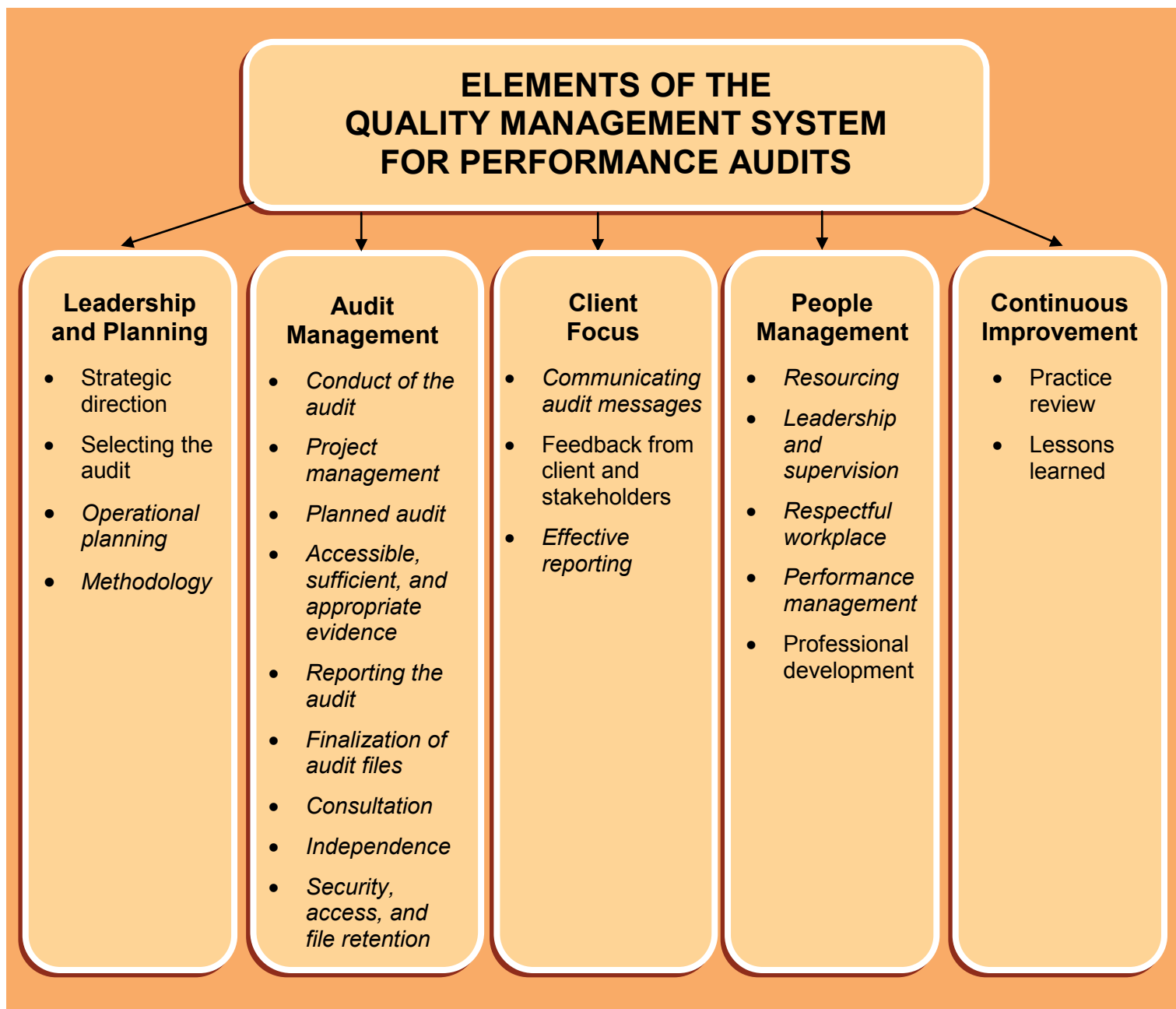
**48. Recommendation.** The Office should

- finalize the specific performance audit expectations for quality reviewers, including incorporating them in the TeamMate electronic documentation tool and related guidance;

- provide more guidance on the determination of the period covered by the audit and the impact on the required audit work;
- clarify and communicate expectations for confirmation and assessment of independence for those involved in reviewing the audit work or advising the audit team (in particular, clarification is needed for internal advisors, such as the performance audit practice team, members of the audit logic matrix committee, and product leaders, as well as for external advisors); and
- remind auditors that changes in criteria, audit scope, and objectives need to be discussed and approved by the responsible assistant auditor general and that the quality reviewer, along with the audited entities, should also be informed of the decision on a timely basis.

***Management has responded. Management agrees with the recommendations. Detailed responses and planned actions are included in Appendix C.***

## Appendix A—Quality Management System Elements for Performance Audits



The elements italicized in the table are included in one or many of the Quality Management System elements or process controls described in Appendix B.

## Appendix B—Quality Management System Elements and Process Controls Reviewed

Our review covers the following quality management system elements and key process controls:

**Conduct of the audit.** As part of the audit work for each of the files we examined, we reviewed the following process controls:

- **Planning.** We determined whether the work was adequately planned and whether issues were selected on the basis of risk, their significance and auditability, and their relevance to the Office's mandate. As well, we determined whether suitable criteria for evaluating the subject matter were identified and developed. Attention was given to the development and application of audit logic matrices and whether planned audit work was carried through into examination and reported.
- **Examination.** We looked at the substantiation files and other audit files to determine whether sufficient and appropriate evidence was obtained to provide a reasonable basis to support the conclusion in each report. We reviewed each report for secondary evidence information and reached a conclusion on the adequacy of the team's rationale for including such information.
- **Reporting.** We reviewed each report to determine whether it addressed high-risk areas and the associated criteria and whether it was relevant, coherent, clear, and credible. We also determined whether oversight of the reports effectively ensured consistency with the Office's mandate and principles and with past corporate decisions.

**Finalization of audit files.** We determined if audit files were closed within 45 days of final approval of each audit report, as required by CICA assurance standards and Office practice requirements.

**Consultation.** We determined whether consultation was sought from authoritative sources and specialists with appropriate competence, judgment, and authority to ensure that due care was taken, particularly when dealing with complex, unusual, or unfamiliar issues. We also determined whether the consultations were adequately documented, and whether the audit team took appropriate and timely action in response to the advice received from the specialists and other parties consulted, including the quality reviewer.

We determined whether the quality reviewer carried out an objective and timely evaluation of

- the significant judgments made by the team,
- the conclusions reached in supporting the auditor's report, and
- other significant matters that have come to the attention of the quality reviewer during his or her review.

We determined whether the work of the quality reviewer was adequately documented, and whether the audit team took appropriate and timely action in response to the advice received from the quality reviewer.

**Resourcing.** Based on interviews with staff and review of documents, we determined whether audit teams had collective knowledge of the subject matter and the auditing proficiency necessary to fulfill the audit requirements. As well, we determined whether the individuals carrying out the audit work had adequate technical training and proficiency. We also considered the number of staff and the timing of their availability.

**Independence.** We determined whether all individuals performing audit work, including specialists, had been independent in carrying out their responsibilities and in forming their conclusions.

**Leadership and supervision.** We determined whether individuals working on the audit received an appropriate level of leadership and direction and that

- adequate supervision of all individuals, including specialists, was provided to ensure that audits were properly carried out; and
- all audit team members were encouraged to perform to their potential.



## Appendix C—Management Response to the 2011 Report on a Review of the Performance Audit Practice

### Introduction

This document provides management's response to the practice review observations and recommendations as well as an action plan. The action plan identifies responsibility for implementing the planned actions and timelines for completion.

All recommendations and observations will be addressed through the Renewal of Audit Methodology (RAM) project. This project involves revising performance audit methodology and including the actual wording of the relevant CICA standards in the manual, as well as interpreting how they should be applied to performance audit. The work done to interpret the standards will make it clear to performance auditors what is required in actual practice to meet the requirements in the standards.

Senior management is fully engaged in RAM and is committed to rolling out the changes to methodology in fall 2011. The rollout will include the revised manual, TeamMate procedures, and templates. Information sessions will be provided to performance auditors to introduce the changes in methodology.

The tables below list the recommendations and key observations, management response and planned actions, and the individuals responsible.

### Recommendations

Practice Review recommendation	OAG response and planned actions	Responsibility
Finalize the specific performance audit expectations for quality reviewers by including them in the TeamMate electronic documentation tool and related guidance.	<b>Agreed.</b> The checklist for quality reviewers is being revised and will be accessible through TeamMate, as well as the intranet, when RAM is rolled out in fall 2011. The checklist will include several areas common to all product lines, as well as areas specific to performance audit. The revised manual is intended to provide guidance on this. Teams will be informed through RAM training in the late fall, as well as through ongoing chapter author information sessions.	Assistant Auditor General (AAG) Professional Practices Group (PPG)/Performance Audit Product Leader

Practice Review recommendation	OAG response and planned actions	Responsibility
Provide more guidance on the determination of the period covered by the audit and the impact on the required audit work.	<p><b>Agreed.</b></p> <p>The revised manual will include additional guidance on identifying and determining the period covered by the audit and/or different lines of enquiry. This will also be emphasized in TeamMate procedures and templates, and will be a topic of discussion at chapter author information sessions.</p>	AAG PPG/ Performance Audit Product Leader
Clarify and communicate expectations for confirmation and assessment of independence for those involved in reviewing the audit work or advising the audit team (in particular, clarification is needed for internal advisors, such as the performance audit practice team, members of the audit logic matrix committee, product leader, as well as external advisors).	<p><b>Agreed.</b></p> <p>The expectations for confirmation and assessment of independence will be clarified as part of the revised manual. Guidance will clearly state the independence requirements for roles such as</p> <ul style="list-style-type: none"> <li>• members of the audit team;</li> <li>• contractors acting as team members;</li> <li>• external advisors;</li> <li>• internal specialists;</li> <li>• members of the Audit Logic Matrix (ALM) Review Committee;</li> <li>• product leader; and</li> <li>• Performance Audit Practice Team staff, where appropriate.</li> </ul> <p>This message will be communicated through RAM training and chapter author information sessions.</p>	AAG PPG/ Performance Audit Product Leader
Remind auditors that changes in criteria, audit scope, and objectives need to be discussed and approved by the responsible assistant auditor general and that the quality reviewer, along with the audited entities, should also be informed of the decision on a timely basis.	<p><b>Agreed.</b></p> <p>Guidance on the need to communicate any substantial changes in objectives or criteria to the quality reviewer and audited entities will be included in the revised manual and emphasized in TeamMate procedures and templates. This will also be mentioned in RAM training and chapter author information sessions.</p>	AAG PPG/ Performance Audit Product Leader

## Key Observations

Practice Review observation	OAG response and planned actions	Responsibility
Some working papers were prepared and reviewed by the same person (paragraph 24).	The importance of reviewing documentation will be emphasized in the revised manual. Moreover, TeamMate no longer allows for the same person to prepare and approve a document.	AAG PPG/ Performance Audit Product Leader
Additional guidance should be communicated to audit teams to advise and explain how to store encrypted emails in audit files (paragraph 30).	Guidance has been provided by the Chief Information Officer/AAG PPG on handling encrypted emails. Guidance on storing documents and maintaining confidentiality will also be provided in the revised manual and in TeamMate.	Chief Information Officer/AAG PPG
Documentation regarding departures from the quality management system was completed after the fact and without documentation of the Product Leader's concurrence (paragraph 36).	Guidance on any departures from the prescribed steps in the process for performance audits will be clarified in the revised manual. The requirement to obtain and document concurrence of the Product Leader will be emphasized in chapter author information sessions.	AAG PPG/ Performance Audit Product Leader