2. Brunei Darussalam

Country Paper
on
Sub-theme 1

Performance Auditing: Concepts, Mandates,
Methodologies and Practices,
Reporting and Problems

Prepared by:
Auditor General's Office,
Brunei Darussalam

THE 7TH ASSEMBLY AND 6TH SEMINAR OF ASOSAI AT INDONESIA

SUB-THEME I

"PERFORMANCE AUDITING: CONCEPTS, MANDATES, METHODOLOGIES AND PRACTICES, REPORTING AND PROBLEMS"

PREPARED BY:

AUDIT DEPARTMENT OF BRUNEI DARUSSALAM

"PERFORMANCE AUDIT : CONCEPTS, MANDATES, METHODOLOGIES AND PRACTICES, REPORTING AND PROBLEMS"

1. INTRODUCTION:

In recent years, due to increased infrastructural developments taking place within Brunei Darussalam, government activities and expenditures had increased substantially and there is now a greater need for more information about the use of resources in the government ministries and departments. It is felt that the traditional financial and compliance auditing do not sufficiently provide for a complete picture of the results of government spending and operations. There is a need to expand the scope of government auditing to include a review on the economy, efficiency and effectiveness of the management of government resources. Towards achieving this aim, the Auditor General of Brunei Darussalam sought and obtained assistance from a SAI of a neighbouring country in September 1994 to conduct classroom lectures on performance auditing and provide guidance on field works training for the auditors. Such training provided the basis on which the auditors learnt about the concepts, approaches and methodologies of performance auditing.

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2. PERFORMANCE AUDITING CONCEPTS:

Performance auditing in Brunei Darussalam Auditor General's Office is concerned with evaluating whether:

* government resources (money, manpower, property and space) have been managed and used economically and efficiently;

* government projects or programmes have been implemented effectively to achieve their objectives and desired results

In Brunei Darussalam's SAI, the terms economy, efficiency and effectiveness are interpreted according to the definitions of the United Kingdom National Audit Office (NAO) which stated that:

Economy is concerned with minimising the cost of resources acquired or used, having regard to appropriate quality. In short, economy mean spending less.

Efficiency is concerned with the relationship between the output of goods, services or other results and the resources used to produce them. How far is maximum

output achieved for a given input, or minimum input used for a given output? In short, efficiency mean spending well.

Effectiveness is concerned with the relationship between the intended results and the actual results of projects, programmes or other activities. How successfully do outputs of goods, services or other results achieve policy objectives, operational goals and other intended effects? In short, effectiveness mean spending wisely.

3. PERFORMANCE AUDITING MANDATES:

Brunei Darussalam's Constitution and Audit Act do not have provisions that specifically empowered the Auditor General to carry out performance auditing, nevertheless the scope of government auditing has been expanding in line with the economic development taking place within the country. Auditing is no longer restricted to ensuring the appropriateness of financial records or the compliance of financial regulations and other legal requirements but greater and improved accountability from the executive

government departments and agencies. Towards achieving this objective of accountability, performance auditing was formally introduced in Brunei Darussalam Auditor General's Office in October 1994. Prior to this, the main focus of the Auditor General's Office was on financial and compliance auditing. Instances of wastage and extravagance were occasionally included in the compliance and financial audit reports, but there was no systematic approach and no proper methodology used until the auditors were formally trained. Since then a number of government projects and programmes had been selected by the Auditor General and performance audits were conducted on them.

4. METHODOLOGIES AND PRACTICES:

4.1 In Brunei Darussalam's SAI, government projects or programmes are identified and selected for performance audits by the Auditor General himself. Generally, the following are some of the criteria used for the selection:

* the projects or programmes are of national importance or of public interest;

* they are susceptible to inherent risks of wastage, extravagance and abuse;

* the potential benefits derived from an audit examination of the projects such as cost-savings and improved management controls are apparent and likely to occur;

* appropriate coverage of the projects can be done within the constraints of available resources of the Auditor General's Office (manpower, time, priority of other audit works, etc).

Notwithstanding the Auditor General's identification and selection of government projects, there were instances when the Permanent Secretary of the Prime Minister's Office requested the assistance of the Auditor General to conduct performance audits on specific projects, and these requests were accepted.

4.2 The following phases are the stages of performance auditing in Brunei Darussalam's SAI:

* Projects Identification and Selection : Other than specific requests made by the Permanent Secretary of the Prime Minister's Office, projects are normally identified and selected by the Auditor General himself based on such factors as evidence of mismanagement, financial materiality, areas of national or public interest, areas with inherent risks and whether projects are auditable within the constraints of the available resources of the Auditor General's Office.

* Proposal Phase : The key tasks involved in this phase are preliminary information gathering, such as obtaining previous audit reports, Ministerial directives, policy pronouncements and statements, auditee's annual reports and financial statements, auditee's organisation charts and budget documents and retrieving relevant legislation. The information obtained are analysed so as to identify key issues, audit objectives, scope and impact. A pre-project conference is then held to enable allocation of works among team members. Finally, contact is made with auditee through letter or telephone call to establish time, date and place for entrance meeting.

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* Scoping Phase : The key tasks involved in this phase are holding entrance meeting with auditee, learning about the auditee's background, its missions, organisation structures and activities through questionnaires, interviews, site visits, file records, management reports and manual. Identify significant activities/operations and management control of auditee, review relevant laws and policies, look for indicators of potential problems, develop and specify audit criteria and hold pre-audit presentation to Audit Management about key areas of concern and to obtain their inputs on the project and its direction.

* Planning Phase : The key tasks involved in this phase are prioritise issues to be developed, determine the work to be done and evidence needed to confirm and support each issue and develop and document audit work programme.

* Implementation Phase: The key tasks involved in this phase are carrying out the work programme for collecting audit evidence, develop audit findings (establish effects and causes),

formulate audit recommendations and hold discussion with auditee.

* Reporting Phase: The key tasks involved in this phase are drafting report outline and the report itself, hold exit meeting with the auditee, amend draft report to incorporate the viewpoints of the auditee and the auditor after the meeting and to issue final report.

5. REPORTING:

5.1 In Brunei Darussalam's SAI, a performance audit report usually included a statement of audit objectives and a description of audit scope and methodology. In order to avoid ambiguity the report should be concise, clear and complete. It should also included a discussion of the auditor's findings and conclusions. The auditor's findings included as many of the five elements of criteria, condition, cause, effect and recommendation as possible. In addition, all significant internal control weaknesses and instances of non-compliance and abuse uncovered in the audit are also disclosed in the

report. However, due to the sensitive nature of questions addressed in a performance audit report and the value judgements involved in a project or programme evaluation, auditors are usually careful in their choice of words and tone so as not to appear as if they are out to find fault with the auditee and as far as possible the report should carry constructive tone. Our performance audit reports also included the auditee's response, incorporating the views of the auditee concerning the auditors findings and recommendations and a description of the planned actions to correct the deficiencies disclosed.

5.2 In Brunei Darussalam's SAI, auditors' reports are normally addressed to the head of the auditee's department in charge of the project or programme being reviewed and copies of the report are also being distributed to the ministry to which the auditee's department come under, the Treasury Department, the Ministry of Finance and the Prime Minister's Office.

6. PROBLEMS:

Some of the problems encountered by the auditors in carrying out performance auditing in Brunei Darussalam's SAI are as follows:

a) One of the main problems encountered by the auditors in doing performance audit is the total absence or lack of performance indicators in many ministries and departments. This mean that auditors have to establish them in order to measure how far actual performance have met the goals set out in the annual performance plan of the auditee's department and to recommend the necessary actions needed to achieve unmet goals. This is a formidable task for the auditors especially in situations where the auditee's management does not have appropriate documentation measuring its own performance.

b) In carrying out performance auditing on government projects or programmes, the auditors often find themselves in situations where they are required to review specialised areas in which they lack the appropriate expertise, and it is

not always feasible to employ consultants or skilled professionals and included them in the audit team.

c) The auditors carried out performance audit on projects or programmes to improve or strengthen management controls. However, the auditee's management may not subscribe to the usefulness of this type of examination. In fact they may feel threatened by the concept of performance auditing. Quite often they believed that only they themselves are the most appropriate persons to comment on the operations and results of their projects or programmes and the auditors with their concepts of finance and figures crunching are not competent enough to judge the "technical" work of their departments.

d) In presenting the audit findings and conclusions in the performance audit report, the auditors are expected to provide recommendations for the users of their reports. They (the users of audit report) want the auditors to provide some remedial measures to correct or improve the

inadequacy of the auditee's performance. But making recommendations in areas where the auditors do not have full or detailed knowledge can be risky. This is because the users of the report, often associate high expectations with the auditor's recommendations, thinking that they are made by competent people. Therefore, to reduce the risk of error, the auditors need to exercise care in making recommendations. Otherwise, if the outcome of their recommendations do not turn up positively, the management of the auditee can shift the entire blame on the auditors.

e) In carrying out performance auditing the auditors often face the problem of keeping within the time limit allowed. Unlike financial and compliance auditings where the auditor can easily refer to previous audits as a basis to calculate the number of the man-days required to complete his works, performance auditing often involves tackling projects with different problems and require different approach that need audit manager's approval at each stage of the job, so estimating and keeping within the limit of time allowed is more difficult. For example,

completing and submitting the final report on time can be quite tricky as it involves negotiation, bargaining and compromising with the auditee, a process which is very time consuming for the auditor who must stay within the time limit of his audit program.

f) Finally, developing clear cut acceptable audit criteria to evaluate auditee's performance can be difficult too, particularly on issues where there are no existing legislation or regulation governing management's decisions. For example, in evaluating a project that has substantial natural environmental impact, the existing laws may not have provisions to which the auditors can rely to provide the necessary audit criteria or standards to judge the auditee's performance, so the auditors often have to quote foreign practices or even rely on common sense to develop the necessary audit criteria.

7. CONCLUSION:

Performance auditing, as a tool for the auditors in Brunei Darussalam's SAI to review the results of government's spendings and operations is still not being widely used on all government projects and activities. This is due partly to insufficient number of well-trained auditors available for conducting such type of auditing, partly because many auditees' ministries and departments are still not fully aware of the auditors' objectives, approaches and methodologies and consequently could not provide appropriate indicators of their performances, and partly because performance auditing concepts, approaches, mandates, methodologies and reporting standards in Brunei Darussalam are still not fully established and clearly defined. Thus, it is the hope and challenge for the SAI in Brunei Darussalam to ensure that as more and more performance audits are being conducted in the near future and as more and more auditors and auditees are being exposed to such type of auditing, the experiences and knowledge gained by the auditors will be fully utilised to better establish and clearly define the concepts, approaches, mandates, methodologies and reporting standards of performance auditing in Brunei Darussalam's SAI.

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3. Cyprus

Country Paper
on
Sub-theme 1

Performance Auditing: Concepts, Mandates,
Methodologies and Practices,
Reporting and Problems

Prepared by:
Audit Office of the Republic,
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Topic:

SUB-THEME 1: Performance Auditing Concepts, Mandates, Methodologies and Practices, Reporting and Other Issues/Problems

Paper By: AUDIT OFFICE OF THE REPUBLIC OF CYPRUS

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1. INTRODUCTION

The Audit Office (AO) has gone through three distinct eras since its creation in 1960. For about a decade and a half, the audit work consisted largely of detailed auditing of individual vouchers, a way of examination which was inherited from the British. It was characterized by highly formal, legalistic review of each voucher, with approval for payment and the settlement of the affected accounts being dependent on the payments conforming to an elaborate set of rules governing the use of public funds. This control focused, quasi-judicial interpretation of the audit function was typical in the 19th and early 20th century. This concept of auditing included functions that remain part of the AO' s mission.

During the second era of the AO, which lasted until the mid 1980's the AO was devoting a good deal of effort to reviewing the legality of agency activities. By then it became evident that it was necessary to design a new approach to financial management and auditing. The Departments and Agencies, should do their own voucher checking and accounting. The AO would concentrate on checking the adequacy of financial management procedures and controls.

While this was not the old-style voucher auditing, the underlying attitudes were more or less the same, the emphasis being placed upon strict compliance with applicable laws and regulations and reporting upon improprieties. This period was marked by the trend to employ professional accountants and other qualified staff of accounting and economic background. Over one third of staff was either professionally or university and college trained in accountancy or economic fields.

The third era of the AO started in the mid 1980's, and followed the recommendations of the 7th International Congress of SAI (Supreme Audit Institutions) held in Montreal in 1971. The Congress supported the progressive broadening of audits beyond the financial arena, and marked the beginning of the development of a new policy oriented towards economy, efficiency and effectiveness in auditing. Our relatively new state was embarking on many costly development projects and the AO was feeling the need to be able to offer valid comments on the economy and efficacy of program administration.

The political and social environment was maturing and both the House of Representatives and the media, were voicing demands for improved public accountability. Initial isolated challenges to the powers of the AO to perform management audits were quickly dispensed and the legislature settled the issue by incorporating such powers in the Public Corporations Law of 1984 and the Municipalities Law of 1985.

2. INTRODUCING PERFORMANCE AUDITS

"Performance", "Value for money" and "Management and Operational" audits are to a substantial extent synonymous terms meaning ".. a systematic and constructive review of management activity to ensure the maximum utilization of all resources in achieving the defined objectives of government and Public Corporations, primarily concerned with the following:

- ***the economic acquisition and proper utilization of all assets***
- ***the efficiency in the use of manpower and the successful discharge of assigned responsibilities by staff***
- ***the appraisal of the adequacy, application and reliability of management controls whether financial or operational***
- ***the compliance with predetermined plans, policies and procedures***
- ***the adequacy, accuracy and promptness of management information, and***
- ***the accomplishment of the objectives or targets set for the particular area or activity".***

In 1986, the AO started its first major performance audit. This work, which was performed by the AO staff, with the assistance of a number of consultants, established a new trend, aiming at the evaluation of the economy, efficiency and effectiveness of carrying out government operations. Indeed the Parliamentary Committee of the Budget had, on numerous occasions in the past indicated that, the scope or the AO's work should be extended beyond regularity and financial matters, to include operational and management audits.

Following this pilot project on performance evaluation, the AO adopted new ideas and additional roles for itself. In short, these include the AO's contribution towards program evaluation and policy analysis. The emphasis is now placed on going beyond its traditional functions, to determine whether government funds are spent efficiently and whether government programs are effective. It is now a routine matter for the AO to include in its work plan a number of performance audits which are mostly self initiated. This is the most important recent development in the role of the AO.

Successful completion of performance audits, requires adoption of a management oriented approach by the auditor, more specialized knowledge and training. While the present practice of the AO is to carry out a few large performance audits each year and report on

them separately, our long term objective is to integrate them with the traditional financial audits and carry them out and report on them concurrently. This will require more capabilities and expertise from our staff.

With time, the new roles are integrated into the AO's auditing and financial reporting responsibilities. Members of the staff have taken training in the area of performance evaluation, in line with our attempt to build a staff capable of carrying performance audits, evaluations, and other studies and investigations of widely varying complexity.

3. OBJECTIVES OF PERFORMANCE AUDITING

While Performance audits carried out by the AO are concerned with economy, efficiency and effectiveness, they also examine accountability. The AO is in a position to identify better practices, because it can have a cross-agency perspective, not enjoyed by other organizations.

While performance audits usually focus on particular programs or activities, they may extend to an issue that is common to or influenced by a range of agencies e.g. purchasing. Audits that cover a number of agencies, increase the relevance and scope of audit findings and recommendations and add value to the overall performance of government agencies. Cross-entity audits have the potential to increase the relevance and scope of audit findings and recommendations and add considerable value to the overall performance to the public sector.

4. PERFORMANCE AUDITING AND FINANCIAL STATEMENT AUDITING COMPARED

Compared with conventional financial statement auditing, performance auditing takes new directions and extensively widens the scope and intentions of audit review and evaluation. Financial reporting is primarily concerned with the regularity and compliance within the rules set in appropriations, expending of public funds and financial reporting. Performance auditing brings attention to goals, objectives and results which take their form in the outputs or effects of a program.

The audit mandate enables the AO to report a performance audit in a form that describes managements performance and presents the facts, findings and an opinion indicating the extent to which management has performed efficiently, effectively and economically.

5. PERFORMANCE AUDIT MANDATES

a. History of Constitutional Provisions

Government accountability is something that the public demands and deserves, and the Audit Office of the Republic serves an important role in achieving it. The AO is an independent Office of the Cyprus Republic, distinct from the three powers composing the State, the Executive, the Legislative and the Judiciary. It examines how public money is spent and recommends to the Executive ways to improve the effectiveness of the public administration.

Following the colonization of the Island in 1878 by the British, the first Auditor under the Colonial Regime was appointed in February 1879, and he was also the Accountant of the colony. In 1883 it was decided to separate the duties of the Auditor and the Accountant. The British rulers recognized the need for separation between the audit function and local administration at an early stage, an arrangement that lasted until 1960, the year of Cyprus Independence.

On independence in 1960, Article 115 of the Constitution provided for the creation of an Independent AO. The Constitution also provides that the Auditor General and his Deputy are appointed by the President of the Republic, like all the other Independent Officers of the State, and not by the Public Service Commission, as it is the case with other Civil Servants. They serve until retirement age, or until they are removed, but only on grounds of impeachment, a procedure that has never been attempted. The terms of their employment and remuneration are determined by the appointing authority. The effect of these arrangements, is to insulate the AG and the AO to a very substantial decree from improper external influence.

These Constitutional provisions indicate that the basic concept underlying the creation of the AO, was to separate as far as possible the auditing institution of the country from the organs responsible for its financial administration, and give it the required independence, in carrying out its functions.

The legal nature and structure of the AO, resemble that of most commonwealth countries, UK, Canada, Australia etc., as opposed to the Courts of Audit, systems which are more common in France, Italy, Greece and other European Countries.

The Auditor General is required by the Constitution to "*...control all disbursements and receipts and audit and inspect all accounts of money and other assets administered, and of liabilities incurred, by or under the authority of the Republic.*" He shall also"*..exercise all such other powers and shall perform all such other functions and duties as are conferred or imposed on him by law.*"

It is assumed that the term "... other functions and duties..." above must conform with the spirit as well as the letter of the main Constitutional provisions. The Constitutional provisions are general and do not prescribe the detailed rules and mechanics of carrying out the audit work. The detailed working procedures and tasks to be performed, are matters left to the discretion of the Auditor General, who will look at the norms and developments currently ruling the auditing profession world-wide, and employ such audit techniques and methods which are generally acceptable for accomplishing similar tasks.

These rather general provisions of the Constitution, have a dynamic and evolving nature. While the basic concept of auditing all government receipts and payments does not change its content, i.e. the techniques and methodologies used to achieve this final audit objective, varies through the years, in a way that allows for the adoption of improved work methods.

In Cyprus the performance audit mandate stops short of commenting on Government policy decisions. It is, however, acceptable for a performance audit to incorporate the audit of information leading to policy decisions, an assessment of whether policy objectives have been met, and an assessment of the results of policy implementation both within the administering body and externally on others. In short, it does not question the appropriateness of the policy objectives.

The AG has a central place in the process of public accountability. The Executive is accountable to the Parliament and relies on the Auditor General for independent assurance as to the fulfillment of the public accountability obligations of these bodies. This independence means that the AG has complete discretion in the selection of areas subject to performance audit.

b. Power to inspect records

In Cyprus the Auditor General has powers to inspect records and enter premises for the effective discharge of the functions of the AO. The Auditor General is provided with various powers, including the power to:

- ***call for persons and records;***
- ***have full and free access at all reasonable times to accounts and records.***

There is no provision in the legislation restricting disclosure of any matters or documents from audit reports. There is complete freedom for disclosing any type of information deems proper. Also the Auditor General has a right of access to records of expenditures of agencies, as well classified defence information.

c. Parliamentary privilege

In Cyprus the Parliament is the primary client of the AO and the audit reports tabled in the Parliament are protected under parliamentary privilege. While parliamentary privilege provides AO with an ability to report independently, it also imposes the obligation to ensure the quality of its work is commensurate with this privilege.

6. METHODOLOGIES AND PRACTICES

a. Audit methodology and strategies

The available resources of the AO are limited and they have to be allocated to numerous audit areas. The traditional financial, regularity and compliance audits are reserved by the audit mandate and constitute a fundamental function of the AO. Furthermore these audits are repetitive, and absorb the majority of available resources.

The recent introduction of performance audits, necessitated the critical review of audit objectives and the revision of work programs, so that unnecessary work of little value has been dropped, and greater emphasis was placed on channeling time saved in performance audits. These audits may be self initiated, or be the result of direct request of Parliament or Government.

Strict criteria are applied for the selection of such audits, and are carefully planned. In the first instance we draw on the knowledge and experience acquired through the conduct of financial and regularity audits and preliminary surveys are carried out where necessary. Selection is based on criteria such as, expected benefits or savings, impact on the general administration, wide applicability, public sensitivity and interest shown by the House of Representatives.

As the AO has evolved and its work load has grown, planning has become much more crucial to the Office's ability to continuously produce quality work. An annual audit plan which is reduced down to general and detailed audit programs is prepared. Audit programs

are sufficiently flexible, to allow the development of initiatives and to cater for adjustments necessitated by new developments, contingencies and special audits.

Through is planning process, the AO is able to identify the most important subjects within each area, and coordinate work across division and branches. Work allocation is made on the basis of importance of audit areas and staff proficiency and aptitudes. A staff rotation system is employed in order to avert complacency, friendly associations with auditees and to stimulate alertness and efficiency. Audit procedures describe adequately the process of audit, including the discussion of audit findings with administrators before the finalization of audit reports.

b. The importance of strategic planning

The AO selects and schedules audit tasks that help achieve its mission, goals and objectives. The planning process, ensures that the resources of the SAI are used in the most efficient and effective manner. Strategic plans are developed annually and aim to:

- ***provide a firm basis for the AO management to give a strategic direction for future audit coverage;***
- ***identify and select audits with the potential to improve public sector accountability and administration;***
- ***produce a work program that can be achieved with available resources;***
- ***provide a basis for accountability;***

c. Audit topic selection

Performance audit topics are normally selected, on the basics that, they will focus on those audits which have maximum value added in terms of improved accountability, economy, efficiency and effectiveness; and secondly, to ensure as far as possible coverage of agency operations within the limitations of audit resources available.

A list of potential audit topics will be selected based on possibility of inadequate economy, efficiency and effectiveness, and generally of poor performance. Those topics are then subjectively ranked against criteria of:

- ***overall estimated audit impact;***
- ***financial materiality;***
- ***significance of the program/project etc. to the activities of the agency.***
- ***political sensitivity or national importance; and***
- ***extent of recent audit coverage.***

d. Stages of performance audit

The basic stages followed during performance audits, are the following:

- ***planning***
- ***preliminary Review***
- ***Detailed Examination***
- ***Reporting***
- ***Follow up***

Once the planning process is complete and a particular activity or topic has been selected to audit, the audit team would usually, but not always, conduct a preliminary study to further examine and understand the activity under audit, identify fundamental issues, define audit objectives, develop the scope of the audit, estimate potential impacts, develop audit criteria, collect preliminary audit evidence and prepare a preliminary study report, either oral or in writing. The output of the preliminary study is normally a report which recommends either terminating or continuing the audit. It is recommended that the audit should continue, the report is likely to include an implementation plan for the conduct of the remainder of the audit.

The detailed examination stage involves the collection and documentation of relevant and reliable evidence, usually in accordance with a detailed audit test program, sufficient to support audit findings, conclusions and recommendations. The detailed stage also involves regular communication with the entity, the discussion of preliminary issues that have emerged during the course of the audit, and a formal interview with the agency at which the audit findings are discussed.

At the conclusion of the detailed examination stage, the AO prepares a draft report, which allows the entity to comment on what would normally be the format of the final report. Once the entity comments have been considered, the report will be finalised. Presentations to the Parliament, the Minister, and the entity may also be conducted, and copies of the final report issued to them.

The follow-up stage of a performance audit, is an integral part of performance auditing and; may serve to increase the likelihood that entity management will implement the recommendations that were agreed; may be valuable in guiding the actions of parliamentary committees and providing feedback on the effectiveness of performance auditing. As one of

its objectives, is to add to the impact of our reports, follow-up activity should be directed to encouraging the implementation of recommendations. rather than finding examples of lack of action. Working with entity management may also assist the entity in implementing recommendations.

e. Managing the audit program

The AO in producing Performance Audit reports, is concerned with timeliness, because it is thought that untimely reports are less likely to produce improvements in public sector administration. In general the procedures followed by the AO in planning performance audits, involve the identification of candidate topics when preparing the "Annual Audit Program" (AAP), which forms the basis for all the audit work for the year ahead.

f. The AAP

The AAP is a key document of controlling and monitoring an individual audit in both the preliminary and detailed examinations stages. AAP is useful in that it can identify:

- ***the task to be completed;***
- ***the resources to be used;***
- ***the timing of each assignment.***

AAP provides sufficient information to enable an informed decision to be made about the value and impact of the audit and also its relative priority in relation to other audits. The budget and timetable are documented in the working papers and progress against these targets monitored and recorded. This is necessary to meet time targets.

g. Auditing Standards

Performance audits are conducted in accordance with auditing standards consistent with the professional standards required of private sector auditors. Ethical principles governing the auditor's and the AO's responsibilities set standards on: independence, integrity, professional competence and due care, confidentiality, professional behavior, and technical issues. These standards are reflected in International and INTOSAI Auditing Standards. The AO has not yet issued its own series of Auditing Standards and Guidelines, but has adopted the above.

h. Audit Objectives

Audit objectives are chosen with a view to defining an audit which has the potential to improve public administration. Performance audits warn against ineffective-inefficient practices and identify and promote good practice. To facilitate the analysis of economy, efficiency and administrative effectiveness the public sector activities are viewed in relation to the following:

- ***the program objectives, which should be clear enough to identify the desired outcomes;***
- ***the financial and other resource inputs used;***
- ***the processes or activities by which the inputs are converted into outputs;***
- ***the goods, services or other results and impact of the program;***

Given the size, complexity and diversity of agencies operations, it is normally impracticable to attempt to assess the overall performance of departments or agencies in any meaningful way. Consequently, performance audits are usually directed towards specific functions, activities, programs or operations of the entity organisation.

i. Audit scope and focus

The scope of the audit determines in practice, the extent and depth of examination during performance audit and the assessment of policy implementation and legislative compliance. Emphasis varies from audit to audit. It also ensures that field work is clearly defined and so assists in producing an audit of reasonable extent and cost. Scope will often be defined by stating what an audit will not cover.

Some aspects of audit receive greater emphasis. Narrowly defined focus on key areas of the audit ensures the achievement of objectives of the audit, avoid inefficiencies, delays and insignificant findings. During the audit the focus will be readjusted, if the results of detailed analysis indicate other areas of audit importance.

j. Audit criteria

Audit criteria form an important tool for the conduct of performance audits, as they are used as the yardsticks against which actual performance is measured. The chosen criteria, will reflect what would be the reasonable standard of performance, to measure the adequacy of systems and practices, and the extent of economy, efficiency and effectiveness of operations, programs, or activities under assessment. When the examination identifies that

actual performance falls short of the standard, an audit finding is generated, indicating that improvements can be made.

Audit criteria, assist performance audits, by setting as far as possible clear grounds of communication between the AO and the management of the agency under audit. Especially, when such criteria are quantifiable, provide the agency management with clear and understandable measures and facilitate the acceptance of audit findings. They also assist the planning and programming of audit and form the basis for data collection. At the preliminary scooping stage of the audit, criteria tend to be more general and sometimes vague, but usually as the examination progresses, these tend to be more specific and detailed and used as a basis for the development of audit programs and procedures.

k. Sources and development of audit criteria

Performance auditing criteria are not available from the accounting profession. Audit teams look at the following sources, to form relevant criteria:

- ***criteria used previously in similar audits;***
- ***laws, regulations and other internal agency circulars;***
- ***criteria published by overseas audit institutions;***
- ***performance standards used by the entity;***
- ***agency related legislation, procedures and policies;***
- ***entities that are similar to the entity, carrying out similar activities or having similar programs;***
- ***professional organisations and standard-setting bodies;***

We often consult with the agency entity management to obtain their views on the development of criteria and if possible, resolved disagreements at an early stage. It is essential to encourage agencies to get involved in the development of audit findings, so that they will be more willing to implement them.

l. Test Programs

The audit objectives are linked to the detailed testing through an audit program, customized for each audit, which in turn attempts to establish the degree to which the set audit criteria are met. The audit procedures used for testing, include observing, interviewing, documenting, testing and checking, and analysing. Factors considered when developing the programs may include: audit objectives, size of task, geographic dispersion, audit

environment, the components of the system to be audited and whether broad issues only have been identified, or specific criteria are available.

In developing an audit program, it is important that the procedures:

- ***relate to the audit objectives, that is they enable relevant evidence to be collected;***
- ***are clearly stated and include sufficient detail to enable them to be readily understood by those carrying out the audit;***
- ***are organised in a logical manner so the audit examination can be conducted as efficiently as possible; and***
- ***form an efficient method of gathering sufficient evidence, that is, they do not call for superfluous testing.***

m. Audit approach

The approach to an audit, will develop as greater understanding of entity operations is orachieved and as initial audit findings are made. Throughout each stage the emphasis should be on producing a final report that has impact and balance. Draft report segments will take shape as the audit progresses, even at the early preliminary planning stages when initial knowledge and insights are being formed. The report writing process should be viewed as a continuous one of formulating, testing and revising hypotheses about the audit topic. Consideration of the impact on the audit report of work being undertaken at any stage is an essential test of the relevance of this work.

n. Evidence

Audit evidence, a fundamental concept in performance auditing as well as in financial statement auditing, is information collected and used to support findings. The conclusions and recommendations in the audit report stand or fall on the basis of such evidence. Consequently, performance auditors must give careful thought to the nature and amount of evidence they collect. An effective audit program helps in obtaining persuasive evidence to support findings in an economic, efficient and effective manner. Evidence is critical to the success of the audit and is a central concern from the planning phase, to the end of the audit. While differences in judgment might also be highlighted, it is important that maximum evidential support be provided in such instances.

The audit findings, conclusions, opinions and recommendations must be based on evidence that meets the basic tests of sufficiency, competence and relevance. Sources of evidence may include: government policy statements and legislation; published program performance

data; interviews; file examination; management reports and reviews: external sources; AO sources; observation; and surveys and questionnaires.

o. Documentation standards

Auditors must adequately document the audit including the basis and extent of planning, audit methods and procedures, research design, the work performed and the audit results and findings. Thorough documentation in the form of working papers is a vital aspect of maintaining a professionally acceptable level of auditing. Working papers aid in the planning and performance of the audit, the supervision and review of the audit work and providing evidence of the audit work performed to support the auditor's opinion.

Working papers serve as the connecting link between the field work and the audit report. Thus they contain the evidence accumulated in support of the opinions, conclusions and recommendations included in the report and are themselves evidence that the auditor has conducted the audit in accordance with approved procedures.

The prime need is to demonstrate the quality of evidence and opinions, conclusions analysis and supporting recommendations, in the interests of presenting a credible report for consideration by the Parliament and agency management. This need becomes even more pronounced in auditing to efficiency and economy criteria. There are several broad characteristics which all working papers should exhibit:

- ***completeness and accuracy;***
- ***clarity and conciseness;***
- ***ease of preparation;***
- ***legibility and neatness;***
- ***relevance;***
- ***organisation;***
- ***and ease of review.***

r. Audit findings

The recommendations made by the AO in performance audit reports, have to be argued in a logical fashion. The development of audit findings, and the formulation of recommendations based on those findings, are critical phases in the audit process. The steps involved are likely to be:

- ***audit criteria (what should be);***
- ***audit evidence (what is);***
- ***audit finding (compare what is to what should be);***
- ***assess the effects of the finding;***
- ***develop audit conclusions and recommendations;***
- ***and estimate likely impacts***

Audit observations and evidence, are compared with the audit criteria, to identify audit findings. The development and evaluation of audit findings, take place throughout the various phases of a performance audit. It starts in the planning stage, with the identification of matters of potential significance and preliminary findings which are then followed up in the detailed examination phase.

The detailed evaluation of audit findings, is generally completed during the preparation of draft report, or near the conclusion of the audit fieldwork. However, it would not be unusual for the evaluation to extend into the final reporting stage, as findings are challenged and further evidence is obtained. It is at this stage that a final decision is reached, on the findings and recommendations that will be reported. Once an audit finding has been identified, its significance is assessed and what causes of lack of performance and if possible the effect quantified. Lack of control, poor decisions or lack of concern for service, may also be assessed and corrective action suggested.

q. Developing recommendations

The causes of a finding are identified, as they form the basis for our recommendations. The cause is that which, if changed, would prevent similar findings. The cause may be outside the control of the organisation under audit, in which case the recommendation should direct attention outside the organisation.

The development of recommendations for improvement in administrative or operational performance, is an important feature of performance audits. Recommendations are developed for findings with significant adverse consequences. While recommendations focus on the improvements needed, rather than how they should be achieved, it is appropriate to indicate broadly, what issues might be examined by management when seeking solutions.

r. Communicating with the entity

There are, legitimately, often differing views on the way in which programs can be managed. To avoid tensions between the entity and the AO, we establish an open, continual and honest communication with audited agencies. Findings are usually presented to agency management for oral comments as they arise. In this way entity responses can be documented and analysed. Where the entity disagrees with the audit findings and recommendations, the reasons for such disagreement should be fully analysed. The AO, has adopted a policy of seeking comment from the agency and anyone else, whose interests might be adversely affected by the report.

7. REPORTING

a. Reporting standards

The AO has adopted the International Auditing Standards for reporting on financial audits, and the pronouncements of the Organisations representing Supreme Audit Institutions, which state that, at the end of each audit, the auditor should prepare a written report setting out the findings in an appropriate form. The report should be easy to understand and free from vagueness and ambiguity, include only information which is supported by competent and relevant audit evidence, and be independent, objective, fair and constructive.

Clear, balanced and objective public reporting of audit observations is fundamental to the audit role in public accountability. The published final performance audit report is the product on which the AO performance audit function is judged by the Parliament and the public at large. We therefore give much thought to the development of the audit report. Its contents and the wording of recommendations, can be contested by entities and attention needs to be paid to the accuracy, logic and clarity of the reports. Any material errors, could be potentially damaging to the credibility of a particular report and to the AO .

Audit reports may come under increasing scrutiny from Parliamentary Committees, the public and the media. The AO methodology, the interpretation of data, and the evidence used to reach audit conclusions can be questioned. For these reasons, it is important that reports are of a high standard and follow the Internationally recognised Auditing Standards and other applicable guidelines.

The AO has established a system of control, to ensure that the quality of the audit and audit report is up to standard. This control system may consist of steering committees formed within the AO, as well as internal peer reviews, undertaken at various stages during the

audit. Learning from other Supreme Audit Organisations, that conduct similar activities, can be an important part of judging and then improving the quality of audit process and product.

b. The continuous report-writing process

Reports produced during an audit, include the initial audit work plan, the preliminary study report the final draft report and the final report. Given the amount of reporting required during an audit, the reporting process should be as efficient as possible. This can be achieved by the use of a continuous report-writing process, that starts at the beginning of the audit with an outline that gradually grows and changes throughout the course of the audit and results in a final audit report.

An alternative approach is to produce papers by topic during the audit. These are merged with relevant sections of the preliminary study report and any other relevant material to produce a report which can be discussed at the exit interview. Ideally, the format of the draft report should be as close as possible to that of the final report, as this allows the entity to see the audit findings in context and comment accordingly.

c. Interim reports and exit interview

At various stages during an audit, interim reports may be prepared, when necessary, to identify and discuss major issues that have emerged during the course of the audit. They assist the evaluation of significant preliminary audit findings with an entity and generally help in communication with the entity, and they describe the issue and its effect on entity operations or program. Suggestions for improvement may be included, if thought appropriate. This may lead to early implementation, of audit recommendations with an immediate effect in improving public administration.

At the conclusion of the fieldwork, is usual to hold a formal exit interview to discuss the preliminary audit findings and offer a first opportunity for the entity to see the context of audit findings and conclusions.

d. Proposed Report

Once the comments from the entity at the exit interview are obtained, a report representing the culmination of the audit field work, and associated analysis and consideration, and the AO' s final conclusions and recommendations, is prepared. This is usually the last opportunity for the entity, to comment on the findings, and a reasonable amount of time should be allowed for the entity to study the proposed report.

Providing an entity with a copy of the proposed report, ensures that the entity is fully aware of the contents of the report before it is tabled in Parliament, or sent to the other recipients.

e. Entity responses

The entity's response should be reviewed to ensure completeness, particularly that each recommendation is commented on as to its acceptability. If it is not complete, a supplementary response may be requested. However, the audit team needs to bear in mind the resulting impact on meeting the targeted tabling date. One way of ensuring that the entity's view is shown in the reports, is to incorporate the entity's response as to whether they agree to the recommendations.

8. OTHER ISSUES/PROBLEMS

a. Client relationships

Performance auditing, by its very nature, can lead to tension between the entity and the AO. The AO generally, tries to manage this tension through developing a relationship with its clients. While the Parliament is the primary client of the AO, there is a good case of AO to develop a secondary client relationship with agencies. Improvements in performance and accountability of public sector agencies, are less likely to occur where there are differences, particularly fundamental differences between the AO and the entity being audited. This does not mean that there should be necessarily always be agreement. However, the basis of any disagreement should be apparent.

The AO should endeavour to work closely with entity management, to achieve an outcome both parties are at least broadly able to agree. This relationship can be built on the concept of open and timely consultation. It is not a case of setting for a low level compromise solution, but a matter of ensuring good communication and understanding of issues and mounting a compelling argument. Often this can be achieved by a balanced presentation of the audit indicating good levels of performance, as well as those that can be improved.

The AO is not currently seeking feedback from the recipients of audit reports, whether the audit reports have led to improvements in public administration, or the AO' s work has been useful. Feedback on level of agencies compliance with the recommendations of the AO, is received from the routine audit visits and by following up what has been implemented annually. In its dealings with Parliament and agencies, the AO usually has a responsibility to act in an apolitical, impartial and objective manner.

b. Skills of performance auditors

The AO's credibility is mainly a product of the quality of its audit reports. Performance audits focus on decision making and management procedures and are by their very nature interdisciplinary. While performance audits could employ persons with highly developed analytical skills who may not be accountants, this is not the case with the AO, that employees mainly accountants and persons with competencies related to that field.

We do not expect to have all the specialist knowledge in the AO. We are in favour of using consultants for specialist tasks, however financial constraints permit this to a minor extent only.

AS/AT

REF.: ASOSAI/RE961127.A01

4. India

Country Paper
on
Sub-theme 1

Performance Auditing: Concepts, Mandates,
Methodologies and Practices,
Reporting and Problems

Prepared by:
Office of the Comptroller & Auditor General,
India

Sub-theme 1: Performance Auditing : Concepts, Mandates, Methodologies and Practices, Reporting and Problems

Country paper by SAI-India

1. Introduction

This country paper has been prepared in response to the Principal Paper on Sub-theme 1 "Performance Auditing Concepts, Mandates, Methodologies and Practices, Reporting and Other Issues / Problems" by SAI-Australia, and reflects the history, concept, mandate and methodology of performance audit, as it is practised in India. The paper has been structured along the same lines as the principal paper.

2. Background

In the wake of the introduction of successive Five Year Plans for social, economic and industrial development, the pattern of Government expenditure underwent a radical and rapid transformation from mere law and order, policing and other administrative expenditure to expenditure for promoting development in various areas - anti-poverty programmes, employment generation programmes, programmes for providing health and sanitation services, and primary education, development of agriculture and irrigation facilities, among others. In addition, Government made massive investments in industry by setting up its own commercial enterprises covering the infrastructure sector - energy, transport, telecommunications - defence production, core sectors producing basic raw materials for industry, as also many non-core areas involving production of consumer goods etc.. While the SAI's traditional audit had extended beyond considerations of mere regularity of expenditure to examination of whether such expenditure was wasteful, extravagant or improper, it was realised that the focus on audit of individual transactions alone would no longer suffice. In response to these changes, the SAI evolved the technique of Efficiency cum Performance Audit (ECPA) in the early 1960's. ECPA was directed towards examination of large programmes, plans and schemes, organisations and activities with a view to examining whether the intended benefits of the programme had been realised as planned, and assessing the extent of achievement of physical and financial targets, realisation of social and economic objectives, economy of operations and efficiency of utilisation of resources.

2.1 Mandate for Performance Audit

SAI-India is a constitutional functionary, and the legal basis for its functions is provided by an Act of Parliament, which vests responsibility on the SAI to audit Government receipts and expenditure, as also enterprises, bodies or authorities owned, controlled or substantially financed by Government. The term "audit" in the Indian context is comprehensive in scope, covering not only appropriation, regularity and propriety audit, but also Efficiency Cum Performance Audit (ECPA)

and systems audit. The SAI's mandate to conduct performance audits has never been challenged.

2.2 *Powers of inspection*

The statutes governing the SAI empower it to inspect any office of the organisations within its audit jurisdiction, call for any books of accounts and other relevant documents that may be required during audit[2], and call for such information as may be required by the SAI for the preparation of any account or report. The Act also directs the auditee agencies to provide facilities for such inspection by the SAI and comply with requests for information in as complete a form as possible and with all reasonable expedition.

2.3 *Scope and coverage of performance audits*

The scope of performance audit by SAI-India covers review of not only projects, programmes and schemes, but also agencies, public sector enterprises, revenue receipts, and financial management by Ministries and Departments. An idea of the extent of performance audit by the Indian SAI can be derived from the fact that nearly 400 performance reviews figure each year in the Federal and Provincial Audit Reports of the SAI. In addition, the Audit Reports feature nearly 4,000 individual audit observations every year. While these observations cover individual transactions or areas, they highlight instances of financial irregularities, losses to Governments, wasteful and extravagant expenditure, and loss of revenue, which represent the ultimate objectives of performance audit, as opposed to certification or compliance audit.

3. Methodology

3.1 *Audit Selection Criteria*

Keeping in view the vast volume of auditable investment in industrial and social economic development and the limited resources available, SAI-India has necessarily to be selective in choosing areas for detailed examination as part of the macro audit planning process. The criteria generally adopted for the selection process include the following :-

- Quantum of investment of public resources in the programme, scheme, activity or organisation

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[2] The SAI can require these documents to be sent to any place chosen by it for inspection.

- Impact of the programme or scheme on industrial or socio-economic development
- Legislative sensitivities
- Topicality and public sensitivities
- Information from financial and regularity audits

3.2 Audit Process

The broad stages in which the performance audit of the selected programme or activity is carried out are :-

- Preliminary study
- Audit planning and finalisation of guidelines
- Audit execution
- Mid-term appraisal
- Reporting
- Follow-up

3.2.1 Preliminary Survey/ Feasibility Report

A preliminary or "pilot" study of the selected scheme is an essential pre-requisite for the performance audit. The objective is to obtain a comprehensive overview of various aspects of the programme, its aims and objectives, the performance indicators and standards set by the policy makers, the delivery mechanism established for the programme etc. with a view to identifying areas requiring in-depth examination and investigation by the SAI. A decision is then taken by the SAI as to whether to conduct the performance audit or not.

3.2.2 Audit Planning / Guidelines Finalisation

After a decision has been taken to go ahead with the performance audit of the selected scheme, a detailed audit plan is developed, based on the pilot study. This plan contains detailed guidelines for audit, spelling out clearly the areas requiring detailed investigation, the audit hypothesis to be tested, the data to be collected at the administrative office and programme field sites and also from the beneficiaries. The questionnaires for data collection are also framed at this stage, along with detailed instructions for data collection.

3.2.3 Execution

5.31 After the finalisation of the audit plan, the performance appraisal proper commences, with the objective of ascertaining whether the programme is being

executed efficiently and economically and the expected outputs are being achieved. The policies, procedures, practices and internal controls followed are examined with a view to ascertaining, among other things, whether :-

- the objectives of the programme have been identified clearly enough to be capable of measurement and proper implementation
- the programme achievements (intermediate and ultimate) are in accordance with the planned targets
- programme costs are within the estimates and are commensurate with the benefits derived from the programme
- the purpose of the programme has already been achieved and whether there is any continuing need for the programme
- the programme is the most effective, appropriate and economical way of achieving the goals set for it
- effective monitoring and internal control mechanisms exist for ensuring that the programmes run on course and according to schedule

5.32 After collecting audit evidence through substantive and system testing, audit findings are formulated, and discussed with / communicated to the auditee agencies with a view to ascertaining their viewpoint for incorporation in the Audit Report.

3.2.4 Mid-Term Appraisal

There is need for continuous monitoring by the SAI of the execution of the audit tests in an ongoing fashion, supplemented, if need be, by a mid-term appraisal of the interim audit findings. Often the SAI finds after deploying a portion of the resources allocated for the audit, that it is not really worthwhile to continue the audit and deploy more resources on it, and a decision could be taken to either abandon or defer the audit or restructure its scope and coverage. Occasionally, an SAI might find that its planned level of resource deployed is not commensurate with the actual volume of audit effort involved, and the resource deployment plan may have to be augmented or the scope of audit restructured in consonance with the available resources. A mid-term appraisal of a performance audit is thus an important milestone, giving the SAI an opportunity to decide whether to continue the audit, restructure its audit scope or coverage, enhance resources deployed for the audit or abandon the audit altogether.

3.2.5 Reporting

This is the final stage of the performance appraisal. The data collected is consolidated and collated for interpretation and detailed analysis. The audit findings are drafted carefully after analysis of the findings of investigations. The draft performance audit report is sent to the Government / auditee agency for ascertaining their viewpoint. Based on their comments, the report is revised, finalised and presented.

3.2.6 Follow-up

There is a formal and effective system of follow-up on the performance audit reports issued by SAI-India. These reports are examined by the Legislative Financial Committees, who make appropriate recommendations to the Executive for implementation. The Committees also monitor the implementation of their recommendations. Even in cases where the Committees are unable to examine the audit findings, reports on action taken on audit findings are called for from the Executive. These "Action Taken Reports" are vetted by the SAI for factual accuracy, before transmission to the Committees.

3.3 All-India Reviews

A unique feature of performance audit conducted by SAI-India is the concept of "All-India Reviews". Most of the socio-economic development schemes being implemented in India are financed by the Federal Government, but are implemented through the Provincial Governments. As Auditor for both the Federal and Provincial Governments, SAI-India has the responsibility of reporting on the economy, efficiency and effectiveness of such programmes to both the Federal and the Provincial Legislatures. This challenge has been tackled through the medium of "All India Reviews". Here, the guidelines for the conduct of the performance review are framed centrally by the Principal Audit Officer of the Federal Government, after conducting pilot field visits to a few provinces and interaction with the SAI's field formations in these provinces. These guidelines, after approval by senior management of the SAI, are then circulated to the field formations of all the provinces, where the programmes are being implemented. The findings of the field formations are analysed and consolidated centrally, before being presented through the SAI's Audit Report to the Federal Legislature. Simultaneously, the audit findings of each field formation are also reported through the SAI's Audit Report to the respective Provincial Legislature.

3.4 Audit Boards

Another innovation by SAI-India in the field of performance audit is the constitution of "Audit Boards" for comprehensive appraisal of selected Public Sector Enterprises functioning in diverse industrial sectors. These Boards, one for each performance review, are constituted by the Comptroller and Auditor General of India and are chaired by the Deputy Comptroller and Auditor General (Commercial). Besides Senior Audit Managers of the SAI's commercial audit wing, two or more external specialists possessing expertise in the area of operation of the undertaking being appraised, are co-opted onto the Board as part time members. This system helps the SAI to have the benefit of independent technical expertise, while finalising highly technical and complex performance audits.

3.5 Auditing Standards

Performance Audits by SAI-India are conducted in accordance with the Auditing Standards issued by the Comptroller and Auditor General of India. These standards stipulate that the SAI's audit work should be planned to ensure high

quality work in a timely and economic, efficient and effective way and that audit should be properly guided, directed and supervised. Also, sufficient understanding of the internal control system needs to be obtained to express an opinion on the reliability, fidelity and integrity of the systems and procedures of the entity and to plan the audit and to determine the nature, timing and extent of audit tests to be performed. Due professional care must be exercised in specifying, gathering and evaluating evidence during audit and the audit conclusions should be supported by sufficient, competent and relevant evidence. Adherence to these Auditing Standards is ensured by the SAI through quality assurance procedures, which include inbuilt systems of detailed direction, guidance and supervision of audit, careful and critical examination of audit conclusions, manuals and job specific audit guidelines / plans, and internal control and inspection systems and procedures.

4. Other issues

4.1 Client relationship

In the SAI's relationship with the auditee organisations, the principles of appropriateness and judiciousness are adhered to, avoiding embarassment to the auditee. An open-minded, constructive and professional attitude is maintained through constant contact and discussions with the auditees. All audit findings and reports are forwarded to the auditee agency at the draft stage for their comments and their responses are invariably incorporated in the final Audit Report of the SAI. The establishment of a constructive relationship between the SAI and the auditee is helped by the SAI's policy of suggesting appropriate changes in systems and procedures to prevent future recurrence of irregularities or losses, rather than shouldering the duty of fixing responsibility on individual officials for lapses.

As regards the primary clients of the SAI, viz. the legislature, especially the legislative financial committees, the SAI maintains an active and mutually beneficial relationship. While it actively assists the legislative financial committees in the examination of the SAI's Audit Reports and finalisation of recommendations for action, it also takes note of legislative sensititivities, though in an informal fashion, as part of the macro level audit planning process.

4.2 Performance indicators

While the responsibility for development of performance indicators and standards normally rests with the planners and administrators who plan and implement the social development programmes, SAI-India often finds that these standards have not been formally set and even where such standards have been set, they are either intermediate in nature (and do not reflect the ultimate objective of the programme) or are framed in such a fashion, as to be incapable of precise measurement. Faced with such situations, the SAI does not fix its own performance indicators, but comments on the absence of such indicators. Where such indicators and standards are available, the SAI critically evaluates them to assess whether they are meaningful and reflect the true effects of development. Non-availability of adequate databases, both in terms of social statistics and for

meaningful comparison of the performance with similar activities elsewhere, and absence of a formal evaluating mechanism either within the executing agency or outside, are other major problems in this regard.

5. Conclusion

SAI-India has been a pioneer in the field of performance audit. Having introduced the system of Efficiency-Cum-Performance Audit (ECPA) in the early 1960's, the experience gained over the last four decades has enabled the SAI to hone its skills in this critical area of audit. This experience has been supplemented by inputs from other INTOSAI members in the form of documentation, training of senior audit managers etc. Conversely, we have also been conducting training programmes in different specialised areas of performance audit for audit managers from SAIs in the African, Asian and Pacific regions for nearly two decades. Interchange of information with members of ASOSAI and INTOSAI through exchange of performance audit guides, manuals, and reports, and participation in seminars, workshops and training programmes furthers the process of continuous enhancement and upgradation of performance audit skills.

5. Indonesia

Country Paper
on
Sub-theme 1

Performance Auditing: Concepts, Mandates,
Methodologies and Practices,
Reporting and Problems

Prepared by:
Supreme Audit Board,
Republic of Indonesia

SUB-THEME 1

COUNTRY PAPER

ON

PERFORMANCE AUDITING CONCEPTS, MANDATES METHODOLOGIES AND PRACTICES, REPORTING AND OTHER ISSUES/PROBLEMS

THE SUPREME AUDIT BOARD OF INDONESIA

PERFORMANCE AUDITING CONCEPTS, MANDATES METHODOLOGIES AND PRACTICES, REPORTING AND OTHER ISSUES/PROBLEMS

Introduction

1. Performance audit was introduced in Indonesia in 1979 through a management audit course held by the Supreme Audit Board of Indonesia (abbreviated BEPEKA) with the assistance of an expert from the International Executive Service Corps (IESC). Performance audit (management audit) became operational around 1979 through a Pilot Project.

2. Since 1982 BEPEKA has developed performance audit in the form of financial audit plus, that is a financial audit cum an assessment of certain aspects of economy, efficiency and effectiveness.

3. In order to develop the implementation of performance audit activities, BEPEKA has issued the Audit Policy of Fiscal Year 1996/1997. The audit policy is geared towards improving the audit quality, including measuring the outcomes of the programs.

Audit Mandate

4. BEPEKA's audit mandate is simply but clearly defined in

article 23, paragraph 5 of the Constitution of the Republic of Indonesia of 1945, which reads as follows:

* "In order to audit the accountability concerning the state finance there shall be a supreme audit board, the regulation of which shall be carried out by law. The audit results shall be made known to parliament."

The elucidation thereof states that :

* "The way in which the government utilizes the state budget which had been approved by parliament shall correspond with that approval. In order to audit the accountability of the government, a body is needed which is free from the influence and powers of the government. A body that is subordinated to the government cannot bear such a heavy responsibility. On the other hand, that body shall also not be one that is superior to the government. Therefore, the authority and obligation of that body shall be regulated by law."

5. The People's Assembly, in its resolution No. IV/MPR/1973, determined the position of BEPEKA and its work relationship with the other high state institutions. Following up this resolution, in July 1973, the legislature enacted Act No. 5/1973 concerning the Supreme Audit Board that thus provides BEPEKA with its principal legal basis for

its audit mandate. To illustrate the audit mandate assigned to BEPEKA in virtue of Act No. 5/1973, the contents of article 2 are presented below :

* BEPEKA shall have the task of auditing the accountability of the government concerning state finance,
* BEPEKA shall have the task of auditing the implementation of the state budget as a whole.
* The execution of the audits referred to in paragraphs (1) and (2) of this article shall be carried out in virtue of statutory provisions.
* The audit results of BEPEKA shall be made known to parliament.

The meaning of "the implementation of the state budget as a whole" is explained in the elucidation of article 2 which states that audits conducted on accountability concerning state finance are to include inter alia the implementations of the state budget (routine as well as development budget), the budgets of the regional governments and those of the public enterprises, in essence, the entire wealth of the state.

6. Since the act containing the statutory provisions for the governing of BEPEKA's audit executions was not available at the time Act No. 5/1973 was enacted, article 21 of the abovementioned Act stipulates that "as long as

the provisions for the regulation of audit specified in article 2, paragraphs (1) and (2) of the Act have not become available, audits by BEPEKA are to be executed on the grounds of statutory provisions currently in force."
The content of this article is explained in the elucidation thereof that reads :

"The phrase 'statutory provisions currently in force' means the present Act and inter alia the Treasury Act (State Gazette 1925 No. 448) as amended and supplemented and the Terms of Reference for the General Audit Bureau (State Gazette 1898 No. 164 and its amendments), exclusive of Article 43 through Article 53 of the Treasury Act and Article 2 of the Terms of Reference for the General Audit Bureau which had been revoked in virtue of Government Regulation in lieu of Act No. 6 of 1964 jo Act No. 17 of 1965."

Public Accountability

7. In discharging his responsibility to the People's Assembly, the President governs the state by paying due attention to the concept of public accountability. The purpose of this concept is to ensure that affairs of the state are conducted with due regard to the interests of the Indonesian people and nation. To support the discharge of public accountability, the internal audit mechanism within

the ministries, departments, public enterprises, and regional governments is strengthened, among others through the establishment of inspectorate-generals, inspectorates and regional inspectorates within the accountable organizations concerned. At the end of each fiscal year, the government prepares an Annual Financial Statement (further referred as AFS), which is compiled from all accounts of the ministries and government agencies.

Auditing Standards

8. In 1995, BEPEKA issued the Government Auditing Standards that guarantees principles such as independence, integrity professional proficiency and due care, confidentiality, professional behavior and technical issues. These standards are adapted from the GAO - Government Auditing Standards 1994.

Audit Policy

9. The audit of the accountability with respect to state finance aims at presenting a statement of the way in which the government implements the state budget so that it corresponds with the budget approved by parliament. This is done by conducting performance audits. The Audit Policy also indicates that BEPEKA should express

an opinion on the AFS by taking into account the following :

* The audit of the AFS by BEPEKA has the purpose of ascertaining and evaluating the fairness of the AFS as a document representing the accountability of the government with respect to the budget execution.
* The audit of the AFS consists of an overall examination of the budget implementation during the fiscal year, followed by the audit of the budget accounts of each ministry/public institution, and finally the audit of the accounting of the state budget and the AFS draft prepared by the Agency for State Accounting within the Ministry of Finance.
* As far as the audit of the budget implementation is concerned, it has always been BEPEKA's intention to enhance its audit quality by the application of performance audit that emphasizes the aspects of economy, efficiency and effectiveness, without discounting the significance of financial and compliance audits.

10. So far, the audit of the AFS conducted by BEPEKA is, in fact, a financial audit to assure the accuracy of the figures. By establishing the Audit Policy, BEPEKA attempts to evaluate the performance of the issues to be audited. These issues are related to foodstuff(especially rice production), health, education, and tourism on the ex-

penditure side, and to tax and oil revenues on the income side. The audit results & findings of those issues are intended to support the evaluation of the worthiness of the AFS.

11. The implementation of the so-called financial audit plus has resulted in disclosing matters such as :

* cost overruns due to improper planning;
* unutilized finished projects;
* excessive procurement and stock.

Audit Process

12. Generally, the audit process follows the stages mentioned in the Principal Paper.

Reporting

13. Since 1995 BEPEKA submits semestral audit reports. These reports usually contain :

* audit results of the Annual Financial Statement;
* audit results of the implementation of the budget at various ministries and agencies (central and local governments) and public enterprises.

14. According to the Budget Act, the government has to prepare a report on the budget implementation of the :

respective fiscal year. The report discloses the budget for revenue and expenditures as realized by all ministries/ institutions, and the difference between the budget and its realisation.

The Government submits the financial statement to parliament in the form and arrangement as stipulated in the Budget Act, to facilitate comparison between the budget and its realization.

BEPEKA also prepares audit reports on its audit activities of the previous year. Fulfilling the provisions of Article 2 of Act No. 5/1973 on BEPEKA, the audit report is presented to Parliament as well as to the Government.

As far as BEPEKA's audit role is concerned, it can therefore be said that Indonesia follows the neutral audit principle, where BEPEKA is outside both the legislature and the executive.

In general, there still exists a certain reluctance on the part of auditees concerning performance audit. BEPEKA's audits are mainly based on :

* compliance with existing laws and regulations;
* possibilities of reducing expenditures or increasing revenues.

Constraints

15. The problems encountered by BEPEKA in conducting performance audits are, among other things, the absence of performance standards for measuring the organization, function, activities, etc. of government agencies. Only a few of the government agencies have established their performance standards.

16. The insufficient number of professional auditors and experts has hampered BEPEKA in conducting performance audits.

6. Japan

Country Paper
on
Sub-theme 1

Performance Auditing: Concepts, Mandates,
Methodologies and Practices,
Reporting and Problems

Prepared by:
Board of Audit,
Japan

SUB-THEME I

COUNTRY PAPER

ON

PERFORMANCE AUDITING CONCEPTS, MANDATES, METHODOLOGIES AND PRACTICES, REPORTING AND OTHER ISSUES/PROBLEMS

BOARD OF AUDIT OF JAPAN

I. CONCEPT

1. Definition

The term "Board of Audit" used in this paper refers to the Board of Audit of Japan under the present Constitution and the Board of Audit Law enacted in 1947.

2. Performance Audit at the Board of Audit

The Board of Audit Law and the relevant statues do not refer to the terminology "Performance Audit", nor spefically mandate the Board to do it. The Board, however, has long been auditing government revenues and expenditures from various viewpoints, including the followings:

- whether statements of account fairly represent execution of budgets and financial position of the State
- whether accounting is in conformity with the budgets, law and regulations
- whether projects are executed economically and efficiently
- whether project goals are achieved and effects produced

Thus, the Board audits the auditees' programs/projects execution and management from viewpoints of economy, efficiency and effectiveness, as defined by the INTOSAI Auditing Standards. The Board's audit from such economy, efficiency and effectiveness perspective is considered identical to the INTOSAI-defined perforamnce audit concept.

3. Evolution of Board's Performance Audit

The evolution of performance audit at the Board has been gradual and progressive, which is quite unique compared with that of Australia, the Principal Paper writer and many other countries. To begin with, the Board has very long history and experience in audit from economy and efficiency viewpoints since the time of its preceding organization, the old Board

of Audit under the Meiji Constitution (1888-1946). The old Board of Audit had audited government projects and programs from economy and efficiency viewpoints.

Audit of project /program effectiveness is, however, relatively new to the Board; audit from such viewpoint started in 1970s and has gradually developed to date. As such, the Board's "performance audit" has so far largely focused on economy and efficiency. However, recognizing growing demands for audit of effectiveness on various government programs and projects from both the legislature and the public, the Board has recently come to place more emphasis on such audit.

The Board's performance audit history mentioned above generally divides into three periods as follows:

(1) 1947 to mid-1950

In this period, Japan was recovering from the devastation caused by the WWII defeat and the government accounting management and control was generally not in good order. Facing a huge number of fraud and irregularity cases, the Board was largely occupied with regularity, financial and compliance audit, although it also conducted economy and efficiency audit as did the old Board of Audit.

(2) mid-1950 to 1970s

As the government accounting generally improved, the cases of irregular accounting practices dramatically decreased. The Board thus began to put more emphasis on audit of economy and efficiency during this period.

(3) 1970s to present

While the economy and efficiency audit remained the core of the Board's audit activities, the Board gradually entered into effectiveness audit, starting from infrastructure projects to various social programs. The Board also continues to conduct regularity and compliance audit of most government activities.

For example, the 249 audit findings appearing in the Board's most recent FY1995 Annual Audit Report divided into:

- 211 regularity/compliance audit findings (88%)
- 32 economy/efficiency audit findings (9%)
- 6 effectiveness audit findings (3%)

While the share of the economy, efficiency and effectiveness audit seems small, their impact is far greater, since government money involved in the audited projects/programs represents much higher proportion than the above.

4. Performance Audit and Financial/Compliance Audit

The Board of Audit Law mandates the Board to examine final accounts of State revenue and expenditure and to report its result in the annual Audit Report together with other audit findings. However, the Board does not conduct CPA-type financial statements audit.

With some exceptions, the Board auditors normally do not examine compliance to budget, laws and regulations for the sole purpose of verifying it : when checking the compliance, the auditors normally also examine it from a viewpoint of whether non-compliance could cause loss to the government. In fact, most audit findings from compliance audit involve cases in which non-compliance has caused, or could cause in future, financial loss to the government.

5. Legislative Background

The Board of Audit of Japan was established by the article 90 of the Constitution of Japan which stipulates:

> Final accounts of the expenditures and revenues of the State shall be audited annually by a Board of Audit and submitted by the Cabinet to the Diet, together with the statement of audit, during the fiscal year immediately following the period covered. The

organization and competency of the Board of Audit shall be determined by law.

Based on this, the Board of Audit Law in article 20 stipulates:

> The Board of Audit shall audit final accounts of State revenue and expenditure in accordance with article 90 of the Japanese Constitution and of other accounts provided by laws. The Board of Audit shall constantly audit and supervise Government accounting to secure its adequacy and to rectify its defects.

The Law also stipulates accounts/bodies subject to Board mandatory and discretionary audit. Major items for Board audit, other than those of the State Government, are:

(mandatory)

- Accounts of corporate bodies in which the State invests half or more of the capital

(discretionary)

- Accounts of bodies directly or indirectly receiving financial assistance from the State such as subsidies, incentive grants, bounties, and compensation;
- Accounts of bodies in which the State invests less than half of the capital;
- Accounts of bodies invested in by State-invested bodies.

As mentioned above, the Law does not specifically entitle or mandate the Board to do performance or 3-E audit. However, through past audit accomplishments and Diet deliberations, it has been generally understood by the Diet, auditees and general public that the Board audit covers both financial/compliance audit and performance audit. The Board, however, is not entitled to audit policies formulated by the Diet. When the Board finds financially aggravating situation in government projects and programs, which is closely related to policy issues and beyond the auditee's control, the Board reports the fact in the annual Audit Report to draw attention of the legislature and the general public to further observe its development.

II. METHODOLOGIES AND PRACTICE

1. Audit Topic Selection

The Board's management establishes basic audit policy/guidelines every year. The basic audit policy/guideline describes major subject areas that should receive the highest priorities in a particular year's audit activities. Some of these subject areas are picked up in mid or long term audit perspectives, and they reflect social/economic issues the Japanese Government currently faces, for example, at present, such as:

- Growing social security/welfare service costs caused by rapidly aging population i.e. public pensioners, medical care recipients;
- Construction and maintenance of highways, bridges, railways and other infrastructures sufficiently resistant to massive earthquake such as recent Great Hanshin Awaji Earthquake;
- Influence of international economic agreement;
- Growing information technology investment.

Based on the established basic audit policy/guidelines, the Board's each Audit Division establishes yearly audit plan showing:

(a) Major audit subjects;
(b) Background and reasons for major audit subject selection;
(c) Audit viewpoints and methods;
(d) Manpower allocation for each audit subject;
(e) Man-days to be allocated for each audit subject;
(f) Auditee agencies' budget scales and other financial/administrative data.

These yearly audit plans also include mid-long term audit perspectives especially for auditing Government mid-long term projects.

2. Audit Processes

In performance audit type assignments, the Board normally picks out problematic programs, and reports, together with such problems themselves, any program execution deficiencies and bottlenecks which cause such problems. The first step of the Board performance evaluation is therefore to pick out, by relevant documents and any other inside/outside information, particular project auditors need to analyze and evaluate. And auditors in the second step execute performance analysis/evaluation of the picked out particular program in the following processes:

(1) Preliminary analysis

Auditors analyze basic policy documents such as:

- Cabinet agreement (s), legislation(s) etc. outlining the policy behind the program;
- Program document showing background and purpose of the program;
- Planning document showing achievement target, target year etc;
- Financial document showing budget and future financial positions of the program;
- Internal ordinances and directives issued during the past project implementation processes;
- Documents and materials acquired in the past audit and the results of their analysis;
- Others

By carefully going through these documents, auditors study political and socioeconomic background of the program, identify each problematic area, and also assess general gravity, scale and character of the problem(s). Through these study and analysis, auditors among other things make advance judgment on whether:

- the problems and expected recommendations are worth reporting in the Board annual Audit Report in light of scale, gravity, and administrative/socioeconomic impact;
- the causes of problems are within the control of the program executor;

- the audit manpower presently available in the Board can achieve the audit goals within the prescribed audit period;
- sufficient administrative/financial data are available inside/outside of the Board;
- sufficient evaluation expertise are available in the Board, and if not, whether they can be obtained from outside experts;
- there are any envisaged audit obstacles and difficulties.

(2) Establishment of Audit Viewpoints

After identifying major problems of the program, auditors make detailed study on the problems, and work out detailed audit viewpoints. The auditors thereafter identify documents to be checked for each of these viewpoints. These documents consist of:

- Documents available in the Board, i.e. statements of accounts attached with vouchers/evidences regularly submitted to the Board by auditee agencies;
- Documents to be checked through on-the-spot field audit in auditee agencies

Note: Auditee agencies should regularly submit statements of accounts together with vouchers and evidences to the Board of Audit based on the Board-enacted Account Verification Regulation.

(3) Establishment of Audit Schedule

Auditors then establish detailed audit schedule. The Board audit cycle starts with audit planning and ends with submission of its annual Audit Report to the Cabinet. The Cabinet then presents the Report to the Diet together with its final statement of accounts. Since the Board submits its Audit Report once every year, the Board auditors in general establish one-year audit schedule stating, among other things, auditee agencies to be visited, on-the-spot field audit man-days, etc. Such one year audit schedule however also takes into account multi-year long term audit goals. Auditors therefore often pursue one year audit goals while pursuing goals for long term audit, results of which will appear

in subsequent year annual Audit Reports. Auditors incorporate these audit schedules in the annual Audit Plan, and get management's approval.

(4) Execution of Audit

After getting management's approval for the annual Audit Plan, auditors start field audit normally from mid-January every year. In executing field audit for approximately two and half months until the start of the new Fiscal Year (April 1), auditors examine the feasibility of the initial Audit Plan, results expected at the end of the audit etc., and revise the initial Audit Plan if necessary based on the results of the field audit conducted in these two and half months. Auditors then get the final Audit Plan approval from the management, and implement the revised Audit Plan. Auditors further get management's approval for modifying the Plan in case auditors face unexpected changes of audit environment/conditions during the subsequent audit implementation period. In the middle of the audit implementation period, auditors report to the management intermediate audit results and discuss need for any re-orientation of audit strategy, theme by theme. Auditors execute audit based on modified audit plan/strategy.

(5) Discussion with Auditee Agencies

At the end of the audit of particular subject, auditors present audit results to auditee agency and discuss the content of the results to reflect on the finding auditee agency's standpoints and comments. Based on the results of the discussion, auditors prepare an official inquiry to the auditee agency. Auditors then receive an answer to the inquiry from auditee agency. In these processes, auditors frequently have discussions with the auditee agency staff until both sides agree to the conclusion reached by the audit.

(6) Preparation of Audit Report

Based on the conclusion agreed upon with the auditee, auditors draft audit finding to be

reported in the annual Audit Report. To review the findings, the Board sets up two layers of screening committees, the first one chaired by each of the five Bureau Director General and the second headed by the Deputy Secretary General of the Board. These committees have intensive discussions on individual audit findings submitted each Audit Division. To prepare fair and impartial Audit Report, individual drafts are examined by both auditors and non-auditors neither of whom is directly involved in the audit in question. After screening and revising by the committees, the finding is finally presented to the Audit Commission, the highest decision-making committee of the Board, for approval and inclusion in the annual Audit Report.

After completion of the Report, the Board sends the Report to the Cabinet. The Cabinet then submits its statement of accounts together with the Report to the Diet. The annual Audit Report is a document indispensable for Diet deliberation on the Government statement of accounts. The Board prepares its annual Audit Report only once a year. The Report however carries Board's many multi-year audit activity results. The Report is open to the public and mass media.

(7) Follow-up Audit

After publishing an annual Audit Report, the Board conducts follow-up review on every recommendation appeared in the Report, and reports the results of this follow-up in the subsequent annual Audit Reports until the recommended actions are taken by the auditee agency.

7. Audit Criteria

Criteria are developed from available documents such as:

- Basic policy documents such as Cabinet agreement (s), legislation(s) etc. which outline(s) the Government policy behind the program to be audited;
- Program document showing background and the purpose of the program;

- Planning document showing achievement target, target year etc.
- Internal ordinances and directives.

Normally, auditors in the first place identify performance measurement indicators shown in these basic policy documents such as:

- Overall program purpose and goals;
- Program outline/details;
- Target date/year for achieving the program goals;
- By-fiscal-year achievement goals;
- Total program budget and budget breakdown;
- Others.

8. Evidence

Like compliance audit findings, performance audit findings must have sufficient supporting evidence. In Japan, auditee agencies regularly submit statements of accounts together with vouchers and supporting evidences to the Board of Audit based on the Board-enacted Account Verification Regulation. These supporting evidences include not only financial but also non-financial documents, such as contract documents and design drawings. Board auditors can first collect basic evidences from such documents stocked in their office. They also extensively request for and collect evidences through field audit.

III OTHER ISSUES AND PROBLEMS

1. Entity Relationship

Since the successful completion of audit missions largely depends on auditee cooperation and understanding, the Board always tries to keep close communications with the audited entity throughout an audit including pre- and post- audit contact to ensure that the audit objectives

are well understood. The Board also emphasizes maintaining an objective, neutral and fair position in reporting its audit findings to the Diet; multiple layers of screening and peer review committees are set up within the Board which examine each case from the viewpoint of both the Board and the auditees.

2. Skills for Performance Auditors

As already mentioned, the Board started at least certain elements of performance audit in considerably early stage, and has recruited audit staff from various backgrounds. Although people with law and economics backgrounds make up more than 50 % of the current 1,248 workforce, the Board has 177 persons with engineering education backgrounds ranging from architecture to electronics.

To fully utilize and develop such human resources, the Board provides continuous training and education opportunities to them. While most of the training courses are conducted in house at the Board 's training center, some are offered by various government training institutions. For more advanced studies, some staff are sent to domestic/foreign universities and research institutions.

The Board also has outside experts in various fields who are seconded from other ministries. Although these experts join the Board on a loan basis, they serve only to the interest of the Board during their term and constantly provide technical advice.