International Peer Review of the Financial Audit Practice of the Icelandic National Audit Office

Report by the Supreme Audit Institutions of the Netherlands, Norway and Sweden, December 2013
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1 Introduction

The Icelandic National Audit Office (INAO) requested the Netherlands Court of Audit (NCA) to assess whether the INAO’s financial audit practice (including compliance audit aspects which are relevant to and part of financial audit) is in accordance with generally accepted practices in government auditing (especially International Standards for Supreme Audit Institutions). In the first half of 2012 the NCA, together with colleagues from the Norwegian and Swedish Supreme Audit Institutions, also performed a peer review on the performance audit practice of the INAO. This report was published in December 2012.

In April 2013 the INAO and the NCA agreed a Memorandum of Understanding to conduct the peer review of the financial audit practice of the INAO. An international team with representatives of the audit offices of the Netherlands, Norway and Sweden conducted the actual peer review in May-August 2013. The draft report was submitted to the Auditor General of the INAO on December 5th 2013. The INAO responded on December 9th 2013. This response is included in chapter 4.

The main objective of the peer review was to identify the extent to which the financial audit practice of the INAO is in line with the *International Standards for Supreme Audit Institutions (ISSAIs)* of INTOSAI\(^1\) and what recommendations could be made to further improve the financial audit practice of the INAO.

It was agreed in the Memorandum of Understanding that the peer review would focus on three main questions:

1. What is the quality of the INAO’s financial audits and to what extent are they in accordance with INTOSAI standards?
2. What recommendations can be given to the INAO to improve the quality of its financial audits?
3. How can the INAO’s risk assessment concerning the financial audits be improved, to reduce the audit gap?

To answer these questions the peer review team developed a questionnaire based on previous experience with peer reviews and the ISSAIs. The

\(^1\) International Organization of Supreme Audit Institutions.
questionnaire consisted of two parts: one part on the general organization, processes and procedures of INAO’s financial audit practice, and another part with a specific checklist for five individual financial audits reviewed by the peer review team. The methodology used to answer these questions is summarized in annex 1. Annex 2 lists all the organizations interviewed by the peer review. The members of the peer review team are summed up in annex 3.

The peer review team conducted its review in accordance with the INTOSAI standard for peer reviews (ISSAI 5600). Standards used in the peer review were mainly based on ISSAIs concerning financial auditing. The very recently (October 2013) adopted ISSAIs 100, 200 and 400 (Fundamental Principles of Public Sector Auditing, Financial Auditing and Compliance Auditing) were not yet endorsed during the execution phase of the peer review, so these were not used.

The peer review’s scope was limited to the financial audit of the accounts for the fiscal year 2012. Monitoring the execution of the Budget (National Audit Act (86/1997), section 8) was not part of the scope of the peer review. Where relevant, improvements made by the INAO in 2013 were also taken into account in drafting this peer review report.

The findings of the peer review are presented in chapter 2 and the conclusions and recommendations are presented in chapter 3.

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2 This task is not a task of the Financial Audit Department.
2 Findings on INAO’s financial audit practice

2.1 Introduction

In this chapter the peer review team presents its main findings on the INAO’s financial audit practice. First of all, we would like to stress the nature of these findings: a critical finding should not be interpreted as a shortcoming per se, but as a comparison with the extensive INTOSAI Standards (ISSAIs). The INAO is still in the process of adopting ISSAIs and is not finished yet. Implementing ISSAIs is a big challenge to all Supreme Audit Institutions (SAIs), especially for relatively small SAIs such as the INAO. In this light, critical findings should be interpreted as observations that can be used by the INAO to further bring its financial audit practice into line with INTOSAI standards.

2.2 Institutional context

2.2.1 Legal tasks

The authority and tasks of the INAO are laid down in the National Audit Act (86/1997). Section 8 of the National Audit Act, which regulates the financial audit, states that the financial audit practice shall at any given time be in particular aimed at:

- ensuring that the financial statements present fairly the operations and financial position in accordance with generally accepted accounting principles;
- examining internal control and whether it assures adequate results;
- ensuring that accounts are in conformity with authorisations under the Budget, the Supplementary Budget or any other Acts of Althingi (Parliament), lawful instructions, business practice or service contracts as applicable;
- examining and verifying the indicators that show the activity and performance of governmental entities and that are reported in the financial statements.
An important development is the amendment of the National Audit Act. A draft Bill 2013 contains the following (main) changes: the Auditor General will be elected by Parliament; increased transparency (right of access to documents); obligatory implementation of ISSAIs. The Bill is expected to be presented to Parliament during the next regular session of Parliament. Especially important for the peer review is the obligatory implementation of ISSAIs (see section 2.2.2).

As can be deduced from the above-mentioned legal tasks with regard to financial audit, the INAO is not specifically required to issue an opinion on the legality and regularity of the financial transactions underlying the accounts. Its task seems to be restricted to auditing the reliability (true and fair view) of the accounts, including the ‘regularity’ of the accounts (not the underlying transactions). However, the INAO has stated that it interprets this task in a broad manner, whereby compliance with laws, regulations and applicable rules is considered as part of the financial audit.

On the other hand, the INAO has a legal task which is unusual for many SAIs: to monitor the execution of the Budget. In many countries this is a task of the Ministry of Finance.

It is also important to note that the INAO performs another role (non-obligatory) that is unusual for SAIs: preceding the financial audit, the INAO helps smaller agencies prepare their accounts. The INAO’s report on the audit of the 2011 central government accounts states: “The INAO has rendered assistance to many agencies in connection with the annual

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3 The Report on the 2011 Central Government Accounts contains the following opinion: “It is the opinion of the INAO that the central government accounts present a true and fair view of the results of the operations of the Treasury, government agencies and funds in Groups A to E entities in 2011, its financial position as of 31 December 2011 and change in cash position in 2011, in accordance with acts of law concerning annual financial statements and government financial reporting.” In the opinion of the peer review team this is an opinion on the reliability (true and fair view) of the accounts, because complying with laws and regulations regarding financial reporting is part of the reliability opinion. The opinion does not contain a statement on the legality and regularity of the financial transactions underlying the accounts.

4 Some (not all) SAIs, for example the Norwegian, Swedish and Dutch SAIs, issue an annual opinion on both the true and fair view (of financial statements) and the legality and regularity (of underlying financial transactions). The legality and regularity audit checks whether public money is received (revenues) and spend (expenses) in accordance with the rules. This is seen as a very important task for SAIs: they must assure not only that the central government issues reliable accounts, which provide an insight into the assets and liabilities (financial position) and revenues and expenses (financial performance), but also assure that the central government provides “value for money” by ensuring that financial transactions are in accordance with applicable laws and regulations.

5 As stated this task is not a task of the Financial Audit Department. The performance of this task is not part of the scope of the peer review.
financial audits to be able to present annual financial statements in the form that is applicable in the regular market but there has been a systematic reduction in such assistance in recent years due to changes in emphasis in audits.”

2.2.2 INTOSAI Standards

A very important and challenging process for the INAO is the implementation of the International Standards of Supreme Audit Institutions (ISSAI). The ISSAI framework, formally established in 2007, reflects the ambition of INTOSAI to provide its members and other interested parties with a framework of professional high-quality auditing standards. The first complete set of ISSAI was presented and endorsed at the INTOSAI Congress in South Africa at the end of 2010.

As noted above, implementation of the ISSAI will be obligatory for the INAO after implementation of the new National Audit Act. The INAO has already decided to implement the ISSAI voluntarily, and this process started late 2011, with, for example, training employees and preparing instructions. An external Certified Public Accountant (CPA) has been hired as a consultant to provide guidance during the implementation process. Implementing the ISSAI on financial auditing, which contain a large number of requirements, is a major challenge to all SAIs, and especially for smaller SAIs such as the INAO. Adoption of the ISSAI is a multi-year process for all SAIs, and the INAO is now in the process of implementing them. This means that the 2012 audits, which were the object of this peer review, were not yet completely “ISSAI-proof”.

The INAO has prepared an ISSAI implementation plan for 2012, including time schedules. There is no formal additional implementation plan for 2013.

In October 2013 INTOSAI endorsed some new fundamental auditing principles. ISSAI 100, 200 and 400 (Fundamental Principles of Public Sector Auditing, Financial Auditing and Compliance Auditing) are very important for the financial audit practice. As the ISSAI were not endorsed yet during the execution phase of the peer review, the financial audit practice of the INAO was not compared to these ISSAI.
2.3 Organization of the financial audit practice

2.3.1 Positioning of the financial audit department

The INAO has two main departments: financial audit and performance audit. The diagram below shows the organizational structure of the INAO:

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          AUDITOR GENERAL
          
    AUDITOR GENERAL'S SECRETARIAT  ADVISORY BOARD
          
    FINANCIAL AUDIT & IT SERVICES
          
    LEGAL & ARCHIVES SERVICES
          
          FINANCIAL AUDIT DEPARTMENT
          
          PERFORMANCE AUDIT DEPARTMENT
          
          JOINT TASKS
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2.3.2 Capacity

The INAO employs 42 staff in total, of whom 21 work in the financial audit practice. The INAO is therefore a relatively small SAI.

The Financial Audit Department is run by a financial audit director. Four audit division managers are responsible for executing the audits with their team of (senior) auditors; the managers actively participate in the audit teams. The Auditor General is also involved in the planning and reporting phases of the financial audits, and is responsible for the overall financial audit practice.

The financial auditors are all highly educated: four CPAs (the INAO employs five CPAs including the Auditor General) and 16 employees with a university degree (the 21st employee is a secretary).

The average age of the INAO’s staff is 53 and the average employment length is 14 years.6

CPAs are responsible for performing the financial audits of the most important audit objects: the larger entities of the A-part of the budget (see section 2.4) and all – not-outsourced - entities outside the A-part. Other auditors (not CPAs) perform the audits of smaller entities of the A-part of the Budget. According to the INAO, it is difficult to hire new CPAs because of government salary restrictions, although at the moment increasing the number of CPAs is not a target in itself at INAO. According to the INAO, in the nearby future

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6 After completion of the peer review these figures changed: average age is now 54, average employment length is now 15,5 years.
there will possibly a need for more CPA-expertise because of the further implementation of the ISSAI and the proposed implementation of International Public Sector Accounting Standards (IPSAS) in Icelandic public sector (Draft Bill on public finance of Parliament).

It is important to note that the INAO has stated in publications that it does not have enough staff to perform financial audits at all audit objects every year (see sections 2.3.5 and 2.5.1). The INAO has stated that it had a deficit for two years and has experienced staff reductions. The scarce capacity also results in a relatively low degree of auditor rotation among audit objects. The INAO is of the opinion that it has a shortage of staff.7

The auditor’s independence from the audit object is very important. The INAO uses “statements of auditor independence” for this purpose.

2.3.3 Audit process and audit manual

The financial audit process is clearly structured into the customary phases of planning, execution and reporting, and is – for the 2012 financial audits, the object of the peer review - partially documented in the document “Risk-based selection of tasks for Financial Auditing”. The main phases distinguished in this document are risk analysis and audit task planning (planning-phase), risk-based audit (execution-phase) and summary and analysis of the conclusions and reporting (reporting-phase). According to ISSAI 1200, manuals and other written guidance and instructions concerning the conduct of the audits have to be prepared. INAO has prepared “Financial Audit Guidelines”, which describe the principles and practice of the financial audit and provides reasons and justifications for deviations from the applicable ISSAI. The INAO has also prepared working papers (templates) for certain audit procedures. The 2012 financial audits did not fully comply yet with these Financial Audit Guidelines. The INAO is in the process of adapting the financial audit practice to the requirements of the Financial Audit Guidelines. Key steps for the INAO are to evaluate whether the Financial Audit Guidelines are ISSAI-proof (and whether deviations are justifiable)8 and to implement the Financial Audit Guidelines in full.

7 The Lima Declaration of INTOSAI, ISSAI 1, states in Section 7, Financial independence of Supreme Audit Institutions: “1.Supreme Audit Institutions shall be provided with the financial means to enable them to accomplish their tasks.”

8 It was not possible for the peer review team to compare the Financial Audit Guidelines with the ISSAI, because only the first chapter and the table of contents could be translated fully in English.
2.3.4 Audit management systems

The financial audit process is incorporated in two audit management systems, Descartes and TeamMate. Descartes is used for larger entities and TeamMate for smaller entities. Descartes contains build-in ISAs but TeamMate does not. Some parts of the audit are documented outside of these two systems in an electronic file system (ONE) or on the harddisk of the INAO.

Partly because of the use of different audit management systems not all financial audits are executed similarly. The use of different systems could lead to inefficiency.

2.3.5 Outsourcing

The INAO can outsource some of its tasks to independent chartered accountants. Section 4 of the National Audit Act gives the INAO permission to outsource its tasks: “The National Audit Office is entitled to appoint independent chartered accountants or other experts in a specific field to carry out specific assignments entrusted to the Office in this present Act or other specific laws”.

The INAO states that it is unable to perform all financial audits itself, because of capacity restrictions. For the year 2012 the INAO hired external audit capacity mostly for the financial audit of the B-part (government enterprises), the C-part (lending agencies), the D-part (government financial institutions), and the E-part (enterprises owned for over 50% by the government) of the Budget. The majority of entities outside of the A-part of the Budget is audited by external audit firms.

In 2012 a total of 39 institutions of the A-part of the Budget were audited by external audit firms, accounting for 5% of A-part expenditure.

A final observation is that the INAO uses the work of hired external auditors for entities in A-part of the Budget without reviewing the quality of their work and the appropriateness of their reports and opinions. It could be argued that according to the ISSAI (1600) the INAO should review the work of hired auditors, because the INAO uses the work of these private sector chartered accountants for its own audit opinion. The INAO also outsources audits for B-E-part of the Budget, but these audits are not used by the INAO for its own audit opinion, so this finding only concerns outsourced audits regarding A-part of the Budget.

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9 International Standards on Auditing, issued by the International Federation of Accountants (IFAC). These ISAs form the basis of most of the ISSAI.

10 The INAO also outsources audits for B-E-part of the Budget, but these audits are not used by the INAO for its own audit opinion, so this finding only concerns outsourced audits regarding A-part of the Budget.
direction, supervision and performance of an audit performed by a “component auditor” in compliance with professional standards and applicable legal and regulatory requirements, and for making sure that the auditor’s report is appropriate in the circumstances.

2.4 Audit objects

Article 1 of the National Audit Act (No. 86/1997) states that the INAO shall: “...audit the central government accounts and the accounts of those bodies that are involved in the operation of an entity on the management of funds for the government...”.

The government accounts are divided into five groups:
1. Group A: the highest authority of the state, i.e., the Office of the President, the Althingi, the Cabinet and the Supreme Court, as well as ministries and government agencies, including certain funds; also those non-government entities for which the Treasury finances all or most of their operations with appropriations or is financially responsible for their operations by law or contract.
2. Group B: government enterprises operating in the market, the costs of which are fully or for the most part financed from revenue of the sales of goods and services to the public and enterprises.
3. Group C: lending agencies owned by the government, other than deposit money banks.
4. Group D: government financial institutions, including banks and insurance companies owned by the government.
5. Group E: unincorporated enterprises and joint-stock companies that are owned by the government for more than one-half.

As noted above, the INAO has stated that because of capacity restrictions it is unable to audit all government bodies every year (see also section 2.5.1).

Some data:
In all, there are 436 audit objects in Part A of the Budget, three in Part B, five in Part C, two in Part D and 25 in Part E. All audit objects in Parts B-E are annually audited, either by the INAO or by hired audit firms.

Of the A-part of the Budget 429 Budget items are subject to audits on expenditure (7 are subject to revenue audit or balance sheet audit). Of these 429 Budget items, there are 85 Budget items with expenditure of more than 1 billion ISK, accounting for 80% of total expenditure, 66 Budget items with expenditure between 500 and 999 million ISK, accounting for 10% of total expenditure, and 278 Budget items with expenditure less than 500 million ISK, accounting for 10% of total expenditure.
2.5 Planning (including risk analysis)

2.5.1 Overall audit planning: annual audit strategy/plan (including overall risk analysis)

The INAO documented its overall annual audit plan for 2012 in the document “Risk-based selection of tasks for financial auditing”. Because of the inability to audit all audit objects every year, it is necessary to prioritize and select the most important audit objects each year. The INAO tries to cover all Budget items every three years, but limited resources have made this difficult: 72 entities have not been audited in the past three years.

The core of the selection of audit objects is formed by ten risk factors. All audit objects are scored on these risk factors, and on the basis of this analysis the audit objects to be audited in year n are selected.

The risk factors are:
- Risk factor A – Scope of expenditures;
- Risk factor B – Serious earlier reservations from the INAO;
- Risk factor C – Change in operation or reorganization;
- Risk factor D – Operation significantly exceeds/within budget year after year – systematic underestimation;
- Risk factor E – Negative equity;
- Risk factor F – Reliable accounting and payment arrangement – insufficient segregation of duties;
- Risk factor G – Budgetary item not audited in the past four years;
- Risk factor H – Fraud and abuse risk;
- Risk factor I – Nature of the budgetary item;
- Risk factor J – Special revenue significantly exceeding appropriations year after year.

In practice the selection is mainly on factor A, scope of expenditures.
The risk that the INAO will not be able to audit every audit object once every three years already became reality, as noted above. For the audits to be effective, it is crucial that INAO’s selection of audit objects is sufficiently risk-based. In addition, the financial audit scope must be wide enough to ensure that an opinion can be given on the true and fair view of the central government accounts.

As noted above, the INAO uses some of its capacity to help some smaller organizations prepare their accounts. In the opinion of the peer review team this should not be a task of the INAO as the external auditor. The INAO has started (2013) to audit smaller, similar organizations as groups instead of as individual audit entities. The INAO has also started (2013) to reduce the performing of non-obligatory services at the request of entities (performing non-obligatory financial audits and/or issuing non-obligatory audit opinions). The INAO also wishes to outsource all audits of B-E-part of the Budget in the future, and concentrate on the A-part of the Budget. However, the INAO is still uncertain whether this is feasible. Finally, not many audit objects currently have an internal audit function. An increase in the number of internal audit departments is possible, in which case the INAO could determine whether it could rely on the work of internal auditors (ISSAI 1610) to reduce the workload.

2.5.2 Individual audit planning: individual audit plan/program (including risk analysis)

ISSAI 1300 requires the auditor to develop an audit plan for each individual financial audit. The INAO has no standard templates for audit plans for individual financial audits. The audit plans used by the INAO’s audit teams differ from each other. The audit plans that were used in the five financial audits reviewed during the peer review were not separate, complete documents. Often, parts of the planned audit steps and procedures were documented only in different parts of the audit management systems, not in a separate, comprehensive document. Some audits lacked some of the necessary elements of an audit plan, for example capacity, milestone planning and quality control measures. Furthermore, there is no procedure for formal approval of the audit plan by the appropriate “engagement partners” (ISSAI 1300), in the case of the INAO the financial audit director and the Auditor General; their involvement is informal and they are concerned chiefly with critical matters. There is therefore a risk that the responsible people are not fully

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11 See also ISSAI 11, principle 3: “SAIs should not be involved or be seen to be involved, in any manner, whatsoever, in the management of the organizations that they audit.”
informed about each audit plan, and are not able to make required changes in an audit easily once the audit has started. Although there is no standard audit plan, the use of Descartes and TeamMate means that some degree of standardization is in place: both these audit management systems (which differ from each other) require the use of some standard audit steps and procedures.

A second observation concerns the risk analysis used in the planning phase of individual audits (ISSAI 1315). In the five audits that were reviewed during the peer review risk analysis was used by the audit teams, but the relationship between the assessed risks according to the risk analysis and the choice of audit procedures (mix of tests of controls and substantive procedures) was not always clear. Often, a standard (substantive-procedures based) audit approach was chosen, with no clear relation to the assessed inherent and internal control risks. Moreover, inherent risks and internal control risks were not always assessed separately.

Furthermore, audit plans are not discussed with the auditees. The advantage of discussing (summaries of) audit plans with auditees is that it gives the auditee insight into the audit effort and improves the audit impact. The announcement of audit activities can trigger auditees in an early stage to direct their attention to improving the systems or procedures concerned.

A final observation concerns ISSAI 1240 on the auditor’s responsibilities relating to fraud in an audit of financial statements. According to this standard, there has to be a discussion about fraud risks in the planning phase among the engagement team members and also with the auditee. Also there has to be a determination by the engagement partner of how and where the entity’s financial statements may be susceptible to material misstatement due to fraud, including how fraud might occur. Such discussions did not always take place or were not properly documented in the audits subject to the peer review.

2.6 Quality control and assurance

The INAO is working hard to implement an ISSAI-proof quality control (QC) system for its financial audits. The INAO already has in place some QC instruments, but there is no written and defined QC effectively in use. INAO is in the process of implementing a more thorough ISSAI-proof QC system, but states that the scarcity of staff is a problem to implement
active and efficient QC measures (for example performing internal reviews). There is a QC document in draft, based on an IFAC-report on QC for small and medium enterprises. This draft is approved by the financial audit director, and now needs approval of the Auditor General. The challenge for the INAO, being a relatively small SAI, is to implement an adequate but at the same time feasible QC system.

The most important QC instruments used by the INAO before the start of the implementation of ISSAI1s were knowledge and experience: hiring adequate auditors (education, experience) and training auditors. Direct supervision by the division manager is also a QC instrument that is already in place; division managers are also part of the team for the larger audits. The INAO recently implemented a QC checklist to ensure the quality of each financial audit. Furthermore CPAs are responsible for the larger and more complex audits. Another measure is to review (although not always visibly so) all reports/accounts by the audit division manager, financial audit director and Auditor General. However, audit files are not reviewed by a qualified auditor outside the audit team; the INAO states that this is due to lack of staff.

In the "Report on transparency 2013" the following principal aspects of the QC system are given by the INAO: accountability for quality issues (all employees responsible; Auditor General ultimately responsible); independence and rules of conduct; approval of new and "business relationships"; personnel issues (sufficient staff, continuing education); success of auditing and other tasks (standard templates, forms, checklists); monitoring (supervision); documentation of working papers.

The QC system which has now been drafted generally contains the main elements of ISSAI 1220 on QC. The (visible) role of the engagement partner is crucial (approval of crucial decisions, like audit plan; supervision; review; etc.); this still has to be formalized. Some other important aspects that can be improved are standard templates (for example for audit plans) and reviewing of audit files by a qualified person outside the audit team.

Apart from these QC measures the INAO uses some quality assurance (QA) methods. External quality controllers visit the INAO to evaluate all audits performed by CPAs (latest visit was November 2010: Auditors Oversight Board). Furthermore, the INAO has hired an external audit firm
in the past (four years ago) to review working papers, to ensure that work was carried out in accordance with ISAs. Peer reviews are also QA instruments: in 1997 by the UK NAO and in 2013 by Dutch, Norwegian and Swedish SAIs.

2.7 Execution

Our review of five individual financial audits found that the audits were in general executed as planned. We did have some observations.

Firstly, we observed some unnecessary differences in the execution of the audits. There is room for more standardization in performing the audits. This observation is related to our observations on the lack of a standard audit plan and the use of two audit management systems.

Secondly, tests of internal control in the audits reviewed often seemed to be performed as a more or less separate audit activity, with the audit evidence needed to form an audit opinion being obtained chiefly by substantive procedures. See our earlier remark in section 2.5.2, where we stated that the risk analysis did not always identify a clear connection between the assessed risks according to the risk analysis and the choice of audit procedures (mix of tests of controls and substantive procedures); a standard (substantive-procedures based) audit approach was often chosen, with no clear relationship to the assessed inherent and control risks. If the internal control risk is low or medium, the auditor can rely partly on tests of controls to reduce the amount of substantive testing. Performing more tests of controls could also increase the audit impact: more findings on the functioning of internal control systems can lead to more recommendations for the auditees and eventually to a better functioning internal control system.

A positive development is the requirement of written representations from auditees (required by ISSAI 1580), although these are not yet used in all financial audits.

Finally, in some of the audits reviewed a lot of audit work was performed late in the audit cycle (spring of year n+1). Earlier execution of audit activities results in a better spread of the audit work across the audit cycle and gives the entities the possibility to correct errors before the financial year is over and the statements are produced.
2.8 Documentation and audit trail

The financial audit process is completely digitalized. All INAO’s employees have access to all files, which works efficiently but is also a risk (considered a small risk by the INAO).

The audits are documented in one of the audit management systems (Descartes or TeamMate), and partly outside of these two systems in an electronic file system (ONE) or on the harddisk of the INAO. Audit findings are recorded in the system by the auditor and reviewed and signed off by the audit manager. As noted above, the audit files are neither reviewed by the financial audit director nor by another auditor outside the audit team.

The peer review team concluded from the review of the five individual audits that, although the audit activities were in general well recorded in the files, in some instances not all audit activities performed were recorded in full and/or signed off by the audit division manager in the audit files (ISSAI 1230). It is important that the audit files contain sufficient information to allow an experienced auditor, not involved in the audit, to independently reconstruct how the audit opinion was formed.

2.9 Reporting

The INAO publishes one summarizing financial audit report on its financial audits in October/November n+1, including the opinion on true and fair view of the accounts. The report, called “The Audit of the Central Government Accounts”, contains a summary of all the financial audits performed during the year, the principal findings of these audits, and comments. There are no findings per ministry or audit object, just an overall opinion on the accounts and a summary of the most important findings.

The report could be considered somewhat lengthy, but the main conclusions and recommendations are presented separately in the beginning of the report. In the main text of the report the more important findings and conclusions and the less important ones are not always clearly distinguished. There is no written procedure to weigh the findings (how findings affect the overall opinion).

The INAO requests the auditees to respond to audit findings and conclusions/recommendations\(^{12}\) presented in the annual report. The

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\(^{12}\) There are various terms for this procedure, like “contradictory procedure”, “adversarial (or) adversary procedure”, “bilateral discussion procedure. This procedure means that (draft) audit
Ministry of Finance and the State Accounting Office receive the draft report for comments. Comments are given verbally, not in writing. The responses to the main conclusions and recommendations are not incorporated in the report.

The Auditor General presents the report to the Budget Committee of Parliament in person. The Budget Committee has issued opinions on the INAO's reports in recent years. They contain questions and attention points for the government. This procedure gives the report more impact, which is a positive development.

The INAO issues a press release, with a summary of the most important findings, and publishes the report on its website. The INAO does not organize briefings.

Finally, the timeliness of publishing the annual report is important. The Budget Committee of Parliament needs to receive the report as soon as possible; publication in November, as occurred in 2012, is (too) late.13 Late publication reduces impact. The INAO tries to publish its annual report as soon as possible after the summer holiday period (it aims at early October) but sometimes the publication takes longer than planned, which is due sometimes to external factors (delay in accounts).

For individual financial audits a report is drafted, auditees are requested to respond to audit findings and conclusions/recommendations (but only in the case of the larger audit objects), and a final report is sent to the auditee and a copy to the ministry involved. The response of the auditee to the main conclusions and recommendations is not incorporated in the final report. The minister is not accountable for agencies and other entities under his/her remit so only copies of individual (final) reports are send to the minister (there is no ministerial response to the audit findings and conclusions/recommendations).

It is also important to note that the individual reports are not published. There is no standard format (template) for all kinds of reports, although there is a standard format for A-part audit reports and many reports have the same construction. Most of the five reports reviewed were generally in agreement with the ISSAIs (400 and 1700), although some requirements were not yet fulfilled. The responsibilities of the auditor and the auditee, for example, were not explicitly mentioned in the reports.

All reports/accounts are reviewed by the audit division manager, financial audit director and the Auditor General (although these reviews are not always visibly recorded in the audit files; ISSAI 1230).

13 In 2013 the 2012 Annual Report was published early October.
According to the ISSAI 300 (ISSAI 400, section 7) the contents of audit reports should be easy to understand and free from vagueness or ambiguity, include only information which is supported by competent and relevant audit evidence, and be independent, objective, fair and constructive. The five individual audit reports reviewed contained the audit findings, but there was (too) much focus on the audit procedures performed by the INAO, which made the reports very descriptive. There was no clear link between the main audit objectives/questions, standards/norms, findings, conclusions and recommendations (for example in table form). Findings were not quantified. There was not always a distinction between the main (more serious) findings and conclusions and the less important findings and conclusions in each individual audit report, although in A-part audit reports the standard practice is to summarize major findings at the end of each report. Finally, there is no audit action list for each financial audit. There is no written procedure to follow up the audit findings, but the INAO does document a compilation of major findings to be used in the risk analysis for the following year. The major findings are also summarized at the end of the published summary annual financial audit report.

14 According to the INAO their reports are already much less descriptive than a decade ago.
3 Conclusions and recommendations

3.1 Introduction

In this chapter the peer review team presents its answers to the three main peer review questions:

- What is the quality of the INAO’s financial audits and to what extent are they in accordance with INTOSAI standards?
- What recommendations can be given to the INAO to improve the quality of its financial audits?
- How can the INAO’s risk assessment concerning the financial audits be improved, to reduce the audit gap?

Once again we would like to stress the nature of our conclusions and recommendations. Critical conclusions should not be interpreted as shortcomings per se, but as comparisons with the extensive INTOSAI Standards (ISSAIs). The INAO is still in the process of adopting ISSAIs and is not finished yet. Implementing ISSAIs is a major challenge to all SAIs and especially to relatively small SAIs such as the INAO. Critical conclusions and accompanying recommendations should be interpreted in this light as observations that the INAO could use to bring its financial audit practice further into line with the INTOSAI standards.

3.2 Main conclusion

Our main conclusion is that the INAO is doing a good job in its financial audit practice and is well on the way to adopt the ISSAIs, but is not there yet. The peer review team sees possibilities to enhance the quality of the INAO’s financial audits further and to comply more fully with the ISSAIs.

Below we present some more detailed conclusions, accompanied by recommendations.
3.3 Specific conclusions and recommendations

3.3.1 In general

Firstly, we conclude in general that the INAO faces some major challenges in its financial audit practice. Some of the main challenges are:

- The INAO is not able to audit all audit objects every year and for this reason uses a risk-based selection of audit objects in order to (1) cover sufficient audit objects to be able to issue its annual audit opinion; and (2) audit every audit object at least once every three years. It is difficult for the INAO to audit every audit object effectively every three years. On the other hand the INAO is able to outsource some of its audit work and the INAO performs some tasks that are not obligatory, such as preparing accounts before auditing them and issuing non-obligatory annual audit opinions to auditees on request.
- The INAO is in the process of adopting ISSAIs, which means it has to invest extra time (changing audit methods and procedures, educating staff, preparing manuals, performing quality control measures, performing additional (obligatory) audit activities, etc.).
- The INAO has stated that it has experienced a reduction in staff and difficulty hiring CPAs in recent years.

Recommendation:

We recommend that the INAO formulates a strategy, including a time schedule, that effectively deals with these challenges:

- which measures, prescribed by the ISSAIs, have to be implemented (when) with priority (ISSAI implementation plan)?
- which audit tasks must the INAO perform itself and which audit tasks can be outsourced?
- which activities can be ended?
- what capacity (in quantity and quality terms) is needed?

This strategy can also be used for communication with Parliament.

Further to this general conclusion and recommendation, we present more specific conclusions and recommendations for each of the subjects of the peer review: institutional context, organization of the financial audit practice, audit objects, planning/risk analysis, quality control and assurance, execution, documentation and audit trail, reporting.
3.3.2 Institutional context

With regard to the institutional context we conclude that the INAO is obliged to perform some audit tasks that are unusual for many SAIs, such as monitoring the execution of the Budget (in many countries a task for the ministry of Finance). We also conclude that the INAO performs a (non-obligatory) role that is unusual for SAIs: helping smaller entities prepare their accounts before auditing them. The INAO has started the challenging implementation of the ISSAIs voluntarily, in anticipation of their intended obligatory adoption of these standards after implementation of the new National Audit Act. Finally we conclude that the INAO is not obliged to issue an opinion on the legality and regularity of financial transactions underlying the annual accounts.

Recommendation:
In view of the size of the INAO, we recommend that the INAO effectively utilizes its resources on only its core tasks and challenges. If possible, the INAO should discuss the necessity of its non-typical roles with Parliament, such as monitoring the execution of the Budget.

3.3.3 Organization of the financial audit practice

Regarding the organization of the financial audit practice we conclude that:

- the financial audit practice is logically positioned in the organization;
- the capacity is relatively small and has been reduced recently (the INAO experiences a shortage of staff);
- hiring CPAs and auditor rotation are difficult;
- the audit process is being revised and Financial Audit Guidelines are being prepared as part of the ISSAI implementation;
- the INAO uses two audit management systems, which can lead to inefficiency and differences in executing and documenting audits;
- the INAO outsources some of its audit tasks (5% of expenditures of A-part and the majority of entities of B-E-part of the Budget) and – concerning outsourced audits regarding A-part of the Budget - relies on the work of these hired external auditors without reviewing the quality of their work and the appropriateness of their reports and opinions.

Recommendation:
We recommend that the INAO further implements the Financial Audit Guidelines in accordance with the ISSAIs, considers switching to one audit management system for efficiency and consistency reasons, and –

15 As stated before this is not a task of the Financial Audit Department.
the case of audits regarding A-part of the Budget - reviews the work of hired external auditors in line with the ISSAIs. The experienced shortage of staff should be addressed in the aforementioned strategy and discussed with Parliament and other stakeholders.

3.3.4 Audit objects

The INAO has to audit a large amount (in 2012 a total of 471) of audit objects, too many to audit every year, given its capacity. The INAO therefore uses a risk-based selection of audit objects and aims to audit all audit objects at least once every three years. Further conclusions and recommendations on this subject are presented below (overall audit planning).

3.3.5 Planning/risk analysis

Planning the financial audits is one of the most crucial phases of the INAO’s financial audit practice.

With regard to the overall audit planning we conclude firstly that risk-based selection of audit objects, based on ten risk factors, is a necessity, but might become more risk-based by giving greater weight to all risk factors (in practice the selection is mainly based on scope of expenditures). We also conclude that the INAO is experiencing difficulties in realizing its aim of auditing all audit objects once every three years, according to the INAO because of a shortage of resources (staff and funds). Furthermore, the INAO has started (2013) auditing similar, smaller audit objects (like schools) as groups, which could lead to more audit efficiency, and is considering outsourcing more audit tasks. Finally, the INAO still performs some non-obligatory services (as noted above), which means less capacity for obligatory tasks, although the INAO has started (2013) to reduce these services.

Recommendation:

We recommend that the INAO makes its selection of audit objects more risk-based, audits similar audit objects as groups, considers a further reduction of its non-obligatory activities, and reconsider its outsourcing strategy.

If there is an increase in the number of internal audit departments at audit objects, we also recommend that the INAO ascertains whether it can use the work of these internal auditors in accordance with ISSAI 1610.
The peer review team feels it is essential that the INAO realizes its aimed audit coverage, either by making sure it can reach its target of “all audit objects once every three years”, or by revising this target (“all audit objects once every x years”). In this context it should be kept in mind that the INAO will need to dedicate part of its existing capacity to comply fully with ISSAIs (see other recommendations). Finally, with respect to the outsourcing strategy, we have two recommendations. Firstly, it could be argued that some amount of reviewing the work of hired external auditors for audits regarding A-part of the Budget is necessary according to the ISSAIs (1600), so some capacity should be reserved for this activity. Secondly, the INAO should choose between efficiency purposes (for example, outsource all audit work outside of A-part of the Budget) and knowledge purposes (retain some audits in B-E parts of the Budget to preserve knowledge of auditing audit objects outside of A-part of the Budget). The peer review team would favour auditing audit objects in all parts of the Budget to preserve knowledge.

With regard to the individual audit planning we conclude firstly that the INAO does not use standard templates for audit plans and that the audit plans it does use are diverse and documented partly in separate documents and partly in the audit management systems. Secondly, the involvement of the engagement partners (financial audit director and Auditor General) and the resulting approval of the audit plan are not formally arranged yet. Audit plans are not discussed with auditees. Furthermore, the risk analysis and the attention to the risk of fraud in the audit planning phase can be improved.

Recommendation:

We recommend that the INAO develops a standard template for audit plans in accordance with the ISSAIs, develops and uses standard audit programs/checklists (customized for every audit) wherever possible, formalizes the role of the engagement partners and the approval of audit plans, discusses audit plans with auditees, and improves the risk analysis and attention to fraud risk.

3.3.6 Quality control and assurance

The ISSAIs give special emphasis to quality control and assurance. We conclude that the INAO is working hard to implement quality control (QC) measures and has finished a draft QC system, which now has to be fully implemented. Not all necessary QC measures were in place yet during the peer review. An important omission yet is the absence of reviews of audit
files by auditors outside the audit team and the formal (visible) involvement of the engagement partners in signing off crucial phases and documents. The INAO states that the scarcity of staff is a problem in realizing an ISSAI-proof QC system. The INAO has implemented some quality assurance methods, such as reviews by external parties.

**Recommendation:**
We recommend that the INAO further implements its developed quality control system and in addition formally arranges reviews of audit files by auditors outside the audit teams and visible involvement of the engagement partners in crucial phases of the audits. The INAO could consider forming a pool of senior auditors to review the work of audit teams. We also recommend to arrange that an outside party performs an external quality assurance review every two to four years.

### 3.3.7 Execution

With respect to the execution of financial audits we conclude that in general the audits reviewed were executed as planned, although some improvements were possible with regard to standardization in performing audits, the use of tests of controls, and, perhaps, the period in which audit work is performed.

**Recommendation:**
We recommend that the INAO considers, where possible, further standardization of audit procedures, more extensive use of tests of controls, and performance of audit procedures earlier in the audit cycle.

### 3.3.8 Documentation and audit trail

Regarding documentation and audit trail we conclude that the audits are in general well documented in the two audit management systems, although the audit files are not reviewed by auditors outside the audit team (see quality control) and in some instances not all performed audit activities were completely recorded and/or signed off in the audit files.

**Recommendation:**
We recommend that the INAO makes sure audit files of all performed financial audits are complete and internally reviewed and signed off.
3.3.9 Reporting

Finally, with respect to reporting, the INAO publishes one overall financial audit report and issues (not publishes) audit reports on all individual audits.

With regard to the overall annual report we conclude that:

- the overall annual audit report can be considered somewhat lengthy, contains a summary of the major findings of all financial audits performed, and in the main text does not always distinguish between the more important findings and the less important ones;
- auditees are requested to respond to audit findings and conclusions/-recommendations, but comments are not required in writing and the responses of auditees to the main conclusions and recommendations are not incorporated in the report;
- the report is used extensively by Parliament (the Budget Committee issues an opinion on the report);
- publication of the report is sometimes late, sometimes because of external factors, which reduces the impact.

With regard to the audit reports on individual audits we conclude that:

- the reports are not published, but sent to the auditee and a copy to the ministry concerned;
- the reports generally contain most of the contents required according to ISSAIs, with some exceptions;
- there is no standard report (template) for all reports (although there is a standard format for A-part audit reports and many reports have the same construction);
- all reports are reviewed by the engagement partners (both financial audit director and Auditor General), although not always visibly so in the audit files;
- the reports are often very descriptive, with (too) much focus on audit activities performed, do not contain a clear link between main audit objectives/questions, standards/norms, findings, conclusions and recommendations, and do not always clearly distinguish between the more important and the less important findings (although in A-part audit reports the standard practice is to summarize major findings at the end of each report);
- auditees are requested to respond to audit findings and conclusions/-recommendations in individual reports, but only for the larger audit objects; also the ministries are not involved in this procedure, and the responses of auditees to the main conclusions and recommendations are not incorporated in the report;
• the reports do not contain an audit action list and there is no written procedure to follow up audit findings.

Recommendation:
We recommend that the INAO further enhances the impact of its reports by developing a standard report (template) presenting all contents required by ISSAIs, by making the reports more concise and less descriptive and by clearly distinguishing between the more important and the less important findings and conclusions.
The procedure of requesting auditees to respond to audit findings and conclusions/recommendations could also be expanded by requiring this procedure for all audit objects audited and by incorporating the auditees’ responses to the main conclusions and recommendations in the reports (with an afterword by the INAO).
Incorporating an audit action list in all reports safeguards the follow up to audit findings in subsequent years.
The timely publication of the overall annual audit report would raise the impact.
4 Response of INAO

The Auditor-General of Iceland responded to the draft report in his letter of December 9th 2013.

“The INAO welcomes the report of the international peer review on the Office's financial audit practice. On the whole the report gives a fair and balanced view of the Office's practices. As stated in the report, the INAO started implementing International Standards of Supreme Audit Institutions (ISSAI) for its financial audit activities in 2011. This process is currently reaching its final stages. The report points out several opportunities for improvement in the INAO's financial audit approach and working methods, based on the ISSAI. The Office will carefully study the report's recommendations and make use of them in bringing the implementation process to a successful completion. When this goal has been reached the Office will continuously monitor its financial audit activities to ensure compliance with the standards.

The INAO is of the opinion that the report contains valuable information and that the peer review has served its main purpose, i.e. to assist the Office in improving the quality of its work. But it should be kept in mind that the speed of improvement will to a large extent be dependent upon the level of funding allocated to the Office by Althingi. Finally, the INAO and its Financial Audit Department wish to extend their sincere gratitude to the peer review team for their meticulous and professional work which has been and will, going forward, be of great benefit to the Office.”

The peer review team would like to thank the Auditor General for this positive response and the friendly words. Of course we share these words with our team members from the Norwegian and Swedish National Audit Offices, with whom we enjoyed working together. We are pleased to have been able to contribute once more to the further strengthening of the policy of the INTOSAI community to help each other move forwards through peer reviews. It is a worthwhile learning experience both for the reviewed SAI as for the reviewing team member SAIs. We hope that the INAO will consider initiating a follow-up peer review, for example after a
period of five years, to assess the improvements made regarding the financial audit practice.

On behalf of the team,
Kees Vendrik,
Vice-president Netherlands Court of Audit.
Annex 1: Audit methodology used in the peer review

The peer review team developed a questionnaire based on previous experience with peer reviews and relevant ISSAI. The questionnaire consisted of two parts:

- a general questionnaire financial audit approach (A), which was completed on the basis of INAO documents, presentations by INAO staff members, interviews with INAO staff members and external stakeholders, and observations;
- a checklist for reviewing five individual financial audits (B), which was completed on the basis of reviews of audit files, interviews with INAO auditors and auditees, and observations.

The five selected individual financial audits were:
- Landspítali Háskólasjúkrahús (The State Hospital);
- Háskóli Íslands (Icelands University);
- Icelandic Health Insurance (benefits);
- RARIK (an energy company wholly-owned by the state);
- Ministry of Environment and Natural Resources.

See annex 2 for a list of interviewed organizations.

**Questionnaire A** covered the following subjects and questions (the questionnaire summarized the relevant ISSAI):

**Institutional context/laws and regulations**

A-1. What is the institutional context of the FA practice (laws, regulations, endorsement of ISSAI etc)?
- Which laws and regulations regulate the FA-function of the INAO
- What is the formal task of the INAO regarding FA according to laws and regulations?
- What are the main rules regarding FA according to the laws and regulations?
- Does the INAO comply (fully or partly) with INTOSAI standards?
- To what extent does the INAO endorse the basic principles of ISSAI 100?

**Organisation/audit process**

A-2. How is the FA practice organized?
International Peer Review of the Financial Audit Practice of the Icelandic National Audit Office

- Is the entire audit process clearly structured and are the roles of all those involved defined clearly and transparently?
- Is the audit process documented in a standard audit manual?
- What are the main phases of the FA process?
- How many employees are involved in FA?
- Are the auditors qualified and independent and how is this documented?
- Is the budget sufficient to perform all FA’s needed?
- Does the INAO perform all FA’s itself or does it hire external public audit firms or external experts?
- Are the FA’s performed according to a standard approach/checklists, or are (some or all) FA’s custom made?
- What audit methodologies are used?

**Audit objects**

A-3. What audit objects are subject to FA’s by the INAO?
- Which are the auditees/audit objects of the FA’s, and where and by whom is this determined (legislation, etc)?
- Are all audit objects audited each year? If not, how does INAO decide which audit objects are selected?
- Is the INAO capable of auditing all audit objects on a regular basis?

**(Overall) risk analysis/planning**

A-4. How does the INAO plan its FA’s (overall) and to what extent does the INAO base its planning on risk analysis?
- How does the INAO plan its FA’s each year?
- Does the INAO annually formulate an overall audit strategy/plan for all FA’s, and audit plans/programmes for all individual FA’s?
- Are audit objects selected on the basis of an annual government wide risk analysis?
- Is the audit approach of each individual FA based on a risk analysis?
- To what extent does the standard planning approach take into account the demands of ISSAI 300 (1.3)?
- What planning arrangements are implemented to safeguard the (efficient and timely) execution of the planned FA’s?

**Quality control/assurance**

A-5. What quality control system is used by the INAO?
- Has the INAO implemented a quality control system for the FA practice?
- If yes, what quality control measures are in place?
- Are all planned quality control measures actually performed in this audit cycle?
- Does the quality control system contain the requirements as mentioned by ISSAI 1220, especially ethical requirements, team assignment and engagement performance (supervision, review)?
**Documentation/audit trail**

A-6. How does the INAO safeguard adequate documentation of the FA’s (audit trail)?
- How is the planning, execution and reporting of the FA’s documented?
- Does the INAO use one or more (digital, paper) information system for documenting purposes?
- How does the INAO safeguard a complete audit trail?
- Does the audit documentation system comply with the requirements as mentioned by ISSAI 1230?

**(Overall) reporting/communication/follow-up**

A-7. How is the reporting process of FA’s organized by the INAO and to what extent is the follow up of audit findings checked?
- How does the INAO organize the reporting phase?
- Are standard formats used for reports?
- Does the INAO report only findings or also recommendations?
- Are draft reports internally reviewed before submitting to auditees?
- Are draft reports submitted to auditees in a contradictory procedure (“check the facts”)?
- To what stakeholders are final reports submitted and are the reports published externally?
- Are audit findings listed in a “audit action list” and does the INAO perform follow up audits in later years?
- Does the INAO present its reports to Parliament or other bodies in person?
- In what other ways are the results of the FA’s brought to the attention of relevant actors?

**Questionnaire B** covered the following subjects and questions (the questionnaire summarized the relevant ISSAIs):

**Planning**

B-1. Is the planning of the selected FA adequate?
- Are the engagement partner and other key members of the engagement involved in planning the audit, including planning and participating in the discussion among engagement team members? (ISSAI 1300.5)
- Does the INAO use any information collected during previous audits to help it estimate adequately resources and timeframe of the audits?
- When planning this audit did the INAO formulate an overall audit strategy and has the INAO developed an audit plan and audit programme (incl. checklists)? (ISSAI 1300.2)
- Were the following activities undertaken at the beginning of the current audit engagement (ISSAI 1300.6):
  - performing procedures regarding the continuance of the client relationship and the specific audit engagement (if applicable);
  - evaluating compliance with relevant ethical requirements including independence;
  - establishing an understanding of the terms of the engagement?
• Is there an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan? (ISSAI 1300.7)

• Is there an audit plan that includes a description of:
  o the nature, timing and extent of planned risk assessment procedures, as determined under ISA 315;
  o the nature, timing and extent of planned further audit procedures at the assertion level, as determined under ISA 330;
  o other planned audit procedures that are required to be carried out so that the engagement complies with ISA? (ISSAI 1300.9)

• Did the overall audit strategy change during the year? If yes did the auditor update and change the overall audit strategy and the audit plan? (ISSAI 1300.10)

• Did the auditor plan the nature, timing and extent of direction and supervision of engagement team members and the review of their work? (ISSAI 1300.11)

• Are risk assessment procedures performed to provide a basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels? (ISSAI 1315.5)

• Are the following included in the risk assessment procedures:
  o inquiries of management, and of others within the entity who in the auditor’s judgment may have information that is likely to assist in identifying risks of material misstatement due to fraud or error;
  o analytical procedures;
  o observation and inspection? (ISSAI 1315.6)

• Did the auditor consider whether information obtained from the auditor’s client acceptance or continuance process is relevant to identifying risks of material misstatement? (1315.7)

• Did the engagement partner and other key engagement team members discuss the susceptibility of the entity’s financial statements to material misstatement and the application of the applicable financial reporting framework to the entity’s facts and circumstances? (ISSAI 1315.10)

• Did the auditor obtain an understanding of the following:
  o the entity and her surroundings (ISSAI 1315.11);
  o the entity’s internal control (1315.12);
  o nature and extent of the understanding of relevant controls (ISSAI 1315.13);
  o control environment (ISSAI 1315.14);
  o the entity’s risk assessment process (ISSAI 1315.15);
  o the information system, including the related business processes, relevant to financial reporting (ISSAI 1315.18);
  o control activities relevant to the audit, being those the auditor judges it necessary to understand in order to assess the risks of material misstatement at the assertion level and design further audit procedures responsive to assessed risks (1300.20);
  o the major activities that the entity uses to monitor internal control over financial reporting, including those related to those control activities relevant to
the audit, and how the entity initiates remedial actions to deficiencies in its
controls? (ISSAI 1315.22)

- Did the auditor identify and assess the risks of material misstatement at:
  - the financial statement level;
  - the assertion level for classes of transactions, account balances and disclosures;
  to provide a basis for designing and performing further audit procedures? (ISSAI
1315.25)

- Did the auditor determine materiality for the financial statements as a whole, and/or to
classes of transactions, account balances or disclosures? (ISSAI 1320.10)

- Did a discussion took place among the engagement team members and a determination
by the engagement partner of how and where the entity’s financial statements may be
susceptible to material misstatement due to fraud, including how fraud might occur? (see
also ISSAI 1240)

- Is the resulting audit plan/programme (incl. checklists) appropriate for the audit (audit
object, risks assessed) and are all necessary audit procedures (substantive procedures
(tests of details and substantive analytical procedures) and tests of controls) taken into
account? (ISSAI 1330; see B-2)

**Execution**

B-2. Is the execution of the selected FA adequate?

- Was the execution of the audit properly supervised?
- Have all planned audit activities according to audit plan/programme been performed
completely?
- Are all audit programmes/checklists completely filled in?
- What problems have arisen during the audit and how have they been solved?
- Has the FA been completed in time?
- Are the planned man hours realized?
- Are the audit files accessible and comprehensible and is all required audit documentation
documented in the files?
- Is the audit trail in the audit files sufficient?
- Has an internal review been performed, timely?
- Was the audit file signed off by the appropriate audit manager?
- (In case of using the work of other auditors or experts:) Is the work of other auditors or
experts adequately reviewed before using it? (ISSAI 1610-1620)
- Did the INAO properly perform the planned audit procedures (substantive procedures
(tests of details and substantive analytical procedures) and tests of controls) (ISSAI
1330)?
- Did the INAO adequately respond to assesses risks (ISSAI 1330)?
- Did the INAO request written representations from auditees (ISSAI 1580)?

**Reporting**

B-3. Is the reporting of the selected FA adequate?

- Does the auditor’s report clearly communicate:
  - title;
Does the report contain a clear opinion in the form of a (standard) audit opinion?

Are reported audit issues properly analysed and concluded?

Have all audit findings been evaluated as to their materiality, legality and factual evidence and all relevant material findings included?

Are all the facts fairly presented?

Are sources of facts, figures and quotations mentioned?

Is there documentary evidence in support of all conclusions and opinions?

Is there a clear audit trail for audit steps, findings, conclusions and recommendations prepared by the auditor and his assistants?

Are all key auditors and audit managers involved in drafting the report?

Is the draft audit report internally reviewed before submitting to the auditee?

Is there any clear statutory provision and internal guidance as to who has the authority to approve and issue the audit report (audit manager, audit panel, other)?

Is the draft audit report, after internal review, provided to the audited body for review and comment within a specified time frame?

To what extent are comments received from an audited body taken into account by the INAO, and are these comments published in the report?

Is the report published externally? If so, are those publications elaborated with a view to being understandable to users of the report and to the general public?

Did the INAO publish a press release?

In what form are the reports distributed (paper, digital) and does the INAO publish on the internet as well?

Are audit findings listed in a “audit action list”?

Is there adequate and sufficient monitoring that audit recommendations are followed up in due course?

Is the report presented to Parliament or other bodies in person?

In what other ways are the results of the FA brought to the attention of relevant actors?
Annex 2: Stakeholders interviewed

Parliament:
- Budget Committee (staff members)

Audited entities (staff):
- State Hospital (Landspítali Háskólasjúkrahús)
- RARIK (Energy Company)
- Ministry of Environment and National Resources

INAQ:
- Auditor General
- Financial audit director
- Financial audit division managers
- Auditors

Other stakeholders:
- Ministry of Finance
- State Accounting Office
Annex 3: Members of the peer review team

*Riksrevisjonen (Office of the Auditor General of Norway):*
Eva Maria Simma, senior audit advisor

*Riksrevisionen (Swedish National Audit Office):*
Eirikur Einarsson, audit director

*Algemene Rekenkamer (Netherlands Court of Audit):*
Thomas Meijer, audit director
Paul Neelissen, senior auditor (CPA)
Carl Roest, audit manager (CPA)