

AG ISA (NZ) 250
THE AUDITOR-GENERAL'S STATEMENT ON
CONSIDERATION OF LAWS AND REGULATIONS¹

Contents

	Page
Introduction	3 - 2501
Scope of this Statement	3 - 2501
Application	3 - 2501
Objectives	3 - 2501
Definitions	3 - 2502
Requirements	3 - 2502
Determining those laws and regulations which, if breached, may be material	3 - 2502
Determining the audit approach to laws and regulations	3 - 2503
When non-compliance is identified	3 - 2504
Application and other explanatory material	3 - 2506
Determining the audit approach to laws and regulations	3 - 2506
When non-compliance is identified	3 - 2507
Appendix 1 – Decision tree for determining the audit approach to laws and regulations	3 - 2509
Appendix 2 – Decision tree for reporting non-compliance in the audit report	3 - 2510

¹ This statement is under review and is likely to be updated later in 2017.

Introduction

Scope of this Statement

1. This Auditor-General's Auditing Statement:
 - (a) establishes the Auditor-General's requirements in relation to ISA (NZ) 250: *Consideration of Laws and Regulations in an Audit of Financial Statements* (ISA (NZ) 250);² and
 - (b) establishes additional requirements and provides associated guidance to reflect the public sector perspective.
2. This Statement and the equivalent auditing standard on which it is based reflect the requirements for considering laws and regulations when carrying out an annual audit.

Application

3. Compliance with this Statement is mandatory for Appointed Auditors who carry out annual audits on behalf of the Auditor-General. This Statement requires compliance with all of the requirements of ISA (NZ) 250, except to the extent that this Statement provides otherwise. Where a conflict between this Statement and ISA (NZ) 250 exists, the requirements of this Statement shall prevail.
4. This Statement applies to audits of financial statements and/or performance information which has been prepared for reporting periods beginning on or after 1 April 2017.
5. There are specific issues of compliance with laws and regulations for the Appointed Auditor to consider when auditing appropriations in government departments (including planning, carrying out fieldwork, and reporting). For further guidance, the Appointed Auditor is to refer to AG-2: *The appropriation audit and the controller function* and/or the applicable audit brief.

Objectives

6. The objectives of the Appointed Auditor are to:

² The ISA (NZ) auditing standards are scoped so that they apply to audits of "historical financial information". However, for the purposes of the Auditor-General's auditing standards and statements, all references to "historical financial information" should be read as the audit of "historical financial and historical performance information".

- (a) obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial and performance information;
- (b) perform specified audit procedures to help identify instances of non-compliance with those laws and regulations that, if they are not complied with, do not have a direct effect on the determination of material amounts and disclosures in the financial and performance information, but are material because compliance may be fundamental to the operating aspects of the entity;
- (c) perform specified audit procedures to help identify instances of non-compliance with those laws and regulations that do not have a direct effect on the determination of material amounts and disclosures in the financial and performance information and are not fundamental to the operating aspects of the entity, but which may still be material because the entity operates in the public sector;
- (d) remain alert during the annual audit for any possible material non-compliance with other laws or regulations, although they may not have been originally identified as relevant during audit planning; and
- (e) report appropriately on non-compliance with laws and regulations identified during the audit.

Definitions

- 7. For the purpose of this Auditor-General's auditing statement the defined terms have the meanings attributed:
 - (a) in the Glossary of Terms issued by the New Zealand Auditing and Assurance Standards Board (the NZAuASB glossary) of the External Reporting Board (although where a term with a specific meaning in the New Zealand public sector differs from the NZAuASB glossary, the New Zealand public sector definition shall prevail); and
 - (b) in the Auditor-General's Glossary of Terms.

Requirements

Determining those laws and regulations which, if breached, may be material

- 8. The Appointed Auditor shall use their judgement when determining which laws and regulations may give rise to material non-compliance, in keeping with the objective in paragraph 6(c) of this Statement. As part of meeting the objective in paragraph 6(c), the

Appointed Auditor shall consider whether there is an instance or pattern of non-compliance with laws and regulations, which may be considered material if it:

- (a) undermines basic accountability arrangements (for example, non-compliance with reporting obligations, or fundamental weaknesses in internal control, or failure to keep proper accounting records);
- (b) is outside the statutory powers of the public entity;
- (c) represents a significant abuse or misuse of powers delegated by Parliament (for example, payments to management or those charged with governance in excess of authorities granted);
- (d) calls into question the probity of a major part or all of the public entity;
- (e) relates to an activity that could be of significant interest to the public; or
- (f) could be seen to disadvantage the public (for example, through actual or opportunity cost to the taxpayer or ratepayer).

Determining the audit approach to laws and regulations (See paragraphs A1 - A2 and Appendix 1)

- 9. In the public sector the Appointed Auditor shall, as part of meeting the requirements of paragraph 12 of ISA (NZ) 250:
 - (a) gain an understanding of any specific laws and regulations that apply to the public entity;
 - (b) familiarise themselves with advice from the OAG, including the applicable audit brief;
 - (c) maintain a general awareness of current events by monitoring:
 - (i) the results of any Parliamentary scrutiny of the public entity or the sector in which it operates;
 - (ii) the outcome of any reviews by government agencies;
 - (iii) the outcome of any court proceedings;
 - (iv) comments in the media; and
 - (d) monitor the development of any new legislative requirements that are likely to affect the public entity.
- 10. The Appointed Auditor shall plan and perform audit procedures in keeping with paragraph 13 of ISA (NZ) 250 to obtain reasonable assurance that the entity has complied with the categories of laws and regulations specified in paragraph 6 (a) of this Statement.
- 11. The Appointed Auditor shall follow any advice from the OAG, including the applicable audit brief, when carrying out audit procedures relating to the categories of laws and regulations specified in paragraphs 6 (b) and (c) of this Statement. Where there is no

advice from the OAG, the Appointed Auditor shall, as a minimum, carry out the audit procedures in paragraph 14 of ISA (NZ) 250.

12. As part of obtaining an understanding of the legal and regulatory framework, in keeping with paragraph 9 above and paragraph 12 in ISA (NZ) 250, the following matters shall be documented in the audit working papers:
 - (a) a description of the legal and regulatory framework applicable to the entity and the industry or sector in which it operates;
 - (b) a description of how the entity complies with that framework;
 - (c) the specific laws and regulations within each of the three categories of laws and regulations as specified in paragraphs 6(a), (b), and (c) of this Statement; and
 - (d) the audit procedures that the auditor plans to perform to assess compliance with the specific laws and regulations within each of the three categories of laws and regulations as specified in paragraphs 6(a), (b), and (c) of this Statement.

13. In meeting the requirements of paragraph 15 of ISA (NZ) 250, the Appointed Auditor shall remain alert during the annual audit for any possible material non-compliance with other laws or regulations, although they may not have been originally identified as relevant during audit planning.

When non-compliance is identified

14. The Appointed Auditor shall not provide opinions (in a legal sense) on a public entity's compliance with laws and regulations. Nothing in the Auditor-General's responsibility to consider laws and regulations in the annual audit, including references to certain laws and regulations disclosed in the audit report or the management letter, should be misconstrued as the auditor providing a legal opinion on the entity's compliance with relevant laws and regulations. (See paragraph A3)

15. The Appointed Auditor shall not report a public entity's non-compliance with laws and regulations to any responsible Minister or to Parliament. The OAG is responsible for making these decisions and shall consider factors such as the frequency or pattern of non-compliance, and the effects of non-compliance, when making its decision. Communication with any Minister about instances of material non-compliance with laws and regulations that arise during the year shall be done directly by the OAG, in consultation with the Appointed Auditor.

16. If there is uncertainty about the nature of non-compliance with laws and regulations, the Appointed Auditor shall request and obtain the public entity's view, which may include any legal advice it has obtained, before consulting the OAG.

Immediate reporting of certain types of non-compliance to the OAG

17. The Appointed Auditor shall immediately tell the OAG about any non-compliance with laws and regulations that:
- (a) is material, and for which the OAG has not provided guidance;
 - (b) calls into question the ethics or behaviour of management and/or those charged with governance or where fraud is suspected; or
 - (c) where management and/or those charged with governance are suspected of being involved in any deliberate non-compliance with a law or regulation.
- (Paragraphs A4 - A5)

Reporting instances of non-compliance

18. The Appointed Auditor shall report instances of material non-compliance with laws and regulations that arise during the year to the appropriate level of management or those charged with governance as soon as the non-compliance comes to the Appointed Auditor's attention.
19. The Appointed Auditor shall immediately inform the appropriate level of management of any non-compliance that is of such a nature that it can be remedied or repaired (for example, illegal investments). This provides management with the opportunity to take prompt action to correct any non-compliance.
20. In addition to the reporting requirements of paragraph 22 of ISA (NZ) 250, the Appointed Auditor shall report in the management letter (to the appropriate level of management or those charged with governance) any concerns they have about the integrity of internal control or other deficiencies that affect the ability of the public entity to monitor its compliance with laws and regulations.
21. All instances of a public entity's non-compliance with laws and regulations identified during the annual audit shall be reported to the OAG in the document summarising the audit conclusions. (Paragraph A6)

Reporting non-compliance in the audit report³

22. The Appointed Auditor shall follow any directions issued by the OAG on reporting non-compliance in the audit report.
23. Non-compliance that has a *pervasive effect* on the financial and performance information⁴ shall be referred by the Appointed Auditor to the OAG Accounting and Auditing Policy team. The OAG Accounting and Auditing Policy team may request the Appointed Auditor to prepare a submission to the Auditor-General's Opinions Review Committee (the ORC).
24. The Appointed Auditor shall follow any directions issued by the OAG covering how any non-compliance is to be reported in the audit report.
25. If the OAG has not issued any directions covering how the non-compliance is to be reported in the audit report, the Appointed Auditor shall consult the OAG Accounting and Auditing Policy team about the appropriate audit report to issue when they identify non-compliance in keeping with paragraph 6(b) to 6(d) of this Statement.

Application and other explanatory material

Determining the audit approach to laws and regulations (Paragraphs 9 - 13)

- A1. The nature and extent of audit procedures is to be determined by the Appointed Auditor, after considering the likelihood and the effect of non-compliance and any advice from the OAG, including the applicable audit brief. Types of audit procedures that might be considered include:
 - enquiring of management about any instances of non-compliance, or any new or unusual activities/transactions (for example, new ventures, tax-based or investment transactions) carried out during the year, and reviewing those activities/transactions;
 - reviewing minutes of management meetings or the public entity's internal compliance reports, as applicable;
 - reviewing systems and practices designed to monitor and report on compliance, or with compliance requirements embedded in them, and the adequacy of the

³ Appendix 2 is a decision tree for reporting non-compliance in the audit report.

⁴ In keeping with the objectives in paragraphs 6(a) and (b) in this statement and the requirements in AG ISA (NZ) 700 and AG ISA (NZ) 705.

public entity's policies and procedures governing compliance with relevant statutory obligations;

- performing random or risk-based transaction tests that incorporate the element of checking for compliance with laws and regulations; and
- performing substantive tests of particular laws and regulations (such as those laws and regulations specifying the determination of material amounts and disclosures in the financial and performance information).

A2. Audit procedures may be substantive in nature or place reliance, where appropriate, on the systems and practices designed to control and monitor compliance, or on both.

If a substantive approach is taken, Appointed Auditors should apply audit procedures that provide a reasonable opportunity of detecting instances of material non-compliance. However, the Appointed Auditor is not expected to review every transaction of the public entity to be satisfied that compliance with laws and regulations has occurred. Typically, substantive procedures will be directed to testing material year-end balances for the purposes of determining their fair presentation and whether they comply with those laws and regulations identified under paragraphs 6 (a), 6 (b) and 6 (c) where non-compliance may be material. For example, confirming whether an investment is lawful.

If the focus is primarily on the systems and practices, audit procedures should be designed to assess the effectiveness of internal control, including the internal control environment, established by management to minimise the occurrence of non-compliance.

When non-compliance is identified (Paragraphs 13 - 26)

A3. The OAG, in consultation with the Appointed Auditor, may also write directly to the Chief Executive or governing body in certain circumstances when non-compliance is identified.

Immediate reporting of certain non-compliance to the OAG

A4. Assessment of non-compliance requires professional judgement and may need to be based on legal advice. If there is uncertainty about the fact of non-compliance with laws and regulations, the public entity should first be asked for its view, which may include reviewing any legal advice the entity has obtained.⁵ The Appointed Auditor is to consider that advice against any existing guidance provided by the OAG. If the OAG has not

⁵ Note that the entity cannot be compelled to give Appointed Auditors or the OAG its legal advice. However, if an entity refuses to provide legal advice to the Appointed Auditor or to the OAG, this amounts to a limitation in scope and may result in a modification of the audit report.

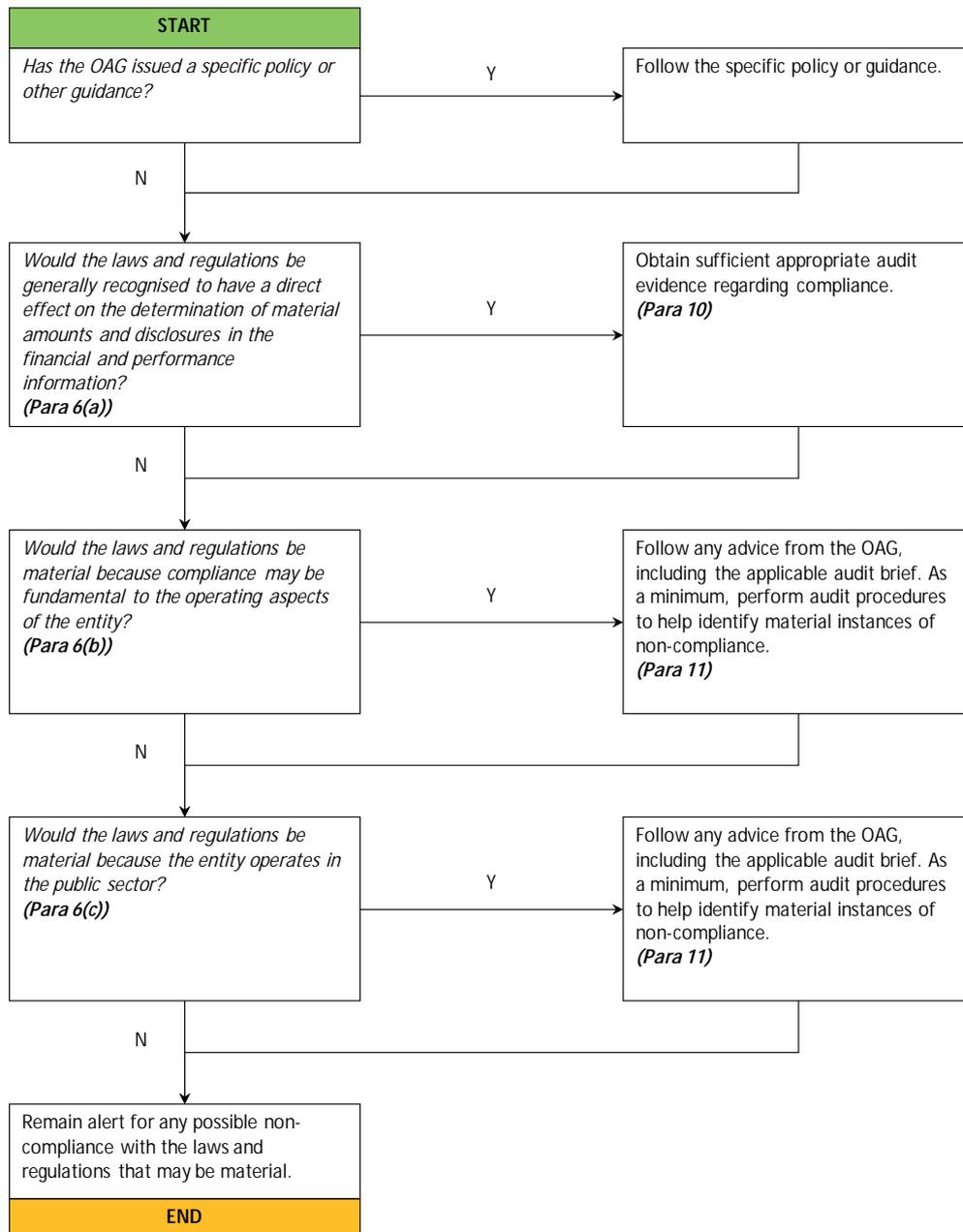
provided any existing guidance, the Appointed Auditor should consult with the OAG. The OAG will then provide the Appointed Auditor with the necessary direction and will determine, as appropriate, the need to report the non-compliance to external parties.

- A5. The Appointed Auditor is required to immediately advise the OAG when management and/or those charged with governance are involved in non-compliance; this is so the OAG can lead any response to the requirements contained in paragraphs 24 and 28 of ISA (NZ) 250.

Reporting instances of non-compliance to the OAG

- A6. Formal reports made to management on compliance with laws and regulations may be appended to the document summarising the audit conclusions. However, the essential action is to give the OAG an account of all non-compliance with laws and regulations identified at the same time that the audit report and the annual report are issued.

Appendix 1 – Decision tree for determining the audit approach to laws and regulations



Appendix 2 – Decision tree for reporting non-compliance in the audit report

