audit office OF NEW SOUTH WALES

2024–2026 Finance Strategy

INSIGHTS FOR BETTER GOVERNMENT

contents

1. Who we are and what we do **1**

2. The need for a finance strategy **1**

3. Our overarching financial objective **2**

4. Our financial resources **2**

5. Measures of being fiscally responsible and financially sustainable **3**

5.1 Being fiscally responsible 3

5.2 Being efficient 3

5.3 Remaining financially sustainable 3

6. Source of funding **4**

6.1 Sources of Revenue 4

6.2 Major categories of expenditure 6

7. How we govern our finances **6**

7.1 Establishment of a Finance and Performance Committee 6

7.2 Robust annual budgeting process 7

7.3 Liquidity Management 7

7.4 Debtor Management 7

7.5 Risk Management 7

7.6 Internal controls certification 7

7.7 Benchmarking our organisation and audit fees 7

8. How we deliver our financial audits **7**

9. How we are held to account **8**

10. Roles and responsibilities **8**

10.1 Office Executive 8

10.2 Audit and Risk Committee 8

10.3 Finance and Performance Committee 9

Appendix one – Significant factors that impact our audit fees **10**

1. Who we are and what we do

The Audit Office of New South Wales is a statutory authority, established under the *Government Sector Audit Act 1983*, that conducts audits for the Auditor-General for New South Wales (the Auditor-General).

The Auditor-General reports to the New South Wales Parliament and is responsible for audits and related services. These audits aim to help Parliament hold government accountable for its use of public resources.

The Audit Office conducts financial and performance audits, principally under the *Government Sector Audit Act 1983* (GSA Act) and the *Local Government Act 1993* (LG Act) and examines allegations of serious and substantial waste of public money under the *Public Interest Disclosures Act 2022*. The Auditor-General can also be requested by the Treasurer, a minister or both Houses of Parliament to perform audit or audit-related services. These can include audits of agencies' compliance with specific legislation, directions, and regulations.

2. The need for a finance strategy

The Audit Office's 2024–2026 Finance Strategy outlines the parameters and principles for how we govern our finances and set our financial audit fees. It provides a framework to ensure the decisions we make support our corporate plan objectives, that our long-term financial sustainability remains intact, that we operate efficiently and that we are always fiscally responsible.

Like all organisations, the Audit Office has finite resources in delivering its legislative mandate and fulfilling its strategic objectives. Our operating model is premised on providing value for money services that pay their way and supporting investment in contemporary tools and methodologies. This means the finite resources need to be managed in an effective and efficient way, and that we make resourcing decisions that are prudent and economical.

The Audit Office is largely self-funded from financial audit fees paid by auditees. These fees are set to cover our planned expenses and future investment, while maximising value. In delivering its mandate, the Audit Office upholds the highest standard in the conduct of its audits and being compliant with professional requirements.

The Audit Office's credibility, and the trust and confidence people have in us, is contingent on the quality of the work we do and our independence and objectivity. While audit quality is paramount in what we do, we also constantly look for ways to make our audits more effective and efficient, and to maximise value to the Parliament and auditees.

The key objectives of the Finance Strategy are to:

- promote robust and effective financial management of available resources
- provide direction and context for decision making in the allocation, management, and use of the Audit Office's financial resources as efficiently and effectively as possible, and with economy
- ensure financial stability and sustainability
- promote transparency with external stakeholders on how we govern our finances and how we set audit fees for audit engagements
- promote effective financial risk management.

3. Our overarching financial objective

The Audit Office's overarching financial objective is to remain financial sustainable, be efficient and always be fiscally responsible. To achieve this objective, our financial management practices are governed by:

- the 2024–2026 Finance Strategy
- the operation of a Finance and Performance sub-committee of the Office Executive to monitor the financial health of the organisation and to provide advice to the Office Executive and Auditor-General
- a comprehensive suite of internal financial management policies
- risk management practices, effective audit functions, ongoing financial management capability investment, and the design, implementation, and operating effectiveness of internal controls
- key measures of our financial performance and position (see further below).

4. Our financial resources

The Audit Office is an organisation that operates with a net asset base of around $15 million to $20 million at any one time. Being a largely self-funded organisation, including self-funding our capital investment, it is important that we have a sound net asset position. It is also important we maintain an appropriate level of liquidity, to fund today's operating costs and future investment in capital. Key highlights from our balance sheet are summarised below.

Total assets at 30 June 2024: $45 million

Cash at bank
$12.7 million

Right of use asset (lease)
$8.1 million

Other current assets
$9.9 million

Debtors
$9.2 million

Other non-current assets (including plant and equipment)
$5.4 million

Total liabilities at 30 June 2024: $28 million

Provisions (mainly employee entitlements)
$15.4 million

Borrowings (lease liability)
$9.5 million

Payables
$3.0 million

5. Measures of being fiscally responsible and financially sustainable

The Audit Office's overarching financial objective is to remain financial sustainable, be efficient and always be fiscally responsible. We have developed a series of metrics to measure our success against this objective. We report our performance against these metrics regularly to the Finance and Performance Committee and the Office Executive.

5.1 Being fiscally responsible

- Compliance with the *Government Sector Finance Act 2018*
- Compliance with Treasurer's Directions and applicable central government directives
- Unmodified Independent Auditor's Report on the Audit Office's annual financial statements
- Procurement practices consistent with the NSW Procurement Framework
- Operating within the approved annual operating and capital budget
- Operating within agreed expenditure control limits
- Robust financial management practices
- Timely implementation of internal and external audit recommendations.

5.2 Being efficient

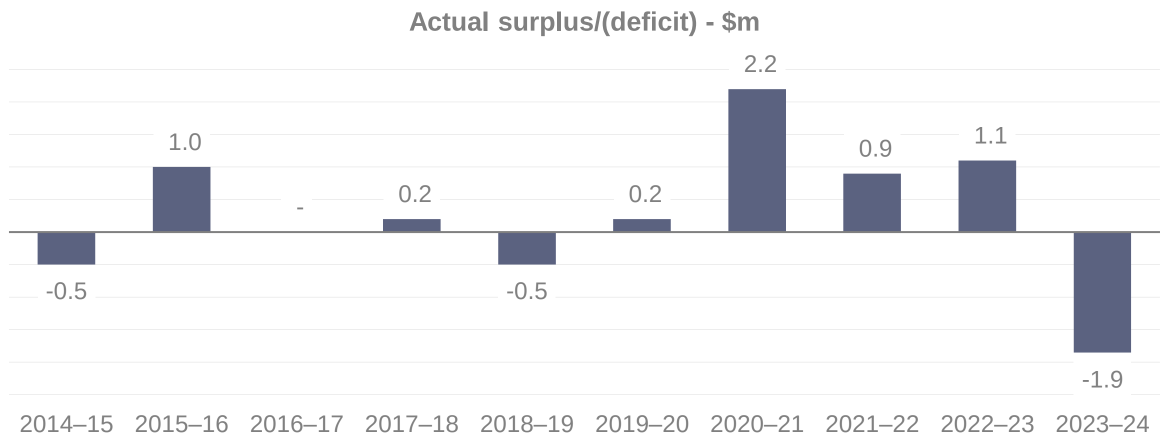
- Completion of financial audits within statutory deadlines
- Annual audit fee increases (excluding scope variations) consistent with the Consumer Price Index (Sydney) at the time of setting the annual budget
- Achieve or exceed annual utilisation target set for audit staff
- Average hourly cost commensurate (in relative terms) with other Australian audit offices
- The cost of in-house audits (in relative terms) is commensurate with similar audits resourced with an Audit Service Provider (ASP) under our financial audit commissioning model.

5.3 Remaining financially sustainable

- To at least break even over the medium term
- Positive net cash inflows from operating activities
- Net assets > $15 million
- Current ratio of at least 1.5
- Working capital > 10 weeks.

5.3.1 To at least break even over the medium term

Unlike professional services firms, the Audit Office does not set its audit fees to achieve large profits. This is demonstrated by our historical financial performance in the chart below.



From year to year there has been fluctuation in the actual surplus or deficit because of the timing of large capital investments, or the timing and/or spend on large corporate plan initiatives. But over the medium term we have generally broken even over the medium term.

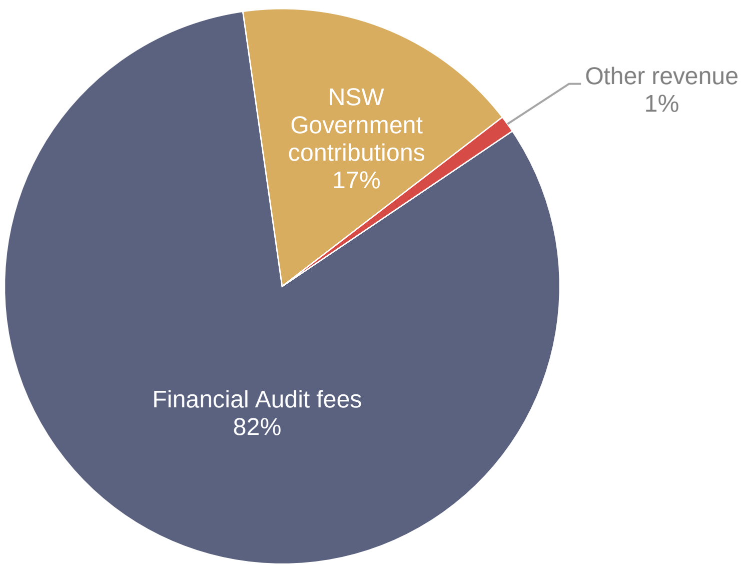
To remain relevant and deliver effective audits, the Audit Office needs to have the financial capacity to tap into innovation and new ways of working without jeopardising its financial sustainability. It is for this reason that aiming to at least breaking even over the medium term is an appropriate financial objective. This gives us the flexibility to budget for small surpluses where we deem it necessary so that we have the capacity to fund future investment in small scale new ways of working, responding to new and emerging technologies, and changing stakeholder needs.

6. Source of funding

6.1 Sources of Revenue

The chart below shows the Audit Office’s actual revenue for 2023–24. The Audit Office has two main revenue streams; revenue earned from conducting financial audits and a NSW Government contribution to fund the performance audit mandate and the reporting of financial audit results to parliament through the Auditor-General’s Report to Parliament. The Audit Office also earns some minor other revenue from other sources such as secondments and interest income.

Revenue dissection at 30 June 2024



1. Financial Audit fees

The Audit Office generally conducts over 500 financial audits each year. This includes financial audits of state, university, and local government entities. The cost of conducting financial audits is paid by the entities, whom we refer to as 'auditees'. This revenue is our main source of income.

Under the GSA and LG Acts, the Audit Office is entitled to recover the cost of an audit from the auditee. Financial audit fees are determined based on the relative size, nature, risks and complexity of an audit. These factors inform decisions around the most optimal team (resource) mix and the estimated hours required to complete the audit. Approved hourly charge-out rates for each role in the audit team are then applied to the estimated hours to calculate the estimated audit fee.

The hourly charge-out rates we set are based on the average 'direct' costs (such as auditor salaries) of each role, and 'indirect support' costs (such as technology infrastructure and software support, training and development expenses, office rental expenses and utilities, the investment in capital items and new ways of working, accounting and audit technical support and corporate support). Charge out rates are set to cover the costs of operating the Audit Office and to ensure we at least break even over the medium term.

Factors that can impact the year-on-year change in audit fees include

1. **Changes in employee salaries** – salaries (and related on-costs) paid to our staff makes up over 65 per cent of the Audit Office's annual operating costs. Staff employed at the Audit Office are covered by either the Audit Office Award or executive contracts. The Audit Office competes with other professional services firm for audit staff, which at times can put upward pressure on salary costs.
2. **Annual escalation of Audit Service Provider (ASP) costs** – under its financial audit commissioning model, the Audit Office resources a percentage of its financial audits to ASPs. This includes large professional services firms, mid-tier firms, and smaller metropolitan and regional audit firms. These arrangements are subject to annual fee escalation. ASPs are generally appointed through a competitive, open tender process to ensure we get maximum value for money.
3. **Audit scope changes** – the scope of a financial audit can change from year to year for any number of reasons. This includes the implementation of a new accounting system, the existence of one-off significant, non-routine accounting transactions (such as a major asset revaluation or significant asset acquisition/disposals), internal control deficiencies detected during the audit that requires us to conduct additional audit procedures to form an opinion on the financial statements, and auditees not meeting key deliverables outlined in the Annual Engagement Plan (such as appropriate and timely information). Scope changes are discussed with auditees before the Audit Office amends the estimated audit fee.
4. **Changes in auditing and/or accounting standards** – from time to time, the auditing and accounting standard setters introduce new or revised standards. Where there are new or revised complex accounting standards that are being implemented, the audit fee may increase to accommodate for the additional effort required to assess management's implementation of the changes. Equally, the introduction of new or revised auditing standards can increase the amount of effort required to comply with the professional requirements and this will result in a higher audit fee. We are transparent about these changes and communicate the potential impact in the Annual Engagement Plan, which is issued at the beginning of each audit.

Refer to Appendix 1 for further information factors that impact the pricing of financial audits.

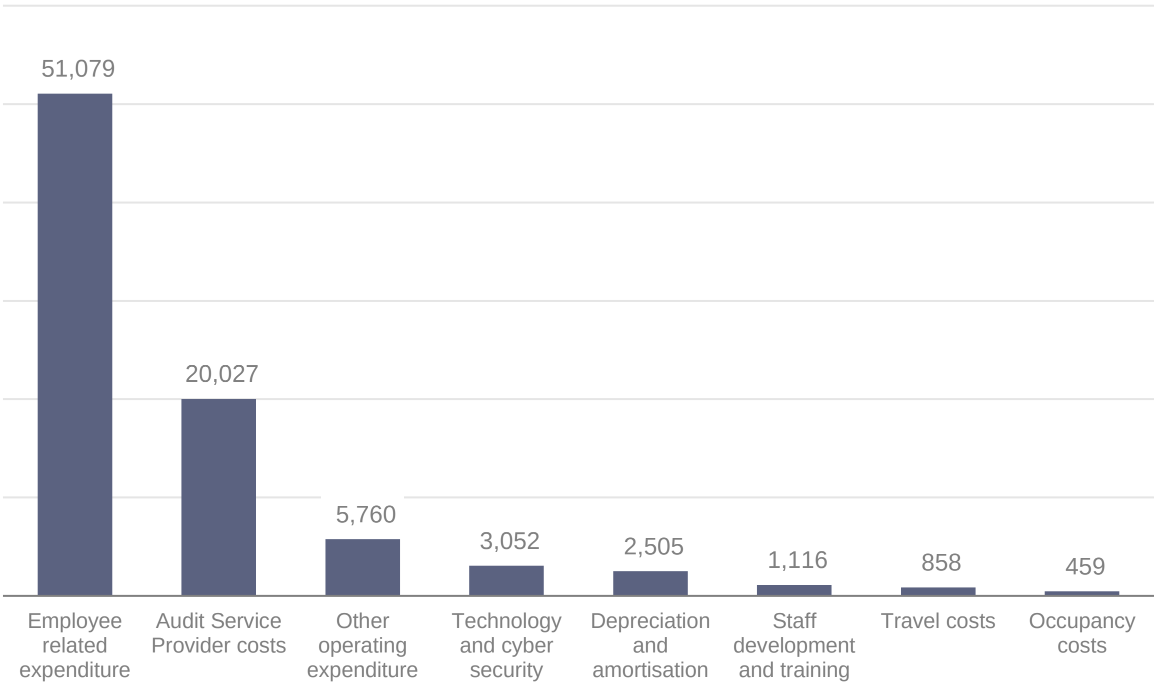
2. NSW Government contribution

The performance audits conducted by the Audit Office are fully funded by the NSW Government through an annual government contribution. This means that auditees do not pay for this audit activity.

The NSW Government also funds the cost of preparing the Auditor-General's Reports to Parliament that report the findings from our financial audits. Similar to our performance audits, auditees do not pay for this statutory reporting function.

6.2 Major categories of expenditure

The chart below shows the Audit Office's actual expenditure for 2023–24.



Operational and capital expenditure help support the operations of the Audit Office and the delivery of corporate initiatives. Our investment in people and operations is guided by our corporate plan and strategic objectives, strategic and operational risks and ensuring compliance with professional requirements and central agency directives.

7. How we govern our finances

We recognise that being fiscally responsible, being efficient and financially sustainable requires sound governance structures, investment in people, process, and technology, and through regular and timely monitoring and reporting. Below is a little bit more detail on how govern our finances.

7.1 Establishment of a Finance and Performance Committee

We have established a Finance and Performance Committee that is a sub-committee of our Office Executive. The committee meets monthly and amongst its responsibilities it:

- ensures the Audit Office has a robust financial management framework, including the annual budget cycle, monitoring, and reporting of financial performance, and forecasting
- ensures the budget allocation process aligns with the strategic priorities in the Audit Office's Corporate Plan, strategic and operational risks, and other relevant branch/operational plans and roadmaps
- recommends strategies for managing fiscal pressures over the budget and forward estimates period
- monitors the monthly financial performance and position of the Audit Office.

7.2 Robust annual budgeting process

The Audit Office's annual budgeting process is comprehensive, and it promotes effective resource allocation, with a strong focus on Audit Office's outcomes (as reflected in its corporate plan) and active mitigation of strategic and operational risks. The process is built around maintaining high levels of accountability for the way resources are deployed. The Audit Office puts a strong emphasis on outcomes when making budget decisions and large investments are typically supported by a business case or project brief, as defined by our project management framework.

7.3 Liquidity Management

The Audit Office has a cash management process that constantly monitors and reports on liquidity in the short and long term to ensure employees and suppliers are paid on time.

7.4 Debtor Management

Effective debtor management is crucial to remain financially sustainable. We invoice auditees for work performed on a regular basis throughout an audit engagement, and our payment terms are 14 days. We have defined debt recovery procedures, which includes different escalation points, to ensure timely settlement of invoices.

7.5 Risk Management

Strategic and operational risks are monitored and reported in accordance with the Office's Risk Management Framework. Risks are regularly reviewed and updated to reflect changes in the internal and external environment.

7.6 Internal controls certification

Each year, the designated Chief Financial Officer provides an internal controls certification to the Auditor-General. This certification, which attests to having an effective system of internal control over financial information, is a core NSW Treasury requirement.

7.7 Benchmarking our organisation and audit fees

Each year the Audit Office participates in a benchmarking exercise with other audit offices in Australia, known as the Australasian Council of Auditors-General (ACAG) Macro Benchmarking. This exercise, facilitated by an independent third party, provides us with an opportunity to measure the efficiency of our operations. Some of the measures we benchmark ourselves against include: the cost of providing audits relative to total public sector assets/transactions; the average number of audit hours delivered by an auditor; the average cost of producing each audit hour; staff mix on audits; and the level of investment in corporate support.

In addition to comparing our efficiency with other jurisdictions, we also periodically analyse our financial audit fees against fees charged by our ASPs for similar audits. We also compare our fees against fees submitted by tenderers when resourcing audits with an ASP.

8. How we deliver our financial audits

The Audit Office delivers its financial audits through a mix of in-house audits and audits resourced with an ASP. In deciding how we should resource our audits, our commissioning model is premised on the objectives that:

- ensure the Audit Office maintains its recognised expertise as the trusted auditor across the NSW public sector
- uphold the highest level of integrity, independence and quality in the delivery of public sector financial audits for the NSW Parliament.

ASPs are generally appointed through an open tender process to maximise value for money. ASPs are generally appointed for a three-year term, with an option to extend for up to a further two years. The option is solely at the discretion of the Audit Office.

Resourcing financial audits with an ASP gives the Audit Office the opportunity to compare its audit processes, audit quality and audit fees. It also helps the Audit Office deliver audits within the statutory deadlines and it gives us the opportunity to learn and share knowledge with private sector firms.

9. How we are held to account

Under s48A of the *Government Sector Audit Act 1983* (the Act), a review of the Audit Office is to be conducted every four years. The review is commissioned by the Public Accounts Committee of the NSW Parliament. The Committee examines the auditing practices and standards of the Auditor-General, and to determine whether the Auditor-General is complying with those practices and standards in the carrying out of their functions under the Act.

The reviews conducted by the Committee, amongst other things, look at the Audit Office's effectiveness, efficiency, and value for money. The reviews are an important source of public accountability for the work we do. For copies of the quadrennial reviews commissioned by the Public Accounts Committee, refer to Parliament of NSW.

We recognise the importance of holding ourselves to account when it comes to being fiscally responsible, financially sustainable and operating efficiently. We regularly report our performance against key metrics in this strategy to the Finance and Performance Committee and Office Executive.

In addition to our internal reporting, we believe it is important in being transparent with our external stakeholders. We do this through the Audit Office's annual report. The annual report includes not only our performance against budget, but also how we perform against other audit offices and how we have performed over an extended period.

10. Roles and responsibilities

10.1 Office Executive

The Office Executive of the Audit Office is committed to high standards of performance, accountability, ethical behaviour, and corporate governance.

The *Government Sector Audit Act 1983* establishes the position and functions of the Auditor-General for New South Wales. The Auditor-General has a range of statutory responsibilities for the governance of the Audit Office.

The Office Executive assists the Auditor-General to meet their statutory responsibilities and provides leadership to the Audit Office in pursuing its strategic direction and delivering against the Corporate Plan. The Office Executive is ultimately responsible for overseeing the Audit Office's financial performance and sustainability.

10.2 Audit and Risk Committee

The Auditor-General has established an Audit and Risk Committee for the Audit Office, in accordance with NSW Treasury's Internal Audit and Risk Management Policy for the General Government Sector (TPP 20-08). The committee is directly responsible and accountable to the Auditor-General for the exercise of its responsibilities. Its responsibilities include risk management, external accountability, compliance and ethics, internal audit, and external audit.

10.3 Finance and Performance Committee

The Finance and Performance Committee is a sub-committee of the Office Executive. The Committee's primary objective is to provide advice to the Office Executive and the Auditor-General relating to the strategic financial direction and financial sustainability of the Office. The Committee's responsibilities include, but are not limited to:

- ensuring the Office has a robust financial management framework, including the annual budget cycle, monitoring, and reporting of financial performance, and forecasting
- ensuring the budget allocation process aligns with the strategic priorities in the Office's Corporate Plan and other relevant branch/operational plans
- recommending strategies for managing fiscal pressures over the budget and forward estimates period
- considering and recommending to the Office Executive proposals to re-allocate funding between proposals and to re-allocate funding between branches.

Appendix one – Significant factors that impact our audit fees

Many factors can impact the financial audit fee we charge for the work we do. The table below identifies the more significant factors that can impact the audit fee. There will always be factors that are more significant for particular auditees, or -auditee specific factors that also need to be considered. The significant factors that impact the audit fee include:

Factor	Impact on audit fee/effort
What is the overall engagement risk?	Engagement risk is, broadly speaking, the risk of our exposure to financial loss and damage to our professional reputation. We have a low tolerance for audits that are not defensible resulting in lost credibility, trust and confidence by government and the public. Engagements with higher engagement risk generally require more time by senior team members, and more time overall responding to the higher risk.
Does the entity have a strong governance and internal control environment?	Strong governance and internal control environments allow us to place more reliance on these elements as part of our engagement approach. Placing more reliance on these elements generally reduces the time we spend on testing transactions and balances in the financial statements.
Does the entity have a history of misstatements?	If an entity has a history of misstatements, unless we can assess otherwise, we have to assume a similar level of misstatements will occur in the future. The more misstatements we expect overall will generally increase the amount of work we have to do. A greater number of misstatements also generally requires more time to assess the impact of the misstatements in the financial statements, and to discuss the misstatements with management.
Does the entity have a strong focus on reliable financial reporting and respond quickly (and accurately) to our requests for information?	A strong focus on reliable financial reporting and responsiveness to our requests for information will generally reduce the time spent on the engagement. A strong focus generally means management provide timely and accurate information in response to our requests – reducing the time spent following up information that was previously requested or requesting more accurate information where the information originally provided was incomplete or not accurate.
Is the entity experiencing significant change in its operations?	An entity experiencing significant changes in its operations generally requires more involvement of senior team members, and more time overall reviewing the financial reporting impact. This involves assessing the appropriateness of the accounting treatment through our engagement procedures.
Does the entity have complex computer processing environments that impact the engagement?	Complex computer processing (IT) environments generally require involvement by Information Systems audit specialists. They specialise in reviewing complex IT environments to ensure we can rely on the systems as part of our engagement approach. Less complex IT environments will generally require less time spent by our audit specialists in reviewing the structure of the environments and the controls implemented to support reliable processing of information.
Does the engagement include a large number of revenue, expense, asset, and liability streams?	The larger number of revenue, expense, asset, and liability streams an entity has will generally increase the time spent on the engagement. This time is required to understand and assess the controls within each of the significant streams, perform engagement procedures to test the streams, and evaluate any issues identified through our procedures.
Does the entity operate financially significant components that require a decentralised engagement approach?	Having centralised financial reporting responsibilities generally reduces the time spent on the engagement. With decentralised responsibilities, time is required to understand the extent of decentralisation, assess the controls in place at the significant components (sites), perform engagement procedures to test the sites, and evaluate any issues identified through our procedures.

Factor	Impact on audit fee/effort
Does the entity have shared services (outsourcing) arrangements?	Shared services (outsourcing) arrangements can have a range of impacts depending on the nature and extent of the arrangements. Key factors include: • the complexity of arrangements with the shared service provider • the pervasiveness of outsourced functions affecting the entity's financial reporting • whether the shared service provider receives an independent audit report over the design, implementation, and operating effectiveness of its internal controls • the nature and extent of issues identified in the shared service provider's controls • the nature, extent, and significance of procedures and controls the entity is required to implement to support the shared service provider's controls.
Does the engagement contain significant accounting estimates or judgements?	Significant accounting estimates and judgements generally require involvement by senior team members to review the financial reporting impact. Estimates and judgements are, by their nature, at greater risk of fraud and error. Senior team members use their experience to assess the appropriateness of management's estimates and judgements against accounting standards, relevant laws and regulations, and other authoritative pronouncements (such as those issued by The Treasury). The impact on audit effort can vary significantly from one year to the next. For example, a desktop asset indexation or annual assessment of fair value requires less time spent on the engagement compared to a full asset revaluation.
Does the engagement contain complex accounting transactions?	Complex accounting transactions generally require more involvement of senior team members, and more time overall reviewing the financial reporting impact. More senior team members use their experience to understand and assess the appropriateness of the accounting transactions, design engagement procedures to validate key aspects of the transactions and evaluate any issues arising from our procedures. The complex nature of these accounting transactions may also require involvement of technical experts (below).
Does the engagement contain balances that require technical expert involvement (tax, superannuation, financial instruments)?	Significant accounts that are subject to technical expert involvement will generally require involvement of senior team members to review the financial reporting impact. We may use our own technical experts (or engage external experts) to review the appropriateness/reasonableness of any methodologies, inputs, assumptions, or judgements used.
Does the entity form part of a group engagement and require completion of group auditor documentation?	An entity will sometimes form part of a consolidated group of entities. As a result, it is likely management are required to provide the preparers of the group financial statements information to help with their preparation. Similar arrangements exist for group assurance engagements. The group auditor requires an entity's auditors to provide documentation about their engagement, including any misstatements or issues identified. The time spent completing this documentation will vary depending on the significance of the entity to the group's financial statements. The time spent completing this documentation is generally charged to the entity (unless specific arrangements are established between the group and entity management).

OUR VISION

Our insights inform and challenge government to improve outcomes for citizens.

OUR PURPOSE

To help parliament hold government accountable for its use of public resources.

Level 19, Darling Park Tower 2
201 Sussex Street
Sydney NSW 2000 Australia

PHONE +61 2 9275 7100

mail@audit.nsw.gov.au

Office hours: 8.30am-5.00pm
Monday to Friday.

audit office OF NEW SOUTH WALES

audit.nsw.gov.au