



Natural  
Resources  
Commission

# Audit strategy and approach

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## Enquiries

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# 1 Introduction

This document sets out the Natural Resources Commission's (NRC's) audit strategy and risk-based approach<sup>1</sup> to auditing outcomes in line with our legislative requirement to provide Government with independent advice on natural resource management, including through the specific function of undertaking audits as required by the Minister<sup>2</sup>.

This strategy and approach covers the NRC's role in auditing the outcomes of Local Land Services' (LLS's) regional delivery at the request of the Minister, as established in the Local Land Services Act<sup>3</sup> and associated Second Reading Speech. This role includes audits of LLS strategic plans to ascertain whether the provisions of the plan are being given effect, and, audits of the activities of LLS to determine whether its functions are being carried out effectively, efficiently and in accordance with State priorities, the state strategic plan and any local strategic plan.

It is principles based, and was derived from an assessment of risks to achievement of priority outcomes. The risk-based approach ensures the NRC delivers an efficient and flexible audit program that provides ongoing assurance to investors whilst monitoring and responding to emerging issues. Investors may include state government, Commonwealth government, industry partners or rate payers.

The strategy and approach also includes an audit determination which contains detail about how the NRC will undertake its audit role and deliver its audit opinion. The determination defines the type of audits the NRC will conduct in reference to established auditing standards to give confidence to auditees and government stakeholders that the NRC is adopting best practice audit methodologies.

The audit strategy and approach, and audit determination, were developed in reference to previous NRC experience conducting 17 audits of the effectiveness of Catchment Management Authorities' implementation of Catchment Action Plans. They also considered audit models developed since the 2007 NRC Audit Framework was published, such as the National Greenhouse Emissions Reporting (NGER) audit framework, and updates to industry standards, such as by the Australian Audit and Assurance Standards Board (AUASB)<sup>4</sup> and International Organisation for Standardisation (ISO)<sup>5</sup>.

This strategy will continue to be adapted over time, particularly in response to the development of functions and governance arrangements of the newly established Local Land Services.

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<sup>1</sup> Closely following, Standards Australia and Institute of Internal Auditors Australia (2010), *Handbook 158-2010, Delivering assurance based on ISO31000-2009 Risk Management – Principles and Guidelines*

<sup>2</sup> These functions are specified in Sections 12 and 13 of the *Natural Resources Commission Act 2003*.

<sup>3</sup> Section 24 of the *Local Land Services Act 2013* establishes the requirement for an independent audit of LLS activities every 5 years. Sections 44 and 54 establish the requirement for an audit of both the state and local strategic plans within 3 years of their approval. The Second Reading Speech for the Bill indicates NRC will be the independent performance auditor for NRM activities in the first instance.

<sup>4</sup> including ASAE 3500 *Performance assurance engagements* and ASAE 3100 *Compliance assurance engagements*.

<sup>5</sup> including *HB 158:2010 Delivering assurance based on ISO31000* and *ISO 19011:2011 Guidelines for quality and/or environmental management systems auditing*.

## 2 Audit strategy

The NRC's audits are a key assurance mechanism supporting devolved regional land and resource management and decision making, and form part of the NRC's wider program of independent review, evaluation and reporting which aims to:

- promote performance, good governance and accountability
- allow for effective devolution while maintaining effective oversight for application of investor funds
- develop practical solutions that have triple-bottom-line outcomes
- support evidence-based decision making, and
- drive continual improvement.

The NRC's audits provide assurance to investors that regional and state-wide plans are being effectively implemented, and are delivering social, economic, cultural and environmental outcomes in line with investor preferences, state-wide standards and targets. These audits also hold auditees to account in their role as public service providers, thus engendering community and investor confidence in their business practices and driving improved performance.

The NRC's approach will focus audit resources on measuring progress against the most important aspects of strategic plan implementation, while also being flexible enough to respond to emerging risks and regional issues.

The proposed priorities for the initial round of audits, as informed by the NRC's preliminary risk assessment are:

- achievement of outcomes in priority areas
- strong governance and accountability to support devolution
- community engagement.

Priority areas for the achievement of outcomes includes:

- the priorities of government investors (state and national),
- state-wide standards and targets, and
- priorities of local industries and communities

for agricultural production, biosecurity, natural resource management and emergency management<sup>6</sup>.

The NRC's audit program will be informed by a more detailed collaborative risk assessment process to be conducted with government investors and the auditees. This will establish areas of highest risk as well as other issues demanding audit priority. The risk assessment and audit program will be reviewed and updated regularly to account for significant changes in the internal and external context of the audits, and also to reflect continued growth in the auditee's maturity and capability.

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<sup>6</sup> Section 4 of the *Local Land Services Act 2013* establishes the meaning of 'state priorities for local land services'

LLS legislation<sup>7</sup> requires the Minister to seek the advice of independent auditors in approving draft strategic plans for LLS. In addition to providing assurance services via audits, the NRC will review draft state and local strategic plans for LLS as part of our role to provide advisory services (including reviews and evaluations).

### 3 Risk-based approach to auditing

In line with audit best practice<sup>8</sup>, the NRC audit work will be targeted toward areas posing the highest risk to the effective implementation of strategic plans and delivery of regional and state-wide outcomes in line with investors' priorities, state-wide standards and targets.

This risk-based approach to auditing allows the NRC to focus resources on assessing progress against the most important aspects of effective implementation, while also being flexible enough to respond pro-actively to emerging risks and regional issues.

The approach also allows flexibility in method and timing of audit work, to allow the NRC to best respond to the issues assessed as posing the highest risk. The NRC will have the option of using:

- a rolling program of comparable audits of implementation of local strategic plans, and
- complementary specific or limited scope audits to target state-wide or region-specific risks as they arise.

The approach has the following features:

- using risk assessment to identify priority areas on which the NRC will target audit work
- using pre-audit risk assessments to tailor the focus of individual audit engagements to the nature and level of relevant risks
- using flexible methods and timing of audit delivery, to allow the NRC to best respond to the highest risks
- using ongoing risk monitoring and evaluation, to inform adaptive audit program management that responds to emerging risks and regional issues (including NRM threats and opportunities).

The following sections outline how the risk-based approach will work in practice.

#### 3.1 Components of the approach

The NRC's risk-based approach to auditing is built on components that allow audit resources to be effectively and efficiently focussed during the program.

The following diagrams show how the NRC contributes to overall assurance and describe the key components of the NRC's audit program. The assurance framework and audit program are consistent with Australian National Audit Office *Better Practice Guide - Implementation of Programme and Policy Initiatives*<sup>9</sup> and *Public Sector Internal Audit: An Investment in Assurance and Business Improvement - Better Practice Guide*<sup>10</sup>.

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<sup>7</sup> Sections 41 (2)(b) and 51 (2)(b) of the *Local Land Services Act 2013*

<sup>8</sup> Standards across many disciplines require auditor to plan and execute audit engagements based on consideration of risk. These standards include those issued by the AUASB, ISO (Standards Australia) and the IIAA.

<sup>9</sup> ANAO October 2006

<sup>10</sup> ANAO September 2012

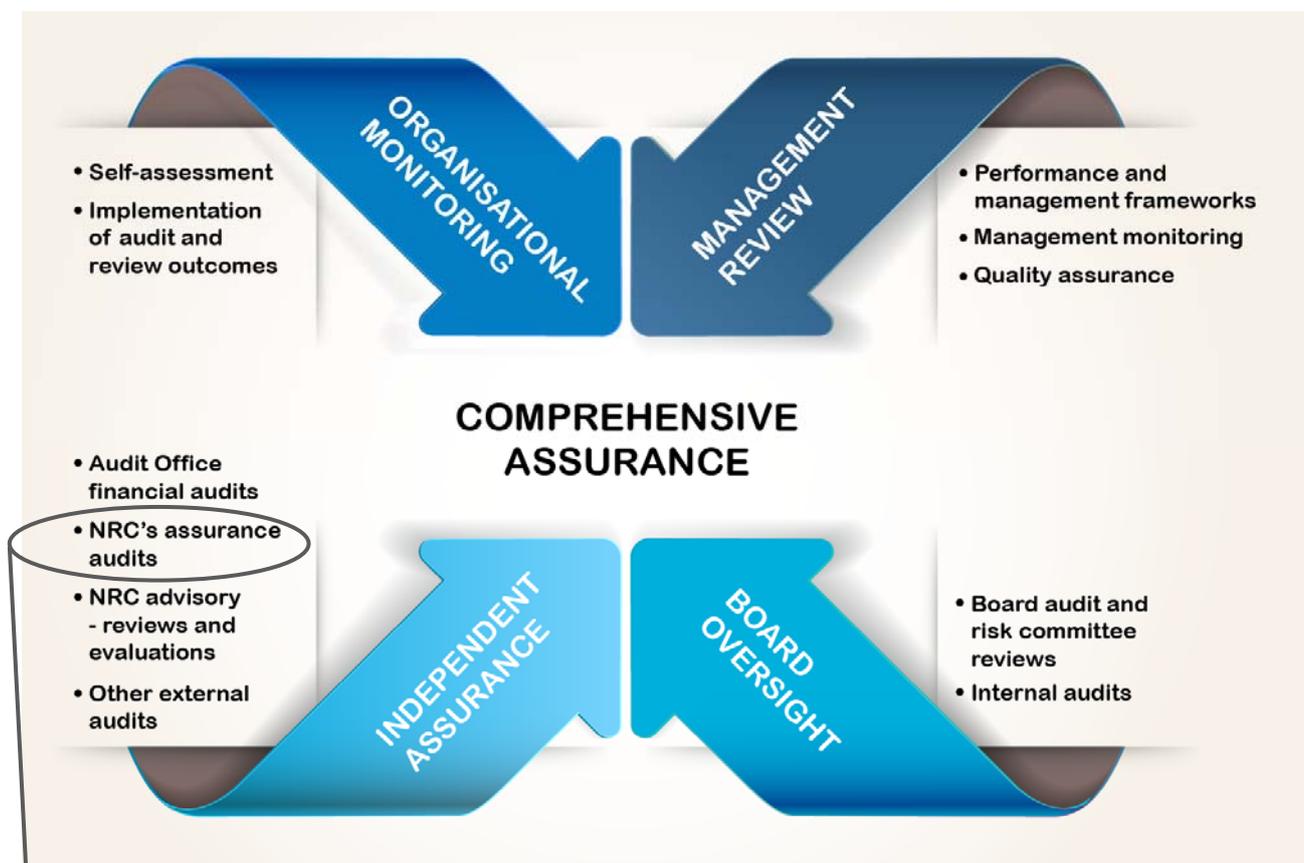


Figure 1: Overview of the NRC's role in providing assurance

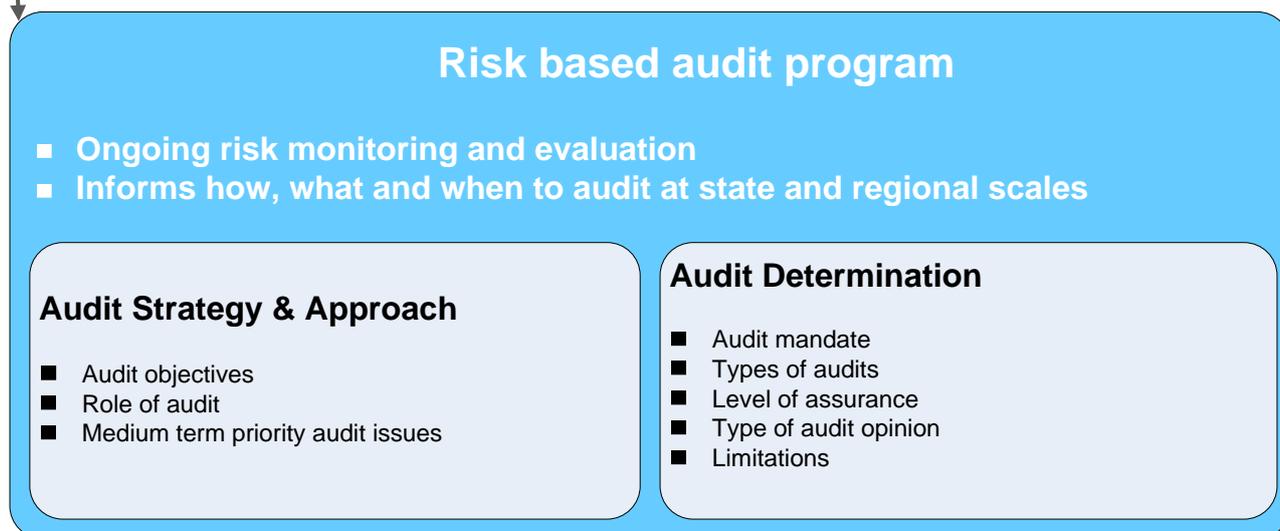


Figure 2: Key components of the NRC's audit program

### 3.1.1 Risks considered by the approach

The NRC will prioritise audit work toward issues that pose the highest risk. The NRC's risk-based approach to auditing considers 'risk' as:

*issues that increase the uncertainty of strategic plan implementation effectively delivering social, economic, cultural and environmental outcomes in line with investors' priorities, state-wide standards and targets<sup>11</sup>.*

In order to best use risk to focus audit resources at specific stages of the audit program, the approach also considers two significant scales of risk:

- the regional scale – where issues may pose a risk that implementation of an individual strategic plan fails to effectively deliver, or maximise, the outcomes identified for that region
- the state-wide scale – where issues may pose a broader risk that investment in land and resource management in NSW fails to effectively deliver, or maximise, outcomes in line with identified state-wide outcomes.

Importantly, the NRC's approach considers that 'risk' may include both threats and opportunities.

The NRC will undertake risk monitoring for issues at each scale. Ongoing monitoring and evaluation will include discussions with stakeholders, while pre-audit risk assessments may involve some targeted preliminary audit work to inform individual engagement planning.

### 3.1.2 Assessing and monitoring risk

The NRC will assess risk at both the state-wide and the regional scales, incorporating the following best practice<sup>12</sup> features:

- identification of risk issues through engagement with key stakeholders; keeping a watching brief on state and regional reporting and performance; and ongoing risk monitoring and assessment
- analysis of issues to understand the significance of each risk – that is, the likelihood that it will increase the uncertainty of the effective implementation of strategic plans, and the consequences for effective delivery of outcomes if it does
- assessment of the level of risk, prioritising issues that pose the highest risk to effective implementation of strategic plans and delivery of outcomes based on the analysis of significance and consequence.

### 3.1.3 Responding to risk assessment

The NRC will respond to risk by adopting the method, timing and frequency of audit work that best reflects the assessment of risk.

The NRC uses risk assessment to continue to review and update its audit strategy to reflect the NRC's assessment of, and response to, existing and emerging issues posing the highest risk to delivery of outcomes.

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<sup>11</sup> Consistent with the ISO 31000 definition of risk as the 'effect of uncertainty on objectives'

<sup>12</sup> Consistent with ISO 31000 - 2009 Risk Management– Principles and Guidelines

The risk assessment will identify whether issues are best dealt with as part of a rolling program (of audits across all regions), or as complementary audit engagements (such as spot audits, themed audits or follow-up audits).

Finally, the risk assessment informs the NRC's consideration of timing for individual engagements, to allow prioritised scheduling for higher risk issues.

### **3.1.4 Using risk to develop individual engagement plans**

The NRC will use pre-audit risk assessments to develop individual engagement plans. These will prioritise which issues need audit attention according to risk, and engagement plans will document how the highest priority risks will be dealt with during audit work.

Individual engagement plans will describe audit criteria chosen to best reflect the nature and level of risk relevant to the audit. For instance, these may vary between regions, recognising that issues at the state-wide scale will not necessarily pose the same nature or level of risk across all regions, and allowing for flexibility in delivery of audit work.

## 4 Audit determination – how NRC will deliver an audit

### 4.1 Preliminary

The audit determination below sets out how the NRC will deliver its audit opinions.

It adopts a simple short-form audit report, that:

- a) gives a direct opinion on how effectively strategic plans are being implemented, and
- b) is based on conclusions regarding how well auditees (and their implementation partners, where relevant) have undertaken specific activities, identified as lines of inquiry, and whether the systems and capabilities are in place to give assurance into the future.

#### 4.1.1 Name of determination

This determination is the 'NRC audit determination 2014'.

#### 4.1.2 Overview of determination

- a) This determination is made to meet requirements of the *Natural Resources Commission Act 2003* (the NRC Act).
- b) Under the NRC Act, the Natural Resources Commission has the function to audit the effectiveness of implementation of plans.
- c) This determination may also be adopted to meet requirements of sections 24, 44 and 54 of the *Local Land Services Act 2013*.

## 4.2 Performance audits

- a) A performance assurance engagement means audit work the purpose of which is to provide the NRC auditor's independent opinion as to the effectiveness of the matter being audited. This determination recognises two kinds of assurance engagement as follows:
  - i. a *reasonable* assurance engagement;
  - ii. a *limited* assurance engagement.
- b) Regional and state scale strategic plan implementation audits are primarily performance assurance engagements. The nature of the audit will be defined in the scope and lines of inquiry for each audit engagement.
- c) In an assurance engagement, the auditor provides an independent opinion about the matter being audited and uses professional judgment in preparing for and carrying out the audit and preparing the assurance engagement report<sup>13</sup>.
- d) The requirements of this determination recognise that NRC auditors are professionals who have the qualifications, skills and experience necessary to exercise professional judgment.

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<sup>13</sup> Australian Government Auditing and Assurance Standards Board, '*Standard on Assurance Engagements ASAE 3500: Performance Engagements*', Reissued September 2008

## 4.3 Compliance audits

- a) A compliance assurance engagement means audit work the purpose of which is to provide the NRC auditor's independent opinion as to an entity's compliance with requirements. This determination recognises two kinds of assurance engagement as follows:
  - i. a reasonable assurance engagement;
  - ii. a limited assurance engagement.
- b) Theme audits and spot audits at the regional or state-wide scale may be, in whole or in part, compliance assurance engagements. Audits of strategic plan implementation may also include elements of compliance assurance engagements. The nature of the audit will be defined in the scope and lines of inquiry for each audit engagement.
- c) In an assurance engagement, the auditor provides an independent opinion about the matter being audited and uses professional judgment in preparing for and carrying out the audit and preparing the assurance engagement report<sup>14</sup>.

The requirements of this determination recognise that NRC auditors are professionals who have the qualifications, skills and experience necessary to exercise professional judgment.

## 4.4 Kinds of assurance engagements

### 4.4.1 Reasonable assurance engagements

A reasonable assurance engagement means an assurance engagement in which the NRC auditor gives an opinion, expressed as a reasonable assurance conclusion, if appropriate in the circumstances of the engagement.

In giving a reasonable assurance conclusion, the NRC auditor is giving an opinion, expressed in the *positive* eg. 'In my opinion, *the strategic plan was being effectively implemented during the period June 2011 to June 2012.*'

### 4.4.2 Limited assurance engagements

A limited assurance engagement means an assurance engagement in which the NRC auditor gives an opinion, expressed as a limited assurance conclusion, if appropriate in the circumstances of the engagement.

In giving a limited assurance conclusion, the NRC auditor is giving an opinion, expressed in the *negative* eg. 'Based on the work described in this report, *nothing has come to my attention that causes me to believe that the strategic plan was not being effectively implemented during the period June 2011 to June 2012.*'

### 4.4.3 Terms of engagement

Before carrying out each assurance engagement, the NRC must prepare the terms of engagement and select the kind of engagement and level of assurance planned. The selection process will consider factors such as the assurance requirements of investors, audit scope and availability of evidence.

The terms of engagement and level of assurance will be determined on a case by case basis.

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<sup>14</sup> Australian Government Auditing and Assurance Standards Board, 'Standard on Assurance Engagements ASAE 3100: Compliance Engagements', Reissued September 2008

## 4.5 Audit conclusions

### 4.5.1 General requirements

- a) The audit conclusion must be consistent with the terms of engagement, and will be supported by conclusions regarding each of the lines of inquiry identified in the terms of engagement.
- b) If the NRC auditor is carrying out a *reasonable* assurance engagement, the auditor will consider the evidence gathered in the course of carrying out the reasonable assurance engagement and give one of the following conclusions for the engagement:
  - i. a reasonable assurance conclusion;
  - ii. a qualified reasonable assurance conclusion;
  - iii. an adverse conclusion;
  - iv. a conclusion that he or she is unable to form an opinion about the effectiveness of CAP implementation.
- c) If the NRC auditor is carrying out a limited assurance engagement, the auditor will consider the evidence gathered in the course of carrying out the limited assurance engagement and give one of the following conclusions for the engagement:
  - i. a limited assurance conclusion;
  - ii. a qualified limited assurance conclusion;
  - iii. an adverse conclusion;
  - iv. a conclusion that he or she is unable to form an opinion about the effectiveness of CAP implementation.
- d) The NRC auditor must only give a conclusion if it is supported by the evidence gathered.
- e) Audit conclusions are formed on the basis of the *inherent limitations* of assurance engagements, for example, that work is based on selective testing of information and that uncertainties affect the nature of, and methods for determining, non-financial data.
- f) Audit conclusions are prepared for the purpose of NRC reporting and should not be used, or relied upon, by readers for any purpose other than that identified in the terms of engagement. The NRC reserves the right to use audit conclusions, in conjunction with other NRC work, in the development of its advice in the normal course of business.

### 4.5.2 Reasonable assurance conclusion

- a) In giving a reasonable assurance conclusion, the NRC auditor is giving an opinion, expressed in the *positive*.
- b) An example of a reasonable assurance conclusion is as follows:

‘In my opinion, the strategic plan was being effectively implemented during the period June 2011 to June 2012.’

### 4.5.3 Limited assurance conclusion

- a) In giving a limited assurance conclusion, the NRC auditor is giving an opinion, based on the work performed and expressed in the *negative*.
- b) An example of a qualified limited assurance conclusion is as follows:

‘Based on the work described in this report, nothing has come to my attention that causes me to believe that the strategic plan was not being effectively implemented during the period June 2011 to June 2012’.

#### 4.5.4 Qualified assurance conclusions

- a) In giving a qualified (reasonable or limited) assurance conclusion, the NRC auditor is giving an opinion that:
- i. there are one or more ineffective areas that are apparent but not pervasive enough to affect the matter being audited as a whole; or
  - ii. there is insufficient evidence in relation to one or more areas, but although the lack of evidence may be important it is not pervasive enough to affect the matter being audited as a whole.

- b) An example of a qualified reasonable assurance conclusion is as follows:

‘In my opinion, except for ‘X’, the strategic plan was being effectively implemented during the period June 2011 to June 2012’

- c) An example of a limited assurance conclusion is as follows:

‘Based on the work described in this report, with the exception of ‘X’, nothing has come to my attention that causes me to believe that the strategic plan was not being effectively implemented during the period June 2011 to June 2012’

In the example above, ‘X’ represents the basis for qualification.

#### 4.5.5 Adverse conclusion

In giving an adverse conclusion, the NRC auditor is attesting:

- a) that there are ineffective areas that are important and pervasive enough to affect the matter being audited as a whole; and
- b) that, because of those ineffective areas, he or she is unable to give:
  - i. a reasonable assurance conclusion; or
  - ii. a limited assurance conclusion; or
  - iii. a qualified assurance conclusion.

#### 4.5.6 Conclusion that auditor is unable to form an opinion about matter being audited

In giving the conclusion that the NRC auditor is unable to form an opinion about the matter being audited, the auditor is attesting that, because he or she was unable to reasonably gather sufficient and appropriate evidence in relation to the matter, he or she is unable to give:

- a) a reasonable assurance conclusion; or
- b) a limited assurance conclusion; or
- c) a qualified assurance conclusion; or
- d) an adverse conclusion.