

Independent Pricing and Regulatory Tribunal  
New South Wales

# Audit Guideline

## Public Water Utilities

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## Amendment record

Issue	Date issued	Summary of amendments made
Revised PWUAG - original	June 2018	First release of final Audit Guideline (2018)
PWUAG – Rev 2	Sept 2018	Changes to section 2.4 under ‘Conflict of Interest’,
PWUAG – Rev 3	May 2019	Draft Audit Guideline for comment
PWUAG – Rev 4	July 2019	First release of final Audit Guideline (2019)

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# 1 Introduction

## 1.1 Purpose

The purpose of this Audit Guideline (**guideline**) is to set out IPART's expectations on the conduct of operational audits of public water utilities (**PWUs**), and to guide auditors and PWUs in carrying out their responsibilities during operational audits. Table 1.1 provides an outline of responsibilities of audit parties.

**Table 1.1 Responsibilities of audit parties**

IPART	Auditor	PWU
Sets the framework to prepare for and conduct operational audits efficiently and effectively	Uses the audit scope to investigate the PWU's operations and systems	Cooperates throughout the audit process Provides information to the auditor and IPART Provides access to the auditor and IPART to works, premises or offices Permits the auditor and IPART to carry out certain inspections and investigations
Makes recommendations to the PWU	Documents audit findings	Completes its reporting requirements as outlined in its Reporting Manual
Reports to the Minister(s)	Provides recommendations and opportunities for improvement	Provides a commitment to address audit findings

IPART audits the operating licences (**licences**) of the following PWUs:

- ▼ Hunter Water Corporation
- ▼ Sydney Water Corporation
- ▼ Water NSW.

The guideline may not provide complete guidance in all circumstances, in which case auditors and PWUs should seek clarification from IPART. In these cases, we will provide specific advice on the application of the guidelines or appropriate departures from the guidelines where necessary.

Basic requirements for operational audits and the related obligations of PWUs are set out in the licences of PWUs. This guideline sets out more detailed expectations for the conduct of operational audits. Where there is an inconsistency between this guideline and the requirements of a relevant licence, the licence requirements will prevail. Additional obligations of auditors will be set out in a contract between IPART and the auditor.

## 1.2 Structure of the guideline

The guideline is structured as follows:

### Chapter 1 – Introduction

This chapter outlines the purpose of the guideline and provides an overview of the regulatory context.

### Chapter 2 - Audit fundamentals

This chapter outlines:

- ▼ How and why we undertake audits
- ▼ The appropriate auditing standards
- ▼ How to deal with matters outside the audit scope
- ▼ Requirements in relation to conflicts of interest
- ▼ Quality assurance requirements.

### Chapter 3 - Operational Audit Procedure

This chapter outlines:

- ▼ The audit process – details of the steps in the audit process, including actions, responsibilities and outputs
- ▼ Escalation of issues – details the process for the escalation of issues
- ▼ Audit timetable – details of the timing of the steps in the audit process.

## 1.3 Changing the guideline

We may change this guideline to:

- ▼ Reflect changes in the legislation or licence conditions
- ▼ Amend the audit information that must be provided to IPART
- ▼ Improve the audit process.

Before we change the guideline significantly, we will consult relevant PWUs and other relevant stakeholders. We will then notify stakeholders of the changes to the guideline and the start date for any new auditing arrangements. In determining the start date, we will consider the time required for PWUs to implement new arrangements.

## 1.4 Auditor or PWU feedback

Over time, auditors and PWUs are likely to identify opportunities for improving the audit framework, or other aspects of the audit process. We encourage auditors and PWUs to provide us with feedback on any issues, and submit recommendations to make the audit process or the licensing framework more efficient and effective.



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## 1.5 National Water Initiative audits

The Bureau of Meteorology (**BOM**) produces an annual Urban National Performance Report (**Urban NPR**) as part of the National Water Initiative (**NWI**). The Urban NPR publicly and independently reports on the performance of PWUs across Australia. The Urban NPR is based on data from NWI performance indicators about customers, health, water resources, assets, environment, pricing and finances.

We undertake audits of the NWI performance indicators as part of the operational audits.<sup>1</sup> However, this guideline does not apply to the NWI component of the operational audits.

The *National Urban Water Utility Performance Reporting Framework* outlines the auditing requirements in relation to NWI performance indicators and provides an audit report template for use by PWUs in collecting data and reporting on a set group of indicators. We use this framework for NWI audits, rather than the guideline. For further information on these audits, please contact us and we can provide the latest handbook from the BOM.

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<sup>1</sup> We undertake this work as part of our obligations as Data Coordinator and Audit Coordinator for NSW PWUs in the National Framework for Reporting on Performance of Urban Water Utilities Deed.

## 2 Audit fundamentals

### 2.1 Introduction

We undertake an operational audit of each PWU annually to assess the PWU's compliance with:

- ▼ Its operating licence conditions
- ▼ Its Reporting Manual
- ▼ Any matters required by the Minister.

In order to assess a PWU's compliance with the above requirements, the audit may also review the PWU's compliance with relevant legislation and recommendations from previous operational audits.

In particular, the audit assesses whether the PWUs provide services that meet the performance standards and other criteria set out in the operating licence. Audits also provide an opportunity to identify where PWUs have demonstrated best practice and exceeded the standard.

We engage an independent auditor<sup>2</sup> to audit each PWU at the PWU's expense.<sup>3</sup> The auditor is appointed to assess compliance against quantitative and qualitative criteria and to provide their professional judgement in a formal report. Auditors must remain independent at all times during the audit process and PWUs must respect that independence.

#### Risk-based approach

We use a risk-based approach to the operational audits, in order to:

- ▼ Efficiently allocate our focus to areas of higher consequences due to non-compliance.
- ▼ Minimise costs to our regulated PWUs.
- ▼ Avoid broader costs to the community.

Risk is a function of both the consequence and likelihood of harm in the absence of regulatory controls. We evaluate the consequence and likelihood using the descriptors in our *Compliance and Enforcement Policy, December 2017*.<sup>4</sup> Once we have considered likelihood and consequence for each licence clause, we consider the overall risk, using a risk matrix.<sup>5</sup> Using this risk-based approach, we focus on those licence clauses that have the highest evaluated risk.

<sup>2</sup> The auditor would generally be an audit team which may include lead auditors, auditors and area specialists (see Section 3.1).

<sup>3</sup> Section 18D of the *Hunter Water Act 1991*, Section 33A of the *Sydney Water Act 1994* and Section 60 of the *Water NSW Act 2014* requires the relevant PWU to pay NSW Treasury "the cost (as certified by the Tribunal) involved in connection with carrying out the operational audit" of the PWU.

<sup>4</sup> IPART, *Compliance and Enforcement Policy, December 2017*, available on our website, <https://www.ipart.nsw.gov.au/files/sharedassets/website/shared-files/licensing-policy-cross-industry-review-of-ipart-compliance-and-enforcement-policy-2017/ipart-compliance-and-enforcement-policy-december-2017.pdf>

<sup>5</sup> Ibid, p7.

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For this reason, we do not require an audit of all the clauses in the PWU's licence every year. The audit frequency of a clause will depend on the risk that a potential non-compliance poses, as well as the PWU's previous performance. Our approach will ensure that auditing reflects the type, size, complexity and consequences of the potential non-compliance. Further, when combined with likelihood, our approach determines the level of risk associated with the PWU's activities.<sup>6</sup>

We will audit all auditable clauses at least once during a 5-year licence period. The audit of the first year of a new licence is likely to be more comprehensive in order to help identify any areas that we should focus on through the licence period.

### **Statement of Compliance**

The PWU must also report on all its licence obligations in an annual statement of compliance, as detailed in each PWU's Reporting Manual.<sup>7</sup> The PWU is to complete the statement of compliance to the best of its knowledge and have it signed by the CEO (or Managing Director or equivalent) and Chairman of the Board or otherwise an authorised Board Director.

### **Stakeholder consultation**

IPART engages with stakeholders during the operational audit process. We also invite submissions from the public. This allows the public to contribute to the operational audits if they have particular issues that they wish to raise regarding the audits or PWU performance. In determining the audit scope we consider issues identified in our public consultation process.

Further, prior to finalising the audit scope, IPART will seek feedback from relevant government agencies (ie, those that are referred to in a PWUs licence) regarding the performance of the PWU during the audit period for the functions administered or regulated by the agency. Agencies may include NSW Health, Environment Protection Authority, Department of Planning and Environment, Department of Industry - Water (including the Water Administration Ministerial Corporation), Natural Resources Access Regulator, and/or Fire & Rescue NSW. If necessary, IPART will follow up with the relevant government agencies in relation to submissions received.

If the auditor considers that further consultation would assist its conduct of the audit, the auditor should contact IPART and all information requests to government agencies should be submitted by IPART, in writing, to the relevant agency contact person. Similarly, if the auditor considers that consultation with customers would assist with the audit, the auditor should again contact IPART and we will consider the most appropriate way to manage any information requests on a case-by-case basis.<sup>8</sup>

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<sup>6</sup> For example, a non-compliance in the area of water quality is more likely to present significant consequences to human health than the consequences of late reporting about customer complaints. Hence, we audit water quality performance every year and retail clauses less frequently.

<sup>7</sup> The template for the statement of compliance is available in the Reporting Manuals for each PWU.

<sup>8</sup> This is not likely to be applicable to private individuals for privacy reasons but is rather intended to include large customers such as councils.

## Auditing of water quality management systems

Auditing of water quality management systems (WQMSs) may require assessment of the individual elements that make up the water quality management systems framework provided by the *Australian Drinking Water Guidelines* (ADWG) and the *Australian Guidelines for Water Recycling* (AGWR). The auditor may assign grades for each audited element to inform its overall assessment grade.

We consider the licence clauses regarding water quality management systems are high risk, and therefore we generally include them in the audit scope every year. However, each of the 12 elements in ADWG and AGWR have a different level of risk and by applying our risk-based approach, we may decide to focus on particular elements in annual audits.

We will consult with NSW Health prior to finalising our audit scopes. The audit scope may provide the auditor with direction regarding the elements to focus on in the annual audit when auditing the water quality clauses.

We do not require an auditor to assign audit grades to individual elements; this is a decision for the auditor. Further, we do not apply any 'rule' of assigning an overall grade based on the lowest grade assigned to an individual element. Instead, the auditor must assign an overall grade which, in the auditor's opinion, weights the relative significance of the individual element grades.

### Overlap with other audits

PWUs may have parts of their operation audited under other frameworks, such as certification schemes or other legislation. We have progressively moved licences towards systems-based licence conditions, which require PWUs to have an Asset Management System (AMS), Environmental Management Systems (EMS), and/or Quality Management Systems (QMS) in place.

Where a system is subject to an operational audit under the PWU's operating licence, the PWU may present the outcome of any surveillance or certification (or re-certification) report to the auditor, in lieu of a formal audit. Acceptance of the report in lieu of a formal audit will depend on whether the systems are certified or not certified.

Specifically, for certified systems:

- ▼ AMS – as we consider that some auditors may not have specific water industry expertise to assess systems and technical aspects relevant to the water industry, IPART will assess the surveillance/certification reports from PWUs. We will then consider whether to accept all or part of the report in lieu of having an audit of the relevant condition.
- ▼ EMS – as we consider specific water industry experience is not necessary to effectively audit an EMS, we generally accept surveillance/certification reports from EMS-specialist auditors, and our auditor should accept these reports in lieu of conducting a formal audit.
- ▼ QMS – as we consider specific water industry experience is not necessary to effectively audit a QMS, we generally accept surveillance/certification reports from QMS-specialist auditors, and our auditor should accept these reports in lieu of conducting a formal audit.

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Where certified systems are not in place, the auditor will assess compliance in accordance with the audit scope or direction provided by IPART.

We will adjust our operational audit scopes to take account of these other audits. We encourage our auditors to use the data and audit opinion from other relevant audits rather than duplicating the audit effort.

For certification reports accepted by IPART, our auditor may review the reports to assess whether they demonstrate compliance with the PWU's licence obligation(s) in relation to the management system. Where compliance cannot be established, the auditor will note their findings and make recommendation(s) to the PWU to improve its management system to achieve compliance. Should the auditor identify that it is not possible to determine compliance or to make recommendations to achieve compliance based on the certification reports, the auditor should advise IPART and IPART will decide if an additional audit of the PWU's management system is required.

PWUs should inform IPART of any upcoming management system audits. This will allow IPART to attend and provide input to an audit where the PWU is seeking consideration of audit results. IPART reserves its right to attend or not attend certification and/or surveillance audits.

## **2.2 Matters outside the audit scope**

In general, we require auditors to stay within the scope of the audit. However, occasionally the auditor may identify issues that may pose a significant risk to public health or the environment which fall outside the scope of the audit.

If these issues relate to the licence clauses the auditor may continue the investigation of the 'out of scope' issue with the concurrence of the IPART representative in attendance at the audit. If the issue is outside the scope of the licence clauses, IPART will refer the matter to the relevant agency.

The auditor should detail any out of scope findings in a covering letter attached to the audit report. The letter may also include any specific concerns the auditor has relating to trends in performance that may lead to potential future non-compliance. IPART will provide a copy of the auditor's letter to the PWU. The auditor should consult with IPART about where and how to document out of scope findings. Where IPART makes recommendations to the Minister regarding the out of scope issues identified, in accordance with its powers under the relevant legislation, IPART will give the PWU an opportunity to address the identified issue(s) in the Status Report on Recommendations.<sup>9</sup>

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<sup>9</sup> The Status Report on Recommendations refers to the annual audit recommendations status report, as required under clause 6.1.2 of the Hunter Water Reporting Manual, clause 9.1 of the Sydney Water Reporting Manual and clause 7.1.2 of the Water NSW Reporting Manual.

## 2.3 Significant risk to public health

Where auditors or IPART staff attending an audit identify an issue that may pose a significant risk to public health, IPART will contact NSW Health and the PWU, to enable the PWU to activate relevant incident management protocols, if necessary.

## 2.4 Independence

### Conflict of interest

Auditors must conduct all audits independently of the PWU.

Auditors who submit a scope of work in response to our Request for Quotes (RFQs) for the PWU audits must include a conflict of interest statement. A template conflict of interest statement is attached at **Appendix A**.

In the conflict of interest statement, the auditor must either:

- ▼ Confirm that the auditor has no conflict of interest or
- ▼ Identify and describe any conflict of interest (including any actual, potential or perceived conflict).

If any member of the audit team, or if the audit firm to which an audit team member belongs, has previously provided services to a PWU, the audit proposal must include a table summarising the history of paid work between the parties in the past two years. Further, the audit proposal should identify and describe any conflicts of interest (including any actual, potential or perceived conflict), as required in the conflict of interest statement.

Where the auditor has identified a conflict of interest (whether actual, potential or perceived), the auditor must specify steps that the auditor proposes to take to manage the conflict. IPART will then consider whether the conflict of interest can be appropriately managed. Where IPART does not consider that the conflict of interest can be appropriately managed, we will engage a different auditor.

While IPART will consider conflicts of interest on a case-by-case basis, conflicts of the following type would generally not be capable of being appropriately managed:

- ▼ An auditor or member of the audit team is engaged in providing other fee-paying services to the PWU during the course of the audit services or is in the process of making an offer to do so.
- ▼ The auditor has provided services to the PWU within the past two years.
- ▼ A material proportion of the auditor's total annual revenue is derived from fee-paying services provided to the PWU.
- ▼ The auditor is not independent of the scoped audit items.
- ▼ The auditor is the incumbent internal auditor for the PWU.
- ▼ The auditor has performed an advisory or technical function for the PWU in relation to the particular project being audited within the last two years.

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If the auditor becomes aware of a conflict of interest (whether actual, potential or perceived) after being appointed to conduct an audit, they must notify IPART as soon as possible after the discovery. The auditor must provide any information to IPART, on request, concerning any conflict of interest. The auditor must have adequate internal procedures to identify and manage potential conflicts of interest before accepting any IPART engagements.

Where a conflict of interest becomes apparent after an auditor has been engaged, we may require the auditor to withdraw from the engagement.

### **The ‘three in five’ rule**

The same auditor<sup>10</sup> should not be used more than three times in every five audits for a particular audit category. The ‘three in five audit rule’ ensures that each PWU is audited by different auditors over time. This allows a new perspective and helps to ensure the auditor’s independence.

This is our preferred and general approach. In exceptional circumstances we may approve an exemption to this rule (for example, if there is a shortage of suitable auditors), and if we are satisfied that a new perspective can be offered (eg, a different audit team), and that the auditor’s independence won’t be compromised.

## **2.5 Quality**

IPART holds auditors undertaking audits for IPART to high professional standards and expects that auditors will conduct audits and prepare reports with rigour.

### **Application of auditing standards**

We require all auditors to:

- ▼ Define the requirements of the audit
- ▼ Systematically plan the audit
- ▼ Collect audit evidence
- ▼ Objectively assess the evidence
- ▼ Report in a clear and accurate manner.

**It is the auditor’s responsibility** to select an appropriate standard. Appropriate standards may include:

- ▼ ASAE 3000 - Assurance Engagements Other than Audits or Reviews of Historical Financial Information
- ▼ AS/NZS ISO 19011 - Guidelines for auditing management systems, Standards Australia
- ▼ ISAE 3000 - International Standard on Assurance Engagements.

Auditors must disclose the standard they have used to conduct the audit in the final audit report.

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<sup>10</sup> This refers to the audit firm, not just the lead auditor or audit team.



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The auditing principles set out in **Appendix B** apply to the conduct of audits, regardless of the auditing standard used. We expect auditors to adopt the audit methods set out in **Appendix C**, and ensure those methods meet the principles outlined in Appendix B.

Lead auditors must use their professional judgement to determine the mix of audit methods needed to obtain sufficient evidence to support an opinion on each item within the scope.

We require auditors to maintain an accurate record of documents sighted. Auditors do not need to submit this record with the final audit report. However, records of audits must be securely and confidentially maintained for a reasonable period (and no less than seven years), given the sensitivity of the material.

### **Peer review**

Peer review is an important quality control process under the IPART audit framework and IPART requires auditors to arrange for peer review of audit reports. A peer reviewer:

- ▼ Should be equivalent or higher in authority and experience to the audit team leader.
- ▼ Is required to demonstrate the same level of independence as the auditor (and submit to IPART a Conflict of Interest statement, as per Appendix A).
- ▼ May be within, or external to the audit firm.

The peer reviewer must have professional experience that is demonstrably equal with, or has authority over, the lead auditor, particularly for assurance. The peer reviewer must be able to objectively evaluate the significant judgements the lead auditor has made and the conclusions they have reached to formulate their opinion.

Our preferred approach is that peer reviewers should not be involved in the conduct of the audit or approval of audit reports. We may approve a different approach if there is a shortage of suitable peer reviewers, and if we are satisfied that the proposed approach adequately controls quality.

The individual(s) proposed to perform the peer review must be nominated in the audit proposal.

The appointment of a peer reviewer should not limit or preclude the lead auditor from using other expertise from outside the audit team to review or assist with particular technical elements of the engagement.

### **Quality assurance**

A robust system of quality control must be in place for all auditors. Many auditors or their employers will have existing quality control frameworks in place, such as AS/NZS ISO 9001 - *Quality Management*.

While providing a robust framework, these systems may not have been designed with consideration of risks specific to IPART audits. Therefore, as part of the audit planning the lead auditor should check that their quality control framework will be effective in managing any associated audit risk.



## Auditor feedback

Where we consider that an audit or auditor has failed to apply the level of professionalism or rigour expected, we will provide the auditor with feedback and ask the auditor to take steps to address any inadequacies. This may occur when the auditor delivers the draft report to us. In some circumstances, a meeting between IPART and the auditor may be required to discuss the issue and agree on amendments.





Where we consider that an auditor is unable to provide audit services to the standard required, we may decline to approve future auditor nominations for that auditor.

## 2.6 Audit grades

An auditor must assess a PWU's compliance with its licence clauses in accordance with the scope specified by IPART, and assign grades for those requirements. When assessing a PWU's assets, the auditor will assess from catchment to consumer (or the equivalent water cycle components applicable to a PWU's operations).

The audit grades are shown in Figure 2.1.

Figure 2.1 Audit Grades

Grades of compliance	Description
 <b>Compliant</b>	Sufficient evidence is available to confirm that the requirements have been met.
 <b>Compliant (minor shortcomings)</b>	Sufficient evidence is available to confirm that the requirements have been met apart from <b>minor shortcomings</b> which to date have not compromised the ability of the utility to achieve defined objectives or assure controlled processes, products or outcomes.
 <b>Non-compliant (non-material)</b>	Sufficient evidence is not available to confirm that the requirements have been met and the <b>deficiency does not adversely impact</b> the ability of the utility to achieve defined objectives or assure controlled processes, products or outcomes.
 <b>Non-compliant (material)</b>	Sufficient evidence is not available to confirm the requirements have been met and the <b>deficiency does adversely impact</b> the ability of the utility to achieve defined objectives or assure controlled processes, products or outcomes.

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Grades of compliance	Description
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**No Requirement**

There is no requirement for the utility to meet this criterion within the audit period.

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## 3 Operational audit procedure

### 3.1 The audit process

This section of the guideline outlines the steps involved in the audit process. We have adopted a systematic audit method to promote consistency across auditors and over time. The auditor is an independent expert acting on behalf of IPART. However, we reserve the right to accept, amend or reject the auditor's assigned audit grades and recommendations.

There are seven steps to an audit, and each of the parties (the PWU, auditor and IPART) is responsible for completing some of the steps. Figure 3.1 provides an overview of each party's responsibilities in the audit process, and the sections that follow provide more detail on these processes.

The operating licences require PWUs to provide certain assistance to IPART and auditors throughout the audit process, including by providing information, providing access to certain works or premises, and permitting other investigations or inspections to be carried out as specified in each licence.

#### Step 1: Audit scoping

We will determine the scope of the audit. The audit scope is based on the conditions in the operating licence (which, in turn is based on the requirements of the enabling legislation) and cover the breadth of a PWU's business. The audit scope also determines the scope of the auditor's contract with IPART.

We use a risk-based approach (described in Section 2.1) to determine which conditions to include in the audit scope, and consider issues identified by relevant government agencies and the public during our consultation process. All licence obligations are also subject to a statement of compliance from the PWU and this also informs our risk-based approach.

#### Step 2: Appointment of auditor

Where possible, IPART will request quotes from at least three auditors for each PWU audit. This gives us a good understanding of the market rate, and ensures we are able to appoint quality auditors. We reserve the right to undertake single-source procurement if market conditions do not permit competitive procurement.

We engage suitably qualified auditors through the NSW Government's Performance and Management Services Scheme Panel for PWU audits. Our assessment criteria for engaging auditors includes relevant team experience, technical and audit expertise, resource availability and cost.

Auditors are assessed against three classifications:

1. **Lead Auditors** are recognised as competent to undertake audits independently<sup>11</sup> or to lead an audit team. All audit work including sign-off on audit reports, must be undertaken by, or under the direct control and supervision of, a lead auditor.
2. **Auditors** are recognised as competent to undertake audits as a member of an audit team. Auditors may not have sufficient experience to lead an audit.
3. **Area Specialists** are senior technical professionals with specific skills, competencies and experience in their industry fields. An Area Specialist may not have the necessary skills and experience to conduct audits.

Any other staff, employees or contractors may only help the audit team in areas such as administrative support and/or auditor training.

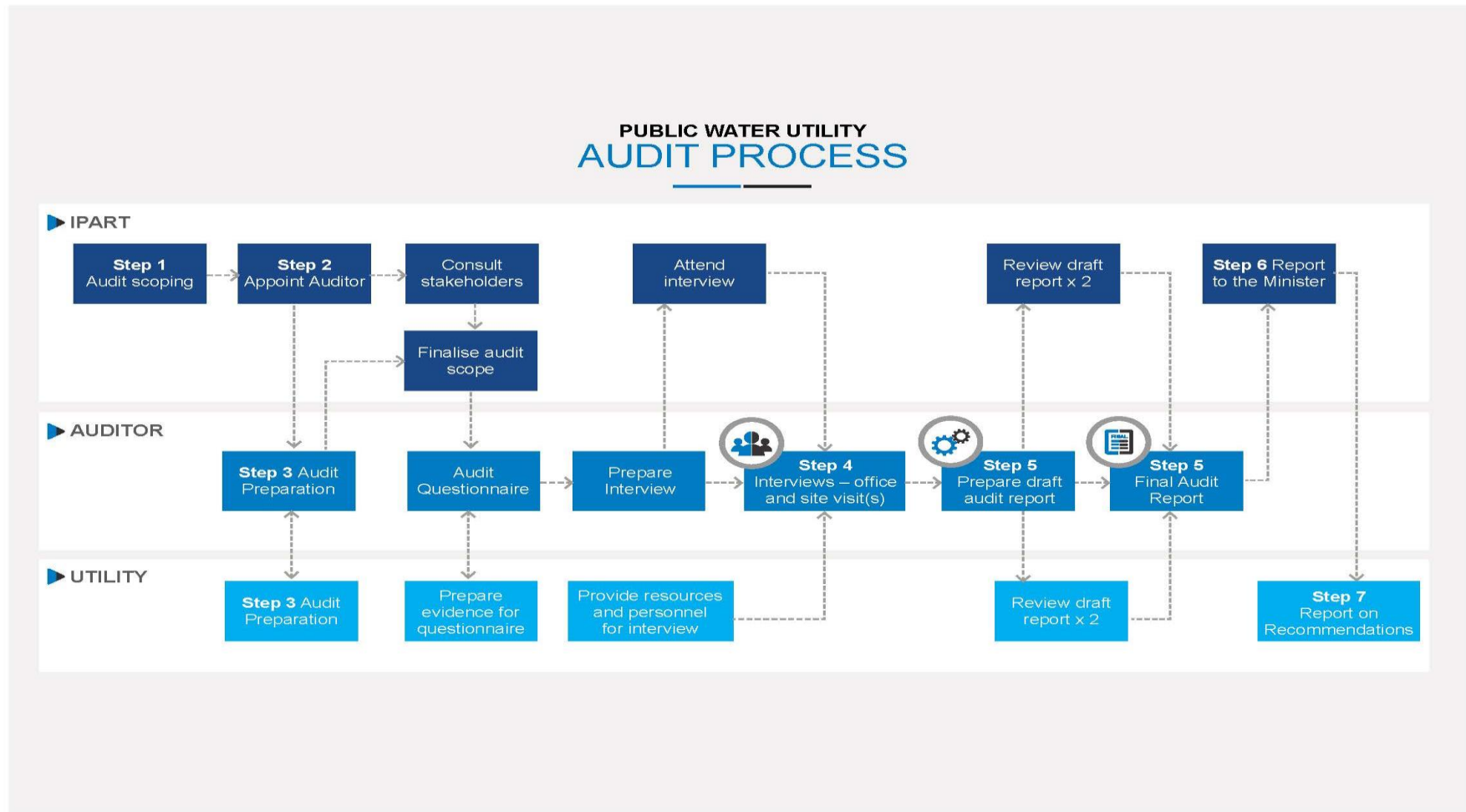
Auditors who submit a scope of work in response to our Request for Quotes (**RFQs**) for the PWU audits must demonstrate that their proposed team members meet the requirements of relevant categories as outlined in Table 3.1.

**Table 3.1 Auditor categories**

Categories	Auditor requirements
Infrastructure performance	Assess adequacy of infrastructure to achieve safe, reliable and continuous performance. It may also include assessing the adequacy of: <ul style="list-style-type: none"> <li>▼ infrastructure performance</li> <li>▼ infrastructure management, and</li> <li>▼ monitoring.</li> </ul>
Drinking water quality	Assess how adequately a PWU implements the <i>Australian Drinking Water Guidelines</i> (ADWG). It may also include assessing the adequacy of: <ul style="list-style-type: none"> <li>▼ any risk assessment</li> <li>▼ the measures adopted to control risks, and</li> <li>▼ the water quality supplied, ie, that it is fit-for-purpose.</li> </ul> Assess the adequacy of catchment management practices, including the adequacy of relevant risk assessments and their outcomes.
Recycled water quality	Assess how adequately a PWU implements the <i>Australian Guidelines for Water Recycling</i> (AGWR). It may also include assessing the adequacy of: <ul style="list-style-type: none"> <li>▼ any risk assessment</li> <li>▼ the measures adopted to control risks, and</li> <li>▼ the water quality supplied, ie, that it is fit-for-purpose.</li> </ul>
Retail supply	Assess the adequacy of the PWUs systems developed to manage customer interactions. This includes: <ul style="list-style-type: none"> <li>▼ complaint handling procedures</li> <li>▼ dispute resolution processes, and</li> <li>▼ hardship and debt management.</li> </ul>
Environmental management	Assess the adequacy of environmental management practices including the adequacy of relevant risk assessments.

<sup>11</sup> They are however required to be part of an audit team to comply with quality assurance and peer review requirements.

Figure 3.1 Public Water Utility Audit Process



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Every audit proposal must include a conflict of interest statement (Appendix A) that confirms the auditor does not have a conflict of interest (perceived or real) with the PWU. If any member of the audit team or their parent organisation has previously provided services to a PWU, the audit proposal must include a table summarising the history of paid work between the parties in the past two years. Further, the audit proposal should identify and describe any conflicts of interest (including any actual, potential or perceived conflict), as required in the conflict of interest statement.

After engaging an auditor, we set the initial schedule for audit milestones. To ensure the appropriate PWU staff members are available for the audit, we will consult the PWU and auditor about our initial milestone schedule. We can adjust this schedule to ensure we get the best outcome from the audit. In general, the final schedule will be consistent with the milestones outlined in Section 3.3.

### **Step 3: Audit preparation**

Once IPART appoints the auditor, we hold a meeting with them. The meeting will cover IPART's expectations, potential locations for field verification site visits and any relevant concerns raised by stakeholders. IPART will also provide contact details of all relevant IPART staff to the PWU and the auditor.

The auditor and PWU will exchange contact information to ensure the audit interview is as efficient and effective as possible. The auditor prepares an audit questionnaire and IPART consults with stakeholders to inform the final audit scope. The auditor, in consultation with the PWU, is responsible for scheduling interviews and the field verification site visit(s).

#### **Audit questionnaire**

The auditor prepares a questionnaire based on the scope of the audit. IPART may review and comment on the questionnaire before it is issued to the PWU. The purpose of the questionnaire is for PWUs to provide evidence of their compliance during the audit period. The PWU must address the requirements of the questionnaire by providing the necessary evidence and also provide a statement of compliance for all remaining licence clauses. The PWU's response to the questionnaire informs the auditor about what they should follow up or clarify at the audit interviews.

IPART will post all of these documents to a confidential file-sharing platform before the audit interviews. Only the auditor, the PWU and IPART will have access to this information on the file-sharing platform. **Appendix E** provides a template guide for the form of the questionnaire.

PWUs should ensure that the information they provide is well referenced, and that relevant page numbers and/or paragraphs are clearly identified.

The auditor must review the answers and evidence provided by the PWU before the interview. This allows for an efficient interview process (ie, in the interview, the auditor should only need to test and validate evidence, clarify any uncertainties and ask for information to fill gaps, rather than covering all the evidence provided in the response to the

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audit questionnaire). The auditors may still request additional information or ask additional questions during the interviews.

### **Scheduling of interviews and field verification site visit**

In consultation with IPART, the auditor and PWU will organise an interview timetable.

- ▼ The **auditor** will indicate how many interview hours are needed for each licence category or licence clause.
- ▼ The **PWU** will identify which business functional areas and personnel will be interviewed by the auditor for these clauses, and will draft the timetable accordingly.

An appropriate period of time (eg, half a day) should be set aside to review and clarify any outstanding matters that were not able to be held/completed in the scheduled interview times.

During the audit, we require at least one field verification site visit. Together with the auditor, we will determine the types of facilities to be inspected and will notify the PWU of the preferred types of facilities for inspection during the scheduling period. Facilities include assets, property or physical elements related to the PWUs operations, such as treatment plants, catchment areas or waterways. Any facility relevant to the matters being audited may be selected for a site visit. The auditor should limit site visit requests to no more than one site for each asset class, excluding asset management/maintenance activities. We require the auditor to confirm sites selected for the field verification site visits prior to issuing the audit questionnaire.

To inform the selection of facilities, we provide the auditor with a list of facilities visited in the previous five audits. We anticipate that at least one day should be set aside for field verification site visits depending on the location and type of facilities to be inspected.<sup>12</sup>

It is helpful to schedule site visits on the second day of an interview program in order to allow time in the office on the days before and after to discuss any matters arising from the interview or the site visit. A short (30 minute) session should be scheduled on day one to outline the field verification site visits (see Step 4 for more details).

If the auditor and PWU agree to run separate interview streams in parallel, this must be discussed with IPART as early as possible. IPART will make best endeavours to understand from the PWUs early in the audit process (before appointing an auditor) if the PWU would be open to running separate interview streams in parallel.

Different parts of the audit scope can be shared between audit team members, depending on the expertise of the team members. The auditor can run separate interviews with the relevant PWU staff in parallel or in separate “streams”. This can offer some time efficiency advantages, particularly for large audit scopes. However, the auditor and PWU must be able to resource the separate interviews effectively, and ensure the interviews are appropriately transcribed. IPART considers that it may be necessary for an auditor to have an assistant or junior colleague available to take notes at the interviews and site visits, especially where more complex clauses are being audited.

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<sup>12</sup> We note that Water NSW will require at least 1.5 days to account for the distances between assets.



## Step 4: Audit interviews

The interview covers the meetings at the PWU's offices and facilities. We may consider web-based (eg, Skype) interviews on request from a PWU to allow PWU employees or contractors to participate in the interviews remotely. The PWU should ensure that it has the appropriate facilities and infrastructure in place to allow for this.

Both IPART staff and relevant members of the audit team should be present at all interviews. PWUs are responsible for ensuring the most appropriate staff members attend the relevant interviews.

There will be an opening (inception) meeting to establish the protocols for the audit<sup>13</sup> and ensure that all necessary arrangements are in place and agreed. In this meeting:

- ▼ We will address the audit approach and the timelines for undertaking the audit.
- ▼ The auditor may also wish to provide an introduction to their team and preferred auditing requirements.

This meeting is usually the first interview session on the first day.

Through the interviews and field verification site visits, auditors must obtain sufficient evidence to be able to provide an audit opinion in accordance with a suitable audit standard.<sup>14</sup> It is the responsibility of the auditor to determine the sufficient level of evidence required and clearly articulate any additional evidence required from the PWU. It is the responsibility of the PWU to take note of the evidence requested by the auditor during the audit interviews and subsequently provide the evidence within the timeframe agreed with the auditor.

In some cases, the auditor may request the PWU to explain its understanding of the licence clause(s) being audited. This will help to determine the PWU's compliance with its operating licence and if any additional evidence is required.

### Field verification site visits

The purpose of a field verification site visit is to enable the auditor to verify how effectively the PWU is implementing the requirements of the licence in practice. It is also an opportunity for the PWU to demonstrate its compliance with the licence in the course of its everyday operations.

The field verification site visit is part of the audit. As such, it is appropriate for the auditor to include questions about implementation of management systems, plans and procedures at the nominated sites in the audit questionnaire. During the site visit, the auditor may seek access to personnel, information, systems and assets to assess implementation of management systems, plans and procedures.

The auditor must link the field verification site visit back to one or more of the sections of the licence that are being audited within the audit scope. Facilities will be selected by the auditor

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<sup>13</sup> For example, the process for managing any disagreements between the auditor and the PWU.

<sup>14</sup> We require auditors to maintain an accurate record of documents sighted; documents must be maintained for a reasonable period and no less than seven years; they must be maintained securely and confidentially, given the sensitivity of the material.



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in consultation with the PWU and IPART, having regard to the audit scope, asset classes of previous site visits, and practical and safety aspects (such as travel or a high risk site) as advised by the PWU.<sup>15</sup> Site selection may also be informed by emerging issues raised during stakeholder consultation.

IPART's preference is that PWUs and auditors avoid multiple streams for site visits as far as possible. No more than three site visits should be conducted in a single day. We may consider up to five site visits in total if the size of the PWU warrants a second day of site visits.

Before the field verification site visit(s), the auditor should schedule a short session during the interviews for the PWU to introduce and familiarise the participants with the site(s) and for the auditor to:

- ▼ Explain how the site visit(s) will demonstrate compliance with the licence
- ▼ Obtain system schematics, maps, technical specifications and design drawings
- ▼ Obtain guidance on personal protective equipment (PPE), if required.

During a field verification site visit, the auditor will review aspects of the PWUs operations and consider compliance with the licence. During the site visit:

- ▼ IPART expects the auditor to ask a PWU's operational staff about site operations and the application of management systems, plans or procedures while on site. These questions should primarily be relevant to the site being visited. The auditor should recognise that the PWU staff available at a particular site may not be able to answer questions relevant to another site. If the auditor has questions about another site, these can be asked separately during the audit interviews.
- ▼ PWUs are responsible for ensuring the appropriate operational staff members are available during a site visit and access to an agreed site is secured. This includes sites that are managed by contractors or other third parties.

During a field verification site visit, the auditor may identify issues that pose a significant risk to public health or the environment but are outside the scope of the audit. If this occurs, the auditor will notify the PWU and IPART at the time of the observation. Section 2.2 of this guideline contains further details on "out of scope" issues and findings.

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<sup>15</sup> Site inductions are mandatory – the auditor and IPART must not touch equipment or enter sites without an induction or appropriately trained personnel in attendance.

## Wrap up and close out sessions

The final session of the audit interview process should involve the following:

- ▼ A **final wrap up**. This item is to cover any outstanding matters. For example, to discuss any concerns from the site verification visits, to answer any questions taken on notice or complete any interviews that ran over time, or where staff were not available when required. This wrap up may not be necessary if both the PWU and the auditors are satisfied there are no outstanding issues to be covered.
- ▼ A **close out meeting**. IPART recommends that auditors, senior management from the PWU and IPART staff are present. The auditor may flag any clauses where the auditor has not assigned a Compliant grade (see section 2.6), or identify areas of concern. Ways of achieving compliance should be discussed and form part of the auditor's recommendations (see Step 7). The auditor should also summarise any outstanding information required or identify any other actions for the PWU or IPART to complete prior to finalising the audit reports. It is the responsibility of the PWU to take note of the evidence requested by the auditor during the audit interviews and subsequently provide the evidence within the timeframe agreed with the auditor. The auditor should flag any likely non-compliance (material) audit grade, so the PWU has an opportunity to address any serious deficiencies or operational issues.

The two items above can be held as one session. However, it is important that suitable personnel are present for the close out meeting.

## Step 5: Audit assessment and reporting

After the audit interview and field verification site visits, the auditor will continue to assess the evidence provided at the interview. Throughout this step, there may be further communication between the auditor and PWU. IPART should be copied in on all correspondence between the auditor and PWU for document control purposes. The PWU and/or the auditor should upload all additional evidence supplied by the PWU to the data transfer site used for the audit.

The auditor must assess the compliance that a PWU has achieved during the audit period. The auditor must prepare a report that addresses all of the elements identified in the audit scope. Where relevant, the auditor should identify where PWUs have demonstrated best practice and exceeded the standard(s) or licence requirements. We have presented the required level of detail and format of the report in the audit report template in Appendix F of this document.

When preparing the audit report, the auditor should use language that is appropriate for a public document. We note:

- ▼ Language should be objective and factual, and should not be overly complex or unnecessarily emotive or alarmist.
- ▼ The report should not include names or other personal details (emails, etc) of PWU or IPART staff members.

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- ▼ The report should not contain any specific material that could pose security issues for the PWU. However, this should be balanced with the need to provide enough detail to support the assigning of an audit grade.

We acknowledge that the audit report may be prepared by more than one audit team member. However, we expect auditors to use their quality assurance process to ensure that a consistent approach to formatting, language, referencing and abbreviations be applied, and that audit reports are free of typographical and grammatical errors.

The auditor must write up the assessment in the first draft audit report. This report must be complete with no sections being left for completion in the second draft. Should the PWU provide further evidence after the first draft, the auditor may alter the audit report to reflect the new evidence. Where the auditor did not assign a Compliant grade,<sup>16</sup> the auditor should identify what is needed for the PWU to achieve compliance. If the auditor has requested further evidence but the PWU has not supplied it, the auditor should make an assessment based on the information/evidence the PWU has already provided.

### **Evidence outside the audit period**

The PWU may provide audit evidence from outside the audit period. We provide the following guidance for auditors:

- ▼ The auditor may consider any new evidence submitted by a PWU, but evidence of events occurring or action taken outside the audit period should not affect the audit grade.
- ▼ The auditor may review and assess new evidence from outside the audit period in its commentary, and subsequent recommendations or opportunities for improvement. The commentary may note that new evidence has already addressed a non-compliance and make no recommendation.

### **Commenting on draft reports**

Both the PWU and IPART will comment on the first draft audit report, including providing further evidence and clarification if needed using the issues register process (see Box 3.1).

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<sup>16</sup> This means a Compliant (Minor Shortcomings), Non-compliant (Non-Material) or Non-compliant (Material) grade is assigned.

### Box 3.1 Comments register process

PWU and IPART comments on the draft report must be made in the template issues register provided by IPART on the file-sharing platform used for the audit. This allows the auditor to compile comments in a central location, as the auditor will need to respond to them and submit its response with the second draft report. Comments by the PWU disputing the auditor's opinion on an assigned audit grade or recommendation needs to be accompanied by supporting evidence. It is not sufficient to make comments such as "we strongly disagree..." without substantiating evidence or justification. PWUs should consider all recommendations (in addition to audit grades and auditor's findings), when reviewing the first draft audit report.

Auditors must respond to all comments using the comments register procedure, explaining whether they have or have not incorporated the comments in the report as well as noting whether they have considered any new evidence. Using this register makes it clear that the auditor considered all issues raised, even if there was no obvious change to the report.

Any other concerns that the PWU or the auditor have should be raised separately and directly with IPART by telephone and/or email.

It is the PWU's responsibility to identify any factual errors, omissions, or required clarifications in the first draft audit report. This is the last opportunity for the PWU to attempt to provide more evidence or clarify information that may influence the compliance grade assigned by the auditor. If the parties do not agree on:

- ▼ The grade assigned by the auditor
- ▼ The evidence provided by the PWU or
- ▼ The evidence required by the auditor.

then we require the PWU and the auditor to discuss this issue with us.

In some cases, IPART may chair a meeting(s) or teleconference(s) to discuss disagreements about assigned audit grades or commentary noted in the first draft report. The meeting(s) can also be used to discuss issues that the PWU considers were not raised, or not adequately discussed in the audit interviews. However, this will be granted at IPART's discretion (by the Director, Regulation and Compliance) where IPART considers that the PWU is engaging appropriately with the audit process.

We expect the PWU to initiate this discussion with the nominated IPART staff member assigned to the audit before the second draft report is prepared. The meeting(s) is considered an out-of-scope item for the auditor appointed by IPART and will be at the PWU's expense.

The auditor may or may not be required to attend the meeting. The auditor may be asked to clarify its commentary or grades, or to further discuss evidence provided by the PWU. In doing so, the PWU will have reference to the escalation of issues approach in Section 3.2, and should not attempt to coerce the auditor into modifying its commentary or grades.

In the discussion, we may clarify the intention of licence clauses or audit procedures. We may discuss the provision of additional evidence to revisit a compliance grade. We will not make comments that compromise the independent assessment of the auditor. Comments from IPART and the PWU should focus on the report content, rather than spelling or typographical mistakes. The report will be subject to quality assurance by the audit team to address these

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issues prior to issuing the final report. After receiving comments, the auditor will prepare the second draft audit report. The auditor must accompany the second draft audit report with the completed issues register which includes responses to all PWU and IPART comments. The auditor should include a separate record of changes between the first draft and the second draft report for ease of comparison (eg, if using MS Word to prepare the draft reports, the auditor could provide a copy of the second draft report showing tracked changes).

The second draft report will reflect any new evidence presented by the PWU, clarify any identified issues and include the auditor's final compliance grades. Any changes to the report from this point should be editorial only.

The PWU and IPART may comment on the second draft audit report, but comments should be limited to the wording of the recommendations, editorial issues and clarification of data only. There is no opportunity to provide further evidence or dispute opinion at this stage. The process for escalation of issues outlined in Section 3.2 should be followed if an issue relating to the audit arises which cannot be resolved through the normal audit process.

The auditor will then compile the final report and provide it to IPART by the milestone date agreed in the contract between IPART and the auditor. Both IPART and the PWU will receive the final report at the same time. IPART will provide all final audit reports to the relevant Ministers and we will make them publicly available on our website. The final reports must be quality assured by an appropriately qualified person, with the relevant experience necessary to undertake this task.

## **Step 6: Report to the Minister**


IPART must report to the relevant Minister on a PWU's compliance with its licence conditions.<sup>17</sup> We will use the auditor's findings as the basis of our Report to the Minister and include the auditor's report as an appendix. If we are aware of other non-compliances throughout the year, either through our regulatory relationship, the statement of compliance, out of scope audit findings or other methods, we will also report these in our Report to the Minister in accordance with the requirements of relevant legislation.

The audit grades in our Report to the Minister may differ from those assigned by the auditor. If IPART decides to depart from the auditor's assigned audit grades, we will write to the PWU as soon as possible to explain the reason for the difference.

If relevant, we will make recommendations to the PWU to improve its operational systems, programs and/or procedures to achieve compliance. Where possible, our recommendations will be outcomes focused to allow the PWU to determine the most efficient way to achieve compliance. Our recommendations may also differ from those made by the auditor to balance service standards with our understanding of customers' willingness and ability to pay. We will provide the PWU with an opportunity to comment on the wording and timing of IPART's draft recommendation(s), where they differ from those made by the auditor, prior to the report being finalised by the Tribunal.

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<sup>17</sup> *Hunter Water Act 1991*, section 18A  
*Sydney Water Act 1995*, section 32  
*Water NSW Act 2014*, section 58.



We may identify opportunities for improvement in our Report to the Minister as well as recommendations. Subject to the requirements set out in the PWUs reporting manual, we do not require the PWU to report back to IPART on opportunities for improvement, although they may choose to do so through the statement of compliance. For more information on auditors' recommendations and opportunities for improvement see the Audit Report template in Appendix F.

PWUs will receive a copy of IPART's Report to the Minister immediately following our submission of the report to the Minister.

The relevant legislation<sup>18</sup> requires that the Minister responsible for Sydney Water and the Minister responsible for Water NSW must table the reports on their compliance performance in both Houses of Parliament within a month of receiving the report(s). There is no requirement for the Minister to table Hunter Water's report in Parliament.

We will post IPART's Reports to the Minister and appendices (including the auditor's report) on our website after they have been sent to the relevant Minister (for all PWUs) and, where relevant, tabled in parliament.

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<sup>18</sup> *Sydney Water Act 1995*, section 33  
*Water NSW Act 2014*, section 59.

## Step 7: Report on audit recommendations

PWUs are to report to IPART on the status of recommendations identified in IPART's report to the Minister by the date specified in its reporting manual. In some cases, we may require a different reporting date for specific recommendations, in accordance with the reporting manual.

The report must include a:

- ▼ Progress report on implementation of recommendations from IPART's report to the Minister.
- ▼ Status update on any outstanding audit recommendations or accepted improvement opportunities from previous years (if the PWU chooses to report on opportunities for improvement, subject to the terms of its reporting manual).

### Evaluation: Feedback from auditors and PWUs

At the conclusion of the audit, following submission of all the reports to the relevant Ministers, we will schedule a workshop-style meeting with the PWUs to identify improvements for the following years' audits.

Our intention is to improve the audit process incrementally, and to minimise regulatory burden on the PWUs. We will also seek auditors feedback through a survey, or similar, to gain an understanding of their views for improving PWU performance and minimising regulatory burden and costs.

## 3.2 Escalation of issues

The audit process requires auditors, PWUs and IPART analysts to communicate on numerous complex issues relating to a PWUs operations and management.

From time to time there will be differences in opinion or understanding regarding aspects such as adequacy of information, interpretation of obligations or audit grades. This is a normal part of the audit process. We have written the guidelines to clarify issues where possible, and to provide a process to discuss areas of disagreement.

To afford the audit team every opportunity to efficiently gather and analyse evidence, the audit guideline has a variety of communication steps, including:

- ▼ Written questionnaires
- ▼ File transfer capabilities
- ▼ Audit interviews
- ▼ Site visits
- ▼ Two draft reports
- ▼ A comments register.

IPART will assign each audit with a nominated IPART representative to oversee the audit. The nominated IPART representative will be familiar with the PWU and the scope of the audit and will attend the audit interviews.



Where an issue relating to the audit arises that cannot be resolved through the normal audit process, the auditor or PWU should always discuss it with the nominated IPART representative in the first instance, as early as possible. In exceptional circumstances, a PWU or an auditor may escalate an issue if they are not satisfied with the initial outcome.

### **Box 3.2 Content or Process?**

An issue of content is an issue relating to a difference of opinion regarding technical issues. These could be a difference of opinion about an obligation, application of drinking water or recycled water management guidelines, or best practice in asset management. These issues usually relate to provision of specific evidence which could be used to support an argument for or against a given audit grade.

An issue of process relates to the conduct of the audit. Behaviours of auditors, IPART or PWU staff, and deviations from the audit guidelines or wording of reporting might be examples of process issues.

IPART will decide if the issue is an issue of content or an issue of process.

Escalation of an issue is a last resort process and should only be considered after the PWU or auditor has attempted to resolve the issue through the normal audit process. An issue can be escalated at any stage in the audit process. Where a PWU or auditor intends to escalate an issue, they should notify IPART as early as possible in the audit process and before finalisation of the audit report. The escalation process is considered an out-of-scope item for the auditor appointed by IPART and will be at the PWU's expense, where the PWU has initiated the escalation.<sup>19</sup>

If an issue is being escalated, initial correspondence should be made by email to the nominated IPART representative, clearly setting out the issue. The PWU or auditor should copy in IPART's Director, Regulation and Compliance on the email. Once the nominated IPART representative has an email clearly outlining the issue (including references to affected licence clauses where relevant), we will call or meet with the notifier to discuss the issue.

The only exception to this is where the issue relates to the behaviour of IPART employees, whereby the Director, Regulation and Compliance should be emailed directly with the Executive Director, Regulation and Compliance copied in for information. From there the Director will arrange a meeting.

All parties should endeavour to keep content issues (see Box 3.2) at an officer level (the nominated IPART representative). It is not appropriate for senior levels of management who were not present at the audit or involved in reviewing evidence and reporting to be discussing technical details of content.

Importantly, auditors have been engaged to exercise their professional opinion as an experienced industry member. Auditors must remain independent at all times during the audit process. If the PWU escalates an issue, it should only be raised with IPART, not with the auditor, and should not be used in any way to influence the auditor. Communication with the auditor must always occur within the audit process described (comments register – see Box 3.1) or with IPART copied in. If the independence of the auditor is in question, IPART will consider appropriate action.

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<sup>19</sup> Any issues raised concerning the contractual agreements between IPART and the auditor or an IPART employee's behaviour and conduct will not be at the PWU's expense.



### 3.3 A summary of major milestones for an operational audit

Each audit is for the audit period. The following schedule (Table 3.2) outlines the expected timeframes to carry out each step of an operational audit. The exact dates of when outputs are due will vary from year to year and the dates will be set during Step 2 and Step 3 of the process.

**Table 3.2 Indicative Audit Schedule**

Audit Step	Output	Responsibility	Timeline
Step 1 – Audit scoping	Audit scope	IPART	6 weeks (Mar- Apr)
	Stakeholder consultation letters	IPART	No later than 4 weeks following audit scope
	Approval of draft audit scope	IPART	2 weeks after end of stakeholder consultation
Step 2 – Appointment of the auditor	Letter of appointment	IPART/Auditor	6 weeks following approval of draft audit scope
Step 3 – Audit preparation	Stakeholder submissions	IPART	After 1 June
	Questionnaire	Auditor	3 weeks after appointment of auditor
	Questionnaire response	PWU	4 weeks after issue of questionnaire
	Statement of compliance	PWU	Date set by IPART
Step 4 – Audit interview		Auditor/PWU (IPART present)	Within 2 weeks of completion of questionnaire
Step 5 – Audit assessment and reporting	First draft audit report	Auditor	3 weeks after Step 4
	Comments on first draft	PWU / IPART	3 weeks after Draft report
	Meeting (if required)	IPART/PWU/ Auditor	During Comments period
	Second draft audit report	Auditor	2 weeks after Comments
	PWU and IPART response	PWU / IPART	1 week after Second Draft Report
	Final audit report	Auditor	1 week after Final comments
Step 6 – Report to Minister	IPART report to Minister	IPART	4 weeks after Final Report
Step 7 – Reporting on recommendations	PWU report on recommendations	PWU	8 – 12 weeks after Minister receives Report (refer to the utility’s Reporting Manual)
Evaluation – Feedback from auditors and PWUs	Survey/workshop to discuss lessons learnt	Auditor/PWUs/ IPART	Following final report submitted to Minister





## Appendices



## A Conflict of interest statement

This conflict of interest statement is given by  
..... (**Auditor**) in  
connection with the proposed audit of  
..... (**Auditee**) for the  
[audit name/type] .....  
which is intended to take place from .....[date] to  
.....[date]

I, ..... [full name], of the Auditor, declare that I  
am authorised to provide this declaration and that:

- ▼ the Auditor does not have any conflicts of interest with the Auditee; or
- ▼ the Auditor included in the attached document a description of all conflicts of interest, real or potential, or perceived conflicts of interest, to the best of my knowledge, with of the Auditee, and an explanation of how such conflicts will be managed.

*[Attach a separate document providing an explanation of all the conflicts of interest, and the proposed process to manage them. Submit this with the audit proposal.]*

Date:.....

Signed:.....

Name:.....

Designation: .....

## B Audit standards and principles

No specific auditing standard is required for the audits. We require all auditors to use a systematic approach to:

- ▼ planning the audits
- ▼ interpreting licence conditions
- ▼ collecting audit evidence
- ▼ objectively assessing the evidence, and
- ▼ reporting in a clear and accurate manner.

Acceptable standards that may help auditors with this approach include: ASAE/ISAE 3000, or AS/NZS ISO 19011.

Auditors must identify the standard they will use in the tender. These standards can be adapted, if appropriate, for the audit. The final report must state the audit was done according to the identified standard.

Auditors are responsible for ensuring the audit procedures they use meet the following audit principles:

- ▼ Faithful representation - information should faithfully represent the outputs and outcomes of the audit. Uncertainties should be minimised, identified and quantified where possible.
- ▼ Completeness - information should be as complete as possible, such that information is not misleading or unreliable.
- ▼ Consistency - consistent methods should be used so comparative assessments can be made over time.
- ▼ Reliability - information and source data should be free of material misstatement and able to be relied upon by users of the information.
- ▼ Transparency - data should be capable of replication by a third party through adequate record keeping. Reference sources, methodologies and approaches to data generation should be clearly documented. Changes to data and methodologies over time should be clearly documented.

## C Audit methods

**Table C.1 Audit methods**

Principle	Definition	Example of method
Inspection	Examining records, documents or physical assets. The auditor must consider the source of the documentation for differing degrees of reliability.	Obtain a summary of PWU water supply main breaks and customers affected and trace figures back to source documentation, and reconcile to the participant's internal record keeping system.
Observation	Looking at a process or procedure being performed by the participant. Generally, this audit procedure is conducted when the particular process ordinarily leaves no audit trail.	Observe the record keeping process and documented procedures in operation.
Inquiry and confirmation	Seeking appropriate information of knowledgeable persons inside or outside the organisation. The response to an inquiry to corroborate information contained in the records.	Inquire how the field work crews collect data and how this data is logged into the data collection system. Confirm data recording is accurate.
Computation	Checking the accuracy of source documents and accounting records, or of performing independent calculations.	Consider sampling of customer property numbers for several main failures via alternative computation methods.
Analytical procedures	Investigation and analysis of data fluctuations and relationships to determine whether there are inconsistencies with other relevant information, or deviations from predicated amounts.	Confirm interpretations of definitions and compare with other interpretations, for example counting of flats and units in customer property numbers. Consider errors and confidence limits.

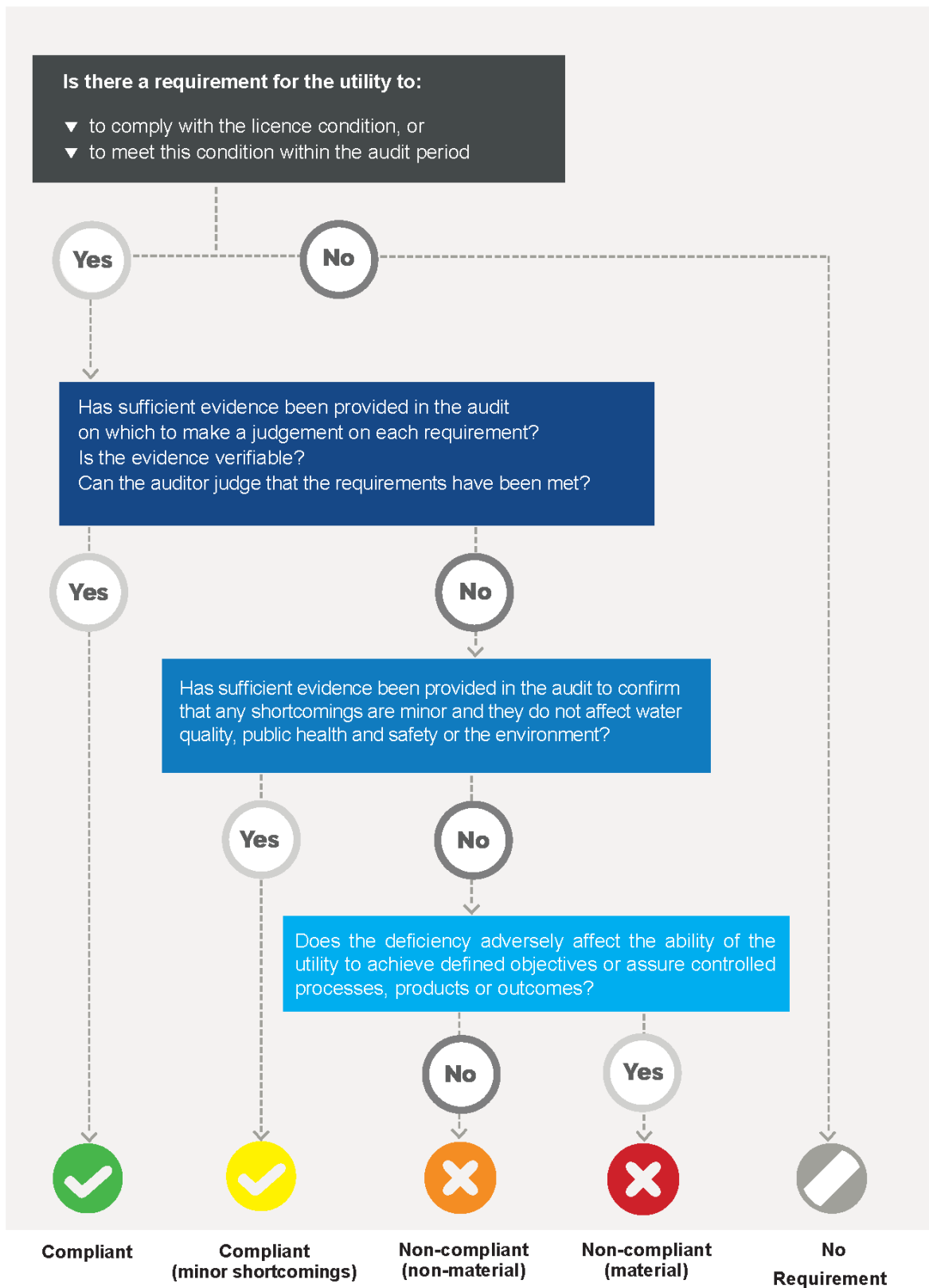
**Source:** Adapted from AS/NZS ISO 19011:2014

A variety of factors will affect the reliability of audit evidence, including:

- ▼ independence of evidence - evidence provided by a party external to the utility is generally considered more reliable than evidence generated internally
- ▼ knowledge and lack of bias of the person providing the evidence to the auditor, and the attention paid to the auditor's request for evidence
- ▼ the directness in which it is obtained - evidence received directly by the auditor is generally considered to be more reliable than evidence received indirectly, and
- ▼ control systems – evidence prepared by PWUs under systems of strong internal control is considered more reliable than evidence prepared under systems of weak internal controls.

Auditors should adopt an attitude of professional objectivity throughout the audit in order to ensure information provided is accurate and complete.

## D Audit grade decision tree





## E Questionnaire template

Table E.1 is a template for the auditor's questionnaire and the PWUs response, to be used before the audit interview. The auditor will prepare a questionnaire based on the scope of the audit for the PWU. The PWU will then answer the questionnaire before the audit interviews.

The evidence the PWU provides will be in separate documents and systems. The questionnaire answer must reference the evidence clearly – including, where relevant, chapter numbers or page numbers. All referenced documents must be provided with the completed questionnaire. All referenced systems must be available in the interview period for the auditor to test. Reports can be provided as evidence, however, information contained in the reports should be referenced (chapter and page numbers) in the questionnaire.

The completed questionnaire and referenced documents will be large and may be difficult to transmit to multiple parties. We have set up a data upload facility, which all three parties can use to upload and see the documents. We will send details of the facility to each party when the auditor is appointed.

The auditor must read the answers and evidence provided before the interview. This method allows for efficient interviews, as the auditor sees much of the evidence before the interview. Then, in the interview, the auditor can test and verify the evidence provided, clarify any uncertainties and ask for information to fill gaps, rather than covering all the content from the beginning.

**Table E.1 Questionnaire template**

Auditor Questionnaire			PWU Response	
Licence Clause	Questions	Type of evidence	Discussion	Evidence
	Questions that detail what the auditor expects to see to show compliance with the licence clause	Documents or systems which might answer the question	Discussion of how the evidence answers the question	<p>Hyperlinks to documents or systems, or detailed naming of documents.</p> <p>To improve audit efficiency, chapter or page numbers for references should be included, where relevant.</p> <p>Providing unreferenced information can increase time and cost of audits.</p>

## F Audit report template

The following pages are a template outlining what we require in an audit report as a minimum. Auditors do not have to use the formatting of the template, as we expect they will use their company's formatting protocols. The template only provides the content and layout of what is required.

The report should include a chapter for each licence obligation category (ie, Water Quality, Asset Management, Customers, etc), and a separate chapter addressing previous IPART recommendations. Each chapter should clearly state compliance grades for each clause and include a summary of findings, including a brief discussion as to why a compliance grade was assigned.

The first draft report must be complete: ie, the auditor should not leave any sections for completion in the second draft.

Where the auditor is waiting on further information, the auditor should make an assessment based on information available to the auditor at the time of finalising the first draft audit report.

### **Report writing style**

The final audit report will be attached to our report to the Minister and so will be publicly available. When preparing the audit report, the auditor should use language that is appropriate for a public document. Language should be objective and factual, and should not include names or other personal details (emails, etc) of the PWU or IPART staff members. The report should not contain any specific material that could pose security risks for the PWU.

### **Recommendations**

Auditors will make recommendations as to how the PWU could improve its compliance with each clause where the auditor did not assign a Compliant grade. The recommendations should address the gaps found in the evidence and help the PWU identify ways to rectify these gaps. The only exception to this requirement is where compliance is dependent on someone or something that is out of the PWUs control. In this event, the auditor should state this in the recommendations column of the template. Where the auditor assigned a Compliant grade, an auditor should not make a recommendation, as we want to balance performance and the investment required to improve it. That is, we want to consider the pricing implications of continual improvement and value for money to the customer before recommending that PWUs implement improvements.

### **Opportunities for improvement**

In addition to recommendations, if the auditor sees an area where an improvement could be made to the operation of the PWUs activities and functions, the auditor can identify this as an

“opportunity for improvement”. The auditor may identify an opportunity for any clause, include those where the PWU has been assigned a Compliant grade. The opportunity for improvement should not have an impact on compliance, but may contribute to the overall improvement of the PWU operations. The PWU can decide whether to implement an opportunity, based on their own assessment of whether the improvement is a prudent and efficient way to achieve its outcomes.

If we adopt the opportunity for improvement in our Report to the Minister, the PWU can decide whether or not it will report on implementation, subject to the requirements of its reporting manual. We will supply to the auditor any information that the PWU provides outlining its response to the opportunity for improvement prior to the next audit. However, we will not follow up the opportunity for improvement in subsequent audits.

## Report contents

The following is a guide on the **minimum requirements** for the audit report.

- ▼ An Executive Summary, summarising the outcome of the audit and the administrative requirements of the report.
- ▼ An Introduction providing more detail on the administrative requirements, audit methods, standards and quality assurance.
- ▼ A detailed audit findings section, providing a full account of the audit findings, audit evidence and discussion of grades, recommendations and opportunities for improvement (if any). We recommend a short summary of the site visits also be included.
- ▼ Previous recommendations and progress to date.

## Executive Summary

In the summary, the auditor is to provide an audit opinion on the compliance of the PWU with its licence.

The audit opinion should include a statement that:

- ▼ the auditor has seen sufficient evidence on which to base their conclusions
- ▼ the audit findings accurately reflect the professional opinion of the auditor
- ▼ the lead auditor and team members have noted what this guideline and the request for quote requires when conducting the audit, determining audit findings and preparing the report, and
- ▼ the audit findings have not been unduly influenced by the PWU and/or any of its associates.

This summary will also include a table with the audit grades and the relevant recommendations for each operating licence clause. The table will also highlight the major findings of the audit and summarise compliance. For any non-compliances or inadequacies, the auditor should discuss the risk which a non-compliance poses to public health, the environment, customer relations, operations or financial areas of the business.



The summary should not include opportunities for improvement, and should not contain progress made on previous recommendations.

The summary should not refer to findings or analyses that are not included elsewhere in the report.

## **Chapter 1 Introduction**

### **1.1 Objectives**

Statement of the objective of the audit.

### **1.2 Audit method**

#### **1.2.1 Audit scope**

Identify the scope of the audit, including timeframe covered by the audit, list of sites visited and licence clauses audited.

#### **1.2.2 Audit standard**

Identify the audit standard used in the audit.

#### **1.2.3 Audit steps**

Briefly summarise the audit steps undertaken, or refer to the Audit Guidelines.

#### **1.2.4 Audit team**

Identify the audit team and the roles of each member.

#### **1.2.5 Audit grades**

Provide the audit grade definitions used in assessing the PWUs performance against the requirements.

### **1.3 Regulatory regime**

This section should discuss the regulatory framework under which the PWU operates. This will cover areas such as the PWUs Act and Regulation, the operating licence, environmental legislation, Memoranda of Understanding, etc.

### **1.4 Quality assurance process**

This section should discuss the quality assurance process undertaken when preparing this report to ensure the integrity of the information provided.

All final audit reports must be peer reviewed.

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## **Chapter 2 Detailed Audit Findings**

This section must include the licence requirement and the full audit findings, a description of the auditor's activities, audit methods and evidence sighted that led to assigning the compliance grade. This section should also include a discussion of evidence and observations considered during the field verification site visit.

Formatting of this section should be logical, with clear headings. The auditor should state the clause number and assigned grade before the findings and reason for the grade.

### **2.1 Site visit report**

Provide a short summary of the sites visited, the assets inspected, the issues reviewed/identified and the evidence presented.

### **2.2 Detailed audit findings by clause**

The audit report should contain a section for each licence obligation category that is audited.

The following table shows a typical reporting template for the detailed audit assessment part of the report.

**S Table 2.1 Detailed audit findings for each clause – hypothetical example**

<b>Clause</b>	<b>Requirement</b>	<b>Compliance grade</b>
2.1.1	eg, PWU must manage drinking water quality to the satisfaction of NSW Health in accordance with the ADWG.	<b>Eg, Compliant - see Appendix X for Compliance grades</b>
<b>Risk</b>		<b>Target for compliance</b>
Describe risk posed to public health and environment by non-compliance.		Discuss what must be provided to be assigned a Compliant grade.
<b>Obligation</b>		
Describe the obligation in the auditor's own words, including interpretation of the clause. Consider the purpose of the clause.		
<b>Evidence sighted</b>		
List examples of evidence sighted including reference documents, records, systems, emails, letters, meeting notes, and any other information which is sighted as evidence that the PWU has met the obligation.		
<b>Summary of reasons for grade</b>		
Briefly summarise the reasons provided for the grade.		
This summary should provide a concise analysis of the evidence. It should specifically focus on how the evidence demonstrates compliance with the clause, or how it indicates that the PWU has fallen short of the obligation.		
This section should not contain extended discussion, nor notes from interviews and site visits.		
<b>Discussion and notes</b>		
The discussion section should be aligned to the 'Audit grade decision tree' and follow the following approach:		
<ol style="list-style-type: none"> <li>1. Discuss evidence and how it demonstrates: <ul style="list-style-type: none"> <li>- Compliance with the obligation in the clause, or</li> <li>- That the PWU has not met the full requirement of the obligation (where the auditor has identified shortcomings or deficiencies and has not assigned a Compliant grade).</li> </ul> </li> <li>2. Where the auditor identifies shortcomings or deficiencies the auditor should clearly distinguish how the evidence demonstrates that there is a shortcoming or deficiency.</li> <li>3. Where the auditor identifies a deficiency the auditor should clearly identify whether the deficiency is material or non-material.</li> <li>4. Explain clearly how the shortcomings or deficiencies contribute to the audit grade.</li> </ol>		
This section should not contain a discussion of matters that do not contribute to the audit grade.		
This section may include notes from interviews and site visits.		
<b>Recommendation</b>		
Recommendations that relate to a particular sub clause should be included in this section.		
The auditor may only identify a recommendation where they have not assigned a Compliant grade.		
The recommendation should clearly articulate how the PWU should address the identified shortcomings/deficiencies and the timeline for the recommendation.		
<b>Opportunities for improvement</b>		
Opportunities for improvement that relate to a particular sub clause should be included in this section.		
The auditor may identify an opportunity for any clause, including those where the PWU is assigned a Compliant grade.		
<b>Supplemental information</b>		
In this section, the auditor should note other considerations that do not contribute directly to the audit grade. This is not required and the auditor should only list these considerations if it will provide value to the overall audit opinion.		

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### **Chapter 3 Previous Recommendations**

This section should list the recommendations from the previous year's audit and any outstanding recommendations from previous IPART operational audit reports that have not been adequately addressed. The auditor must review evidence to determine whether the recommendations (i) have been completed by the utility, (ii) are ongoing, or (iii) have not been undertaken. The auditor must discuss progress and provide an update on the anticipated completion date.