

Audit Guideline for Energy Businesses

Final decision

24 April 2018

An appropriate citation for this paper is:

Essential Services Commission 2018, Audit Guideline for Energy Businesses: Final decision, 24 April

Copyright notice

© Essential Services Commission, 2018



This work, Audit Guideline for Energy Businesses, is licensed under a Creative Commons Attribution 4.0 licence [creativecommons.org/licenses/by/4.0/]. You are free to re-use the work under that licence, on the condition that you credit the Essential Services Commission as author, indicate if changes were made and comply with the other licence terms.

The licence does not apply to any brand logo, images or photographs within the publication.

Contents

1. Introduction	1
1.1. Why we undertook a review of the audit guideline	1
1.2. Review process	1
2. Feedback on the audit guideline	2
2.1. Stakeholder submissions	2
2.2. Audit time frames	3
2.3. Auditor term of engagement	4
2.4. Standards of assurance	6
2.5. Cost of audits	12
3. Audit guideline implementation	11
References	12

1. Introduction

1.1. Why we undertook a review of the audit guideline

Guideline 22: Electricity and Gas Industries – Regulatory Audits of Energy Businesses was last updated in January 2014. Since then the Essential Services Act 2001 was amended to introduce a new function for the commission to monitor and report on the compliance by licensees. To assist us in meeting these new objectives we enhanced our audit program to ensure it provides:

- independent assurance that licensees understand and comply with their licence obligations
- an assessment of the accuracy of self-identified breaches reported by licensees, and the effectiveness of the systems, processes and controls to produce these reports.

Since 2014, we have also made changes to the audit framework by including different types of audits. The audit tools within the framework allow us to check in on newly licensed businesses (baseline health check), target specific compliance issues unique to a licensee (tailored audit), or examine industry wide compliance concerns (pulse check or thematic audit).

In summary, we undertook this review to ensure the guideline reflects our objectives under the Essential Services Act 2001, is reflective of our way of working and that our processes align with current audit practices.

1.2. Review process

We commenced this review by seeking independent external advice from an audit firm. First, we asked the audit firm to review our existing auditing processes and the feedback given to us from participants of previous audit programs. We then sought their advice on proposed improvements to the guideline which would ensure our audit processes are efficient, transparent and consistent. We were also keen to ensure that the outcomes derived from the audit process add value to the industry as well as consumers.

Based on the recommendations we received from the audit firm, we facilitated a briefing session on 1 December 2017 with stakeholders and released the revised guideline for consultation.

Once the consultation period ended, we invited parties who provided a submission to meet with us during February and March to discuss their feedback.

This paper addresses how we acted upon the feedback we received on the revised guideline in submissions and our meetings with stakeholders.

2. Feedback on the audit guideline

2.1. Stakeholder submissions

We received submissions from:

- AGL
- AusNet Services
- Australian Gas Infrastructure Group
- CitiPower, Powercor, United Energy
- Consumer Action Law Centre
- EnergyAustralia
- GloBird Energy
- Jemena
- Origin Energy
- RSM Australia Pty Ltd
- Others¹

Feedback on the revised audit guideline centered on four key issues which are addressed in this chapter:

- audit time frames
- auditor term of engagement
- standards of assurance
- cost and scheduling of audits

¹ Three stakeholders provided confidential submissions.

2.2. Audit time frames

Stakeholder feedback

Licensees and audit firms expressed concern that the proposed timings allocated to key steps in the audit process found in table 7 of the guideline were too short. This includes the time frames for planning, fieldwork and reporting stages of an audit. EnergyAustralia and CitiPower, Powercor, United Energy considered the audit guideline should provide for flexibility in meeting audit time frames. They have requested flexibility in the event either party could not meet the prescribed timings outlined in the draft guideline.

We believe the Audit Guideline should include a provision to allow the Commission to extend the timeframes that are set out in the table on page 21 ... the Commission could consider granting an extension to the timeframes to allow the licensee to consider whether it needs to re-negotiate the quote and scope of work with the auditor.²

We suggest that the audit timeframes outlined in the guideline instead be marked as indicative because the level of audit assurance and testing required, auditor availability etc. will impact on the timeframes.³

Many licensees requested we refer to 'business days' rather than 'days'. Jemena noted:

The suggested change would provide additional time for the Commission to consider approval of auditors and finalisation of the audit scope.⁴

Stakeholders suggested this amendment would assist in alleviating pressure on procurement, auditor nomination and audit preparation, whilst also allowing the commission more time to approve auditor nominations.

Our response to stakeholder views

The audit guideline establishes the time frames for each of the key stages of an audit, for example the planning phase, receipt of an auditor nomination, fieldwork and reporting and the submission of

² EnergyAustralia, Submission to the Essential Services Commission 'Draft Audit Guideline for Energy Businesses' February 2018, p. 2.

³ CitiPower, Powercor, United Energy, Submission to the Essential Services Commission 'Draft Audit Guideline for Energy Businesses' February 2018, p. 2.

⁴ Jemena, Submission to the Essential Services Commission 'Draft Audit Guideline for Energy Businesses' January 2018, p. 2.

audit deliverables⁵. These time frames aim to guide licensees and auditors on our expectations and are indicative of the effort required within each audit stage.

Concerns regarding the time frames of an audit should be highlighted to commission staff during the audit planning stage so that all parties agree on the key dates for delivery. This process is allowed for by clause 7.1.7 of the audit guideline:

The commission reserves the right to re-consider the time frame. This may be extended if the complexity or the difficulty of an audit so requires, or relevant functions have been outsourced, at the commission's discretion and in consultation with the auditor and the licensee subject to audit.⁶

As the guideline allows for and promotes robust discussions between the parties during the planning phase we do not believe it is necessary to change the number of days allocated to key audit stages. Audit timings will vary depending on the audit type being undertaken and the timings will be agreed at the onset of each audit by all parties once the scope has been confirmed. As such, the timings noted in the guideline remain as indicative.

We have addressed stakeholder concerns regarding day count by amending the audit guideline to count days as 'business days' rather than calendar days. This increases the time frames of key audit stages thereby also addressing the need for some flexibility in the prescribed timings.

2.3. Auditor term of engagement

Stakeholder feedback

Stakeholders submitted the auditor term of engagement should be extended (and not limited to) three consecutive audits as noted in the draft guideline.

One stakeholder commented:

The inclusion of this clause imposes an additional cost and potential delay to audits whilst regulated businesses navigate through internal processes to appoint a new auditor after 3 consecutive audits. We think that there needs to be careful consideration of the value of the strong understanding and relationships audit firms have of their clients' business and the

⁵ Audit Guideline for Energy Businesses, 24 April 2018, p. 26.

⁶ Audit Guideline for Energy Businesses, 24 April 2018, p. 25.

resulting efficiency and quality of the audit report that might be compromised by regular changes in audit firms.⁷

In particular, Australian Gas Infrastructure Group noted issues with auditor nomination and availability of audit firms.

The revised Guideline only allows a Licensee to engage an Auditor for a maximum of three consecutive audits. While we understand the basis of this requirement there may be times when other panel Auditors may not be appropriate due to conflicts or availability due to the number of audits.⁸

Our response to stakeholder views

In our draft guideline, the commission introduced a limit to the number of audits undertaken by a firm for a licensee to promote independence and reduce conflict of interest. The draft guideline proposed to limit the number of engagements to three consecutive audits. Our rationale being that the frequency of audits may begin to decrease over time for some licensees, meaning a licensee who has a good audit and compliance profile would be audited less frequently (for example, three audits, over five years) than a licensee with a poor audit and compliance history (for example, multiple audits over 18 months).

Based on feedback from stakeholders, and having reviewed the practices of other regulators and agencies in managing auditor rotation, we have reconsidered our view. We have amended the audit guideline to allow an auditor term of engagement of up to a maximum of five consecutive years in line with Australian Securities and Investments Commission guidelines. This change was deemed appropriate as the consultation process highlighted that an extended period of engagement would be of benefit to licensees and audit firms by creating efficiencies and would not pose a risk to auditor impartiality and independence as this is secured by the professional standards auditors are required to comply with.

⁷ Confidential, Submission to the Essential Services Commission 'Draft Audit Guideline for Energy Businesses' February 2018.

⁸ Australian Gas Infrastructure Group, submission to the Essential Services Commission 'Draft Audit Guideline for Energy Businesses' February 2018 p. 2.

2.4. Standards of assurance

Guideline 22: Electricity and Gas Industries – Regulatory Audits of Energy Businesses previously only referred to one auditing standard: Standard on Assurance Engagements ASAE 3100 Compliance Engagements. Upon receiving independent external advice from an audit firm, the draft guideline was updated and included:

- The existing Standard on Assurance Engagements ASAE 3100 Compliance Engagements
- Standard on Assurance Engagements ASAE 3402 Assurance Reports on Controls at a Service Organisation
- Standard on Related Services ASRS 4400 Agreed-Upon Procedures Engagements to Report Factual Findings.

These additional standards were included in the draft guideline to provide flexibility for the type of audits the commission may request.

Stakeholder feedback

Many audit firms advised that the Standard on Assurance Engagements ASAE 3402 Assurance Reports on Controls at a Service Organisation was not applicable for the types of audits the commission undertakes. RSM Australia Pty Ltd advised:

ASAE 3402 is designed to provide assurance on controls at a service organisation that are likely to be relevant to the user entities' internal control as it relates to financial reporting'... 'This [sic] objectives above appear more aligned to an assurance engagement to be conducted in accordance with ASAE 3100 Compliance Engagements.⁹

Another stakeholder advised that the Standard on Assurance Engagements ASAE 3402 Assurance Reports on Controls at a Service Organisation did not align with our expectations that a licensee's relevant obligations should form the core criteria of the audit, and noted in their confidential submission:

⁹ RSM Australia Pty Ltd, Submission to the Essential Services Commission 'Draft Audit Guideline for Energy Businesses' February 2018, p. 1-2.

A 3402 assurance engagement requires the Service Organisation to clearly define the system of policies, procedures and controls which form the audit criteria (rather than the relevant regulatory obligations as the criteria) ¹⁰

Our response to stakeholder views

To confirm the most appropriate audit standards to reference in the guideline we consulted each of the audit firms who provided submissions to the draft guideline. Based on these discussions we have made the following changes.

We have removed:

- references to Standard on Assurance Engagements ASAE 3402 Assurance Reports on Controls at a Service Organisation as this standard is more aligned with financial auditing, and is not applicable for the types of audits the commission seeks.

We have added:

- Standard on Assurance Engagements ASAE 3000 Assurance Engagements Other than Audits or Reviews of Historical Financial Information to support the Standard on Assurance Engagements ASAE 3100 Compliance Engagements. (These two standards work together to facilitate comprehensive audits on compliance. ASAE 3100 applies the requirements in ASAE 3000 for attestation engagements and adapts those requirements, as necessary, to direct engagements on compliance.¹¹)
- Standard on Assurance Engagements ASAE 3150 Assurance Engagements on Controls (as this standard requires auditors to review the design and effectiveness of controls.)

We have maintained:

- Standard on Assurance Engagements ASAE 3100 Compliance Engagements (as this standard provides assurance on whether a licensee has complied with the compliance requirements)
- Standard on Related Services ASRS 4400 Agreed-upon Procedures Engagements to Report Factual Findings. (This standard allows us flexibility in the type and level

¹⁰ Confidential, Submission to the Essential Services Commission 'Draft Audit Guideline for Energy Businesses' February 2018.

¹¹ Australian Government, Auditing and Assurances Standards Board, Standard on Assurance Engagements ASAE 3100 Compliance Engagements, February 2017, p. 9.

of testing which can be requested. In particular, using this standard the commission may obtain unique or specific factual findings on a discrete area of a licensee's business operations which may or may not be unique to other audits or organisations.

On the following page in Table 1 we have provided a description of each audit type, assurance standard and level that the commission may request.

Table 1 Audit framework and standards of assurance

This matrix illustrates the standards and assurance levels applicable to each audit tool within the audit framework.

Audit tool	Description	Assurance standard	Assurance level
Pulse check	<ul style="list-style-type: none"> This desktop review is used to gain insight into a licensee's processes and controls. The licensee does not need to engage an auditor; instead, they must complete a survey and obtain sign off from their audit and risk committee and/or chief executive officer prior to submission. Information gathered by this tool can be used by the commission to better understand industry wide-issues and to promote and encourage better practice. 	Not applicable.	Not applicable.
Baseline health check	<ul style="list-style-type: none"> This audit tool is generally used for newly licenced entities and provides baseline assurance on key licence obligations for example as life support, 	<ul style="list-style-type: none"> The commission will usually request Standard on Assurance Engagements ASAE 3000 and 3100 Assurance Engagements on Compliance to provide an assurance report on whether the 	<ul style="list-style-type: none"> The commission will usually request reasonable assurance. In a reasonable assurance engagement, an auditor states that

hardship program, sales and marketing, compliance performance reporting, disconnections and reconnections, and billing.

- This audit tool includes sample testing and an assessment of selected obligations.

entity has complied in all material respects with the compliance requirements, throughout the specified period or as at a specified date.

- In some circumstances, the commission may consider requesting ASAE 3150 Control Engagements to provide an assurance report on the suitability of the design of controls to achieve identified control objectives, and, if applicable, fair presentation of the description of the system, implementation of the controls as designed and/or operating effectiveness of controls as designed.

the controls tested comply with the regulatory obligations they were tested against; or

- In some circumstances, the commission may consider limited assurance. In a limited assurance engagement, an auditor will generally state that they are not aware of any material non-compliance with the regulatory obligations tested.

Thematic audit

- This audit tool focuses on a small number of obligations to provide information on an industry level.
- Previously titled ‘targeted review,’ this type of engagement focuses on selected obligations applicable to one or more industry-wide issues identified as high risk, or warranting review by the commission.
- Auditors are required to sample test the

- The commission will usually request Standard on Assurance Engagements ASAE 3000 and 3100 Assurance Engagements on Compliance to provide an assurance report on whether the entity has complied in all material respects with the compliance requirements, throughout the specified period or as at a specified date.
- In some circumstances, the commission may consider requesting ASAE 3150 Control Engagements to provide an assurance report on the suitability of the design of controls to achieve

- The commission will usually request reasonable assurance.
- In a reasonable assurance engagement, an auditor states that the controls tested comply with the regulatory obligations they were tested against; or
- In some circumstances, the commission may consider limited assurance. In a limited assurance engagement, an auditor will generally

	design and operating effectiveness of key processes and controls identified for each obligation outlined in the audit scope.	identified control objectives, and, if applicable, fair presentation of the description of the system, implementation of the controls as designed and/or operating effectiveness of controls as designed.	state that they are not aware of any material non-compliance with the regulatory obligations tested.
Tailored audit	<ul style="list-style-type: none"> This audit tool focuses on a defined range of obligations or controls specific to a licensee to test compliance on a specific process or control. The auditor's approach for assessment, sampling methodology and test plan is to be agreed with and approved by the commission, generally requiring substantive analysis. This audit will provide a report of factual findings, which can be used to determine a licensee's compliance to enable us to form a view of their current technical capacity. 	<ul style="list-style-type: none"> The commission will request Standard on Related Services ASRS 4400 Agreed-upon Procedures Engagements to Report Factual Findings. 	<ul style="list-style-type: none"> The commission expects a report on factual findings, no conclusion or explicit assurance provided – the report should detail of exact findings resulting from each procedure conducted.

2.5. Cost of audits

Stakeholder feedback

Some stakeholders expressed concerns about the financial demands an audit can place on a business. In particular, GloBird Energy noted:

Even though we are supportive of the commission's changes and we understand how important audits are, we would like the commission to consider the costs and time involved for an audit to be performed. For smaller energy retailers, this can be onerous and costly.¹²

CitiPower, Powercor and United Energy also expressed reservations that the cost of audits would be made more difficult with the timings and term of engagement established in the draft guideline:

This limitation will lead to increased costs of auditing based on direct audit costs and also indirect costs of staff time to bring auditors up to speed on complex systems and processes within the business. The likely outcome will be to increase costs, slow the audit process down and make the outlined timeframes less achievable.¹³

Our response to stakeholder views

While the guideline does not refer to the costs associated with an audit, it does clarify the types of audits that may be undertaken to ensure that all audits are the 'best fit' for the circumstances. In clarifying the different types of audits to be used, it is anticipated that audits will become more efficient, and the cost of audits will be minimized as they become more tailored.

To address stakeholder concerns we have clarified the timings of audit phases and increased the auditor term of engagement. The commission is supportive of minimising any 're-work' an auditor may have to undertake, which can impact the cost of an audit, as noted in clause 5.2.1 of the guideline:

The commission seeks to avoid duplication of effort and repetition of audit work previously performed. Therefore the auditor is expected to make use of other recent independent audits, where relevant to issues in the scope of the current audit.¹⁴

The commission appreciates the efforts required by licensees when undertaking an audit. Changes made to the guideline such as increasing the dialogue between parties at the onset of an audit will

¹² Globird Energy, Submission to the Essential Services Commission 'Draft Audit Guideline for Energy Businesses' January 2018, p. 1.

¹³ CitiPower, Powercor, United Energy, Submission to the Essential Services Commission 'Draft Audit Guideline for Energy Businesses' February 2018 p. 1

¹⁴ Audit Guideline for Energy Businesses, 24 April 2018, p. 12.

ensure there is a greater understanding of what we seek to achieve by the audit and the standards of assurance to be applied. This will assist in managing the expectations of all parties and lead to less re-work and cost for licensees

3. Audit guideline implementation

This concludes our consultation on the audit guideline. We thank all stakeholders for their input and collaboration.

To ensure we continue to promote the long term interests of Victorian consumers we welcome ongoing feedback on the audit guideline from industry participants.

The audit guideline is effective from 24 April 2018.

References

Australian Gas Infrastructure Group 2018, Submission to the Essential Services Commission *Draft Audit Guideline for Energy Businesses*, February 2018.

Australian Government, Auditing and Assurances Standards Board, Standard on Assurance Engagements ASAE 3100 Compliance Engagements, February 2017.

CitiPower, Powercor, United Energy 2018, Submission to the Essential Services Commission *Draft Audit Guideline for Energy Businesses*, February 2018.

Confidential, Submission to the Essential Services Commission *Draft Audit Guideline for Energy Businesses*, February 2018.

EnergyAustralia 2018, Submission to the Essential Services Commission *Draft Audit Guideline for Energy Businesses*, February 2018.

Essential Services Commission 2018, Audit Guideline for Energy Businesses, 24 April 2018.

GloBird Energy 2018, Submission to the Essential Services Commission *Draft Audit Guideline for Energy Businesses*, January 2018.

Jemena 2018, Submission to the Essential Services Commission 'Draft Audit Guideline for Energy Businesses' January 2018.

RSM Australia Pty Ltd 2018, Submission to the Essential Services Commission *Draft Audit Guideline for Energy Businesses*, February 2018.