

# 2019 Audit and Review Guidelines

Water Licences

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**Economic Regulation Authority**

WESTERN AUSTRALIA

D249868

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# 1. Overview

The *Audit and Review Guidelines: Water Licences* inform water licensees and external auditors about the Economic Regulation Authority's requirements for conducting operational audits (audits) and reviewing asset management system (reviews).

The guidelines describe the framework auditors<sup>1</sup> must use to assess the effectiveness of the measures taken by licensees to meet the conditions of their licence and manage their assets. The framework uses a risk-based approach to focus audits and reviews on high-priority areas. It also uses common rating scales to rate licensees' performance so the ERA can compare the performance of individual licensees and groups of licensees over time.

The ERA has published separate guidelines for energy and gas licensees<sup>2</sup> due to the different legislative framework for their audits and reviews.<sup>3</sup>

## 1.1 Compliance with these guidelines

Audits and reviews that commence on or after the date the ERA publishes these updated guidelines must follow these guidelines.<sup>4</sup>

## 1.2 Mandatory auditing requirements

To ensure consistency of reporting on audits and reviews, the guidelines include many mandatory requirements for auditors and licensees. For example, auditors must:

- Adopt a risk based approach to auditing using the risk evaluation model set out in AS ISO 31000:2018.
- Use the compliance rating scales, set out in Table 6, to assess compliance with licence conditions.
- Use the process and policy, and performance rating scales, set out in Tables 9 and 10, to assess the effectiveness of the asset management system.
- Ensure their audit and review plans comply with Chapter 3.
- Ensure their audit and review reports comply with Chapter 5.

Licensees must prepare post-audit and post-review implementation plans that comply with section 5.3 of this document.

The words 'must' and 'requires' in these guidelines are used to identify mandatory requirements.

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<sup>1</sup> The *Water Services Act 2012* requires audits and reviews to be undertaken by an 'independent expert'. The guidelines use the term 'auditor' for the independent expert that undertakes the audit or review.

<sup>2</sup> [Audit and Review Guidelines: Electricity and Gas Licences](#).

<sup>3</sup> The *Electricity Industry Act 2004* and the *Energy Coordination Act 1994* place the responsibility for appointing auditors on the licensee.

<sup>4</sup> The commencement date for an audit or review is the date the ERA appoints the auditor.

## 1.3 Audit principles

The guidelines include several references to the principles outlined in the Auditing and Assurance Standards Board's *Australian Auditing Standards* and *Standards on Assurance Engagements* (audit principles). While these standards have been developed by the AASB for the accounting profession, the audit principles also apply to audits and reviews.

Auditors must apply the audit principles to their audits and review. The standards allow auditors to use their professional judgment when applying the audit principles to audits and reviews.

## 1.4 Regulation of audits and reviews

The *Water Services Act 2012* (Water Act) sets out conditions for audits and reviews. Water licences also include conditions for audits and reviews.

### 1.4.1 Legislative licence conditions

Under the Water Act,<sup>5</sup> it is a condition of every licence that the licensee provides the ERA with:

- An operational audit conducted by an independent expert appointed by the ERA at least once in every period of 24 months (or any longer period that the ERA allows).
- A report by an independent expert engaged by the ERA as to the effectiveness of the asset management system at least once in every period of 24 months (or any longer period that the ERA allows).

Regular audits by an independent expert (auditor) provide a level of assurance that the licensee is complying with the conditions of its licence.<sup>6</sup>

Regular reviews by an auditor provide a level of assurance that the licensee is maintaining an effective asset management system.

The ERA must provide a copy of the audit or review report to the Minister within two months of receiving it.<sup>7</sup>

### 1.4.2 Other licence conditions

Water licences also include conditions for the conduct of audits and reviews.<sup>8</sup>

One of those conditions is that licensees must cooperate with the auditor and comply with these guidelines.

<sup>5</sup> Sections 24 and 25 of the Water Act.

<sup>6</sup> The term 'operational audit', or 'audit', in these guidelines should not be confused with an audit performed by the Department of Health under the Memorandum of Understanding (MoU) that applies between the licensee and the Department as a condition of a licensee's potable water licence.

<sup>7</sup> Regulation 7(2) of the *Water Services Regulations 2013*. The ERA must also prepare a report for the Minister on the audit or review report setting out the ERA's opinion on the auditor's findings and the recommendations the ERA has made, or proposes to make, and the actions the ERA has taken, or proposes to take, in response to the audit or review report.

<sup>8</sup> The ERA publishes all [water licences](#) on its website.

## 1.5 Purpose and scope

Audits and reviews have a separate and distinct purpose and scope.

### 1.5.1 Audits

The purpose of an audit is to assess the effectiveness of measures taken by the licensee to meet the conditions of its licence (licence obligations<sup>9</sup>).

An audit should focus on the systems and processes used to ensure compliance with the standards, outputs and outcomes required by the licence.

The scope of the audit must consider:

- **Process compliance** – the effectiveness of systems and procedures in place throughout the audit period, including the adequacy of internal controls.
- **Outcome compliance** – the actual performance against standards prescribed in the licence throughout the audit period.
- **Output compliance** – the existence of the output from systems and procedures throughout the audit period (specifically, proper records which provide assurance that procedures are consistently followed and controls are maintained).
- **Integrity of reporting** – the completeness and accuracy of the compliance and performance reports provided to the ERA.
- **Compliance with any individual licence conditions** – the actual performance against the requirements imposed on the specific licensee by the ERA or specific matters raised by the ERA.

The audit report should identify areas of non-compliance and recommend corrective action as necessary.

### 1.5.2 Reviews

The purpose of a review is to assess the licensee's asset management system, which includes the asset management plan, and the staff and IT resources that support the plan.

An asset management plan sets out the measures the licensee will take to properly operate and maintain assets. The plan must detail the licensee's business strategies to ensure it maintains an effective asset management system over at least a five-year period.

The scope of the review must include an assessment of the adequacy and effectiveness of the asset management system by evaluating the following asset management processes:<sup>10</sup>

- asset planning
- asset creation/acquisition
- asset disposal
- environmental analysis

<sup>9</sup> This includes general licence conditions, individual licence conditions (conditions specific to the licensee), and legislative obligations called up by the licence (the [Water Compliance Reporting Manual](#) lists the legislative obligations called up by the licence).

<sup>10</sup> Appendix 4 provides more information about asset management processes.

- asset operations
- asset maintenance
- asset management information system
- risk management
- contingency planning
- financial planning
- capital expenditure planning
- review of the asset management system.

In addition to evaluating each asset management process, auditors must evaluate and report against each of the effectiveness criteria in Table 23.<sup>11</sup>

## 1.6 Risk-based approach to audits and reviews

### 1.6.1 Risk assessment

Auditors must apply a risk-based approach to planning and conducting audits and reviews.

Auditors must determine the audit or review priority for each licence obligation or asset management process by assessing the relevant risk factors and controls in place. Auditors should focus the audit or review on higher priorities, with less extensive coverage of medium and lower priorities.

To achieve consistency of risk assessment across the different utility sectors and licences, auditors must use the risk evaluation model<sup>12</sup> described in Appendix 3.

Section 3.2.3 includes more information about the method auditors must use for assessing risk and determining audit and review priorities.

### 1.6.2 Assurance engagements

Once the auditor has assessed the audit or review priority for each licence obligation or asset management process, the auditor must assess if the licensee has complied with its licence obligations or has an effective asset management system.

#### 1.6.2.1 Audits

When assessing if a licensee has complied with its licence obligations, the auditor must apply a level of scrutiny that corresponds to a 'reasonable assurance engagement'. A reasonable assurance engagement is:

An assurance engagement in which the assurance practitioner reduces engagement risk to an acceptably low level in the circumstances of the engagement as the basis for the assurance practitioner's conclusion. The assurance practitioner's conclusion is

<sup>11</sup> Auditors are not obliged to use Table 23 as the basis for their evaluation of the effectiveness criteria. For example, they may instead review the licensee's operations against ISO 55000 (Asset management — Overview, principles and terminology). However, auditors must always report their findings against the 12 asset management processes, and associated criteria, set out in Table 23.

<sup>12</sup> The risk evaluation model is based on AS ISO 31000:2018.



expressed in a form that conveys the assurance practitioner's opinion on the outcome of the measurement or evaluation of the underlying subject matter against criteria.<sup>13</sup>

### 1.6.2.2 *Reviews*

The auditor may perform a review of the asset management system at the lower level of scrutiny of a 'limited assurance engagement'.<sup>14</sup> A limited assurance engagement is:

An assurance engagement in which the assurance practitioner reduces engagement risk to a level that is acceptable in the circumstances of the engagement but where that risk is greater than for a reasonable assurance engagement as the basis for expressing a conclusion in a form that conveys whether, based on the procedures performed and evidence obtained, a matter(s) has come to the assurance practitioner's attention to cause the assurance practitioner to believe the subject matter information is materially misstated.<sup>15</sup>

Auditors should not perform a limited assurance engagement if:

- The review is the first review for the licensee.
- The previous review identified serious deficiencies.
- The licensee has made material changes to its asset management system since the previous review.

In these cases, auditors should perform a reasonable assurance engagement.

Auditors must indicate in the review plan whether they intend to perform a limited or reasonable assurance engagement.

### 1.6.3 *Areas of special focus*

The ERA may direct a licensee to require the auditor to assign a higher audit priority to specific licence obligations, asset management processes, effectiveness criteria, or the inspection of specific asset infrastructure (area of special focus).

The ERA will usually select an area of special focus in response to information obtained from a range of sources, including previous audits or reviews, annual compliance reports, media reports or referrals from other government agencies. An area of special focus may also examine the licensee's compliance with legislation that has been introduced or amended since the previous audit or review.

<sup>13</sup> Paragraph 12(a)(i)(a) of ASAE 3000.

<sup>14</sup> Although auditors may perform a limited assurance engagement for reviews, they should review asset management processes and criteria that have been assigned a review priority of 1, 2 or 3 (refer to section 3.2.3) at a higher level of scrutiny. Auditors should describe in the observations section of the report the audit procedures they used to support their findings. Reviewing one or more processes or criteria at a higher level of scrutiny does not preclude auditors from providing a 'limited assurance conclusion' (that is, that based on the procedures performed and evidence obtained, no matters have come to the auditor's attention to cause the auditor to believe the review information is materially misstated).

<sup>15</sup> The nature, timing, and extent of procedures performed in a limited assurance engagement is limited compared with that necessary in a reasonable assurance engagement but is planned to obtain a level of assurance that is, in the assurance practitioner's professional judgement, meaningful. To be meaningful, the level of assurance obtained by the assurance practitioner is likely to enhance the intended users' confidence about the subject matter information to a degree that is clearly more than inconsequential. Paragraph 12(a)(i)(b) of ASAE 3000.

The ERA will try to provide the licensee with advance notice of areas of special focus. This may be by including the information in the ERA's letter reminding the licensee of the upcoming audit or review of its licence.<sup>16</sup>

The ERA may also meet with the licensee and the auditor to discuss the handling of any areas of special focus in the audit or review plan before the auditor submits the plan to the ERA for approval.

## 1.7 Frequency of audits and reviews

The ERA may extend, maintain or reduce the amount of time between audits and reviews. The minimum period between audits and reviews will not be less than 24 months.<sup>17</sup>

### 1.7.1 Extending the audit or review period

#### 1.7.1.1 Audit or review outcomes

The ERA may extend the audit or review period for a licensee assessed as:

- having a strong compliance framework that is achieving a high level of compliance with the conditions of their licence,
- or
- having an effective asset management system with processes that meet the required levels of performance.

Extending an audit or review period allows the ERA to reduce the cost of regulation, while maintaining a suitable level of oversight of a licensee's performance.

#### 1.7.1.2 Inactivity

Some licensees do not immediately commence activities authorised by the licence after it has been granted. In these circumstances, the licensee may request an extension to their first audit or review period.

The ERA will decide a request for an extension on a case-by-case basis.

The ERA generally does not extend the first audit or review period beyond seven years, even if the licensee has not yet commenced any activities authorised by the licence.

The seven-year maximum aims to minimise the risk the licensee can no longer produce the historical records required by the auditor for the audit or review.<sup>18</sup>

<sup>16</sup> This letter is normally sent three months before the end of the audit or review period.

<sup>17</sup> Under the Water Act, the minimum amount of time between audits and reviews is 24 months (refer to section 1.4). For a new licence, the ERA calculates the audit or review period from the date the ERA granted the licence.

<sup>18</sup> Many records only have to be kept for seven years (or less). For example, financial records only have to be kept for seven years after the transactions covered by the records are complete (s.286 of the *Corporations Act 2001 (Cth)*).

### **1.7.2 *Maintaining or reducing the audit or review period***

The ERA may decide not to extend the audit or review period for a licensee it has assessed as:

- needing to materially improve the level of compliance with the conditions of their licence, or
- operating an ineffective asset management system.

For these licensees, the audit or review period may be maintained at 24 months or reduced (if it was previously more than 24 months).

## **1.8 The audit and review process**

The following chapters discuss the stages of the audit and review process in detail.

Appendix 5 includes a flowchart of the audit and review process.

## 2. Auditor selection

The ERA is responsible for engaging an auditor to conduct the audit or review.

The ERA will undertake a selection process<sup>19</sup> to identify an auditor who has the required expertise and experience to conduct the audit or review to an acceptable standard. The ERA will also consider the independence of the auditor as it relates to the licensee.

Section 2.1 sets out the criteria the ERA will consider to determine the suitability of an auditor to conduct the audit or review.<sup>20</sup>

### 2.1 Auditor selection criteria

#### 2.1.1 Expertise and experience

##### 2.1.1.1 Audits

To determine the suitability of an auditor to conduct an audit, the ERA will consider:

- The experience of the auditor in performance and compliance auditing. It is desirable for the auditor to have experience in undertaking regulatory audits or non-financial assurance audits of utilities or other regulated businesses within the previous three years.
- The audit skills and experience of the audit team. The ERA will consider:
  - Each audit team member's audit expertise and experience.
  - The lead auditor's (for example, partner, manager or similar) knowledge and experience of conducting regulatory audits or non-financial audits of utilities or other regulated businesses.

##### 2.1.1.2 Reviews

To determine the suitability of an auditor to conduct an effectiveness review of the asset management system, the ERA will consider:

- The experience of the auditor in asset management practice. It is desirable for the auditor to have relevant asset management experience in utilities or other regulated businesses within the previous three years. Relevant experience might include development of asset management systems, asset performance reviews, asset project management or strategic asset planning.
- The engineering and technical expertise of the review team, including:
  - Each review team member's professional qualifications relevant to the licence(s).
  - Each review team member's knowledge and experience of asset management practice in the utility sector relevant to the licence(s).

<sup>19</sup> The ERA will appoint the auditor on a fixed price contract, based on the scope of work described in the ERA's request for quotation (RFQ). If the scope of work or audit procedures change during the audit or review and additional work is required, the ERA will obtain a quote from the auditor and consult with licensee before approving the work.

<sup>20</sup> The RFQ will require the auditor to address these criteria in their quote.

- The lead auditor’s (for example, partner, manager, senior engineer or similar) knowledge of, and experience in, managing effectiveness reviews of asset management systems.

## 2.1.2 Quality of previous audits and reviews

The ERA will consider the quality of previous audits and reviews conducted by the auditor.

## 2.1.3 Auditor independence

The ERA will consider the professional independence of the auditor as it relates to the licensee and any related entity,<sup>21</sup> particularly where the auditor undertakes other professional work for the licensee or a related entity.

Auditor independence requires that the auditor and the licensee take suitable measures to avoid conflict of interest situations when performing an audit or review.

### 2.1.3.1 Conflict of interest

Under the *Corporations Act 2001 (Cth)* (Corporations Act) an auditor may have a conflict of interest at a particular time if:

because of circumstances that exist at that time:

- the auditor, or a professional member of the audit team, is not capable of exercising objective and impartial judgement in relation to the conduct of the audited body; or
- a reasonable person, with full knowledge of all relevant facts and circumstances, would conclude that the auditor, or a professional member of the audit team, is not capable of exercising objective and impartial judgement in relation to the conduct of the audit of the audited body.

[Section 324CD of the Corporations Act]

Section 324CD of the Corporations Act includes a comprehensive framework for identifying circumstances that may give rise to a conflict of interest.

The professional codes of conduct for audit and assurance practitioners are broadly consistent with the Corporations Act, but may be less prescriptive in their approach to resolving conflicts of interest. Auditors who are members of a professional accounting body should apply the code of ethics of that body to determine whether they meet the minimum standards for professional independence for an audit or review.

The following section outlines the factors<sup>22</sup> the ERA requires all auditors, regardless of whether they are a member of a professional accounting body or not, to take into account to assess whether they meet the minimum standards for auditor independence.

<sup>21</sup> A related entity has the same meaning as in section 9 of the *Corporations Act 2001 (Cth)*.

<sup>22</sup> The factors are drawn from the Corporations Act and Compiled APES 110 Code of Ethics for Professional Accountants.

### 2.1.3.2 Threats to independence

Auditors<sup>23</sup> and licensees must ensure there are no conflicts of interest that may threaten the auditor's independence.

The ERA will advise the licensee in writing of the auditors who will be invited to submit a quote for the audit or review.<sup>24</sup> The licensee must notify the ERA if one or more auditors present an independence threat.<sup>25</sup>

Licensees and auditors should pay particular attention to independence threats due to:

- **Self-interest** – occurs when:
  - An auditor or a member of the audit or review team could benefit from a financial or non-financial interest in a licensee or the related entity.
  - or
  - The total fees from the licensee represent a large proportion of the fees of the auditor expressing the audit opinion.<sup>26</sup>
- **Self-review** – occurs when:
  - The auditor or a member of the audit or review team has undertaken other non-audit work for the licensee that is being evaluated in relation to the audit or review.
  - A member of the audit or review team was previously an officer or director of the licensee.
  - or
  - A member of the audit or review team was previously an employee of the licensee who was in a position to exert direct influence over matters the auditor will examine during the audit or review.
- **Familiarity** – occurs when, due to a close family relationship with a licensee, its directors, officers or employees, an auditor or a member of the audit or review team is, or is perceived to be, too sympathetic to the licensee's interests.

Auditors should assess the risk of a self-review threat based on work:

- Undertaken by the auditor, or a member of the audit or review team, for the licensee within the previous 24 months.
- The auditor is currently undertaking for the licensee.
- or
- The auditor has submitted an offer, or intends to submit an offer, to undertake for the licensee within the next 6 months.

Paragraphs 290.4 to 290.31 of APES 110 discuss these, and other, independence threats in more detail.

<sup>23</sup> Auditors must satisfy themselves there are no conflicts of interest before submitting their quote.

<sup>24</sup> This will be included in the ERA's letter notifying the licensee of the upcoming audit or review.

<sup>25</sup> Refer to Appendix 5 for more information.

<sup>26</sup> Paragraph 7.3.12 of the Australian Accounting Bodies Independence Guide (February 2013) discusses a scenario about this specific self-interest threat.

Auditors must consider whether any other relevant relationships exist that may create a threat to the auditor's independence. Section 324CH of the Corporations Act discusses relationships that may pose an independence threat in more detail.

### 2.1.3.3 Auditor rotation

#### **Consecutive audits or reviews conducted by the same auditor**

There is a self-review or familiarity threat to auditor independence where the same auditor conducts consecutive audits or reviews of the same licensee. To mitigate against this risk, auditor rotation is common practice for statutory audits.<sup>27</sup>

The number of consecutive audits or reviews that the same auditor may conduct is limited to two.

An auditor who has conducted two consecutive audits or reviews will be eligible to conduct another audit or review for the licensee once another auditor has conducted at least one audit or review.

#### **Application of the auditor rotation policy to audits and reviews**

The auditor rotation policy applies to persons who will play a substantial role in the audit or review. This includes:

- if a person is appointed as an individual auditor:
  - the person
  - a service company, or similar, employing the auditor providing the audit service,or
- if an audit company is appointed as the auditor:
  - the lead auditor; that is, the person who is primarily responsible to the audit company for the conduct of the audit or review<sup>28</sup>
  - the review auditor; that is, the person who is primarily responsible to the audit company for reviewing the performance of an audit or review.

For example, the same audit company may complete three or more consecutive audits or reviews if different lead and review auditors are appointed at least for every third audit or review.

If the lead or review auditors have completed two previous audits or reviews for the licensee, they may not conduct a third audit or review even if they are now employed by a different audit company.

<sup>27</sup> The Corporations Act (section 324DA), and the professional codes of conduct for auditors and assurance practitioners set limits on the number of consecutive audits that can be undertaken by an auditor. The Corporations Act also prohibits an auditor from conducting financial audits of the same business for more than 5 out of 7 successive years.

<sup>28</sup> The ERA will apply this test to a person, other than the person who approves the audit report, if it considers that the person will have a direct influence over the development of the opinion of the audit company about the audit or review.

## 2.2 Documents required

When submitting a quotation to the ERA, auditors must provide the following:

- A completed quotation form.
- A copy of the curriculum vitae for each audit or review team member demonstrating their skills and experience relevant to the audit or review.<sup>29</sup>
- A high-level work program demonstrating how the milestones and key deliverables specified in the ERA's request for quotation will be achieved.<sup>30</sup>
- A statement confirming that the auditor will conduct the audit or review in accordance with the guidelines.
- A declaration of independence prepared by the auditor.

### 2.2.1 Declaration of independence

A declaration of independence must include a statement that the auditor, and each audit or review team member, is, and will remain, compliant with the independence criteria set out in these guidelines throughout the audit or review.

The auditor may determine the format of the declaration.

Some professional bodies have developed their own declaration templates. In that case, the auditor must ensure the declaration specifically refers to the requirements set out in these guidelines.

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<sup>29</sup> If, at any time, a new member is added to the audit or review team, the auditor must provide a copy of the new member's curriculum vitae to the ERA.

<sup>30</sup> Responsibility for the timely delivery of the audit or review report rests with the auditor. For licensees who have business operations over a number of facilities distributed across the State, the auditor should acknowledge that they will visit more than one facility during the audit or review engagement.



### 3. Audit or review plan

The auditor is responsible for developing the audit or review plan and submitting it to the ERA for approval.

#### 3.1 Background

The Standard on Assurance Engagements ASAE 3000 states:

The assurance practitioner shall plan the assurance engagement so that it will be performed in an effective manner, including setting the scope, timing and direction of the engagement and determining the nature, timing and extent of planned procedures that are required to be carried out in order to achieve the objective of the assurance practitioner.<sup>31</sup>

ASAE 3000 provides a list of the main matters auditors should address in an engagement plan, including:<sup>32</sup>

- The characteristics of the engagement defining its scope, including the terms of the engagement.
- The expected timing and the nature of the auditor's communications.
- The results of the auditor's acceptance of the audit<sup>33</sup> and, where applicable, whether knowledge gained on other engagements performed by the lead auditor is relevant.
- The audit engagement process.
- The assurance practitioner's understanding of the entity and its environment, including the risks that the subject matter information may be materially misstated.
- Identification of intended users and their needs, and consideration of materiality and the components of assurance engagement risk.
- Personnel and expertise requirements, including the nature and extent of experts' involvement.
- The effect of the internal audit function on the engagement.

The requirements for audit and review plans specified in this Chapter build upon the principles set out in ASAE 3000.<sup>34</sup>

#### 3.2 Minimum contents

The audit or review plan must include:

- The audit or review objectives.
- The auditor's scope of work.
- A table identifying the risk assessment and audit or review priority rating for each applicable licence obligation or asset management process.

<sup>31</sup> Paragraph 40 of ASAE 3000.

<sup>32</sup> Paragraph A86 of ASAE 3000.

<sup>33</sup> Paragraph 22 of ASAE 3000 sets out the criteria used to determine when the auditor might accept an audit engagement.

<sup>34</sup> ASAE 3100 also discusses planning for compliance engagements.

- The auditor's proposed audit procedures.
- A statement confirming that the audit or review report will comply with the ERA's prescribed format.

### 3.2.1 *Audit or review objectives*

The audit or review plan must set out the objectives and purpose of the audit or review. The auditor must confirm that they will perform the audit or review consistent with the regulatory framework prescribed in the Water Act, the licences and these guidelines.

### 3.2.2 *Scope of work*

The audit or review plan must set out the scope of work, including:

- **Audit or review period** – The period covered by the audit or review and, if applicable, the previous audit or review.
- **Assurance engagement** – The type of assurance engagement the auditor will perform.
  - For audits, the plan must confirm the audit is a reasonable assurance engagement.
  - For reviews, the plan must state if the review is a limited assurance engagement or a reasonable assurance engagement.
- **Previous recommendations** – A review of the recommendations from the previous audit or review and the actions taken by the licensee to address the recommendations. The outcome of the auditor's examination may affect the audit priority for one or more licence obligations.

The plan must include a statement confirming the auditor will consider the recommendations from the previous audit or review, if applicable.

- **Compliance reports and compliance registers (audit plans only)** – A review of the compliance reports lodged by the licensee during the audit period.<sup>35</sup> The outcome of the auditor's examination may affect the audit priority for one or more licence obligations.<sup>36</sup>

The plan must identify the compliance reports that have been reviewed by the auditor.

If the licensee has a compliance (or breach) register,<sup>37</sup> the auditor must determine whether the compliance reports are consistent with the register.

- **Site visits** – A list of the sites the auditor will visit during the audit or review.

If the licensee's operations are located across different sites, the auditor must visit enough sites to obtain a representative sample of the licensee's business operations. If the licensee operates in metropolitan and regional areas, the auditor must visit at least one regional site as well as a metropolitan site. The auditor should, where possible, visit sites that are different to those visited during previous audits or reviews.

It is the auditor's, not the licensee's, responsibility to determine the sites the auditor will visit. There may be circumstances where the ERA will direct that a specific site is

<sup>35</sup> Licensees must provide the ERA with an annual compliance report detailing any contraventions of licence obligations for the financial year. The auditor may also need to review a compliance report that has been lodged after the audit period that covers part of the audit period.

<sup>36</sup> Refer to section 3.2.3.2.

<sup>37</sup> Licensees with an effective regulatory framework usually maintain a compliance (or breach) register that lists each licence obligation that the licensee failed to comply with during the audit period.

visited, for example, if the ERA has identified an area of special focus for the audit or review.

The auditor must visit the licensee's business operations to conduct the audit or review; performing audit procedures remotely is not allowed.

- **Personnel and documentation** – For each site, the persons who will be interviewed and the documentation that will be examined.<sup>38</sup>

If one or more entities perform licence obligations or asset management processes on behalf of the licensee, the auditor must identify those obligations or processes in the audit or review plan. The auditor must specify in the plan any persons or documentation of the other entity they will interview or examine.<sup>39</sup>

- **Work schedule** – The auditor's proposed work schedule, including:
  - Details of the activities to be performed during the audit or review (including report preparation).
  - The audit or review team members who will be undertaking the activities.
  - The amount of time allocated to each activity.

### 3.2.3 *Audit and review priority*

The audit or review plan must set out the audit or review priority for each licence obligation, asset management process and effectiveness criterion.

#### 3.2.3.1 *Method*

As explained in section 1.6, auditors must apply a risk-based approach to planning and conducting an audit or review.

The ERA's risk evaluation model is based on AS ISO 31000:2018 (Risk Management – Guidelines). Appendix 3 describes the risk evaluation model in more detail.

Auditors must use the risk evaluation model to determine the audit or review priority for each licence obligation or asset management process. This, in turn, will determine the nature and extent of the audit procedures.<sup>40</sup>

Auditors may use recent work<sup>41</sup> of other independent experts<sup>42</sup> to determine audit or review priorities.<sup>43</sup>

<sup>38</sup> If the ERA requires further information about these documents, it will contact the auditor directly.

<sup>39</sup> This often occurs where the licensee is a special purpose vehicle whose sole function is to operate the assets covered by the licence on behalf of the asset owners, or where the licensee outsources some of its functions to a contractor.

<sup>40</sup> Section 3.2.4 includes more information about audit procedures.

<sup>41</sup> Work undertaken within the last nine months of the audit or review period.

<sup>42</sup> For example, other regulators or external financial auditors.

<sup>43</sup> Where an auditor relies on the work of other parties, the auditor should explicitly disclose this in the audit or review plan.

### 3.2.3.2 *Audit priority*

As part of every audit, auditors must examine all the licence obligations that apply to the licensee.<sup>44</sup> If the ERA has advised the licensee, or the auditor, that a specific licence obligation should be included in the scope of the audit, the auditor must include this obligation in the audit plan.

#### *Determining the audit priority*

Auditors must assign an audit priority of 1 to 5 to each licence obligation.<sup>45</sup> Appendix 3 explains how to calculate an audit priority.

Sometimes the auditor may assign an audit priority that differs from the priority calculated on the basis of Appendix 3:

- **Assigning a higher audit priority** – If the ERA has identified one or more areas of special focus, auditors should assign an audit priority of 1, 2 or 3, as applicable, to the relevant licence obligations. This ensures the auditor will assess the effectiveness of controls for those obligations.

Auditors should also assign an audit priority of 1, 2 or 3 to licence obligations rated non-compliant in the previous audit that the licensee has not yet<sup>46</sup> fully rectified.

When assigning an audit priority, auditors should take into consideration any contraventions disclosed in the licensee's compliance (or breach) register or annual compliance reports for the audit period.

- **Assigning a lower audit priority** – Auditors may reduce the audit priority for a licence obligation if the licensee has demonstrated a high level of compliance over previous consecutive audits.

If an auditor wishes to reduce one or more audit priorities, the auditor must explain this in the audit plan. The ERA will consider a proposal to reduce an audit priority on a case-by-case basis.

Every applicable licence obligation must be subject to some level of audit procedures for the entire audit period.<sup>47</sup>

#### *Licence obligations that are not applicable (N/A)*

While developing an audit plan, the auditor may determine that one or more licence obligations do not apply to the licensee's business operations. Instead of assigning an audit priority to these licence obligations, the auditor must mark the obligations in the audit plan as 'not

<sup>44</sup> This includes general licence conditions, individual licence conditions (conditions specific to the licensee), and legislative obligations called up by the licence. The ERA's [Water Compliance Reporting Manual](#) lists the general licence conditions and the legislative obligations called up by the licence. Auditors should review the licensee's licence to determine if any individual licence conditions apply to the licensee.

<sup>45</sup> Auditors must not group licence obligations when determining audit priority. However, auditors may group similar licence obligations when determining audit procedures, or when making observations and recommendations. Licence obligations may be considered similar if they involve a part of a legislative instrument (for example, a clause or division of a code) or if they are managed by a business function or member of staff that is responsible for complying with the obligations.

<sup>46</sup> At the time the audit plan is being prepared.

<sup>47</sup> Licence obligations that were only applicable for part of the audit period only need to be audited for that period.

applicable'. The auditor must also provide a brief explanation why these obligations will not be assessed.

### Presentation of audit priority in the audit plan

The audit plan must include a table identifying the risk assessment and audit priority rating for each licence obligation. Table 1 provides an example of an audit priority ratings table.

**Table 1: Presenting audit priority ratings in an audit plan**

Licence obligation reference no. (Refer to Water Compliance Reporting Manual)	Licence obligation (cl = clause, Sch = Schedule)	Consequence (1 = minor, 2 = moderate, 3 = major)	Likelihood (A = likely, B = probable, C = unlikely)	Inherent risk (low, medium, high)	Adequacy of existing controls (strong, medium, weak)	Audit priority (Refer to Table 21)					
						1	2	3	4	5	N/A
21	Water Services Act, section 95(3)	3	C	medium	strong		✓				
160	Water Services Act, section 12 Clause 3.1.2 of the licence	2	C	low	strong					✓	

### 3.2.3.3 Review priority

As part of every review, auditors must assign a review priority to each of the 12 asset management processes and each of the effectiveness criteria for those processes.

#### Determining the review priority

Appendix 3 explains how to calculate the review priority for asset management processes and effectiveness criteria.<sup>48</sup>

Sometimes the auditor may assign a review priority that differs from the priority calculated on the basis of Appendix 3:

- **Assigning a higher review priority** – If the ERA has identified one or more areas of special focus, auditors should assign a review priority of 1, 2 or 3, as applicable, to the relevant asset management process or effectiveness criterion.

Auditors should also assign a review priority of 1, 2 or 3 to asset management processes or effectiveness criteria rated deficient in the previous review that the licensee has not yet<sup>49</sup> fully addressed.

<sup>48</sup> Although Appendix 3 mainly focuses on audits, the processes described in Appendix 3 for determining audit priorities can be equally applied to determine review priorities for asset management processes and effectiveness criteria.

<sup>49</sup> At the time the review plan is being prepared.

- **Assigning a lower audit priority** – Auditors may reduce the review priority for an asset management process or effectiveness criterion if they were rated as effective over previous consecutive reviews.

If an auditor wishes to reduce one or more review priorities, the auditor must explain this in the review plan. The ERA will consider a proposal to reduce a review priority on a case-by-case basis.

Every applicable asset management process and effectiveness criterion must be subject to some level of audit procedures for the entire review period.

### **Effectiveness criteria that are not applicable (N/A)**

While developing the review plan, the auditor may determine that one or more effectiveness criteria do not apply to the licensee's asset management system. Instead of assigning a review priority to these criteria, the auditor must mark the criteria in the review plan as 'not applicable'. The auditor must also provide a brief explanation why these criteria will not be assessed.

### **Presentation of review priority in the review plan**

The review plan must include a table identifying the risk assessment and review priority rating for each of the 12 asset management processes and their associated effectiveness criteria. Table 2 provides an example of a review priority ratings table.

**Table 2: Presenting review priority ratings in the review plan**

Asset management process & effectiveness criteria reference no. (Refer to Table 22)	Asset management process & effectiveness criteria	Consequence (1 = minor, 2 = moderate, 3 = major)	Likelihood (A = likely, B = probable, C = unlikely)	Inherent risk (low, medium, high)	Adequacy of existing controls (strong, medium, weak)	Review priority (Refer to Table 21)					
						1	2	3	4	5	N/A
<b>1</b>	<b>Asset planning</b>	<b>2</b>	<b>C</b>	<b>medium</b>	<b>strong</b>				✓		
1.1	Asset management plan covers the processes in this table	2	C	medium	strong				✓		
1.2	Planning processes and objectives reflect the needs of all stakeholders and are integrated with business planning	1	C	low	strong					✓	
1.3	Service levels are defined in the asset management plan	1	C	low	strong					✓	

### 3.2.4 Proposed audit procedures

The audit or review plan must describe the procedures the auditor proposes to use to assess the licensee's compliance with each licence obligation or the effectiveness of each asset management process (audit procedures) for each audit or review priority rating.<sup>50</sup>

#### 3.2.4.1 Overview

The ERA's risk evaluation model ensures the depth of procedures applied in an audit or review is commensurate with the risk. Higher risk areas of the licensee's operations require more extensive audit procedures.

Auditors should apply ASAE 3000, ASAE 3100, ASA 500 (Audit Evidence) and ASA 530 (Audit Sampling) to determine the level and type of audit procedures for each licence condition or asset management process.<sup>51</sup> Items with a priority rating of 1 or 2 should be examined more extensively than items with a lower priority rating, see Table 3 for examples.

#### 3.2.4.2 Sample procedures

Paragraph A53 of ASA 500 states:

An effective test provides appropriate audit evidence to an extent that, taken with other audit evidence obtained or to be obtained, will be sufficient for the auditor's purposes. In selecting items for testing, the auditor is required by paragraph 7 to determine the relevance and reliability of information to be used as audit evidence; the other aspect of effectiveness (sufficiency) is an important consideration in selecting items to test. The means available to the auditor for selecting items for procedures are:

- (a) Selecting all items (100% examination);
- (b) Selecting specific items; and
- (c) Audit sampling.

Audit sampling may be particularly relevant for licence obligations that require the licensee to complete an action within a specified timeframe. Auditors may also use sampling when they have rated the strength of controls as weak.

The size of the selected sample should comply with ASA 530 (Audit Sampling):

The level of sampling risk that the auditor is willing to accept affects the sample size required. The lower the risk the auditor is willing to accept, the greater the sample size will need to be.<sup>52</sup>

[...]

The sample size can be determined by the application of a statistically-based formula or through the exercise of professional judgement.<sup>53</sup>

While specific details of the proposed sample procedures do not have to be provided in the audit or review plan, the auditor should collect 'sufficient appropriate evidence'<sup>54</sup>

<sup>50</sup> See Table 3 for examples of audit procedures for each priority rating.

<sup>51</sup> As discussed in section 3.2.3, auditors must determine an audit or review priority for each licence obligation or asset management process. The audit procedures should be commensurate with the assigned audit or review priority.

<sup>52</sup> Paragraph A10 of ASA 530.

<sup>53</sup> Paragraph A11 of ASA 530.

<sup>54</sup> Clause 12 of ASAE 3000.

commensurate with the audit or review priority of the licence obligation or effectiveness criterion.

### 3.2.4.3 Summary of audit procedures

The audit or review plan must include a tabular summary of the type of audit procedures the auditor will apply for each audit or review priority level. Table 3 provides an example.

**Table 3: Examples of possible audit procedures for each audit or review priority**

Audit or review priority (refer Appendix 3)		Examples of possible audit procedures
1	High priority	Interview supervisory and operational personnel Inspect relevant documents Obtain evidence policies, procedures and controls are in place and working effectively <sup>55</sup> Examine compliance reports and breach register Obtain confirmations from third parties if applicable
2		Examine reports and correspondence with other regulators (e.g. Building and Energy) Closely inspect applicable asset infrastructure Examine asset management system effectiveness criteria Sample, at a high level, output and timeliness procedures Recalculate a sample of relevant performance indicators
3	Moderate priority	Interview supervisory and operational personnel Inspect relevant documents Obtain evidence policies, procedures and controls are in place and controls are working effectively <sup>56</sup> Examine compliance reports and breach register
4		Physically examine applicable asset infrastructure Examine asset management system effectiveness criteria Sample output and timeliness procedures Walkthrough the process to calculate relevant performance indicators
5	Low priority	Interview supervisory or operational personnel Undertake a desktop review of relevant documents Undertake a desktop review of policies, procedures and controls in place View compliance reports and breach register Visit applicable asset infrastructure Undertake a desktop review of asset management system effectiveness criteria Sample, at a low level, output and timeliness procedures

<sup>55</sup> A controls assessment is mandatory for audit priorities 1, 2 and 3, or if the auditor identifies non-compliance with a licence obligation.

<sup>56</sup> This is mandatory for audit priority 3, and optional for audit priority 4.



Table 3 is for illustrative purposes only. Auditors may apply their own policies for audit procedures when they prepare an audit or review plan.

Auditors who apply their own policies must include sufficient information about these policies in the audit or review plan to indicate the scope of procedures the auditor will apply for each audit or review priority rating.

### **3.2.5 Reporting format**

The audit or review plan must include a statement confirming the audit or review report prepared by the auditor will comply with the format prescribed in Chapter 5 of the guidelines.

## **3.3 Assistance provided by the ERA**

The licensee's previous audit or review report is available from the ERA [website](#). A copy of the applicable licence(s) will be provided to prospective auditors as part of the ERA's request for quotation.

At the licensee's or auditor's request, the ERA may meet the auditor to discuss any specific concerns about the preparation of the audit or review plan.

## 4. Conducting the audit or review

This section outlines the general principles the auditor and licensee must follow to ensure the audit or review is conducted in a thorough and timely manner.

### 4.1 Assistance provided by the licensee

Licensees must facilitate the audit or review process by providing to the auditor, as needed and in a timely manner:

- Access to the facilities and business premises identified in the audit or review plan.
- Access to materials and information sources that the auditor needs to conduct the audit or review, including data, reports, records and any other relevant information.
- Access to the relevant person(s) in each of the licensee's business units that are being audited.
- An introduction to persons, other than employees of the licensee, who are relevant to the audit or review.

### 4.2 Fieldwork

During the audit or review, auditors must undertake one or more visits to the licensee's facilities<sup>57</sup> to access information, make enquiries and interview relevant personnel. If one or more functions are performed by another entity on behalf of the licensee,<sup>58</sup> the auditor should make reasonable enquiries of the other entity.

Auditors should assess the licensee's:

- **Control environment** – the licensee's management philosophy and operating style, organisational structure, assignment of authority and responsibilities, the use of internal audit, the use of information technology and the skills and experience of the relevant staff members.
- **Information system** – the suitability of the licensee's information systems to record the information needed to comply with the licence, accuracy of data, security of data and documentation describing the information system.
- **Control procedures** – the presence of systems and procedures to monitor compliance with the licence or the effectiveness of the licensee's asset management system, and to detect or prevent instances of non-compliance or under-performance.
- **Compliance attitude** – the action taken by the licensee in response to any previous audit or review recommendations, and an assessment of the licensee's attitude towards compliance.
- **Outcome compliance** – the actual performance against standards prescribed in the licence throughout the audit or review period.

<sup>57</sup> The audit plan must identify the sites the auditor will visit. Refer to section 3.2.2.

<sup>58</sup> For example, the licensee's parent company or a contractor.

## 4.2.1 Audits

Auditors only have to assess a licensee's controls<sup>59</sup> (control environment and control procedures) for:

- **Audit priority of 1, 2 or 3** – licence obligations with an assigned audit priority of 1, 2 or 3. If the auditor raises an audit priority after the planning stage from 4 or 5 to 1, 2 or 3, the auditor must also assess the licensee's controls.
- **Non-compliant** – licence obligations that the auditor has rated non-compliant.<sup>60</sup>

If a licensee's controls have changed during the audit period, the auditor must examine both the former and current controls. If the auditor identifies inadequacies with the controls, the auditor must disclose them in the observations section of the report. Although the auditor must review both controls, the auditor only has to rate the controls currently in place.

## 4.3 Audit evidence

ASAE 3100 provides guidance on the quantity and quality of audit evidence auditors should obtain when conducting an audit or review:<sup>61</sup>

Compliance engagements require the application of assurance skills and techniques to gather sufficient appropriate evidence as part of an iterative, systematic assurance engagement process. [...]

When compliance requirements apply throughout the specified period, the assurance practitioner may consider the nature and frequency of the compliance activities undertaken, and modify the nature, timing and extent of evaluation and/or testing to be undertaken on compliance activities. [...]

Auditors should use their professional judgement to determine what constitutes sufficient audit evidence for each audit or review they perform.<sup>62</sup>

Auditors must develop a comprehensive set of working papers throughout the audit or review. The working papers should be detailed enough to provide sufficient evidence to support the auditor's observations and recommendations included in the audit or review report. The ERA may request access to the auditor's working papers.

### 4.3.1 Specific requirements for assessing output compliance (audits only)

Some licence obligations require licensees to develop processes to ensure that they complete activities within prescribed timeframes. Examples include responding to customer complaints, connecting and re-connecting customers on time and providing annual compliance and performance reports to the ERA.

<sup>59</sup> This involves the auditor performing a controls assessment and providing a controls rating.

<sup>60</sup> Assigned a compliance rating of 2, 3 or 4.

<sup>61</sup> Paragraphs A37 and A38.

<sup>62</sup> Refer to section 3.2.4 for more information about audit procedures.

Auditors must perform suitable audit procedures to determine whether a licensee has complied with these licence obligations in a timely manner. The audit priority assigned to the licence obligation will guide the nature and extent of the audit procedures.<sup>63</sup>

## 4.4 Professional scepticism

Auditors must adopt an attitude of professional scepticism throughout the audit or review. ASAE 3000 defines professional scepticism as:<sup>64</sup>

an attitude that includes being alert to, for example:

- Evidence that is inconsistent with other evidence obtained.
- Information that calls into question the reliability of documents and responses to enquiries to be used as evidence.
- Circumstances that suggest the need for procedures in addition to those required by relevant ASAEs.
- Conditions that may indicate likely misstatement

<sup>63</sup> The nature and extent of audit procedures will also depend on the licensee's control environment. If a licensee has a strong control environment with a high level of visibility of the required compliance outcomes, then the auditor may be able to rely on the data provided by the licensee to assess compliance. If the licensee has a weak control environment, the auditor should perform more detailed audit procedures, including audit sampling or re-performing processes, to assess the level of compliance.

<sup>64</sup> Paragraph 11(a).

## 5. Audit or review report

Auditors must provide a comprehensive report to the ERA clearly expressing their opinion on the findings of the audit or review.

ASAE 3000 provides a useful reference framework for the structure and content of assurance reports.<sup>65</sup> ASAE 3100 provides further guidance for the reporting of compliance assurance engagements.<sup>66</sup>

### 5.1 Minimum contents

The audit or review report must include:

- an executive summary
- the audit or review objectives
- the auditor's scope of work
- deviations from the audit or review plan
- a list of the recommendations from the previous audit or review
- a table summarising the licensee's performance
- the auditor's observations
- the auditor's recommendations
- a statement from the auditor approving the content of the report.

Auditors may also include any additional information they deem relevant to the audit or review outcomes.

#### 5.1.1 Executive summary

The audit or review report must include an executive summary.

##### 5.1.1.1 Audits

The executive summary of the audit report must include:

- A statement confirming the audit has been conducted to assess the licensee's compliance with the conditions of its licence.
- A brief description of the type of licence(s) held by the licensee, the business that holds the licence(s), and any substantial changes to either since the previous audit.
- A summary of the actions taken by the licensee in response to the recommendations in the previous audit report.<sup>67</sup>
- A summary of the findings and recommendations arising from the current audit.
- The opinion of the auditor on the control environment operated by the licensee.

<sup>65</sup> Refer to paragraphs 79 – 81 of ASAE 3000.

<sup>66</sup> ASAE 3100 requires auditors to also comply with ASAE 3000.

<sup>67</sup> The assessment will be a summary of the information included in Table 4 (section 5.1.5).

- An overall assessment of compliance with the licence, including the non-compliances found by the audit and the integrity of the licensee's reporting to the ERA and other statutory organisations.
- Any other information the auditor considers relevant.

### 5.1.1.2 *Reviews*

The executive summary of the review report must include:

- A statement confirming the review has been conducted to assess the effectiveness of the licensee's asset management system.
- A brief description of the assets reviewed and any substantial changes to those assets since the previous review.<sup>68</sup>
- A brief description of the business that holds the assets, and any substantial changes to the business since the previous review.
- A summary of the actions taken by the licensee in response to the recommendations in the previous review report.<sup>69</sup>
- A summary of the findings and recommendations arising from the current review.<sup>70</sup>
- An overall assessment of the effectiveness of the licensee's asset management system.
- Any other information the auditor considers relevant to the review.

### 5.1.2 *Audit or review objectives*

The audit or review report must set out the objectives and purpose of the audit or review. It must also describe the methodology used by the auditor to conduct the review.

### 5.1.3 *Scope of work*

The audit or review report must set out the scope of work, including:

- **Audit or review period** – The period covered by the audit or review and, if applicable, the previous audit or review.
- **Type of assurance engagement** – The report must confirm the type of assurance engagement the auditor has performed.
  - For audits, the report must confirm the audit is a reasonable assurance engagement.
  - For reviews, the report must state if the review is a limited assurance engagement or a reasonable assurance engagement.
- **Compliance reports (audit plans only)** – The compliance reports that have been reviewed by the auditor.
- **Site visits** – A list of the sites visited by the auditor during the audit or review.

<sup>68</sup> For small licensed sewerage schemes, the auditor must disclose in the executive summary whether the scheme is a limited effluent or a septic tank effluent disposal (**STED**) system.

<sup>69</sup> The assessment will be a summary of the information included in Table 5 (section 5.1.5).

<sup>70</sup> The information must be presented in a tabular format (asset management process, matter and recommendation).

- **Personnel and documentation** – Details of the:
  - Licensee’s representatives<sup>71</sup> who participated in the audit or review.
  - Documents and other information sources examined by the auditor during the course of the audit or review.
- **Work schedule** – The auditor’s work schedule, including:
  - Details of the activities performed during the audit or review.
  - Details of the audit or review team members and hours utilised by each member.
  - The period over which the audit or review has been performed.
- **Other** – Any other information the auditor considers relevant to the audit or review scope of work.

#### 5.1.4 *Deviations from the audit or review plan*

The audit or review report must describe any deviations from the audit or review plan.

For example, if the auditor has revised the audit priority for one or more licence obligations, the auditor must identify this in the report.<sup>72</sup> Auditors must include a brief explanation for the revision.

Auditors must also identify any licence obligations or effectiveness criteria that were assessed after the approval of the audit plan by the ERA, as ‘not applicable’.<sup>73</sup> Licence obligations or effectiveness criteria that have been assessed as ‘not applicable’<sup>74</sup> should not be included in the performance summary or observations section of the report.

#### 5.1.5 *Recommendations from previous audits or reviews*

The audit or review report must include the recommendations from the previous audit or review that were resolved during the current audit or review period, or are unresolved at the end of the current audit or review period.

The recommendations must be based on those in the previous audit or review report<sup>75</sup> and set out in the format specified in Table 4 or 5, as applicable. Where the licensee has not addressed a previous audit or review recommendation, the auditor must make a new recommendation(s) covering the outstanding matter(s).

<sup>71</sup> If the auditor has interviewed personnel of another entity (for example, a parent company or contractor), the auditor must also provide details of those persons.

<sup>72</sup> If the auditor raises an audit priority to either a 1, 2 or 3, the auditor must rate the adequacy of controls. Refer to section 4.2.

<sup>73</sup> Auditors must include a brief explanation for their assessment.

<sup>74</sup> In the audit or review plan or during the course of the audit or review.

<sup>75</sup> The auditor must allocate a new recommendation number to the unresolved recommendation. For example, in Table 4 (Part B) the number allocated to the original recommendation was 03/2016. A new recommendation number has been allocated for the current audit: 05/2018. For more information, refer to Section 5.1.8.

**Table 4: Status of recommendations addressing non-compliances from the previous audit**

<b>A. Resolved during current audit period</b>				
<b>Recommendation reference</b> (no./year)	<b>Non-compliance / Controls improvement</b>  (Rating / Licence obligation reference number <sup>76</sup> and licence obligation / Details of non-compliance or inadequacy of controls)	<b>Auditor's recommendation</b>	<b>Date resolved</b>	<b>Further action required</b> (Yes/No/Not Applicable)  <b>Details of further action required</b> (including current recommendation reference, if applicable)
02/2016	<b>C2</b> <b>(76) Water Services Regulations 2013 – Regulation 65(1)</b>  The audit identified instances of incomplete records for three lots for which water services are being charged.	The licensee should update the records with the missing information.	20/3/17	No.
<b>B. Unresolved at end of current audit period</b>				
<b>Recommendation reference</b> (no./year)	<b>Non-compliance / Controls improvement</b>  (Rating / Licence obligation reference number <sup>77</sup> and licence obligation / Details of non-compliance or inadequacy of controls)	<b>Auditor's recommendation</b>	<b>Further action required</b> (Yes/No/Not Applicable)  <b>Details of further action required</b> (including current recommendation reference, if applicable)	
03/2016	<b>B2</b> <b>(129) Water Services Code of Conduct (Customer Service Standards) 2013 - Clause 26(6).</b>  The licensee must review its financial hardship policy at least once in every 5 year period and, as part of the review process, consult with relevant consumer organisations.	The licensee needs to review its financial hardship policy which was last reviewed six years ago.	Yes Complete the review of the policy that commenced in December 2017. Refer to Recommendation 05/2018.	

<sup>76</sup> The reference number allocated to the licence obligation in the Water Compliance Reporting Manual.

<sup>77</sup> As above.



**Table 5: Status of recommendations addressing asset system deficiencies from the previous review**

<b>A. Resolved during current review period</b>				
<b>Recommendation reference</b> (no./year)	<b>Process and policy deficiency / Performance deficiency</b>  (Rating / Reference number, Asset management process & effectiveness criterion / Details of deficiency)	<b>Auditor's recommendation</b>	<b>Date resolved</b>	<b>Further action required</b> (Yes/No/Not Applicable)  <b>Details of further action required</b> (including current recommendation reference, if applicable)
02/2016	<b>A3</b> <b>(5.3) Asset Operations –</b> <i>Assets are documented in the asset register.</i>  The condition assessment of sewerage assets is not undertaken on a regular basis.	Update the sewerage assets structural condition on a regular basis.	20/3/17	No
<b>B. Unresolved at end of current review period</b>				
<b>Recommendation reference</b> (no./year)	<b>Process and policy deficiency / Performance deficiency</b>  (Rating / Reference number, Asset management process & effectiveness criterion / Details of deficiency)	<b>Auditor's recommendation</b>	<b>Further action required</b> (Yes/No/Not Applicable)  <b>Details of further action required</b> (including current recommendation reference, if applicable)	
03/2016	<b>A4</b> <b>(9.1) Contingency Planning –</b> <i>Contingency plans are documented, understood and tested to confirm their operability and to cover higher risks.</i>  The contingency plan for loss of power to the sewerage plant had not been tested for three years.	Test the contingency plan for loss of power to the sewerage plant on a regular basis and at least every two years.	Yes - test the contingency plan. Refer to recommendation 05/2018.	

## 5.1.6 Performance summary

Auditors must assess a licensee's performance by assigning a rating to each licence obligation, asset management process and effectiveness criteria.<sup>78</sup> The audit or review report must include a table listing the auditor's ratings (performance summary table).

The following sections describe:

- The framework auditors must use to rate a licensee's performance.<sup>79</sup>
- The format auditors must use for their performance summary table.

### 5.1.6.1 Audits

When assessing a licensee's audit performance, auditors must rate the licensee's compliance with the conditions of its licence (compliance rating). If an auditor is unable to rate a licensee's compliance because the licensee did not perform the activity during the audit period, the auditor must assess the obligation 'Not Rated' (N/R) and explain why in the observations section of the report.

Auditors must also provide a rating for the licensee's control procedures and control environment<sup>80</sup> (controls rating) for licence obligations with an audit priority of 1, 2 or 3, or that have been assessed to be non-compliant in the audit.<sup>81</sup> If an auditor has not rated the controls for a licence obligation, the auditor must assess the obligation 'Not Performed' (N/P).

Table 6 sets out the ratings scales auditors must use to rate each licence obligation

**Table 6: Compliance and controls rating scales (audits)**

Controls rating		Compliance rating	
Rating	Description	Rating	Description
A	Adequate controls – no improvement needed	1	Compliant
B	Generally adequate controls – improvement needed	2	Non-compliant – minor effect on customers or third parties
C	Inadequate controls – significant improvement required	3	Non-compliant – moderate effect on customers or third parties
D	No controls evident	4	Non-compliant – major effect on customers or third parties
N/P	Not performed – A controls rating was not required	N/R	Not rated – No activity took place during the audit period

<sup>78</sup> Licence obligations or effectiveness criteria that have been assessed as 'not applicable' (either during or after the planning stage), should not be rated or included in the performance summary.

<sup>79</sup> The rating frameworks for audits and reviews are different as the purpose and scope of audit and reviews are different. Refer to section 1.5.

<sup>80</sup> Section 4.2 (Fieldwork) explains the terms 'control procedures' and 'control environment'. Control procedures are 'the presence of systems and procedures to monitor compliance with the licence, and to detect or prevent instances of non-compliance'. Control environment is the 'licensee's management philosophy and operating style, organisational structure, assignment of authority and responsibilities, the use of internal audit, the use of information technology and the skills and experience of key staff members'.

<sup>81</sup> Refer to section 4.2.

To assess the effect on customers or third parties, auditors should consider factors such as the number of persons affected, the severity of the breach (the degree to which it affects customers and third parties), and whether the breach was systematic or a one-off occurrence.

### Table format

Auditors must present their ratings in a format consistent with Table 7.

**Table 7: Performance summary table for audits**

Licence obligation reference no. (Refer to the Water Compliance Reporting Manual)	Licence obligation	Audit priority (rated 1 (highest) to 5 (lowest))	Controls rating (Refer to the 4-point rating scale in Table 6 for details)					Compliance rating (Refer to the 4-point rating scale in Table 6 for details)				
			A	B	C	D	N/P	1	2	3	4	N/R
1	Water Services Act Section 21(1)(a)	2		✓						✓		
2	Water Services Act Section 21(1)(b)	4					✓	✓				

Auditors must rate any licence obligations that the licensee has contravened during the audit period as non-compliant. This includes situations where the auditor samples a number of transactions to determine a licensee's compliance with a particular licence obligation and identifies a small number (including single occurrences) of non-compliance.

Auditors should only rate a licence obligation non-compliant if there is supporting evidence. If there is no supporting evidence,<sup>82</sup> the auditor should assess the adequacy of the controls for the obligation. If the controls are assessed to be deficient (rated C or D), the auditor should make a recommendation to address the deficiency.

A contravention of a licence obligation may result in consequential contraventions of other licence obligations. If this is the case, the auditor should explain this in the observations section of the audit report.<sup>83</sup>

If the contravention only occurred for part of the audit period and the matter was resolved before the end of the audit period, the auditor should rate the licence obligation as non-compliant. If the auditor is satisfied that the licensee has addressed the cause(s) of the non-compliance, the auditor may decide not to make a recommendation. The audit report must disclose how the cause(s) of the non-compliance was resolved.

<sup>82</sup> For example, the licensee asserts that it has complied with the obligation but is unable to provide supporting proof of compliance (often because of poor record keeping).

<sup>83</sup> Refer to section 5.1.7.

The auditor must provide information in the observations section of the audit report to support the ratings in the table.

### **Compliance and controls ratings summary table**

The audit report must include a table listing the number of licence obligations that were given each combination of compliance and controls ratings. The table allows licensees and the ERA to confirm the auditor has rated all relevant licence obligations, and provides a simple summary of the licensee's compliance during the audit period.

Auditors must ensure the table is consistent with the ratings in the audit summary table<sup>84</sup> and observations section of the audit report.<sup>85</sup>

The table must follow the format of Table 8.

**Table 8: Compliance and controls ratings summary table**

		Compliance rating					
		1	2	3	4	N/R	Total
Controls rating	A	9	-	-	-	-	9
	B	2	3	-	-	-	5
	C	-	-	-	-	-	0
	D	-	-	-	-	-	0
	N/P	-	-	-	-	29	29
	Total	11	3	0	0	29	43

### **5.1.6.2 Reviews**

When assessing the effectiveness of the licensee's asset management system, auditors must rate both the adequacy of the licensee's processes and policies (process and policy rating) and the licensee's performance (performance rating) for each asset management process and effectiveness criterion.<sup>86</sup>

Table 9 sets out the rating scales auditors must use to rate the adequacy of a licensee's processes and policies.

Table 10 sets out the rating scales auditors must use to rate the licensee's performance.

<sup>84</sup> Table 7.

<sup>85</sup> Refer to section 5.1.7.

<sup>86</sup> Appendix 4 identifies for each asset management process the outcome(s) if the licensee is performing the process effectively, and the criteria the auditor must use to determine the effectiveness of each process (effectiveness criteria).

**Table 9: Process and policy rating scale (reviews)**

Rating	Description	Criteria
<b>A</b>	Adequately defined	<ul style="list-style-type: none"> <li>Processes and policies are documented.</li> <li>Processes and policies adequately document the required performance of the assets.</li> <li>Processes and policies are subject to regular reviews, and updated where necessary.</li> <li>The asset management information system(s) are adequate in relation to the assets being managed.</li> </ul>
<b>B</b>	Requires some improvement	<ul style="list-style-type: none"> <li>Processes and policies require improvement.</li> <li>Processes and policies do not adequately document the required performance of the assets.</li> <li>Reviews of processes and policies are not conducted regularly enough.</li> <li>The asset management information system(s) requires minor improvements (taking into consideration the assets being managed).</li> </ul>
<b>C</b>	Requires substantial improvement	<ul style="list-style-type: none"> <li>Processes and policies are incomplete or require substantial improvement.</li> <li>Processes and policies do not document the required performance of the assets.</li> <li>Processes and policies are considerably out of date.</li> <li>The asset management information system(s) requires substantial improvements (taking into consideration the assets being managed).</li> </ul>
<b>D</b>	Inadequate	<ul style="list-style-type: none"> <li>Processes and policies are not documented.</li> <li>The asset management information system(s) is not fit for purpose (taking into consideration the assets being managed).</li> </ul>

**Table 10: Performance rating scale (reviews)**

Rating	Description	Criteria
<b>1</b>	Performing effectively	<ul style="list-style-type: none"> <li>The performance of the process meets or exceeds the required levels of performance.</li> <li>Process effectiveness is regularly assessed, and corrective action taken where necessary.</li> </ul>
<b>2</b>	Improvement required	<ul style="list-style-type: none"> <li>The performance of the process requires some improvement to meet the required level.</li> <li>Process effectiveness reviews are not performed regularly enough.</li> <li>Recommended process improvements are not implemented.</li> </ul>
<b>3</b>	Corrective action required	<ul style="list-style-type: none"> <li>The performance of the process requires substantial improvement to meet the required level.</li> <li>Process effectiveness reviews are performed irregularly, or not at all.</li> <li>Recommended process improvements are not implemented</li> </ul>
<b>4</b>	Serious action required	<ul style="list-style-type: none"> <li>Process is not performed, or the performance is so poor the process is considered to be ineffective.</li> </ul>

**Table format**

Auditors must set out their ratings in a format consistent with Table 11.

**Table 11: Performance summary table for reviews**

Asset management process & effectiveness criteria (Refer to Table 23)	Process and policy rating	Performance rating
<b>1. Asset planning</b>	B	2
1.1 Asset management plan covers processes in this table	B	1
1.2 Planning processes and objectives reflect the needs of all stakeholders and are integrated with business planning	A	1
1.3 Service levels are defined in the asset management plan	C	2
1.4 Non-asset options (e.g. demand management) are considered	C	2
1.5 Lifecycle costs of owning and operating assets are assessed	B	3
1.6 Funding options are evaluated	B	3

Auditors must provide information in the observations section of the review report<sup>87</sup> to support their ratings in the table.

For licensees who provide sewerage and non-potable water services, auditors may assign separate ratings to the sewerage system (sewage collection, sewage treatment and disposal of treated sewerage) and the non-potable water supply scheme (water treatment and non-potable water reticulation/re-use infrastructure). When exercising this option, auditors should only assign separate ratings for four of the twelve asset management processes: asset operations, asset maintenance, risk management and contingency planning.

**5.1.7 Auditor's observations**

The audit or review report must include a section that explains for each licence obligation, asset management process or effectiveness criterion the basis for the auditor's ratings and recommendations.<sup>88</sup>

<sup>87</sup> Refer to section 5.1.7.

<sup>88</sup> Licence obligations or effectiveness criteria that have been assessed as 'not applicable' (either during or after the planning stage), should not be rated or included in the observations section.

Auditors must provide sufficient information to support their ratings and recommendations, including:

- key findings of the audit or review fieldwork
- sources of information used to assess compliance or effectiveness
- audit procedures performed to assess compliance or effectiveness<sup>89</sup>
- assessments of policies and procedures performed during the audit or review
- interviews conducted with licensee staff or external parties
- the assessment of compliance or effectiveness over the audit or review period.

The ERA may require the auditor to undertake further audit procedures (including an increased level of sampling) if it considers that the audit procedures performed are inadequate. For example, this may occur when the original audit procedures did not examine the licensee's compliance with a particular licence obligation(s) or the effectiveness of a particular asset management process, to a level commensurate with the audit or review priority in the audit or review plan.

For licensees who provide sewerage and non-potable water services, auditors must make separate observations for the sewerage system and non-potable water supply scheme. As a minimum, separate observations are required for asset operations, asset maintenance, risk management and contingency planning.

Auditors must present their observations and recommendations in a tabular format. The table must include: the reference number,<sup>90</sup> the regulatory obligation<sup>91</sup> or asset management process,<sup>92</sup> the audit or review priority, the auditor's observations and recommendations, and the applicable ratings.<sup>93</sup>

Tables 12 and 13 are examples of tables presenting the auditor's observations and recommendations.

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<sup>89</sup> Refer to section 3.2.4.

<sup>90</sup> For audits, the reference number is the number assigned to each licence obligation in the [Water Compliance Reporting Manual](#). If individual licence obligations apply to the licensee, these should also be included in the table. The auditor has discretion over the numbering of individual licence obligations.

For reviews, the reference number is the number assigned to the asset management process or effectiveness criterion in Table 23.

<sup>91</sup> Refer to 'obligations under' and 'summary description' set out in the tables in sections 9 to 12 of the [Water Compliance Reporting Manual](#).

<sup>92</sup> Or effectiveness criterion.

<sup>93</sup> For audits, the controls rating and the compliance rating. For reviews, the process and policy rating and the performance rating.

**Table 12: Audit observations and recommendations**

Reference no. <sup>94</sup>	Licence reference & Summary of licence obligation	Audit priority	Observations & Recommendations	Control rating	Compliance rating
<b>Water Services Act 2012</b>					
1	The licensee must provide a water service authorised by the licence to persons entitled to the service under the Act, except to the extent otherwise provided for by the Act. <i>Water Services Act, section 21(1)(a)</i>	2	Confirmed by interview that, during the audit period, the licensee provided water services to persons entitled to those services under the Act. Further confirmed by examination of bills issued during the audit period.  The auditor considers that the licensee has no systems and controls in place to manage compliance with section 21(1)(a) of the Act.  <b>Recommendation 01/2019:</b> The licensee should implement a compliance register which records all its obligations in terms of the Water Legislation. This register should identify, per individual compliance obligation, appropriate policy and procedure documents and responsible employees.	D	1
23	The licensee must comply with requests made by FESA or a local government under sections 96(3) and 96(4) of the Act to the extent practicable and within a reasonable time. <i>Water Services Act, section 96(5)</i>	4	Confirmed by interview that, during the audit period, FESA did not request the licensee to install, remove, repair or maintain a fire hydrant.	NP	NR

<sup>94</sup> The reference number is the number assigned to each licence obligation in the Water Compliance Reporting Manual. If individual licence obligations apply to the licensee, these should also be included in the table.



**Table 13: Review observations and recommendations**

Reference no. <sup>95</sup>	Asset management process or effectiveness criterion	Review priority	Observations & Recommendations	Process and policy rating	Performance rating
1	<b>Asset planning<sup>96</sup></b> Asset planning focuses on meeting customer needs in the most effective and efficient manner (delivering the right service at the right price)			B	2
1.1	Asset management plan covers the processes in this table.	4	<p>Through discussion with the office manager and inspection of the Asset Management Plan (AMP), we determined that the AMP provides some direction on the licensee's asset management framework and practices, including an overview of the major elements of the assets within the water supply works.</p> <p>The AMP could be expanded and restructured to accommodate the following elements of an effective AMP:</p> <ul style="list-style-type: none"> <li>• Lifecycle stages, from acquisition to disposal</li> <li>• Description of the network's core/tier 1 assets and extended assets</li> <li>• Legislative and other compliance obligations</li> <li>• Contingency arrangements</li> <li>• Service levels (specific to assets)</li> <li>• Arrangements for review and update of the AMP.</li> </ul> <p><b>Recommendation 01/2019:</b> Expand and restructure the AMP to accommodate the items raised in the findings above. The AMP should reference the licensee's systems, processes and procedures in place to manage each of the 12 key components of the asset management lifecycle.</p>	B	2

<sup>95</sup> The reference number is the number assigned to the asset management process or effectiveness criterion in Table 23.

<sup>96</sup> Auditors must base the overall effectiveness rating for each asset management process on the combination of the ratings for each effectiveness criterion.

### 5.1.8 Recommendations

The audit or review report must include recommendations on the actions the licensee should take to address:

- **(audit) compliance rating** – Licence obligations that were rated non-compliant.<sup>97</sup>
- **(audit) controls rating** – Licence obligations that were rated C or D.
- **(review) performance rating** – Asset management processes or effectiveness criteria that were rated 3 or 4.
- **(review) process and policy rating** – Asset management processes or effectiveness criteria that were rated C or D.

Auditors who wish to make recommendations for licence obligations, asset management processes or effectiveness criteria that received a rating other than those in the list above should provide those recommendations directly to the licensee. They should not be included in the audit or review report.

Auditors must present their recommendations in the tabular format shown in Table 14 (audits) or Table 15 (reviews).

**Table 14: Recommendations to address current non-compliances and control deficiencies**

A. Resolved during current audit period			
Licence obligation reference no. <sup>98</sup> / Recommendation reference from previous audit (if applicable)	Non-compliance / Controls improvement (Rating / Licence obligation / Details of non-compliance or inadequacy of controls)	Date resolved & action taken by the licensee	Auditor's comments
123 (01/2016)	<b>C3</b> <b>Water Services Code of Conduct (Customer Service Standards) 2013 - Clause 24</b> The audit identified instances where customer requests for bill redirection were not implemented.	20/3/19 – The licensee has reviewed their billing processes and made amendments to capture and report against customer requests for bill redirection.	No further action required.
B. Unresolved at end of current audit period			
Recommendation reference (no./year)	Non-compliance / Controls improvement (Rating / Licence obligation reference number & licence obligation / Details of non-compliance or inadequacy of controls)	Auditor's recommendation	Action taken by the licensee by end of audit period
02/2019	<b>B2</b> <b>(76) Water Services Regulations 2013 - Regulation 65(1)</b> The audit identified incomplete records in relation to two new lots. The documented process clearly identifies	Correct the records for the two lots identified by the audit. Undertake an audit of land records, with priority given to new lot	The two lot records have been completed. An audit of land records created over the last 10 years is scheduled for the next

<sup>97</sup> A licence obligation with a compliance rating of 2, 3 or 4.

<sup>98</sup> Refer to the Water Compliance Reporting Manual.

	the information to be recorded in land records, but it appears the process was not followed when the records were created for the new lots.	records created over the past five years.	internal records audit in 2019.
03/2019	<p><b>C1</b>  <b>(146) Water Services Code of Conduct (Customer Service Standards) 2013 – Clause 35(2)</b>  The complaints handbook is out-of-date as it states that unresolved complaints are referred to the Department of Water rather than the Energy and Water Ombudsman.</p>	<p>Update the handbook reference to replace the Department of Water with the Energy and Water Ombudsman as the entity that unresolved complaints are referred to.</p> <p>The licensee should implement a process to regularly review the handbook at least every two years.</p>	<p>The complaints handbook is undergoing a complete review, which will not be completed until 30 September 2019.</p> <p>The compliance register has been updated to require two yearly reviews of the complaints handbook,</p>

**Table 15: Recommendations to address current asset system deficiencies**

<b>A. Resolved during current review period</b>			
<b>Reference<sup>99</sup> / Recommendation reference from previous review (if applicable)</b>	<b>Process and policy deficiency / Performance deficiency</b> (Rating / Asset management process & effectiveness criterion / Details of deficiency)	<b>Date resolved &amp; action taken by the licensee</b>	<b>Auditor's comments</b>
7.3 (03/2017)	<p><b>A3</b>  <b>Asset Management Information System – Security access controls appear adequate, such as passwords.</b>  For 6 months during the review period, the password system for the Asset Management Information System could be easily by-passed by any staff member.</p>	20/3/19 – The licensee has implemented a system change ensuring the integrity of password security of the IT system. Only relevant staff with unique passwords can now access the Asset Management Information System.	No further action required.
<b>B. Unresolved at end of current review period</b>			
<b>Recommendation reference</b> (no./year)	<b>Process and policy deficiency / Performance deficiency</b> (Rating / Reference number, Asset management process & effectiveness criterion / Details of deficiency)	<b>Auditor's recommendation</b>	<b>Action taken by the licensee by end of review period</b>
01/2019	<p><b>A3</b>  <b>(6.3) Asset Maintenance – Maintenance plans (emergency, corrective and preventative) are documented and completed on schedule</b>  Preventative maintenance tasks for some pump stations were not</p>	<p>Focus on completing the outstanding preventative maintenance plans.</p> <p>Review the maintenance planner to identify the reasons why the overdue maintenance tasks were not detected.</p>	<p>The outstanding maintenance tasks are due to be completed by 30 September 2019.</p> <p>An error in the programming of the maintenance planner has been identified. The error is preventing the planner from raising an</p>

<sup>99</sup> Refer to Table 23 for the effectiveness criterion number.

	completed on schedule with some tasks being one year overdue.		error report when maintenance tasks are overdue. The supplier is currently trying to resolve the problem.
02/2019	<p><b>C2</b>  <b>(1.8) Asset Planning – Likelihood and consequences of asset failure are predicted.</b></p> <p>Likelihood and consequence of asset failure should be predicted in the asset management plan for infrastructure assets.</p> <p>Despite a number of recent pump failures, the likelihood and consequence ratings for these assets have not been updated in the asset management plan.</p>	<p>Update the likelihood and consequence ratings for main water pumps in the asset management plans.</p> <p>Review the asset management system fault management processes to ensure recurrent failure of assets triggers a review of the time to fail and likelihood of failure estimates.</p>	<p>The recommendation has not been addressed.</p> <p>The Manager, Assets will lead a project to review the asset fault management processes, but due to other high priority projects, this will not commence until 1 October 2020.</p>

Auditors must use the numbering convention described in Tables 14 and 15 to reference recommendations.<sup>100</sup>

Recommendations from the previous audit or review that were not resolved at the end of the previous audit or review period<sup>101</sup> must be included in Table 14 or 15, as follows:

- If the recommendation was resolved before the end of the current audit or review period, the recommendation must be included in Part A of Table 14 or 15 under the existing recommendation number.
- If all, or part, of the recommendation remained outstanding at the end of the current audit or review period, the recommendation must be included in Part B of Table 14 or 15 and allocated a new recommendation number.<sup>102</sup>

Recommendations must be ‘stand-alone’; the reader should be able to understand the findings that led to the recommendation without having to refer to other parts of the audit or review report.

Auditors should avoid repetition of recommendations where possible. If a recommendation covers many licence obligations or effectiveness criteria, the auditor should include it once in the observations section of the report and reference it in the observations for the other licence obligations or effectiveness criteria. The recommendations section of the report should have a single entry for the recommendation that includes each licence obligation or effectiveness criterion that it applies to.

Auditors must make recommendations that identify specific and measurable actions that the licensee should take and, if applicable, the outcomes that the actions are expected to achieve.<sup>103</sup>

<sup>100</sup> Auditors may prefix the recommendation number with an A (for audits) or R (for reviews).

<sup>101</sup> Part B of Tables 4 and 5.

<sup>102</sup> Auditors must include the new recommendation number in Table 4 or 5 to facilitate cross-referencing. See Part B of Tables 4 and 5 for an example.

<sup>103</sup> For example, the auditor should avoid phrases such as ‘the licensee should investigate [...]’ or ‘the licensee may consider [...]’.

### 5.1.9 Approval of the report by the auditor

Auditors must confirm their approval of the audit or review report by:

- stating the audit or review report is an accurate presentation of their findings and opinions
- attaching the signature of a person authorised to make the above statement on behalf of the auditor
- including the date the above signature was attached to the report
- including the address and contact details for the auditor.

Alternatively, auditors may provide this information in a cover letter attached to the report.

## 5.2 Post-audit and post-review implementation plans

The licensee must develop and submit to the ERA a post-audit or post-review implementation plan.

The post-audit or post-review implementation plan must identify for each recommendation made by the auditor:<sup>104</sup>

- The action(s) the licensee proposes to take to address the auditor's recommendation.
- The position(s) or business function(s) in the licensee's organisation responsible for undertaking the proposed action(s).
- The date the licensee will complete the proposed action(s).

The information must be presented in a tabular format. Table 16 is an example of a post-audit implementation plan.

**Table 16: Example of a post-audit implementation plan**

Recommendation reference (no./year)	Non-compliance / Controls improvement (Rating / Licence obligation reference number & licence obligation / Details of non- compliance or inadequacy of controls)	Auditor's recommendation	Action proposed to be taken by the licensee	Responsible person(s)	Target completion date
01/2019	<b>A2</b> <b>(102) Water Services Code of Conduct (Customer Service Standards) 2013 – Clause 12(3)</b> The auditor examined a sample of "Supply and	The licensee should ensure that bills refer to the fact complaints about the provision of a water service by the licensee or a failure by the licensee to	The licensee will review its billing process to ensure that all bills include the required information.	Regulatory Manager	30/06/2020

<sup>104</sup> Refer to section 5.1.8.

	Water Consumption Notices” and found one of the notices did not comply with the requirements of regulation 12(3). The notices did not state that complaints about the provision of a water service by the licensee or a failure by the licensee to provide a water service can be made in accordance with the licensee’s complaints procedure.	provide a water service can be made in accordance with the licensee’s complaints procedure.			
02/2019	<b>D1</b> <b>(103) Water Services Code of Conduct (Customer Service Standards) 2013 – Clause 13(1)</b> The licensee’s obligations spread sheet records this obligation but does not list a control therefore.	The licensee should develop and implement controls to ensure compliance with this obligation.	The licensee will ensure adequate controls are available to ensure customers are informed, on request, of the basis of the estimate and the reason for the estimate.	Credit Manager IT Manager	31/12/2020

The table can be adapted to apply to post-review implementation plans.

## 5.3 Reporting to the ERA

Auditors should forward a draft audit or review report to the ERA for comment before submitting the final report for approval.

The final version of the report must be provided in both Microsoft Word<sup>105</sup> and Adobe Acrobat format. The PDF version of the report must have the electronic signature of the auditor.<sup>106</sup>

The ERA prefers to receive the reports by email to [licensing@erawa.com.au](mailto:licensing@erawa.com.au), but will also accept documents stored on a USB or CD-ROM.

### 5.3.1 Confidential information

The ERA will provide a copy of the draft audit or review report to the licensee for comment.<sup>107</sup> If the licensee considers that the report contains confidential or commercially sensitive information, it must identify the information and advise the ERA accordingly. The ERA will consider a request from a licensee to redact this type of information prior to the ERA publishing the audit or review report on its website.

<sup>105</sup> The ERA will only use the Word version of the report to extract information to prepare internal ERA documents as well as a PDF version of the report for publication on the ERA website. The ERA will not circulate the Word version outside the ERA.

<sup>106</sup> The ERA will redact the signature before publication of the report on the ERA website.

<sup>107</sup> Refer to Appendix 5.

Licensees must not make a blanket claim of confidentiality or commercial sensitivity. If a licensee makes a request to redact this type of information, it must identify the exact information it is requesting the ERA to redact, provide specific reasons why the information should be redacted and, if necessary, provide sufficient evidence or supporting material to substantiate its request.

The ERA is unlikely to redact information that is already in the public domain, or on the basis that the information is commercially sensitive because it identifies potentially poor performance by the licensee. If the ERA considers a request is excessive or not substantiated, it will try to reach a negotiated outcome with the licensee as to what is redacted.

## 6. ERA approval of the report

The ERA will commence the approval process when it has received the final audit or review report and the post-audit or post-review implementation plan.

### 6.1 Approval

Upon approval of the audit or review report, the ERA will:

- Notify the licensee accordingly.<sup>110</sup>
- Publish the report and, if applicable, the post-audit or post-review implementation plan on the ERA website.

The ERA will also provide a copy of the report to the Minister for Water.<sup>111</sup> The ERA will publish the report on its website after it has been provided to the Minister.

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<sup>110</sup> The ERA will inform the auditor that the report has been approved and request them to submit their final invoice.

<sup>111</sup> Regulation 7 of the *Water Services Regulations 2013* provides that the ERA must give a report to the Minister on the audit or review within two months after receipt of the audit or review report.



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## Appendix 2 Documents referred to in the guidelines

Auditing Standard ASA 315	Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment <a href="http://www.auasb.gov.au/admin/file/content102/c3/ASA_315_Compiled_2015.pdf">http://www.auasb.gov.au/admin/file/content102/c3/ASA_315_Compiled_2015.pdf</a>
Auditing Standard ASA 500	Audit Evidence <a href="http://www.auasb.gov.au/admin/file/content102/c3/ASA_500_Compiled_2017.pdf">http://www.auasb.gov.au/admin/file/content102/c3/ASA_500_Compiled_2017.pdf</a>
Auditing Standard ASA 530	Audit Sampling <a href="http://www.auasb.gov.au/admin/file/content102/c3/ASA_530_27-10-09.pdf">http://www.auasb.gov.au/admin/file/content102/c3/ASA_530_27-10-09.pdf</a>
APES 110 (Compiled) <sup>112</sup>	Code of Ethics for Professional Accountants (2010) <a href="https://www.apesb.org.au/uploads/home/02112018000152_APES_110_Restructured_Code_Nov_2018.pdf">https://www.apesb.org.au/uploads/home/02112018000152_APES_110_Restructured_Code_Nov_2018.pdf</a>
AS ISO 31000:2018	Risk management – Guidelines
Standard on Assurance Engagements ASAE 3000	Assurance Engagements Other than Audits or Reviews of Historical Financial Information <a href="http://www.auasb.gov.au/admin/file/content102/c3/ASAE_3000_revised_2017.pdf">http://www.auasb.gov.au/admin/file/content102/c3/ASAE_3000_revised_2017.pdf</a>
Standard on Assurance Engagements ASAE 3100	Compliance Engagements <a href="http://www.auasb.gov.au/admin/file/content102/c3/ASAE_3100_Compliance_Engagements.pdf">http://www.auasb.gov.au/admin/file/content102/c3/ASAE_3100_Compliance_Engagements.pdf</a>

<sup>112</sup> APES 110 (2010) will be replaced with AEPS 110 (2018) from 1 January 2020. The new Code of Ethics is available on the [Accounting Professional & Ethical Standards Board website](#).

## Appendix 3 Risk-based approach to audits and reviews

The first stage of an audit or review is to conduct a preliminary assessment of the risk the licensee has not complied with one or more licence obligations or has not managed its assets effectively (preliminary risk assessment). The purpose of the assessment is to identify higher risk areas and focus the audit or review accordingly.

Auditors must document their initial risk assessment in the audit or review plan. During the fieldwork phase of the audit or review, the initial risk assessment should be reviewed and, if needed, amended to reflect the audit or review findings.

The ERA's approach to assessing risk in audits and reviews is in Diagram 1. The approach is based on AS ISO 31000:2018 (Risk Management – Guidelines).

**Diagram 1 – Risk management approach**



The following section explains the main elements of a preliminary risk assessment for audits and reviews.

### *Establish the context*

At the start of an audit or review, auditors should establish the relevant context of the licensee, including:

- the business objectives of the licensee
- organisational culture, structure, roles and accountabilities
- the relevant legal and regulatory environment that applies to the particular industry
- industry codes
- the licence conditions
- the ERA's regulatory functions and objectives
- for reviews, current asset management practices.

### *Identify the risks*

For audits, auditors must identify the risks that may affect the licensee's compliance with its licence obligations. Auditors must identify risks for each licence obligation.

For reviews, auditors must identify the risk that may affect the effectiveness of the licensee's asset management processes.

Auditors should identify risks based on their knowledge of the licensee's business<sup>113</sup> and the relevant regulatory framework. For illustrative purposes, the remainder of this appendix focuses on audits, but the processes for calculating audit priorities can be equally applied to determining review priorities for asset management processes.

## Analyse the risks

Auditors must analyse compliance risks using the following two-stage process:

1. Identify the consequences and likelihood of the inherent risks to give an overall inherent risk rating.
2. Identify and assess the strength of the existing internal controls mitigating the inherent risks.

These steps are explained in more detail below.

### *1. Identify the consequences and likelihood of the inherent risks to give an overall inherent risk rating*

An 'inherent risk' is the risk of an event occurring if there were no controls in place.

To calculate the 'inherent risk' for a licence obligation, auditors must first identify the consequences of the risk occurring. Auditors should use the classifications (major,<sup>114</sup> moderate<sup>115</sup> and minor<sup>116</sup>) for licence obligations included in the ERA's Water Compliance Reporting Manual to determine the consequences of the risk occurring.

Next, auditors must determine the likelihood of the risk occurring by using the 3-point rating scale described in Table 17.

**Table 17: Likelihood ratings**

	Level	Criteria
A	Likely	Non-compliance is expected to occur at least once or twice a year.
B	Probable	Non-compliance is expected to occur once every three years.
C	Unlikely	Non-compliance is expected to occur once every 10 years or longer.

Auditors must combine the consequence rating and likelihood rating to arrive at an overall inherent risk rating using the 3-point rating scale described in Table 18.

<sup>113</sup> Auditors should develop their knowledge of the licensee's business in consultation with the licensee.

<sup>114</sup> Type 1

<sup>115</sup> Type 2

<sup>116</sup> Not reportable (NR)

**Table 18: Inherent risk rating**

Likelihood	Consequence		
	1. Minor	2. Moderate	3. Major
A. Likely	Medium	High	High
B. Probable	Low	Medium	High
C. Unlikely	Low	Medium	High

Table 19 describes the three inherent risk ratings: low, medium and high.

**Table 19: Description of inherent risk ratings**

Level	Description
High	Likely to cause major damage, disruption or breach of licence obligations
Medium	Unlikely to cause major damage but may threaten the efficiency and effectiveness of service
Low	Unlikely to occur and consequences are relatively minor

## *2. Identify and assess the strength of the existing internal controls mitigating the inherent risks*

Once the auditor has identified and classified the inherent risks, they must assess the strength of the existing internal controls mitigating each inherent risk.

Licensees that have implemented effective controls to mitigate inherent risks should have fewer non-compliances than licensees who do not have effective controls. Auditors must examine the following internal control<sup>117</sup> components to assess the licensee's ability to manage its risks:

- **Control environment** – corporate culture, corporate governance, organisation structure, assignment of authority and responsibility, documentation of policies and procedures, human resource practices, records management, etc.
- **Licensee's risk assessment process**
- **Information systems** – including management and regulatory reporting and the business processes relevant to the licence conditions;
- **Control activities** – authorisation, segregation of duties, physical controls and security, IT controls etc.
- **Monitoring of controls** – management review, internal audit, other audits, veracity of management information etc.

The adequacy of controls must be assessed by using the 3-point rating scale described in Table 20.

<sup>117</sup> Auditing and Assurance Standard ASA 315 June 2011, Auditing and Assurance Standards Board.

**Table 20: Preliminary adequacy ratings for existing controls**

Level	Description
Strong	Controls mitigate the identified risks to a suitable level
Moderate	Controls only cover material risks; improvement required
Weak	Controls are weak or non-existent and do little to mitigate the risks

Auditors usually make a preliminary assessment of controls during the planning stage of the audit. Auditors should revise the risk assessment during the audit as they gather evidence on the effectiveness of the controls in place, and present the updated assessment in the audit report.

### *Evaluate the risks*

The next stage in the audit planning process is for the auditor to determine an audit priority for each of the licence obligation. The determination is based on the combined rating for inherent risk and control adequacy.

Auditors must determine the audit priority by using the 5-level audit priority scale described in Table 21.

**Table 21: Assessment of audit priority**

		Preliminary Adequacy of existing controls		
		Weak	Moderate	Strong
Inherent risk	High	Audit priority 1	Audit priority 2	
	Medium	Audit priority 3	Audit priority 4	
	Low	Audit priority 5		

The audit priority determines the audit objectives and the nature and extent of the audit procedures required.

Refer to section 3.2.4 for a discussion on the relationship between the audit priority and the audit procedures required to assess compliance.

### *Treat the risks*

If the auditor identifies risks that are not adequately mitigated by the internal control environment, the auditor must include recommendations in the audit report to strengthen the controls to address those risks.

## Appendix 4 A guide to the asset management system effectiveness framework

An asset management system comprises the processes and plans needed to ensure the physical assets continue to provide a specified level of service in a cost-effective manner throughout their useful life.

Assets should only exist to support service delivery objectives. When a service is in the planning stage it is necessary to identify the assets needed to meet a specified level of service. The extended life of assets involved in the delivery of water services requires decisions about asset acquisition to take account of the full operating costs over the asset's design life, so it is essential to understand the life-cycle of the assets used to deliver services.

### Asset life-cycle

Table 22 describes the four phases of the asset life-cycle that provide a structure to incorporate the entity's asset requirements into its broader strategic and corporate planning documentation.<sup>118</sup>

The life-cycle of an asset or group of assets has four distinct phases: planning, acquisition, operation and disposal.

**Table 22: Asset life cycle**

Activity	Supporting documentation
<b>Planning</b>	The need for the asset is identified and the requirement for a new asset is planned for and justified. Key elements include: asset planning strategy, planning for uncertainty, business cases, risk management, cost/benefit analysis, accounting treatment and consideration of non-asset alternatives.
<b>Acquisition</b>	The asset is purchased, constructed, or otherwise created. Key elements include: acquisition process, risk evaluation and procurement method.
<b>Operation</b>	The asset is used for its intended purpose. This stage may be marked by periodic refurbishment or major repair, requiring the asset to be taken out of service for periods of time. Key elements include: monitoring, maintenance, information management, asset valuation, utilisation and functionality.
<b>Disposal</b>	This is initiated when the economic life of the asset has expired, when there is no longer a need for the service provided by the asset or the asset in the provision of the service has been disposed of. Key elements include: retirement, replacement, renewal and redeployment.

Leadership and accountability are relevant to all stages of the asset management life-cycle. The key elements of leadership and accountability include governance, attestation, performance management, achievement of defined outcomes and continuous improvement. Typically, those responsible for planning and acquisition decisions in an organisation differ from those responsible for operation and disposal of the assets. Problems may arise due to

<sup>118</sup> Asset Management Accountability Framework, February 2016 (Victorian State Government)

this fragmentation of management responsibilities for assets over their life-cycle. For this reason, licensees need to ensure that leadership and accountability for the activities associated with each stage of the asset life-cycle have been assigned within the organisation, and that there is effective monitoring of asset management performance.<sup>119</sup>

## **Asset management processes**

The main processes in the asset management life-cycle are:

1. asset planning (including development and maintenance of an asset management plan)
2. asset creation and acquisition
3. asset disposal
4. environmental analysis (all external factors affecting the system)
5. asset operations
6. asset maintenance
7. asset management information system
8. risk management
9. contingency planning
10. financial planning
11. capital expenditure planning
12. review of the asset management system.

Table 23 examines each of these asset management processes in more detail and sets out the desirable outcomes, effectiveness criteria and a suggested approach to reviewing them. The suggested review approach is an example only and auditors should adapt the approach to each review.

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<sup>119</sup> As above.



**Table 23: Asset management processes and effectiveness criteria**

Process	Outcome	Effectiveness criteria	Example of review approach
<p><b>1. Asset planning</b> Asset planning strategies focuses on meeting customer needs in the most effective and efficient manner (delivering the right service at the right price).</p>	Asset planning is integrated into operational or business plans, providing a framework for existing and new assets to be effectively utilised and their service optimised.	<p>1.1 Asset management plan covers the processes in this table</p> <p>1.2 Planning processes and objectives reflect the needs of all stakeholders and are integrated with business planning</p> <p>1.3 Service levels are defined in the asset management plan</p> <p>1.4 Non-asset options (e.g. demand management) are considered</p> <p>1.5 Lifecycle costs of owning and operating assets are assessed</p> <p>1.6 Funding options are evaluated</p> <p>1.7 Costs are justified and cost drivers identified</p> <p>1.8 Likelihood and consequences of asset failure are predicted</p> <p>1.9 Asset management plan is regularly reviewed and updated</p>	<ul style="list-style-type: none"> <li>Assess the adequacy of the asset planning process</li> <li>Assess the adequacy of the asset management plan</li> <li>Assess whether the asset management plan is up-to-date and implemented in practice</li> <li>Assess whether the asset management plan clearly assigns responsibilities and whether these have been applied in practice</li> </ul>
<p><b>2. Asset creation and acquisition</b> Asset creation/acquisition is the provision or improvement of assets.</p>	The asset acquisition framework is economic, efficient and cost-effective; it reduces demand for new assets, lowers service costs and improves service delivery.	<p>2.1 Full project evaluations are undertaken for new assets, including comparative assessment of non-asset options</p> <p>2.2 Evaluations include all life-cycle costs</p> <p>2.3 Projects reflect sound engineering and business decisions</p> <p>2.4 Commissioning tests are documented and completed</p> <p>2.5 Ongoing legal / environmental / safety obligations of the asset owner are assigned and understood</p>	<ul style="list-style-type: none"> <li>Assess the adequacy of policies and procedures covering the creation and acquisition of assets</li> <li>Select a sample of asset creations/acquisitions over the review period and confirm adequate procedures have been followed and actual costs are as predicted</li> </ul>
<p><b>3. Asset disposal</b> Asset disposal is the consideration of alternatives for the disposal of surplus,</p>	The asset management framework minimises holdings of surplus and underperforming assets and lowers service costs.	<p>3.1 Under-utilised and under-performing assets are identified as part of a regular systematic review process</p>	<ul style="list-style-type: none"> <li>Assess the adequacy of policies and procedures covering the identification of under-performing assets, disposal of assets and replacement strategy</li> </ul>

Process	Outcome	Effectiveness criteria	Example of review approach
obsolete, under-performing or unserviceable assets.	The cost-benefits of disposal options are evaluated.	3.2 The reasons for under-utilisation or poor performance are critically examined and corrective action or disposal undertaken 3.3 Disposal alternatives are evaluated 3.4 There is a replacement strategy for assets	<ul style="list-style-type: none"> <li>Determine whether a regular review of the performance of assets is undertaken</li> <li>Select a sample of disposals over the review period and confirm adequate procedures have been followed</li> </ul>
<b>4. Environmental analysis</b> Environmental analysis examines the asset management system environment and assesses all external factors affecting the asset management system.	The asset management system regularly assesses external opportunities and threats and identifies corrective action to maintain performance requirements.	4.1 Opportunities and threats in the asset management system environment are assessed 4.2 Performance standards (availability of service, capacity, continuity, emergency response, etc.) are measured and achieved 4.3 Compliance with statutory and regulatory requirements 4.4 Service standard (customer service levels etc) are measured and achieved.	<ul style="list-style-type: none"> <li>Review achievement of performance and service standards over the review period</li> <li>Investigate any statutory or regulatory breaches and assess corrective action taken</li> <li>Review the adequacy of reporting and monitoring tools</li> </ul>
<b>5. Asset operations</b> Asset operations is the day-to-day running of assets (where the asset is used for its intended purpose).	The asset operation plans adequately document the processes and knowledge of staff in the operation of assets so service levels can be consistently achieved.	5.1 Operational policies and procedures are documented and linked to service levels required 5.2 Risk management is applied to prioritise operations tasks 4.3 Assets are documented in an asset register including asset type, location, material, plans of components, and an assessment of assets' physical/structural condition 5.4 Accounting data is documented for assets 5.5 Operational costs are measured and monitored 5.6 Staff resources are adequate and staff receive training commensurate with their responsibilities	<ul style="list-style-type: none"> <li>Assess the adequacy of policies and procedures covering operations functions</li> <li>Assess the adequacy of staff resourcing and training</li> <li>Confirm the policies and procedures have been followed during the review period by examining the asset register, observing operational procedures, analysing costs, etc.</li> <li>Assess the significance of exceptions identified and whether adequate corrective action has been taken</li> </ul>
<b>6. Asset maintenance</b> Asset maintenance is the upkeep of assets.	The asset maintenance plans cover the scheduling and resourcing of the maintenance tasks so work can be done on time and on cost.	6.1 Maintenance policies and procedures are documented and linked to service levels required 6.2 Regular inspections are undertaken of asset performance and condition 6.3 Maintenance plans (emergency, corrective and preventative) are documented and completed on schedule	<ul style="list-style-type: none"> <li>Assess the adequacy of policies and procedures covering maintenance functions</li> <li>Confirm the policies and procedures have been followed during the review period by examining maintenance schedules, analysing costs, etc.</li> </ul>

Process	Outcome	Effectiveness criteria	Example of review approach
		<p>6.4 Failures are analysed and operational/maintenance plans adjusted where necessary</p> <p>6.5 Risk management is applied to prioritise maintenance tasks</p> <p>6.6 Maintenance costs are measured and monitored</p>	<ul style="list-style-type: none"> <li>Assess the significance of exceptions identified and whether adequate corrective action has been taken</li> </ul>
<p><b>7. Asset management information system</b></p> <p>An asset management information system is a combination of processes, data and software supporting the asset management functions.</p>	<p>The asset management information system provides authorised, complete and accurate information for the day-to-day running of the asset management system.</p> <p>The focus of the review is the accuracy of performance information used by the licensee to monitor and report on service standards.</p>	<p>7.1 Adequate system documentation for users and IT operators</p> <p>7.2 Input controls include suitable verification and validation of data entered into the system</p> <p>7.3 Security access controls appear adequate, such as passwords</p> <p>7.4 Physical security access controls appear adequate</p> <p>7.5 Data backup procedures appear adequate and backups are tested</p> <p>7.6 Computations for licensee performance reporting are accurate</p> <p>7.7 Management reports appear adequate for the licensee to monitor licence obligations</p> <p>7.8 Adequate measures to protect asset management data from unauthorised access or theft by persons outside the organisation</p>	<ul style="list-style-type: none"> <li>Assess the adequacy of policies and procedures covering the general control and security of the computer systems used to provide management information on compliance with service standards / licence obligations</li> <li>Confirm management reports on service standards / licence obligations are reviewed and substantial exceptions to service standards / licence obligations are promptly followed up and implemented</li> </ul>
<p><b>8. Risk management</b></p> <p>Risk management involves the identification of risks and their management within an acceptable level of risk.</p>	<p>The risk management framework effectively manages the risk that the licensee does not maintain effective service standards</p>	<p>8.1 Risk management policies and procedures exist and are applied to minimise internal and external risks</p> <p>8.2 Risks are documented in a risk register and treatment plans are implemented and monitored</p> <p>8.3 Probability and consequences of asset failure are regularly assessed</p>	<ul style="list-style-type: none"> <li>Assess whether the risks that most affect the management and performance of the assets have been identified</li> <li>Assess the adequacy of policies and procedures covering risk management</li> <li>Assess whether the risk management policies and procedures have been applied in practice</li> <li>Assess the adequacy of staff understanding and training on risk management</li> </ul>

Process	Outcome	Effectiveness criteria	Example of review approach
<p><b>9. Contingency planning</b></p> <p>Contingency plans document the steps to deal with the unexpected failure of an asset.</p>	Contingency plans have been developed and tested to minimise any major disruptions to service standards.	9.1 Contingency plans are documented, understood and tested to confirm their operability and to cover higher risks	<ul style="list-style-type: none"> <li>Determine whether contingency plans have been developed and are current</li> <li>Determine whether contingency plans have been tested. If so, review the results to confirm any improvements identified have been implemented.</li> </ul>
<p><b>10. Financial planning</b></p> <p>Financial brings together the financial elements of the service delivery to ensure its financial viability over the long term.</p>	The financial plan is reliable and provides for the long-term financial viability of the services.	<p>10.1 The financial plan states the financial objectives and identifies strategies and actions to achieve those</p> <p>10.2 The financial plan identifies the source of funds for capital expenditure and recurrent costs</p> <p>10.3 The financial plan provides projections of operating statements (profit and loss) and statement of financial position (balance sheets)</p> <p>10.4 The financial plan provides firm predictions on income for the next five years and reasonable predictions beyond this period</p> <p>10.5 The financial plan provides for the operations and maintenance, administration and capital expenditure requirements of the services</p> <p>10.6 Large variances in actual/budget income and expenses are identified and corrective action taken where necessary</p>	<ul style="list-style-type: none"> <li>Obtain a copy of the financial planning, budgeting and reporting process and assess its effectiveness</li> <li>Obtain a copy of the current financial plan (including budget/actual) and assess whether the process is followed</li> </ul>
<p><b>11. Capital expenditure planning</b></p> <p>The capital expenditure plan provides a schedule of new works, rehabilitation and replacement works, together with estimated annual expenditure for these works over the next five or more years.</p> <p>Since capital investments tend to be large and lumpy, projections would normally be</p>	The capital expenditure plan provides reliable forward estimates of capital expenditure and asset disposal income. Reasons for the decisions and for the evaluation of alternatives and options are documented.	<p>11.1 There is a capital expenditure plan covering works to be undertaken, actions proposed, responsibilities and dates</p> <p>11.2 The capital expenditure plan provides reasons for capital expenditure and timing of expenditure</p> <p>11.3 The capital expenditure plan is consistent with the asset life and condition identified in the asset management plan</p> <p>11.4 There is an adequate process to ensure the capital expenditure plan is regularly updated and implemented</p>	<ul style="list-style-type: none"> <li>Understand the capital expenditure planning process and assess its effectiveness</li> <li>Obtain a copy of the capital expenditure plan for the current year and assess whether the process is being followed</li> </ul>

Process	Outcome	Effectiveness criteria	Example of review approach
<p>expected to cover at least 10 years, preferably longer. Projections over the next five years would usually be based on firm estimates.</p>			
<p><b>12. Review of AMS</b> The asset management system is regularly reviewed and updated.</p>	<p>The asset management system is regularly reviewed and updated.</p>	<p>12.1 A review process is in place to ensure the asset management plan and the asset management system described in it remain current</p> <p>12.2 Independent reviews (e.g. internal audit) are performed of the asset management system</p>	<ul style="list-style-type: none"> <li>• Determine when the asset management plan was last updated and assess whether any substantial changes have occurred</li> <li>• Determine whether any independent reviews have been performed. If so, review the results and action taken</li> <li>• Consider the need to update the asset management plan based on the results of this review</li> <li>• Determine when the asset management system was last reviewed.</li> </ul>

## Appendix 5 Audit and review process summary

The purpose of this appendix is to summarise the audit and review process to be undertaken by the licensee, the auditor and the ERA.

The ERA will consult with the licensee throughout the audit and review: before appointing the auditor, before approving the audit plan and before approving the audit or review report.

At each stage, the ERA will provide the licensee with all relevant information. Licensees will be given sufficient time to consider the information and provide their comments to the ERA.<sup>120</sup> If the ERA requests feedback from the licensee, the licensee must provide its response in writing.

When making its decision, the ERA will give reasonable consideration to the licensee's comments. If the ERA and licensee cannot agree, the ERA will take all reasonable steps to resolve the matter. If the ERA and licensee cannot reach a resolution, the ERA will make its own decision.

### Appointment of auditor

1. **(list of auditors)** The ERA draws up a list of potential auditors.
2. **(consultation with the licensee)** The ERA writes to the licensee notifying them of the upcoming audit or review. The letter will include the list of potential auditors and ask licensees to advise the ERA if they have knowledge of any matter that the ERA should consider when selecting an auditor. This could include conflicts of interest (such as consultancy services provided by the auditor) or recent or pending disputes between the licensee and the auditor.
3. **(adding auditors to the list)** If the consultation between the ERA and the licensee reduces the available pool of auditors to an unacceptable level, the ERA will, if possible, add additional auditors to the pool and repeat the process in step 2.
4. **(request for quotation)** The ERA issues a request for quotation (RFQ) to the auditors. The RFQ will require auditors to provide information responding to the requirements in Chapter 2 of these guidelines, and the offered price to conduct the audit or review. The ERA will appoint the auditor on a fixed price basis.
5. **(auditor selection)** The ERA selects a preferred auditor on the basis of value for money: price and the capacity to perform the audit or review to an acceptable standard. The ERA will notify the licensee of the ERA's proposed selection and provide the licensee with a copy of the selected quotation and a completed checklist summarising the other, unsuccessful, quotations.
6. **(consultation with the licensee)** The ERA invites the licensee to comment before the appointment of the auditor is finalised. For example, the licensee may wish to comment on the proposed audit scope, auditor expertise, audit financial terms or impact on its operations. If the licensee raises any issues, the ERA will try to resolve them by consulting with the licensee and, if needed, the auditor. If the issues cannot be resolved the ERA may select the second choice auditor and repeat step 5. Otherwise, the ERA will proceed to appoint the preferred auditor.

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<sup>120</sup> The ERA will advise the licensee of the due date for any action that must be taken by the licensee.

7. **(auditor appointment)** The ERA writes to the preferred auditor confirming their appointment. The letter will request that the auditor contact the licensee to commence the preparation of the audit or review plan.

### **Approval of the audit or review plan**

8. **(entry meeting)** Sometimes an audit or review entry meeting may be required. This will normally be identified at the end of the auditor approval process or at the commencement of the audit or review.<sup>121</sup> The ERA will arrange the entry meeting, which may be a meeting in person or a teleconference, depending on the location and availability of the participants.
9. **(scope of work)** Before the auditor can prepare the draft audit or review plan, the scope of the audit or review must be finalised. The scope of the audit or review will be detailed in the RFQ, but may be amended following feedback from the licensee or auditor during the latter stages of the auditor approval process. Similarly, if an entry meeting is held, the scope of the audit or review may be amended by the outcomes of the meeting.
10. **(draft audit or review plan)** When the scope of the audit or review has been finalised, the auditor prepares the audit or review plan. It is likely that the auditor will contact the licensee to obtain the information required to prepare the audit or review plan. The auditor must submit the draft audit or review plan to the ERA for approval.
11. **(consultation with licensee)** The ERA reviews the draft audit or review plan and provides a copy of the draft plan, and the ERA's comments on the draft plan, to the licensee. The ERA will invite the licensee to provide comments on the draft plan by the due date determined by the ERA.<sup>122</sup> The ERA will forward the comments to the auditor, who may submit a revised draft plan to the ERA. This process is repeated until the audit or review plan is finalised.
12. **(audit or review plan approval)** The ERA approves the audit or review plan. Although the ERA will try to agree the scope and content of the audit or review plan with the licensee, the ERA may approve the plan without the licensee's agreement.

### **Approval of the audit or review report**

13. **(fieldwork)** After the ERA has approved the audit or review plan, the auditor performs the audit or review fieldwork.
14. **(draft audit or review report)** The auditor prepares the draft audit or review report. The auditor must submit the draft audit or review report to the ERA for approval.
15. **(consultation with licensee)** The ERA reviews the draft audit or review report and provides a copy of the draft report, and the ERA's comments on the draft report, to the licensee. The ERA will invite the licensee to provide comments on the draft report by the due date determined by the ERA. The ERA will forward the comments to the auditor, who may submit a revised draft report to the ERA. This process is repeated until the audit or review report is finalised. Although the ERA will try to agree the scope and content of the

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<sup>121</sup> For example if there is a need to discuss any areas of special focus that have been identified by the ERA.

<sup>122</sup> For example, licensees may wish to provide comments on the suitability, safety and timing of any proposed site visit(s), the timing of audit and review procedures and obligations that the licensee considers may not be applicable to the licensee's operations.

audit or review report with the licensee, the ERA may approve the report without the licensee's agreement.

16. **(post-audit or post-review implementation plan)** When the ERA has received the final audit or review report, the ERA will forward a copy of the report to the licensee. If applicable, the ERA will request the licensee to submit a post-audit or post-review implementation plan for the ERA's approval. The ERA may request the licensee to amend the draft post-audit or post-review implementation plan.
17. **(audit or review report approval)** When the audit or review report and, if applicable, the post-audit or post-review implementation plan have been finalised, the ERA's Secretariat will forward the documents to the ERA's Governing Body for approval.

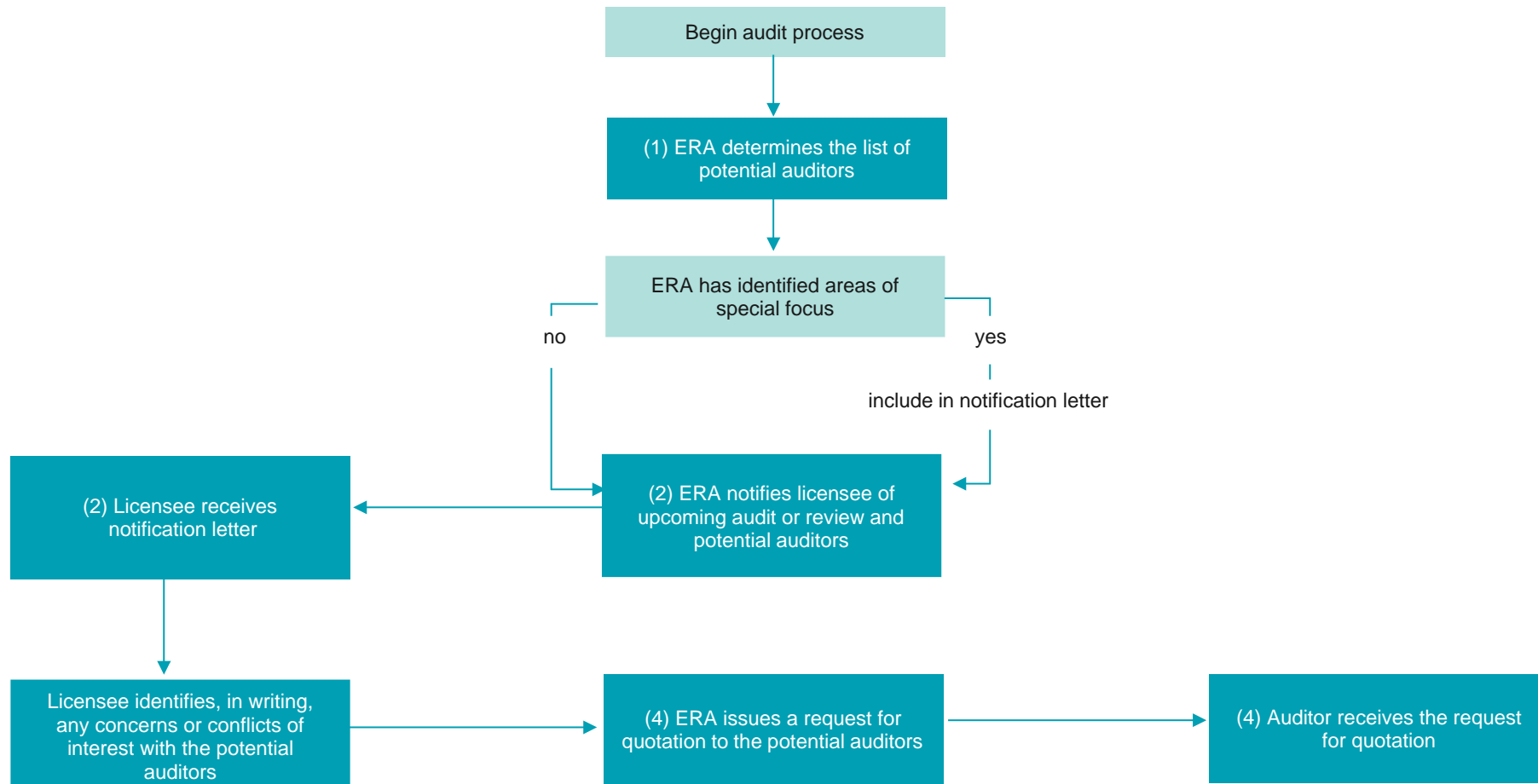


*Appointment of auditor*

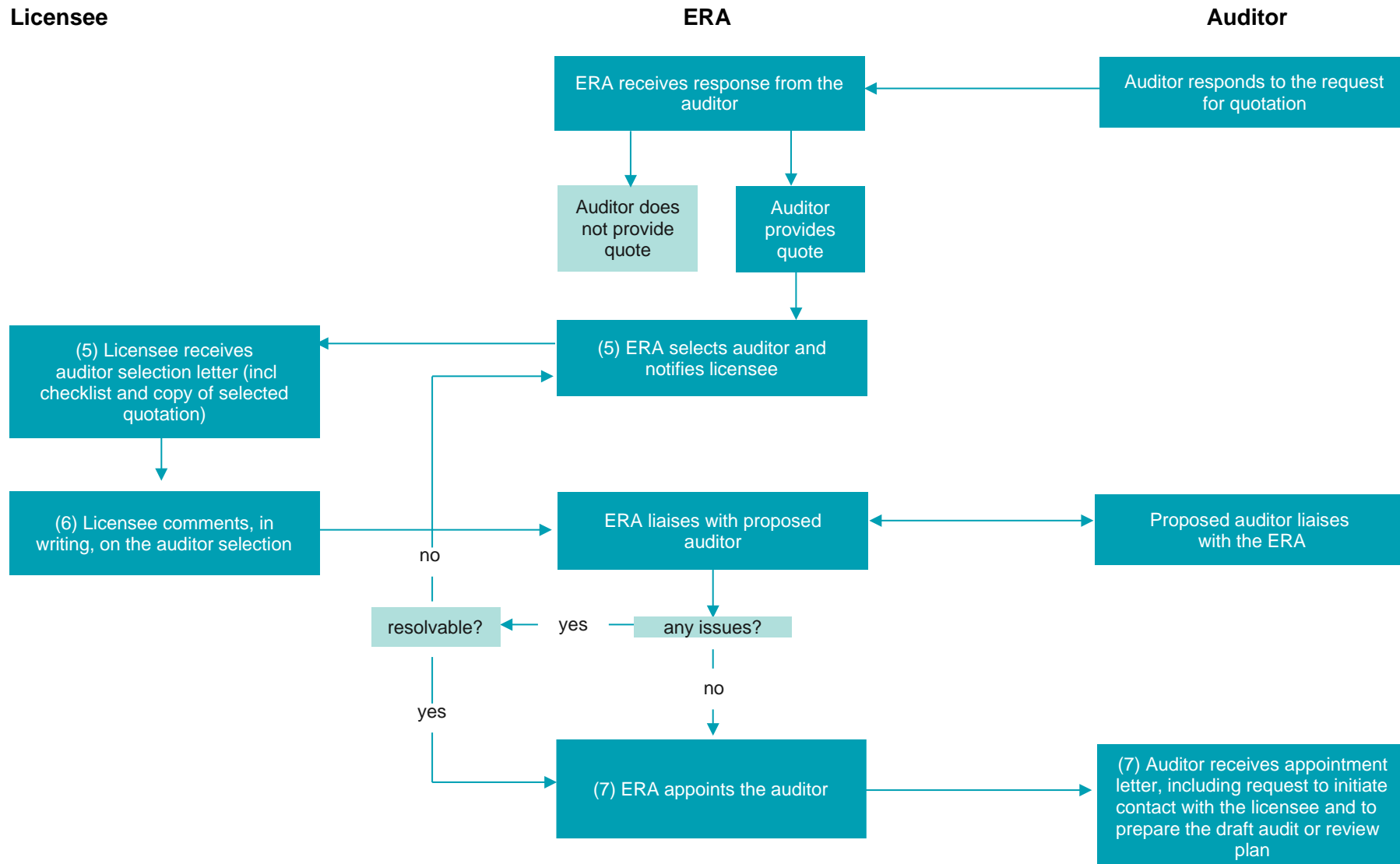
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**ERA**

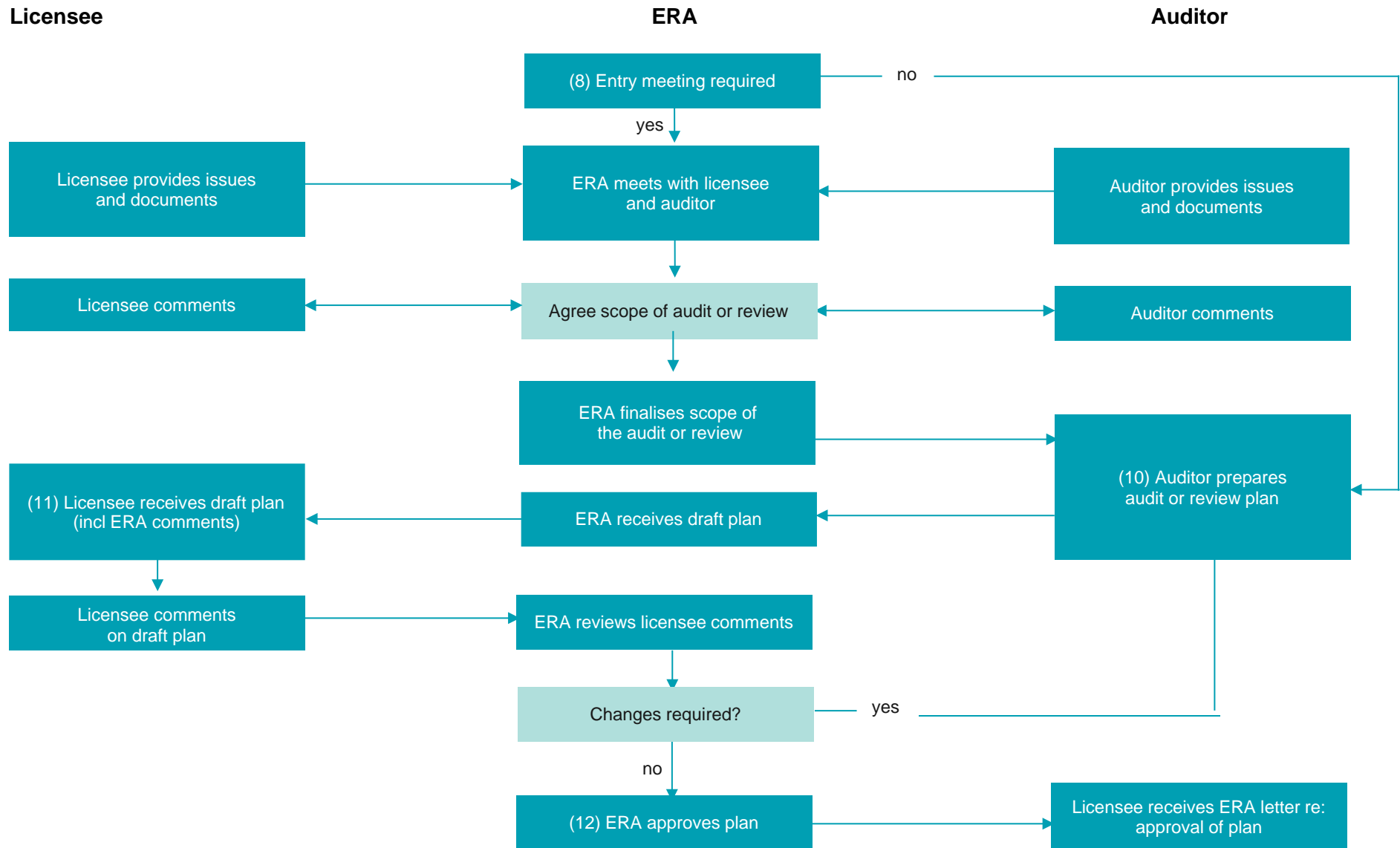
**Auditor**



Appointment of auditor (continued)



*Approval of the audit or review plan*



*Approval of the audit or review report*

