Internal control assessments from 2021

The Queensland Audit Office (QAO) has developed new assessment tools for internal controls.

These tools aim to take internal control assessments beyond an effective or ineffective result, to identify where an entity has opportunities to improve the efficiency and/or effectiveness of its controls. Entities should consider these opportunities in light of the investment required and the benefit this will provide.

The assessment tools are scalable to an entity's size and complexity, and are principle-based, so they respond to factors that influence an entity's practices.

We will continue to report on deficiencies in internal controls. These assessment tools complement our reporting on internal control deficiencies. We will start to phase out our previous traffic light processes from 2021–22 as we roll out our assessment tools across different sectors of government.

Over time, we will use information from these assessments to share learnings and better practice across the public sector.

Effective internal controls

Internal controls are the people, systems, and processes that ensure an entity can achieve its objectives, prepare reliable financial reports, and comply with applicable laws. Management is responsible for cost-effective internal controls that respond to the risks it has assessed in these areas.

Through our financial audits, we focus on controls related to financial reporting and compliance. We have aligned our assessment tools with our financial audit processes. The tools focus on common controls across government entities and are consistent with the principles included in the Financial and Performance Management Standard 2019.

Annual assessment and deep dives

We have prepared an annual assessment tool for understanding where entities sit on a maturity scale for effective internal controls.

The tool should allow entities to highlight areas for targeted improvement, and where we may consider performing a deep dive assessment.

We are developing deep dive assessment tools for:

- asset management
- change management
- culture
- governance
- grants management
- information systems
- monitoring
- procure-to-pay
- records management
- risk management.

Each assessment tool uses four levels of maturity, consistent with our financial statement preparation maturity model. These are defined as:

- developing—an entity does not have this control, or it is not operating effectively, so the identified risk is not managed
- established—an entity shows basic competency in this area, so legislative requirements are met or the identified risk is managed
- integrated—an entity is developed in this area or regularly demonstrates this, so that controls work together to respond to the identified risk; however, the efficiency or effectiveness of controls could still be improved
- optimised—the entity consistently demonstrates this control and is a leader of best practice in this area.

Entity assessments

The assessment tools are entity driven. This means each entity sets its own target of maturity between established and optimised, and assesses its practices to determine if it has met them.

QAO does not expect that all entities will sit in the integrated and optimised categories, nor always aim to be in those categories. Entities should always consider the cost of moving categories in the context of the benefits this will provide.

How to set your maturity expectation

An entity should establish an expectation that is commensurate with its business. As entities implement internal controls to treat risk—the risk of not achieving their objectives, fraud or error in financial reporting, or non-compliance with legislative requirements—the desired positioning should reflect the level of risk for their entity. The higher the risk, the greater the investment in internal controls is likely to be, to reduce risk to an acceptable level.

The desired positioning of maturity will also differ depending on the size, complexity, age, structure, and available resources of each entity.

Entities may adjust their expectations during a period of change, for example, a machinery of government change, internal restructure, or changes to program delivery or major systems.

QAO's guide to expectations of maturity for entity types

Public sector entities are expected to have basic controls to meet a legislative requirement or address a risk (established). Smaller entities may not invest in their processes to mature beyond this level. Larger, newly established entities, or departments following a machinery of government change, may also assess themselves at this level for a period of time, but we would expect them to put plans in place to mature their processes.

We expect large stable entities would have invested in their controls over a period of time and assess themselves as integrated or optimised. Where an entity is not at these levels, this should reflect the risk assessment and cost-benefit analysis it has performed. There may be limited circumstances when large entities have only established basic controls and have assessed the risk of fraud or error, or non-compliance, as low, or that the cost of improving controls would outweigh the benefit provided by increased efficiency or effectiveness.

We have set out categories for three types of entities, which can be used to guide individual entity expectations:

1. Large and/or established—dependent on employee numbers, complexity of business activities, and length of time of current structure.
2. Newly established—less than three years in current structure.
3. Small—less than 50 employees.

Entities that do not fit into the categories above can use these expectations to guide their benchmarking.

QAO's expectations are a guide only, and entities can set their own expectations of maturity depending on their individual circumstances, including legislative requirements and identified risks.

Performing a self-assessment

Management needs to assure itself regularly that its internal controls are working and continuing to address the risks the entity faces. Given management's in-depth knowledge of the internal controls, we encourage it to perform a self-assessment using our annual assessment tool.

Depending on the size of the entity, this may be coordinated centrally, but is likely to involve multiple control owners across the entity. Where possible, this should leverage existing assessments done through internal audit or annual assurance processes.

Reporting self-assessment results

If they perform a self-assessment, entities can choose their internal reporting process. Audit committees will receive feedback from QAO. Chief financial officers may choose to also report their assessments, which could be included as part of an annual assurance report on their entity's internal controls.

QAO's assessment process

Using an entity's self-assessment

If entities perform a self-assessment, we will review and provide feedback on it. This is QAO's preferred approach as it relies on each entity's own in-depth knowledge.

Our assessment will then form part of our audit evidence. It will be used to inform our audit strategy, including whether we will test the operating effectiveness of controls and rely on them to reduce our overall testing.

This reflects the alignment between our existing financial audit processes and our new assessment tools.

Reporting by QAO

We will continue to report deficiencies and significant deficiencies in internal controls and financial reporting processes. We will choose where we report those matters depending on their magnitude and potential impact.

We will report the outcomes of our internal control assessments to those charged with governance. This is likely to include audit committees and directors-general/chief executive officers. Our reporting will include our observations of strengths and opportunities for improvement. Management will also have an opportunity to comment on its desired positioning. This will reflect its assessment of risk and the cost-benefit of further investing in internal controls.

Any themes emerging across the public sector, including areas for improvement or better practice, may be included in our reports to parliament.

Roll out from 2021–22

As we start rolling out our assessment tools, we are individually contacting the entities in scope for 2021–22 to discuss what this means for them and how we can best work together. This will then be formally communicated in their external audit plan.

Refinement of the assessment tool

As we trial and release our new assessment tools, we welcome your feedback to help us keep improving our tools. Please discuss our assessment tools with your QAO engagement leader and send any further questions or feedback to qao@qao.qld.gov.au.

Queensland Audit Office

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