

# **International Peer Review of the Performance Audit practice of the Icelandic National Audit Office**

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# 1 Introduction

In January 2012 the Icelandic National Audit Office (INAO) and the Netherlands Court of Audit agreed on a Memorandum of Understanding (MOU) to conduct a peer review on the performance practice of the INAO. An international team with representatives of the audit offices from Norway, Sweden and the Netherlands conducted the actual review in the first half of 2012. On November 12<sup>th</sup>, the draft report was sent to the Auditor General of the INAO. The INAO responded on November 16<sup>th</sup>. This response is included in chapter 5.

The primary objective of the peer review was to assess whether the performance auditing practice of the INAO provides Parliament with independent, objective and reliable information on government performance. The main focus of the peer review was to contribute to the development of the performance audit practice of the INAO.

In the MOU it was agreed to focus the review on three main questions:

- To what extent are the performance audit reports and performance audit practice at the INAO in accordance with international standards;
- What factors explain possible shortcomings in the quality of performance audits;
- What impact does INAO performance auditing have on government performance.

To answer these questions the peer review team studied a sample of eight reports published in 2011 and related documents (see annex 1). Furthermore interviews were held with the Auditor-General of the INAO and its staff on performance audit practice in general and more specific on the selected reports, with representatives of five ministries and with members of the Constitutional and Supervisory Committee (CSC) of the parliament (see annex 2). The CSC is responsible for the response to all performance audit reports of INAO.

The peer review team conducted its review in accordance with ISSAI standards on peer review (ISSAI 5600). Standards used in the peer review were based on ISSAI standards and guidelines, mainly ISSAI 3100 on the key principles for performance audit and ISSAI 40 on quality control.

## **2 The Icelandic National Audit Office (INAO) in 2011**

### **2.1 Practice in general**

The authority and tasks of the INAO are laid down in the National Audit Act (86/1997). Article 9 of the National Audit Act that regulates the performance audit states that performance audit “covers the handling and utilization of public funds, whether economy and efficiency is being taken care of in the operations of institutions and state owned enterprises and whether applicable lawful instructions are being complied with in this context”. Objectives of performance according to article 9 are:

- examine the management and utilization of public funds;
- evaluate whether operations are economic, efficient and effective;
- recommend ways to improve economy, efficiency and effectiveness.

The INAO is independent in carrying out its duties (article 3). Nevertheless, the presidential committee of Parliament may call for reports on any specific examinations which fall under the mandate of the INAO. The INAO states that in 2011 approximately 15 percent of its tasks were launched at the request of Parliament, ministries or others.

The INAO currently (2012) has a staff of 42, whereof 10 are employed in the performance audit department. The department consists of a director, two assistant directors and seven auditors.

In 2010 the INAO changed its performance audit practice. INAO wanted its reports to be brief and focused and to operate in a more efficient, flexible way. Reports became smaller and were conducted in less time; from start to finish, they usually take less than half a year.

The INAO published 27 performance audits reports in 2011. They are of a wide variety and consist of follow up reports, one page recommendations and full stretched performance audits. All reports are published on the website and not on paper.

Being a small department, lines of communication obviously are direct and formal procedures are limited. Audit teams are small and for most audits consist of an auditor and a manager (director or assistant director). The INAO refers to the ISSAIs as serving as their guidance. Besides that some procedures are laid down or are being developed. For instance:

- strategy map 2011-2012 (mission and objectives)
- code of ethics
- audit plan format
- performance audit process

The quality of reports is considered by internal reviews carried out by staff members from outside the team and also outside the Performance Audit division to provide for open and objective feedback. Externally the quality is reviewed by sending a draft version to the relevant ministries and agencies.

The performance audit division has set out a performance audit division scorecard designed for keeping track of external (impact, customers' satisfaction) and internal (timeliness, education etc.) goals.

## **2.2 Answers to the main questions**

Regarding the main questions the peer review team has the following view:

- To what extent are the performance audit reports and performance audit practice at the INAO in accordance with international standards?
- What factors explain possible shortcomings in the quality of performance audits?

According to ISSAI standards "performance audit is an independent and objective examination of government undertakings, programs or organizations, relating to one or more of the three aspects of economy, efficiency and effectiveness, with the aim of leading to improvements." To this aim the topics should be significant and auditable. The audits should be planned and carried out in a manner which ensures an independent audit of high quality. The report should be transparent, clear, reader friendly, congruent, convincing, constructive and add value to the stakeholders (parliament and auditees). Finally the ISSAIs stress the importance of a follow-up strategy (ISSIA 3000 and 3100).

The INAO has implemented several measures to reach this objective. The strengthened internal quality measures, the survey amongst their stakeholders to check the usefulness of the reports, the structured

performance audit process and the instrument of pre-study show that the INAO has a professional approach to performance audit. Moreover, the follow-up strategy ensures that their recommendations and the resulting policy changes stay under ongoing scrutiny. The INAO stands for an impressive quantitative production of compact reports that are in general easy to read according to most stakeholders.

However, the speedy delivery of short readable reports from the INAO also holds the risk of not always giving the design of audits sufficient attention to secure a methodologically solid audit and a clear, coherent and convincing report. Also there is a risk of not giving sufficient attention to a clear description of methodology and sources of information. A short report can also be less convincing to critical readers if it has insufficient attention to a clear separation between background information, audit questions, audit criteria, findings, conclusions and opinions.

In our sample we have established that this risk materialises. We feel that more attention for methodology and more structured reporting would help to improve the quality of the audits and the persuasiveness of the reports.

Some recommendations on audit methodology and reporting are further elaborated in chapter 4.

- What impact does INAO performance auditing have on government performance?

INAO measures its own impact. INAO uses a survey to obtain information amongst others on the accessibility of the reports for parliament and ministries, and on the usefulness of the reports for parliament (to supervise government) and ministries (the recommendations). Around 90 percent of the respondents are positive on both questions according to the scorecard of INAO. 100 percent of the ministries are of the opinion that the reports are accessible.

The interviews the peer review team had with the ministries show more variety in the responses. Some of them pointed out that although the reports are easy to read and the topics are relevant and give a good overview of risks and shortcomings, the added value could be higher if the INAO produced more genuinely new information or conducted more analysis of the provided data. According to the interviewed members of parliament (CSC) the reports are relevant and INAO is valued because they are “not afraid” to be critical. Sometimes the reports and especially the recommendations are perceived to be a little too directive. Pointing out the problem and suggesting a direction for solution is in their opinion often enough for an effective message.

Improvement of the strategic planning, more attention for audit methodology and communication might help to lead to more added value. Some recommendations on these points are further elaborated in chapter 4.

### 3 Good practices of the INAO

INAO has succeeded to improve its **productivity** remarkably the last couple of years, by choosing to publish more and more compact reports. It has given INAO the opportunity to cover a wide range of topics each year even though it operates with a small division. Ministries and parliament indicate that most topics that INAO covers are also **significant topics**. Ministries as well as Parliament benefit from this new policy. Furthermore it enhances the visibility of the INAO and draws the attention of media and public to its work, thereby potentially adding more value to Icelandic society.

INAO aims to be in the top ranks of performance auditing and has demonstrated an impressive **drive to improve** its quality. Examples are the improved audit process, the system of quality control, and the recent improvement of the follow-up studies to include not only the follow up on recommendations but also the recent developments in policy. This makes the follow up reports more in line with ISSAI standards and, according to the CSC, more relevant to parliament.

The **reports are accessible and easy to read**, particularly due to the short summary with major findings and recommendations on the first pages and the short messages on the side that provide the reader with the essence of the section.

Being a small team every staff member has a relatively large impact on the performance of the division. Working culture in such an environment is of great importance. The peer review team has spoken one or several times with the staff of the performance audit division. **Drive and enthusiasm characterize the working environment.**

## 4 Suggestions for improvement

INAO aims at more focus in their audits by narrowing the scope of the audits. We feel the ambition of the INAO to be focused and efficient can be further enhanced by a more **deliberate strategic planning process**. The choice of audit topics and the approach is preferably the outcome of a careful analysis on the expected added value of INAO. Such an analysis can lead to more focus in the INAO program as a whole by making explicit choices not only on topics, but also on types of audit.

The eight selected audits in the peer review sample mainly focused on procedures and regulations and the compliance to these rules. INAO might consider adding more diversity in type and depth of audits, amongst others by **including more audits deliberately aimed at effectiveness or efficiency of the policy**. These type of audits are more demanding and will take more time to deliver than the average INAO report. But including one or a few of these types of audits can provide the added value and extra analysis the stakeholders are looking for.

More focus could also be reached in the **audit design**. At this moment INAO has a practice that focuses the audit on what is deemed the most important topic encountered during the study. This approach has the advantage of being flexible, but it may pose a risk to the coherence of the audits. A more explicit audit design (with attention to how aim, audit questions, methods for data collection and analysis and criteria interrelate) will help to conduct the audit in a structured way, with strong evidence and becoming less dependent on readily assessable data and signals provided by the auditees. Also, a thorough analysis of the data is easier if the methodology for this is planned at the start of the study. As a result of the new performance audit practice, INAO is making less use of instruments like a question tree and design matrix for designing audits than they did in the past. However we feel INAO could, especially in the somewhat bigger audits, benefit from the use of some sort of structuring technique.

A more explicit audit design will help to further **strengthen the structure of the reports**. The reports of INAO could benefit from a clearer division between audit questions, findings, conclusions and recommendations and

from an explicit explanation of the relation between them (congruency). Providing more evidence and reasoning for every conclusion and recommendation would make the reports less vulnerable for criticism, that the conclusions and recommendations are primarily the opinion of the INAO. Providing more information on methodology and data sources in the report or in a separate document on the website will also help to make the reports more convincing.

To be effective, **communication between auditees and INAO is of crucial importance**. The way INAO communicates with the auditees varies. Most communication focusses on data gathering. Discussions on the audit plan and criteria at the beginning of the process and on findings, conclusions and possible recommendations at the end of the process, can enhance the acceptance of the audit by auditees. They can also help the INAO to adjust its approach when necessary.

The performance audit division could be strengthened by **more sharing of knowledge and skills**. Since INAO carries out many relatively small audits the audit teams are small in size also. For a small organization like INAO working with bigger teams might often be not feasible. However, the INAO could stimulate more knowledge sharing and consultation between colleagues. For instance by stimulating consulting of colleagues outside the team especially in the planning phase while designing the audit methodology and when the main conclusions and recommendations are developed. Another way to share knowledge can be to organize periodical meetings for all staff members to discuss methodology and audit approaches used in specific audits.

## 5 Reaction of INAO

The Auditor-General of Iceland responded to the draft report in his letter of the 16<sup>th</sup> of November.

“ The INAO welcomes the peer review report on the performance audit practice of the Office, which on the whole gives a fair and balanced view of the named activity. The review itself was a useful learning experience for the NAO and its Performance Audit Division and the peer review team’s analysis of the Division’s working practices and suggestions for improvement are highly valuable. They will undoubtedly assist the Office in improving the quality of its work. Therefore, the INAO finds that the peer review has served its key purpose, that is to help the Office to ensure that its audits comply with applicable professional standards. The INAO has already started implementing some of the team’s suggestions for improvement. They are being considered in the current strategic planning process for the years 2013-15 and in relation to changes in the structure of the reports. Suggestions for improvement in other areas will also be carefully studied. The INAO and its Performance Audit Division are grateful for the team’s input in enhancing the quality of the Office’s work into the future.”

## Annex 1: Audits included in the peer review

Auditnr.	Type	Ministry	Title	Publication month
1	VFM	Education, Science and Culture	The Icelandic Student Loan Fund	June
2	VFM	Finance	Human Resource Management - 2: Government HRM Policy and Current Situation	September
3	VFM	Fisheries and Agriculture	Outsourcing Public Services to the Farmers Association in Iceland	Mars
4	VFM	Welfare	Mergers - 5: Directorate of Health	June
5	VFM	Welfare	Binding Service Agreements - 2: Ministry of Welfare	December
6	Recomm	Education, Science and Culture	Icelandic Research Fund: Delegation of Resources	February
7	Recomm	Fisheries and Agriculture	Payments to Ovine Farmers	December
8	Follow-up	Interior	Transportation Construction	May

## **Annex 2: Interviewed Stakeholders**

*Parliament:*

Members and staff of the Constitutional and Supervisory Committee (CSC) )

*Ministries (staff):*

Ministry of Education, Science and Culture

Ministry of Finance

Ministry of Fisheries and Agriculture

Ministry of Welfare

Ministry of Interior

## **Annex 3: Members Peer Review Team**

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