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Dear Michele

## **Re: Energy Industry Guideline 22 - Regulatory Audits Consultation**

We thank you for the opportunity to provide feedback to the Essential Services Commission (“the Commission”) on the proposed Guideline No. 22 Regulatory Audits of Energy Business and welcome the proposed enhancements to the guideline.

Overall, we believe that the proposed guideline represents a significant positive move toward achieving more timely and far improved outcomes from the regulatory audit process. The requirements for a risk based audit plan and methodology will result in a greater focus on auditing the key compliance risks for each industry participant including monitoring and reporting systems. As a result we would expect the new audit approach will result in improved quality of audits and increase the Commission’s ability to make more relevant comparisons of audit findings and conclusions. We find the guideline to be straightforward to follow and the related Audit Deed clearly sets out the relative roles within the tripartite relationship.

You have asked for feedback in four specific areas:

- The establishment of a panel of auditors serving the interests of timeliness, efficiency and effectiveness
- How well the proposed changes will drive achievement of improved timeliness
- How well the proposed changes will improve consistency of audit ratings
- How well the Commission will be able to implement the proposed guideline and deed

Our feedback is set out below:

### **Feedback on establishing a panel of auditors**

1. We agree that the establishment of a panel of auditors will support improved timeliness, efficiency and effectiveness of audits. In our experience we would also expect that leveraging a panel arrangement will also improve the quality of audits and consistency of outcomes for the Commission.

### **Feedback on achievability of time frames**

2. We agree that the proposed changes will support the achievement of more timely audits.
3. We observe that the Proposed Guideline sets out significant detail on timelines for the audit after commencement of fieldwork. In our experience a clearly defined planning process that ensures all stakeholders have a consistent set of expectations for the audit is also vital. Consequently some further clarity over the Commission’s expectations for the planning process may be helpful.
4. It may be also worthwhile for the Commission to consider implementing KPIs for each audit service provider and licensee which measure as a minimum the timeliness of each critical phase of the audit (planning, fieldwork, draft report, final report).

5. Section 7.12.1 (e) of the Guideline states that Detailed Reports (at both draft and final stage) should contain a Compliance Plan for each identified compliance breach, whereas Section 8.1.2 requires that Licensee Management action responses are provided to the Commission within 30 days of a report being finalised.

This means that reports could be finalised before full licensee consideration of the Compliance Plans being sought, and recommendations may not be tailored or consider all relevant information.

It may be worthwhile for the Commission to clearly specify the purpose and depth of detail in Compliance Plans (included in the draft report) and whether or not Auditee / Licensee Management feedback is required in the Compliance Plans.

Requiring the energy licensee to provide a formal response after the audit is beneficial, but must not be considered an opportunity to re-open the audit and related actions. In our experience, ensuring that, before finalisation all proposed audit actions are considered by the Auditor, the Commission and the licensee (at the right level of management) is important.

6. Section 8.1.5 of the Guideline summarises the key activities to be undertaken in the audit. It may be beneficial to consider an additional column to show which stakeholders are involved in each phase (i.e. the Commission, Licensee, etc.). At the moment it is unclear to what extent the Licensees are involved in the exit meeting, draft report, final report phases in this document.
7. Section 3.2 of the Guideline requires that a risk assessment is completed to drive audit frequency. While high level guidance on the key elements to be considered in the risk assessment is documented, there is limited documented guidance on how these risk assessments will work, whether the risk assessments will be based on an inherent (before management controls) or residual (after management controls) basis.  
  
As the risk assessment is such a critical step, not only in defining audit frequency, but also audit focus, the preparation of detailed reports on a regular basis, clearly setting out the Commission's risk assessments and rationale for those assessments –and communication of these with relevant licensees and auditors may be worthwhile.
8. Section 3.2.7 requires licensees to conduct their own risk assessment, at the obligation level, however there is no guidance on how this assessment should be conducted. Further guidance on how such a risk assessment should be completed may be worthwhile. It may also be worthwhile to require the licensee to share their risk assessment with the relevant auditor and the Commissions.

#### **Feedback on providing consistent ratings**

9. We agree that the Harvey Ball grading of licensees against the areas outlined in section 7.4.1 such as policy, culture / practices, procedures, systems and training / skills will be useful in providing consistent qualitative information of each licensee's practices.
10. We note that Compliance audits will now require assurance opinion under ASAE3100. However there may be some elements of the scope which will not be covered by the assurance opinion (i.e. qualitative assessment of culture). The Commission may need to provide more guidance in relation to which elements under audit will fall under the assurance opinion, and which will not. Otherwise service providers may make their own interpretation, which could differ between providers.
11. In addition we would recommend that the Guideline also comment on what type of assurance opinion under ASAE3100 the Commission would prefer. ASAE3100 allows for a reasonable assurance (positive opinion) or limited assurance (negative opinion).
12. Clause 2.1.3 makes reference to a number of relevant standards including AS 3806-2006 for Compliance, AS/NZS ISO 31000:2009 for Risk Management Principles and Guidelines and the COSO Enterprise Risk Management Integrated Framework.

We believe that further guidance on when each framework should be applied would assist auditors determine what is appropriate in each circumstance. This would assist comparability in audit outcomes.

13. Section 5.2 refers to the term “compliance risk appetite” with reference to AS 3806. Further guidance on what this means and how this is to be used by auditors in the context of Regulatory Audits would be beneficial as the term “compliance risk appetite” is not a defined term and risk appetite is an area where definitions can be unclear.

#### Feedback on the draft Deed

14. The draft deed clearly sets out the roles of each party. We note that, as we have agreed with the Commission in the past, it may be appropriate to make modifications to certain elements of the deed with regards to:
- a) Auditor Intellectual Property
  - b) Indemnities
  - c) Insurance
  - d) Definition of the draft audit report and its purpose and use

Should the Commission continue to accept previously agreed modifications in these areas, we do not see any impediment to the implementation of the deed.

We would welcome the opportunity to discuss these comments with you further and look forward to the introduction of an enhanced audit process. Thank you once again for the opportunity to provide comment.

Yours sincerely



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