

Office of the Auditor General of Canada

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

Practice Reviews Conducted in the 2009–10 Fiscal Year

May 2010

Practice Review and Internal Audit

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Introduction

1. The Office of the Auditor General (the Office) 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, financial 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 November 2009. This work was done in accordance with the monitoring section of the General Standards of Quality Control for Firms Performing Assurance Engagements of the Canadian Institute of Chartered Accountants (CICA) Handbook. It was also done in accordance with the Practice Review and Internal Audit Plan 2009–10, which was recommended by the Audit Committee and approved by the Auditor General. This plan is based on systematic monitoring of the work of all audit principals in the Office on a cyclical basis.
4. To meet the CICA standards, the Office establishes policies and procedures for its work. These are outlined in an audit manual, various other guidance tools, and a Quality Management System (QMS) for each product line. The QMS for performance audits and supporting audit methodology ensure that quality is built into the audit process. These guide auditors through a set of required steps to ensure that performance 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.
5. This report consolidates the results of the performance audits we reviewed in 2009–10 and summarizes the findings.

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 QMS has been appropriately designed and effectively implemented, and
- the QMS has been appropriately applied so that reports issued are supported and appropriate.

Scope and methodology

7. We conducted practice reviews of eight performance audits over the reporting period—two audits tabled in March 2009 and six tabled between April and November 2009.
8. We stayed abreast of the performance audit practice by reviewing the Performance Audit Manual, the QMS, practice advisories, Office policies, the CICA assurance standards, and other documents relevant to performance audits.
9. Our reviews included an examination of documentation and a review of electronic (TeamMate) and paper audit files. We examined files related to the planning, examination, and reporting of the audits. Our review focused on the most significant approvals, decisions, and reporting matters of the performance audit. We also reviewed the substantiation file, which contains examination evidence most pertinent to audit report content and ensures that observations, conclusions, and recommendations of the audit report flow logically and are well supported. We also interviewed audit team members, quality reviewers, and other internal specialists, as appropriate.

Quality Management System elements and key process controls reviewed

10. We focused our work on selected elements of the Quality Management System for performance audits (Appendix A) that we consider as high risk. These are the following:

- Conduct of the audit
 - Planning
 - Examination
 - Reporting
- Finalization of audit files
- Consultation
- Resourcing
- Independence
- Leadership and supervision
- Security

11. We also looked at how the quality reviewers carried out their responsibilities for quality control. 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 the audit team made and the conclusions reached. The quality reviewer is an important element of the Office's quality control system and is involved in individual audits from initial planning decisions to the closing of the audit file. See Appendix B for a description of the key process controls reviewed for each selected element of the QMS for performance audits.

Rating system

12. For individual performance audits under review, we applied one of the following ratings to each selected element of the QMS:

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

13. After completing the practice reviews, we provided an overall conclusion on whether each performance audit report we examined was supported and appropriate. If multiple elements of the QMS are non-compliant, the audit conclusion is at risk.

Reporting standards

14. This report has been prepared in accordance with the monitoring section of the General Standards of Quality Control for Firms Performing Assurance Engagements of the Canadian Institute of Chartered Accountants (CICA) Handbook. The standards require that information be communicated on monitoring procedures performed, the conclusions drawn from the monitoring procedures, the description of deficiencies, and the actions taken to resolve these deficiencies.

Results of the Reviews

Summary of compliance with the Quality Management System and process control elements

15. We found that, for the eight performance audit files that were reviewed, the reports were supported and appropriate. In addition, they generally complied with the elements of the QMS reviewed and with the CICA standards for assurance engagements. Improvement is needed in the examination and reporting phases of the audits, in file finalization, in independence, in consultation with quality reviewers, and in security.

16. One of the eight performance audit files reviewed was fully compliant on all elements of the QMS reviewed. Another three files reviewed were compliant in all areas of the QMS reviewed but one: independence. This is an improvement compared to the reviews conducted in 2008–09 where all files needed improvement in more than two elements of the QMS reviewed. The other four files reviewed needed improvement in more than one area of the QMS.

17. The 2008–09 practice reviews identified 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 in 2009–10 to update and strengthen the design and implementation of the QMS. This priority is being addressed through initiatives such as major updates of the audit manuals and associated methodology and a review and update of the professional development curriculum.

18. Efforts have been made to address this strategic priority throughout the year and are ongoing. In addition, various workshops were also held with upcoming chapter authors to share best practices and reinforce office policies. Given that the eight performance audits reviewed in 2009–10 were already well under way when the results of the 2008–09 reviews were finalized, we did not expect all of the previous year's observations to be fully addressed in the files reviewed this year.

Strengths and good practices

19. In the course of our practice reviews, we identified the following strengths and good practices.

Involvement of senior management

20. All except one of the eight audit files reviewed demonstrated appropriate and timely involvement of senior management. 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. Compared to last year, this is an area showing improvement in practice.

Consultation

21. All audit files reviewed demonstrated an improvement in documenting the disposition of advice received from internal specialists, advisors, and audited entities.

Period covered by the audit

22. Our 2009 *Report on a Review of the Performance Audit Practice* highlighted that the period covered by the audit was not disclosed in the audit reports as required by assurance standards and Office policy. In all eight files reviewed this year, we noted that the period covered by the audit is now disclosed in the audit reports.

Information-gathering instrument

23. We noted that an audit team adopted an efficient and effective tool for gathering basic documentation. To collect information, entities were asked to respond to an information-gathering instrument developed by the team on systems and practices within the entity. This provided an efficient means of gathering basic information. It further accelerated the report clearance process on the accuracy of basic facts on which observations were based.

Opportunities for improvement

24. The Practice Review and Internal Audit team has seen many examples of good audit work in the files we reviewed in the 2009–10 fiscal year. However, there are still areas that need improvement across the performance audit practice. They are based on the findings most commonly identified in the individual practice reviews.

Use of audit programs

25. Office methodology and assurance standards require developing audit procedures to guide auditors in conducting their audit work.

26. In three out of the eight audit files reviewed, we found an absence of audit programs, incomplete audit programs, or an absence of a summary of findings and conclusions on work performed. In two files, we could not determine if all the audit work planned was carried out, or if significant modifications to the planned audit approach were made during the examination cycle. We also found that there was little description of the work carried out, of the results of the audit procedures, or of the audit conclusions. It was also difficult to determine what key

judgments were made throughout the examination and reporting phases because they had not been documented. In all cases, audit teams had to provide more information to the reviewers and add documentation to the audit files to support their findings.

27. In one audit file reviewed, audit programs were developed but not completed and linked to the audit work performed. While reports were substantiated, without assistance from the audit team, the reviewers could not determine whether sufficient and appropriate evidence had been gathered in the conduct of the audit and why work originally planned was not completed.

28. This observation was brought to the attention of the Performance Audit Product Leader and of the Assistant Auditor General of the Professional Practices Group early during the 2009–10 practice review cycle. In March 2010, a practice advisory was issued that now requires audit teams to have audit programs for their audits. A workshop on audit programs was also offered to selected practitioners for performance audits that will be reported in 2010 and beyond.

Documentation

29. In addition to being complete, accurate, and clear, audit files and working papers containing the evidence need to be structured in a logical way to provide for ready access to the audit evidence. In three of the eight audit files reviewed, we found that not all working papers pertinent to the audit were stored in the audit files. As noted last year, some of the audit evidence was stored outside the audit file in emails or in other paper or electronic folders or files. Audit teams had to provide further evidence to the practice review teams to support compliance with standards.

30. We did see, however, in the eight files reviewed, an overall improvement in the structure of the audit files. Generally, files were better structured, and it was easier to find the working papers associated with the work done, the evidence of review by various parties consulted, and the key decisions made throughout the audit.

31. Auditors have made an effort to use the TeamMate electronic tool to document their work and are becoming more familiar with it. All files reviewed used TeamMate to varying degrees. Files structure is still inconsistent, but overall, using a documentation protocol helped teams organize their files. Significant updates to TeamMate, including the streamlining of audit procedures and updates to the performance audit methodology introduced in March 2010, will continue to contribute to better documentation of audit files.

32. Finally, we noted again this year that some team members, including quality reviewers, are still not accessing the TeamMate file. It is important that all team members access the audit file to document their work and to review the audit work performed.

Quality reviewers

33. Quality review is an important element of quality assurance within the Office. Current practice is to appoint a quality reviewer for every performance audit. Compared to the results of last year's practice reviews, in the eight audit files reviewed in 2009–10, we found improvement in the timeliness of the reviews, comments provided to audit teams, and how the teams addressed the comments.

34. However, there are still inconsistencies in how the quality reviewers conduct their reviews. The nature and extent of quality reviewers' work vary considerably from one file to another.

35. In two files, the quality reviewers did not notice that more work was needed from the audit team to complete the audit programs and audit files. As noted in previous years, five of the eight files reviewed still did not fully meet the requirements of the assurance standards and Office policy.

36. Moreover, for three files, audit teams had to adjust the audit evidence or had to carry out additional audit procedures in order to have appropriate and sufficient documentation on the areas selected for detailed review by quality reviewers. However, in light of the nature of the comments of the quality reviewers and additional work to be performed by audit teams, we noted that neither the quality reviewers nor practitioners questioned whether the observations the quality reviewers made were applicable to the rest of the audit file.

Extent of review

37. Assurance standards require that working papers are reviewed and that the review responsibilities are determined on the basis that more experienced team members review the work performed by less experienced team members. This helps determine, among other things, that the evidence obtained is sufficient and appropriate to support the audit report and that adequate supervision and review throughout the audit was performed.

38. In three of the eight audit files reviewed, there was a lack of evidence that working papers were reviewed on a timely basis. In two files, we observed that many electronic working papers had been signed off or reviewed in bulk toward the end of the audit rather than throughout the audit process. Moreover, we noted that the documentation on file was insufficient to determine the extent of the review of the audit work being conducted and completed. In four files, we again observed this year that some working papers were prepared and reviewed by the same person.

39. We have noted that in March 2010, the Office reactivated the separate preparer/reviewer functionality in TeamMate. This will help ensure that more experienced team members review the work performed by less experienced members and comply with assurance standards.

Change in audit objectives and scope of work to be performed

40. Although the audits reviewed concluded on the reported audit objectives and criteria, in two audit files reviewed, we found changes to the audit objectives communicated to the audit entity. In one of these two files, the reasons for the changes were not found on file, nor was there evidence that the relevant internal specialists and quality reviewer were informed of the change.

41. We further noted in the same two files that examination plans or audit programs have not been updated to reflect the changes to the audit criteria and objectives. In one case, the audited entities were informed of the revised criteria and objectives at the time of the draft audit report. In our view, this poses a risk to the Office should a disagreement with management occur about the criteria and objective of the audit. In addition, unnecessary or incomplete audit work could result from a change in criteria if the audit program or examination plan is not adjusted.

File finalization

42. Office policy on finalizing audit files requires that performance audit files be completed 45 days after the date the report is released. Until July 2009, this date was defined as the date when the final approval form was signed. Subsequent to that date, the report release date was changed to the date that the report is tabled in Parliament.

43. Of the eight performance audit files reviewed, three files were kept opened after the finalization policy date. Documentation supporting the reasons for keeping the files opened was lacking. Where there was documentation, it was not in accordance with Office policy. We noted, however, that all four files from the November 2009 report were closed by the deadline. This is an improvement compared to last year.

Independence

44. Assurance standards require that auditors be independent of the entity they are auditing. Accordingly, threats to independence and safeguards used to reduce such threats to an acceptable level must be assessed and documented. The Office has specific policies and procedures designed to avoid independence concerns. Notably, each individual involved in the audit is required to complete a declaration of independence form for each assurance engagement they are assigned to.

45. In three audit files reviewed, not all audit team members had completed an independence form. In one other file, we found that the exceptions forms were stored in the audit file while they should have been in the personal employee file in the Human Resources Department. Moreover, in five audit files reviewed, we did not find completed declaration of independence forms for external advisors or consultants.

46. When the audits were conducted, the Office policy did not require that all individuals, who were advising the engagement team on the conduct of the audit, complete a declaration of independence form. A revised practice advisory issued in December 2009 clarified that all individuals involved in reviewing the audit work or advising engagement team members on the conduct of their work (for example, quality reviewer, internal advisor, advisory committee member, internal specialists) are expected to assess, document, and address threats to independence at the beginning of every assurance engagement by completing an independence form.

Other observations noted in our reviews

47. Secondary evidence. The Office guidance on secondary evidence states that secondary data or evidence can only be used if in some measure its relevancy, reliability, and validity can be factually demonstrated. In two audit files reviewed, the secondary evidence obtained from third parties provided in the report was not appropriately substantiated and documented.

48. Security. The Office Policy on Control Procedures for the External Circulation of Performance Audit Documents requires that a controlled document register be maintained, that controlled documents distributed be returned within a week of the report tabling, and that the Office's Departmental Security Officer be advised of any controlled documents that have not been returned within a week.

49. In all audit files reviewed, we observed that controlled documents were not returned within the required one-week period. Moreover in two audit files, documentation to verify recovery of controlled documents was missing from files or had not been accurately updated. All audit teams reviewed were, however, actively following up on outstanding controlled documents. This is an improvement compared to the last practice review cycle.

Follow-up of Management Actions on Recommendations of Previous Practice Reviews

50. As indicated earlier, management made it a strategic priority in the 2009–10 fiscal year to update and strengthen the design and implementation of the Quality Management System. In response to significant changes in international and Canadian auditing standards, findings of internal practice reviews, and feedback received from practitioners, the Office has identified the

need to renew its audit methodology for the three product lines: annual audit, performance audit, and special examination. This initiative, Renewal of Audit Methodology (RAM), has many components including a change management component to ensure an effective transition. A separate project dealing with the review of the Office's overall training strategy is also under way.

51. The Office has informed us that many outstanding recommendations made in previous practice review reports will now be addressed as part of RAM, the training strategy, and other initiatives. We will continue to monitor how management considers recommendations made in previous years in these projects.

Conclusion and Recommendations

52. We conclude that the eight performance audit reports were supported and appropriate. Furthermore, based on the eight performance audit reports reviewed, our cumulative knowledge, and the follow-up on management actions taken on recommendations from previous years, we conclude that for the elements of the Quality Management System (QMS) we reviewed, the design is appropriate. However, implementation of the QMS still needs improvement.

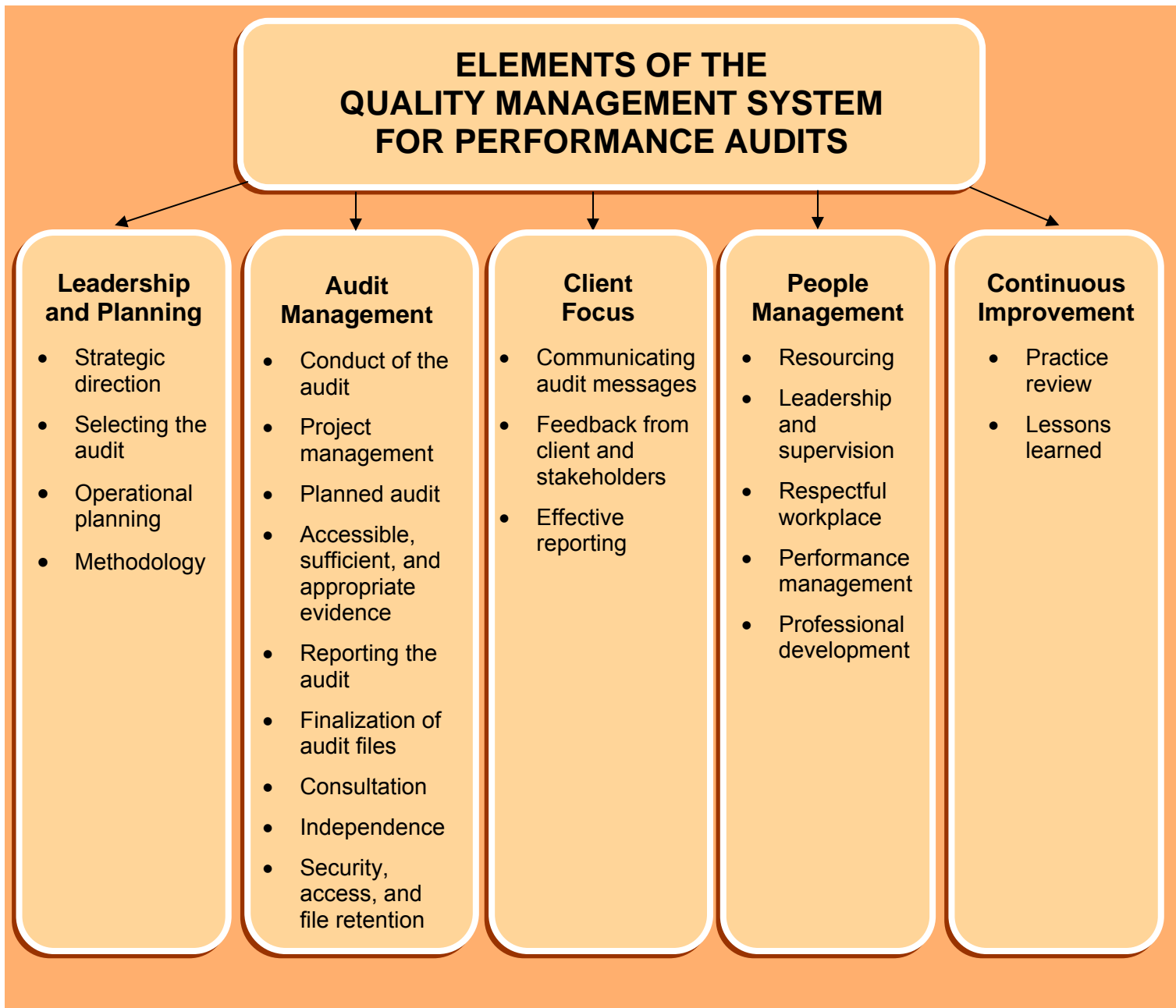
53. We discussed our observations and recommendations with management, who agreed with the recommendations.

54. Recommendations. The Office should

- prepare an action plan to address the observations raised in the report;
- consider the observations noted in the report when reviewing the training approach and curriculum—specifically, training should be offered on the role, nature, and extent of the quality reviewer's work; and
- review its Policy on Control Procedures for External Circulation of Performance Audit Documents.

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

Appendix A—Quality Management System for Performance Audits



Appendix B—Quality Management System Elements and Process Controls Reviewed

Our review covers the following Quality Management System elements.

Conduct of the audit—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.

Conduct of the audit—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 the report. We reviewed the report for secondary evidence information and reached a conclusion on the adequacy of the team's rationale for including such information.

Conduct of the audit—Reporting. We reviewed the 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 Report 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 the 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, in particular 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.

Resourcing. Based on interviews with staff and a 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 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 the audit, including specialists, were 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;
- all team members were encouraged to perform to their potential; and
- all received appropriate recognition.

Security. We determined whether the audit teams followed appropriate procedures to ensure confidentiality and appropriate access to sensitive information. More specifically, we checked if the audit teams took protective measures in regard to classified information and adequately controlled the external circulation of draft versions of the performance audit plan and report.

Our review covers the following key process controls.

Review by the quality reviewer. We determined whether the quality reviewer carried out, in a timely manner, an objective evaluation of the significant judgments made by the team; the conclusions reached in supporting the report; and other significant matters that came to the attention of the quality reviewer during his or her review.

Documentation. We determined whether the work of the quality reviewer was adequately documented.

Subsequent actions. We determined whether the audit team took appropriate and timely action in response to the advice received from the quality reviewer.

Appendix C—Management Response to the 2010 Report on a Review of the Performance Audit Practice

Introduction

For the eight performance audit reports reviewed and based on cumulative knowledge and the follow-up on management actions taken on recommendations from previous years, Practice Review concluded that for the elements of the Quality Management System (QMS) reviewed, the design is appropriate. However, implementation of the QMS needs improvement. The eight performance audit reports were supported and appropriate.

This document provides management's response to the practice review recommendations and observations that have been made as well as its associated action plan. The action plan also identifies responsibility for implementing the planned actions and timelines for completion.

The following key overarching elements apply to all parts of our practice review action plan.

- 1. Renewal of Audit Methodology (RAM) project.** This project includes revising and updating our audit methodology, including adopting the recommendations from the performance audit streamlining project. The RAM project also includes revising and updating related audit tools, checklists, and training and developing a change management component to ensure that our methodology is put into practice.
- 2. Involvement of senior management.** It is crucial that senior managers are involved, in a timely and appropriate manner, in all phases of the audit, key judgements, and key conclusions resulting from the audit work.
- 3. Monitoring of the action plan.** Individual projects within the action plan are themselves being monitored through existing mechanisms (for example, a steering committee regularly meets to oversee the RAM project). The Office's Executive Committee will also monitor progress and ensure that audit methodology is fully complied with in practice. Success in addressing the issues raised in the Report will also be monitored by the ongoing practice review program.

Responses and Action Plan

Practice Review observations	OAG response and planned actions	Responsibility
<p>Recommendation:</p> <p>The Office should prepare an action plan to address the observations raised in the report.</p>	<p>Agreed.</p> <p>The following actions will address the observations:</p> <ul style="list-style-type: none"> • The Renewal of Audit Methodology (RAM) project will involve revising and updating our audit methodology, including adopting the recommendations from the performance audit streamlining project. The RAM project also includes revising and updating related audit tools, checklists, and training as well as developing a change management component to ensure that our methodology is put into practice. • In the interim, we will remind auditors through, as appropriate, workshops for chapter authors, audit training, the September 2010 staff update sessions, and other fora to address the following issues related to implementing existing methodology (significant actions already under way are noted below): <ul style="list-style-type: none"> • Use of audit programs—interim action taken is reflected in the report documentation. (paragraphs 25–28) • Documentation. (paragraphs 29–32) • Quality reviewers—A workshop is planned for June to provide guidance to all quality reviewers for the November 2010 and April 2011 reports. The Assistant Auditor General, Professional Practices Group (AAG-PPG) is developing a tool to provide guidance for quality reviewers in all product 	<p>Product Leader¹/AAG, Professional Practices Group/all AAGs</p>

¹ The Office has appointed assistant auditors general as product leaders for each of its audit practice lines. The primary functions of a Product Leader are to provide leadership for the audit practice line, provide oversight for the audit practice line, and contribute to the quality of individual audits.

Practice Review observations	OAG response and planned actions	Responsibility
	<p>lines, which will be available in December 2010. (paragraphs 33–36)</p> <ul style="list-style-type: none"> • Extent of review. (paragraphs 37–39) • Change in audit objectives and scope of work to be performed. (paragraphs 40–41) • File finalization—an automatic file closure process is now in place, which will prevent further instances of office policy on file finalization not being followed. (paragraphs 42–43) • Independence. (paragraphs 44–46) • Secondary evidence. (paragraph 47) • Security. (paragraph 48) 	
<p>Recommendation:</p> <p>The Office should consider the observations noted in the report when reviewing the training approach and curriculum. More specifically, training should be offered on the role, nature and extent of the quality reviewer's work.</p>	<p>Agreed.</p> <p>For 2010–11, management has identified four priorities for audit training: Canadian Auditing Standards, International Financial Reporting Standards, Quality Reviewer, and AAG Milestone training. There will be no other significant training initiatives put in place during this time. In March 2010, the Office approved a Strategic Training Approach to implement a vision that by September of 2012, the Office will have a curriculum and training plan in full operation for all three product lines that reflects new standards and updated methodologies. All practice review recommendations relating to training will be inputs to the development of this curriculum and training plan.</p>	<p>Product Leader/AAG, Professional Practices Group</p>

Practice Review observations	OAG response and planned actions	Responsibility
Recommendation: The Office should review its Policy on Control Procedures for External Circulation of Performance Audit Documents.	Agreed. For the Fall of 2010, in time for the distribution of PX drafts for the April 2011 report and Entity Plan Summaries for the November 2011 report, we will review the policy. In particular, we will examine the list of documents requiring control procedures and reconsider the one-week timeline in the current policy.	Product Leader/ Departmental Security Officer