

Autumn 2019



**ECOSAI**  
CIRCULAR 2019





ECOSAI is regional forum of Supreme Audit Institutions encompassing countries from Europe, Caucasus and Central Asia, Middle East and South Asia

Founded in 1994, the ECOSAI aims to promote the public sector auditing profession in member countries through exchange of ideas, experiences and by holding seminars, conferences, workshops and training courses.

#### **Natalya Godunova**

President ECOSAI & Chairwoman,  
Accounts Committee for Control over  
Central Government Budget Execution,  
Republic of Kazakhstan (SAI Kazakhstan)

#### **Javaid Jehangir**

Secretary General ECOSAI &  
Auditor General of Pakistan (SAI Pakistan)

### **ECOSAI Governing Board Members**

- SAI of the Islamic Republic of Afghanistan
- SAI of the Republic of Azerbaijan
- SAI of the Republic of Turkey

The terms of these three members will expire in 9th ECOSAI Assembly scheduled in 2022.

The publisher wishes to thank all the individuals and organizations who have contributed towards this publication.



The ECOSAI Journal is the official organ of ECOSAI and has the objective of providing member SAs with the forum of sharing experiences in different areas of public sector auditing.

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### **Editorial Team**

#### **Muhammad Afnan Alam**

Director International Relations & Coordination (IR&C) Wing /  
Authorized Representative of Secretary General ECOSAI,  
Department of the Auditor General of Pakistan

#### **Syed Imran Baqir**

Dy. Director International Relations & Coordination (IR&C) Wing,  
Department of the Auditor General of Pakistan

#### **Mrs. Shandana Nauman Khan**

Dy. Director International Relations & Coordination (IR&C) Wing,  
Department of the Auditor General of Pakistan

### **ECOSAI Secretariat**

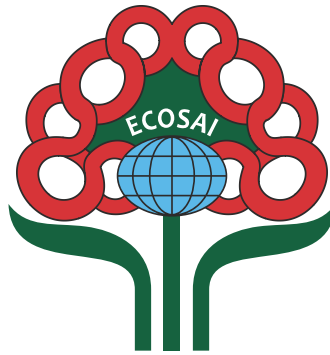
Office of the Auditor General of Pakistan, Constitution Avenue,  
Islamabad, Pakistan

Phone : +92519219177

Facsimile +92519224052

E-mail : [saipak@comsats.net.pk](mailto:saipak@comsats.net.pk)





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## MESSAGE OF SECRETARY GENERAL ECOSAI

ECOSAI Circular focuses on fostering knowledge sharing in the area of public auditing with the intent to promoting professional and technical cooperation among member SAs. It gives me immense pleasure to present Autumn issue of ECOSAI Circular 2019.

I am glad to share with our readers the outcome of valuable efforts of President, ECOSAI, for strengthening professional cooperation within and without the region. In a bid to broaden the horizon of ECOSAI, SAs of Qatar, Kuwait, Palestine and Belarus have joined the Organization as 'Observer' during the 8th ECOSAI Assembly held on October 22, 2019 at Istanbul, Turkey. Joining of ECOSAI as observer of these SAs is aimed at enabling the member SAs to learn from experiences of SAs working in diverse geographical region under different governance frameworks and mandates but faced with a range of challenges common to ECOSAI region. I congratulate the President, ECOSAI for his dynamic leadership role. I am optimistic that the 'Observer' SAs will afford this opportunity to ensure exchange wide-ranging and rewarding experience.

The ECOSAI Circular precisely targets the professional enrichment of member SAs. I hope you will enjoy reading the current issue as much as I did. I take this opportunity to thank all the contributors for making the present issue rich in contents and encourage ECOSAI members to become more proactive in contributing to the Organization's initiatives for the benefit of all.

**Javaid Jehangir**  
Auditor General of Pakistan  
Secretary General ECOSAI

The background features a light blue gradient with abstract geometric shapes. In the top right, there are overlapping triangles in shades of orange, red, and grey. In the bottom left, there are overlapping triangles in shades of purple and blue. Thin, dark lines intersect diagonally across the page.

# News from Member SAls





## Supreme Audit Office (SAO), Afghanistan Islamic Republic of Afghanistan

### AFGHANISTAN

#### Appointment of the new Auditor General of the Islamic Republic of Afghanistan



On his appointment by H.E. the President of the Islamic Republic of Afghanistan, Mr. Mohammad Naiem Haqmal assumed the Office of the Auditor-General, Afghanistan on 02 March 2019.

Mr. Mohammad Naiem Haqmal, son of Mr. Mohammad Kateb, was born in 1980 in a devout and intellectual family in Saripul Province of Afghanistan.

Mr. Haqmal is a fellow member of the Association of Chartered Certified Accountants (ACCA). He is also a member of the Chartered Institute of Public Finance and Accountancy (CIPFA) since 2015. With his Bachelor's degree in Applied Accounting from Oxford Brooks University, England, he obtained his Master's in Business Administration (MBA) in 2013 from World Wide Science Business School, specializing in strategic management. Mr. Haqmal is fluent in English and speaks official languages, Dari and Pashtu.

Mr. Haqmal has received several managerial and professional trainings covering subjects of Statements of Financial Position Analysis, Accounting Principles and Framework, Financial Audit, Environment Management System, Cost and Price Analysis, Financial Disclosure, Standards for Financial Statements, Business Writing and Cyber Security Awareness, from USAID and UNDP inside and outside of the country.

Mr. Haqmal has over 12 years of professional

experience in management, accounting, financial management and auditing since 2006 across the private sector, International and multi-lateral agencies, projects, Banking, and Government. In the private sector, he worked as Finance Manager with Afghanistan Holding Group (AHG), a financial services firm in 2012 where he dealt with capacity building of the finance and accounting staff and tax-related matters. He has also been teaching ACCA subjects at the American University of Afghanistan (AUAF) since 2014.

His experience with international and multilateral agencies includes dealing with accounting matters in CARE International, as a Finance Officer with the UNDP in the area of Sub-National Governance for two years and as Financial Analyst for three years with the USAID.

His experiences in Government include as Finance Officer in World Bank project in the Ministry of Agriculture, Irrigation, and Livestock and subsequently with his excellent performances in the project, as Finance Manager of the project and as Audit Specialist in Internal Audit in the Ministry of Finance.

Before assuming the Office of the Auditor-General, Afghanistan, Mr. Haqmal served as the Chairman of the Kabul Bank Receivership Commission and as the Deputy Minister (Acquisition, Technology, and Logistics) in the Ministry of Defense of Afghanistan.

## Supreme Audit Office (SAO), Afghanistan Islamic Republic of Afghanistan

### Appointment of the new Deputy Auditor General of the Islamic Republic of Afghanistan



**Mr. Fazel Hadi** Fazel possess over 10 years of professional experience in the field of audit. Started his career with KPMG Afghanistan, he has served different entities both in public and private sector. Prior to his appointment as Deputy Auditor General, he was serving the American University of Afghanistan as head of Internal Audit.

In addition, Mr. Fazel has served as Senior Audit Advisor with USAID – AMANAT project, Senior Audit Specialist with PFMR-2 of World Bank and as Deputy Chief Internal Auditor at the Azizi Bank. He has also served as independent member of the Audit Committee in different commercial banks.

As the founder, the President and Chairman of the Board for Institute of Internal Auditors Afghanistan, Mr. Fazel has always strived to promote the profession in the country.

He has obtained his Bachelor degree in Economics from Kabul University and Master's in Business Administration from AUAF. Furthermore, Mr. Fazel is a certified Fraud Examiner from the Association of Certified Fraud Examiners and has received several professional and managerial trainings in identifying and detecting fraud, Auditing, Management, Accounting, and investment from various institutions.

In addition to his professional activities, Mr. Fazel is an active audit lecturer and has provided training programs on different platforms.

#### Changes and recent developments

The Supreme Audit Office is endeavouring to keep pace with the requirement of the updated ISSAIs framework; meet the conditions set by the development partner's benchmarks and achieve and effective basis of an independent SAI to deliver quality audit products. The following changes are noteworthy

Monitoring mechanism for status of implementation of audit recommendations by the auditee - a mechanism for the following up on the audit findings

has been developed to monitor, collect and analyse the status of implementation of the audit recommendations by the audit entities. This is also a benchmark under development partners' agreements. The information base of follow up provide basis for verified status of implementation of the audit recommendations. It highlights the value added by audit.

Professional Capacity Development – on the basis of the overall framework of the INTOSAI Capacity Development Committee (CDC), the SAO has put in place a long term professionalisation and capacity development plan and strategy. The strategy seeks to capacity development through a multi-pronged approach which includes inhouse training and training with the support of other SAIs, professional certification, recruitment of already professionally qualified personal. The SAO in 2019 has set up Training and Capacity Development Centre. The Centre is responsible for conducting an annual programme for about 100 fresh entrants / auditors with syllabus based on standard materials and courses comprising papers of accounting, audit and assurance, public financial management, Afghanistan Business and Administrative Laws, IS / CAATS, etc.

#### Additionally, SAO has also undertaken the following for capacity development and training.

- o English proficiency classes for 122 staff based on need analysis through an MoU with an English teaching Institute.
- o Foundation in Accountancy class for 139 staff who are proficient in English.
- o IPSASs class for 13 staffs to enable them to pursue IPSAS based certification / diploma.
- o Thee SAO has recruited 20 ACCA students as Internees for six months.

Functional Review of the SAO - As per a Government-wide initiative, the SAO has undertaken functional review to assess its organisational structure, operation and processes, adequacy of the staff and skill-sets, their efficiency and effectiveness and to identify redundancies, duplicacies, non-aligned processes and structures, and adequacy to meet the SAO's mandate as an institution of public trust and contribute to accountable, transparent and effective public financial management in the country. It also seeks to assess how best to meet the requirement of the ISSAI framework. An international functional review expert is at advance stage of completing the work.

According to the ISSAIs framework, the SAO shall carry out its functions and responsibilities as a Supreme Audit Institution, and as a member of INTOSAI, ASOSAI, ECOSAI, and INCOSAI.

Research, Development and Training Committee (RDTC)- The SAO set up a research, development and training committee with the prime objective of conducting research and studying the best / good practices and applicable standards and emerging changes and innovations in the field of auditing, financial reporting, IT audit, internal control system and internal audit, CAATTs, etc., and to provide inputs for development, updating and innovating the SAO's audit approach, methodology, audit process and management and quality control and for training and capacity building of the SAO staff through training.

The RDTC, based on the ISSAIs and ISSAI implementation Handbooks has developed manual and audit toolkits for financial audit and compliance audit to provide standardised and ready-to-use toolkits and templates including for availability of audit working papers and absorb principles, practices, standards and guidelines of the ISSAIs.

**Financial Audit within SOEs & SOCs Audit Directorate -Due to inadequate capacity and skills,** earlier, the SAO was not able to undertake audit of the financial statements of the State owned Enterprises / Corporations (SoEs/SoCs) for which the SAO is mandated. In 2019, SAO has undertaken and completed audit of three (03) SoEs/SoCs. One of these, was piloted by including SAO staffs who underwent training conducted by the Swedish National Audit Office. The SAO has planned at least 10 SoEs/SoCs audit in 2020.

Establishment of IT Audit Directorate – Though SAO Afghanistan started conducting IT audits in 2017, it

was conducted by staff within the IT Department which mainly dealt with IT infrastructure and equipment. In 2019, however, a full-fledged IT Audit Directorate has been set up. This was a significant achievement, and a first step to separate IT audit professional work from IT support and administration. This is also based on the recognition of the importance of IT audit in achieving SAO's strategic objectives in providing assurance on IT governance, integrity, security, effectiveness and efficiency of IT systems/programs in light of emerging technology risks faced by Government of Afghanistan (GoA).

To this end, SAO Afghanistan is committed to building sustainable capacity to conduct quality IT Audits in Government Sector, and achieving the following goals and objectives:

- To Have Adequate IT Audit Capacity, Organizational and Professional Development
- To Expand Coverage of IT Audit
- To Provide Timely, Effective and High-Quality IT Audit Services

Quality Assurance Guidelines- The SAO has prepared Quality Assurance guidelines to achieve quality in all areas of SAO's activities and to have a robust quality assurance (QA) system. The main purpose of the guidelines is to emphasize the importance of QA in the effective delivery of SAO's mandate and a step by step guide for the quality assurance reviewers (QARs).

Audit Report Proof Reading Committee - The SAO is seeking to assure quality audit products through several means. One being dedicated team to go through the draft audit reports, which have already travelled through the audit teams and the middle level supervision but pending final approval. A Proof Reading Committee (PRC) established in June 2019 under the supervision of Professional Deputy Auditor General is responsible for review and value addition through assurance about quality of audit reports.

Design and Preparation of Stakeholders Engagement Strategy and Action Plan - The SAO recognizes the importance of demonstrating relevance to citizens and other stakeholders in order to strengthen the SAO capacities and effectiveness in holding the government to account for the use of public resources. We acknowledge that by communicating simply and clearly with our stakeholders, they will have clear expectations, a greater understanding of our work and responsibility. We believe this approach involves not

just agreeing with our stakeholders, but also understanding and recognizing their beliefs, ideas, values, and perceptions. Developing stakeholder relationships that demonstrate this shared understanding, provides a foundation upon which interactive communication can exist with stakeholders whose interests are vested in our work.

**The Objectives of the Stakeholder Engagement Plan are:**

- Identifying and categorizing stakeholders based on their degree of influence on the decision-making process and degree by which they are directly impacted by the result
- Listen to the need and concern of all stakeholders
- Providing the necessary information that stakeholders need to understand the options and that decision-makers need to make informed decisions.
- Consulting with decision-makers to determine options for addressing stakeholders need and considering and easing their concerns
- Engaging or preparing with stakeholders in the decision-making process
- Attract public confidence on SAI for better transparency and accountability
- Enhance CSO's and citizen's participation in promoting legitimacy, transparency, accountability, and independence of SAO.
- Strengthen Strategic communications with Stakeholders and obtaining their strategies and policies.
- Strengthen the quality and efficiency of audit through cooperation with development partners and other entities.
- Improve Government's Accounting services and General Administration by Transparency and enhance support to operations of SAO.



## Appointment of New Vice-President for Legal, Parliamentary, Annual Reports and Provinces Affairs of SAC

### IRAN

By virtue of a letter of appointment issued by Prof. Dr. Adel Azar, President of SAC, Mr. Mohsen Emrani, was appointed as new Vice-President for Legal, Parliamentary, Annual Reports and Provinces Affairs of SAC, replacing Dr. Sadegh Mennati Nejad, who was in charge of this Vice-Presidency for the past three years. During the inauguration ceremony, Prof. Dr. Adel Azar appreciated Dr. Mennati Nejad's efforts during his vice-presidency and added that Dr. Mennati Nejad could establish a relaxed atmosphere among SAC, the Parliament and executive organizations across the country.

Next, the President of SAC introduced Mr. Mohsen Emrani as the new Vice-President for Legal, Parliamentary, Annual Reports and Provinces Affairs of SAC, who is characterized with brilliant records in the Office of Public Prosecutor as well as much experience

### SAC Successfully Hosted the 2nd International Training Course on Performance Auditing



SAC hosted a six-day International Training Course



in SAC.



on Performance Auditing delivered by Mr. Sheraz Manzoor Haider, Director General of International Relations & Coordination Wing of SAI Pakistan, from 20 to 25 July 2019 in Tehran.

The course, attended by auditors and senior auditors of SAC, included some significant theoretical and practical themes in the field of performance audit; among them, some practical case studies on Pakistan, Canada, Australia and Islamic Republic of Iran.



At the closing ceremony, Mr. Sheraz Manzoor Haider delivered a summary report on the course as well as positive resultant outcomes and feedbacks and praised the constructive views of SAC's high-ranking officials, in the direction of enhancing auditors' empowerment and knowledge-sharing, especially in the field of performance auditing.

### **The President of Supreme Audit Court (SAC) of I.R. Iran attended INCOSAI XXIII Moscow, Russia (23-28 September 2019)**

Professor Dr. Adel Azar, President of SAC, accompanied by Dr. Sasan Mobini Dehkordi, Director General of Fars Province and Mr. Ehsan Haji bagheri, Head of International Affairs Department, joined heads of about 200 Supreme Audit Institutions at the

23rd International General Assembly (GA) of Supreme Audit Institutions (INCOSAI), hosted by SAI Russia in Moscow from 23 to 28 September 2019.

Dr. Adel Azar took part in the opening ceremony at the international conferences hall (Moscow Manege). The session was attended by Vladimir Putin, the President of Russia, Chairman of SAI Russia and the new Chairman of INTOSAI, high-ranking officials from Russian Senate, State Duma, and the mayor of Moscow. Among other international officials in the GA, were Secretary General of INTOSAI, President of SAI UAE and the former Chairman of INTOSAI, and the representatives of the United Nations and the World Bank.

On the final day of the GA, Dr. Azar voted positive for the Moscow Declaration. It is worth noting that, during the GA, Dr. Adel Azar held separate bilateral meetings with the heads of over ten SAIs, namely Russia, Turkey, Spain, China, Indonesia, Iraq, Oman, Kuwait, Kazakhstan and Armenia, in which, some important bilateral and multilateral subjects were discussed. Besides, on 26 September, the Iranian delegation also attended the Forum of Jurisdictional SAIs, alongside 30 countries.





## PAKISTAN

Mr. Javaid Jahangir, Auditor General of Pakistan and Mr. Zulfiqar Khan, Director participated in the XXIII Congress and 72nd and 73rd Governing Board Meetings of the INTOSAI from September-23-28, 2019 at Moscow, Russian Federation. Besides participation of Auditor General of Pakistan in the XXIII Congress, the Auditor General of Pakistan also attended several bilateral meetings with member heads of Supreme Audit of Institutions for further



strengthening the bilateral relations between the SAIs.

Mr. Javaid Jahangir, Auditor General of Pakistan participated in International Consortium on Governmental Financial Management (ICGFM) conference as an organizational member from December 2-4, 2019 at Washington DC, USA.

Mr. Javaid Jahangir, Auditor General of Pakistan alongwith four member delegation participated in 8th ECOSAI Assembly, 8th ECOSAI Symposium, 24th ECOSAI Governing Board meeting from October 21-23, 2019 at Istanbul, Turkey. The SAI Pakistan is a permanent secretariat of ECOSAI and part in important decision making during the event.



## 8<sup>th</sup> ECOSAI General Assembly held in Istanbul, Turkey

### TURKEY



8th ECOSAI General Assembly Meeting was held in Istanbul on 22 October 2019, and the SAIs of Afghanistan, Azerbaijan, Iran, Kazakhstan, Kirgizstan, Pakistan, Tajikistan, Turkish Republic of Northern Cyprus (TRNC) and Turkey attended as members while the SAIs of Belarus, Palestine, Qatar and Kuwait attended as observers.

In the General Assembly Meeting, ECOSAI 2019-2022 training plan and the ECOSAI membership of the SAIs of Belarus, Palestine, Qatar and Kuwait as observers were approved. In addition, the ECOSAI Charter was updated and approved in the meeting.

In the ECOSAI Assembly Meeting, the SAI of Kazakhstan was elected as the President of ECOSAI for the period of 2019-2022. The SAIs of Turkey, Kazakhstan, Afghanistan, Azerbaijan and Pakistan were elected as Governing Board members; and the SAIs of Iran and Kyrgyzstan were elected as members of the Audit Committee.

Our delegation, headed by the President of the TCA, Seyit Ahmet BAŞ, attended the said event and carried out many bilateral meetings.

### 24<sup>th</sup> ECOSAI Governing Board Meeting was held in Istanbul

The 24th Governing Board meeting started with the opening speech of Mr. Seyit Ahmet Baş, President of the Turkish Court of Accounts and ECOSAI on 21st October 2019 in Istanbul, TURKEY. Following the adoption of the agenda, Auditor General of Pakistan, as the ECOSAI Secretariat, presented the ECOSAI Activity Report.

After the presentation of the 2018 Financial Statements of ECOSAI by the Secretariat, the 19th ECOSAI Training Committee report was presented.

During the meeting, report on the publication of the ECOSAI Circular by the SAI Pakistan; report on presentation of ECOSAI as "Observer" in ASOSAI; and report on ECOSAI Trainings held in 2019 were presented, as well. Also, a discussion was held on the introduction of SAIs as "Observer" members in ECOSAI.



Finally, after the report on MoUs signed between ECOSAI member SAIs was presented and other relevant matters were discussed, the meeting ended with the closing address of Mr. Seyit Ahmet Bas.

### 19th ECOSAI Training Committee Meeting was held in Istanbul

19th ECOSAI Training Committee meeting started on 21 October 2019 with the participants from the SAIs of Afghanistan, Azerbaijan, Kazakhstan, Pakistan and





Turkey.

During the meeting, the Committee decided on the 2019 - 2022 training agenda of ECOSAI. In this scope, decision was made in principle on the "Audit of Public Debts" training program to be held in Kazakhstan in 2021.

In addition, use of ECOSAI web-site to facilitate implementation of the Guide to Learning Management System was discussed.

Moreover, the possibility of signing of MoU between ECOSAI members on bilateral co-operation including training programs and exchange of visits of small groups of experts among SAls was discussed.

Finally, the ECOSAI Training Plan for 2019 - 2022 to be approved by the Governing Board was finalized.

### Our Website is now Available in French

As part of our efforts for increasing the recognition of the Turkish Court of Accounts (TCA) among the



international supreme audit institutions and informing a wider community about our activities, the TCA website is now available in French.

Along with the audit activities conducted, information and documents on the trainings organized within the scope of bilateral and multilateral agreements and current news about the TCA will be published on this website.

### "Risk Management" and "IT Audit" Workshops Organized with the State Audit Bureau of Qatar

The study visit of the delegation from the State Audit Bureau (SAB) of Qatar, who paid a visit to our country within the framework of the bilateral cooperation between the Turkish Court of Accounts (TCA) and the



SAB, on the topics of "Risk Management" and "IT Audit" was held on 15-18 October 2019.

In the first part of the 4-day programme, risk management standards, fundamental principles and components of institutional risk management and practice examples related to these were discussed. In the second part of the programme, the two SAls shared their experiences and knowledge on "IT Audit".

### "Financial Audit" Training for the Auditors of the SAI of Afghanistan

The training on "Financial Audit" organized for the professional staff of the Supreme Audit Office of the Islamic Republic of Afghanistan within the framework of the Memorandum of Understanding signed between the Turkish Court of Accounts (TCA) and the Supreme Audit Office of the Islamic Republic of Afghanistan started on 30 September 2019.

The objective of this training was to increase the professional development and capacities of the auditors of the Supreme Audit Office of the Islamic Republic of Afghanistan. Within the scope of the training, the TCA auditors provided information on the financial audit methodology and planning stage of financial audit, in particular.

At the end of the training program, TCA President Seyit Ahmet BAŞ granted the certificates of participation to 10 auditors participating in the training.

### Turkish Court of Accounts Delegation attended the 23rd INCOSAI

The 23rd INCOSAI, Congress of the International Organisation of Supreme Audit Institutions (INTOSAI) was held in Moscow, Russian Federation, on 23 September 2019.



During the congress, panels were organized in the light of the themes of "Information Technology for the Development of Public Administration" and "The Role of the Supreme Audit Institutions in the Achievement of National Priorities and Goals"; the meetings of main committees were held; and in addition, the meeting of "Forum of Jurisdictional SAIs" was conducted.

23. INCOSAI ended with the 73.Governing Board meeting, which was chaired by the SAI of Russian



Federation, which will carry out the presidency of INTOSAI in the next three years. The congress also approved the Moscow Declaration, which included the aims of responding effectively to opportunities brought by technological advancement, providing independent external oversight on the achievement of nationally agreed targets including those linked to the SDGs, and enhancing the impact and value of SAIs.

The Turkish Court of Accounts (TCA) delegation, which attended the said Congress as headed by the President of the TCA, Mr. Seyit Ahmet BAŞ, carried out several bilateral meetings and signed memoranda of understanding.

### Memoranda of Understanding were signed with the SAIs of China and Korea

Memoranda of Understanding were signed between our institution and the SAIs of China and Korea on 27 September 2019 in Moscow. The said agreements were signed during the 23rd INCOSAI, and they aim to



share knowledge and experience regarding the two countries particularly on public external audit methodology and methods.

### Workshop on Audit of Municipal on 24-25

September 2019, a workshop was held in Ankara to exchange mutual knowledge and experience within the framework of EU TAIEX Projects on the Audit of Municipal Revenues.

The workshop was attended by Mr. Luis Carlos Sánchez, the Acting Chairman of Autonomous Regions and Cities Control Department assigned in the SAI of Spain, Mr. Jorge Ferrán Dilla, the Director of Legal



Consultancy Unit from the same department, and professional staff members from the TCA.

The workshop, which covered the audit of municipal



revenues such as taxes, duties, charges and fees, ended with a closing ceremony with the participation of Mr. Zekeriya Tüysüz, Vice President of the TCA. Revenues



### **“Information Technologies Audit” Training for the SAI of Kuwait**

In the framework of the bilateral agreement between our institution and the SAI of Kuwait, the training program on “Information Technologies (IT) Audit” for the staff members of the SAI of Kuwait started on 15 September 2019 in the capital city of Kuwait, and it was hosted by the SAI of Kuwait.

The training program has 50 participants from the SAI of Kuwait, and it takes place in two periods between the dates of 15-26 September 2019. During the training program, the participants received training on basic IT concepts, IT risks, IT controls, relevant standards and basic control areas (IT governance, information security, external procurement, operation, maintenance, business continuity and disaster recovery planning, system development, project management and application controls) and learnt about the good practice examples.



**Performance Audit Training for the Delegation from the SAI of Moldova A delegation, which was** headed by Member Ms. Marina COVALI from the Court of Accounts of the Republic of Moldova, attended the training program about “Performance Audit” on 09-13 September 2019.

The program included 13 participants from the SAI of Moldova and it provided training on the planning, execution, reporting and monitoring stages of the performance audit and gave examples of best practices. In addition to international standards, basic approaches and audit experiences of TCA in the field of performance audit were also discussed by TCA’s auditors during the training program.

The President of TCA, Mr. Seyit Ahmet BAŞ, presented the certificates to the participants at the end of the training.

### **The Turkish Court of Accounts Carried out the External Audit of the Economic Cooperation Organization (ECO) and the ECO Cultural Institute**



The organization was established in 1985 with the aim of contributing to the development of member countries, removing trade barriers within the ECO region and developing intra-regional trade and encouraging the integration of ECO region with global markets, and strengthening cultural and historical ties between the member countries. Turkey has been a member of the organization as a founding country since 1985.

The funds transferred by the member states to the Organisation for Economic Co-operation and the audit of expenditures from these funds for the year 2018 was carried out. The audit was conducted through auditors appointed by Turkey, Iran and Pakistan.

During the audits, the payments related to the expenditures, the bank records and the accounting transactions related to the expenditures were examined through the documents proving the expenditures made from the sources transferred by the ECO Secretariat.

As a result of audits; a report was drawn up on whether the expenditures are realized in line with the legal agreements, the regulation of the cooperation organization and the specified objectives.

### **Sampling Methodology Knowledge and Experience Sharing Workshop**

The workshop for mutual knowledge and experience sharing in the field of the Application of Audit Sampling Methodology and Techniques within the scope of the EU TAIEX Program started on 30 July 2019 in Ankara.

Prah Natasa, Head of Audit Division of Slovenia Budget Audit Bureau, Stegić Marin, Deputy Director of Croatia European Union Programs Implementation System Audit Agency (ARPA) and the TCA auditors participated in the workshop.

In the two-day long workshop, works conducted by the EU Commission in this respect, EU practices and other significant matters were discussed.

### **Training Program for Auditors from the SAI of TRNC**

In the framework of the bilateral agreement between the TCA and the SAI of TRNC, a 5-day training program on 22-26 June 2019 was organized for the auditors of the SAI TRNC with the contributions of Turkish Coordination and Cooperation Agency (TİKA), and it



The said trainings aimed to increase the professional competencies and capacities of the auditors of the SAI of TRNC. In the scope of the 5-days program, the TCA auditors delivered trainings on the planning, executing, reporting phases and good practices of "Financial Audit"

At the end of the training program, TCA President Seyit Ahmet BAŞ, gave the training certificates to the auditors that participated in the training.

### **Environmental Audit Information and Experience Sharing Workshop**

The workshop for sharing information and experience within the scope of EU TAIEX Program in the fields of environmental audit and flood risk management audit was organised on 9.7.2019 in Ankara.

Deputy President Dietmar Weihrich of the SAI of Sachsen-Anhalt State (Germany), environmental audit project manager Olaf Hoffmann, officials from DSI, AFAD, the Ministry of Agriculture and Forest, and TCA staff attended the workshop.



was hosted by the TCA.

The workshop, which continued for two days, focused on EU directives particularly on the issue, country practice of Germany and other important issues.



### Training Program for Auditors from the State Audit and Administrative Control Bureau of Palestine was Completed

Within the framework of the bilateral agreement between the TCA and the State Audit and Administrative Control Bureau of Palestine, a 5-day training program was organized for the auditors of the State Audit and Administrative Control Bureau of Palestine on 24-28 June 2019.

The said training aimed to increase the professional



competencies and capacities of the auditors of the State Audit and Administrative Control Bureau of Palestine. In the scope of the program, the TCA auditors delivered trainings on the planning, executing, reporting phases and good practices of "Audit of State Owned Enterprises"

At the end of the training program, the TCA President Seyit Ahmet BAŞ, gave certificates to the auditors that participated in the training.

### The Turkish Court of Accounts carried out the Financial Audit of the D-8 Organization for Economic Cooperation

The Turkish Court of Accounts (TCA) carried out a financial audit on the funds transferred by the Member States to the D-8 Organization for Economic Cooperation and the expenditures made out of these funds in 2017 and 2018.

The Developing-8 (D-8) Organization for Economic Cooperation was established in 1997 to create new opportunities and diversify trade relations and to develop economic cooperation through concrete joint projects between Turkey, Pakistan, Iran, Malaysia, Nigeria, Egypt, Bangladesh and Indonesia and to increase the participation of these countries in the international decision-making process.



Cooperation

### The Turkish Court of Accounts (TCA) celebrates Its 157th Anniversary

On 29 May 2019, the Turkish Court of Accounts (TCA) celebrated the 157th anniversary of its establishment with its current designation as well as the 1179th year of establishment since its original foundation by the Turkish states.

The TCA has a deep-rooted history dating back to the Court of Integrity (Divan-İlshraf), which was the audit body of the historical Turkish states, namely the Karahanids, Gaznavids and Seljuks, and to the Court of Accounts, which was established on 29 May 1862



during the Ottoman Empire. Today, the TCA is one of the most important institutions in Turkish public management. Furthermore, it is also an active supreme audit institution in the international arena particularly as the EUROSAT President.

To commemorate its 157th anniversary, the TCA organised a national program, which included a symposium attended by members of the judiciary, academicians and participants from public institutions. In addition, the celebrations included an art exhibition covering the creations of the TCA personnel as well as a Turkish folk music concert performed by the TCA personnel.

### **TCA has become a member of the INTOSAI CBC Subcommittee on Peer Reviews**

The term "peer review" refers to an external and independent review of one or more elements of the organisation and/or operation of a SAI by a team of professional peers from one or more SAIs.

The Subcommittee on Peer Reviews was created under the scope of the INTOSAI Capacity Building Committee (CBC) at its inaugural meeting in London, 13 – 14 March, 2006 with the following tasks:

- To assess and document existing peer review arrangements in the INTOSAI community.
- To foster an environment where such voluntary reviews are seen as beneficial to both the SAI undertaking the review and the SAI choosing to undergo it and establish global and regional mechanisms for initiating peer reviews.
- To update the CBC guidelines on peer reviews and the developed checklist on the basis of the experience of SAIs and provide further good practices on how to undertake voluntary peer reviews.
- To disseminate the results of peer reviews, as appropriate and as agreed to by participating SAIs.
- The role and importance of the peer review as one of the foremost capacity building tools was underlined in the first INTOSAI Strategic plan 2010 – 2016 and that position is maintained in INTOSAI Strategic plan 2017 – 2022.

TCA believes that peer review is a helpful tool to enhance the capacities of SAIs through submitting an

external assessment and giving information by a peer SAI or a group of SAIs. For this reason, TCA has become a member of the Subcommittee on Peer Reviews in order to follow contemporary developments and approaches regarding enhancing capacities of SAIs in the changing world. Furthermore, TCA aims to benefit from other peers and give support to them through sharing experiences.

### **Training on the Economic Efficiency of Investment Funds was held for the SAI of Qatar**

In the framework of the bilateral agreement between our institution and the SAI of Qatar, a two-day training program on "Economic Efficiency of Investment Funds" was held on 15-16 May 2019 for the auditors of the SAI of Qatar.

In the scope of the program, the training was given on the definition of investment funds, their categories, indicators of the economic efficiency of investment funds, audit of the financial statements of investment funds and the reports on the economic efficiency of investment funds.

### **TCA President Seyit Ahmet BAS attended the International Conference Held by the Romanian Court of Accounts**

TCA President Seyit Ahmet BAŞ attended the international conference held by the Romanian Court of Accounts within the scope of the Romanian Presidency of the Council of the European Union in Bucharest. 53 participants from 22 countries, 13 of which were represented at the presidential level, attended the international conference, which was held on 07.05.2019 with the themes of "Audit Innovations in European Union and Increasing Guiding Roles of the SAIs". In the conference, presentations were delivered on such topics as New Approaches to Public Sector Audit in Europe, Digitalisation of Audit, Increasing the Contributions of the SAIs to the Lives of Citizens and Social Impacts of Audit.

President BAŞ held bilateral and multilateral cooperation talks with the representatives of many countries including Romania, Poland, Moldova, Spain, Czechia and Portugal during and after the conference.

**A Delegation from the SAI of Qatar, the Incoming ARABOSAI President, paid a study visit to the President of the TCA, Seyit Ahmet BAS**, received the President of the State Audit Bureau of Qatar, Sheikh Bandar Bin Mohammed Bin Saoud Al Thani, and the accompanying delegation from the SAI of







Qatar on 24 April 2019.

The study visit of the SAI of Qatar started with this welcome meeting; then, the TCA made presentations on the data analysis system (VERA) used by the TCA, the application of audit management program (SayCap) and the TCA's experience about the IT audit in the scope of new methodologies. Moreover, the visiting delegation shared information on project Archer, which is about the restructuring of the SAI of Qatar.



In addition, during the meeting, evaluations were made on the trainings and other activities realized in the framework of the cooperation agreement between the TCA and the SAI of Qatar; and emphasis was made on having a closer collaboration in the field of audit between the TCA and the SAI of Qatar for the future periods.

President BAŞ gifted Sheikh Bandar Bin Mohammed Bin Saoud Al Thani a "cufic" plate with a panel inscription that represents the Divan-ı İşraf (Court of Control), which was an entity that performed the audits tasks related to the state's financial transactions in the historical Turkish states of Karakhanids, Ghaznevids and Seljuks. Visit to the TCA

**ECOSAI Workshop on Ethics Audit in Antalya,**

## TURKEY

The workshop on "Introduction to Ethics Audit" for the member SAIs of the Economic Cooperation Organization Supreme Audit Institutions (ECOSAI) was held in Antalya on 15-19 April 2019, and it was hosted by the Turkish Court of Accounts (TCA).

The workshop continued for five days, and trainings



were given on "What is Ethics Audit", "Why should SAI conduct Ethics Audit", "Implementation and Reporting of Ethics Audit", "Ethics Audit Approaches in Public Entities" under the main title of "Introduction to Ethics Audit", and good practice examples were discussed.

The opening of the workshop was made by the President of the TCA, Mr. Seyit Ahmet BAŞ; and there were 28 participants from the ECOSAI member SAIs of Afghanistan, Azerbaijan, İran, Kazakhstan, Kirgizstan, Mongolia, Pakistan, Tajikistan and the SAIs of other countries like the TRNC, Kuwait, Palestine and Qatar.

## Cooperation Protocol signed with the United Nations High Commissioner for Refugees (UNHCR) Turkey Office

TCA President Seyit Ahmet Baş and Representative of UNHCR Turkey Katharina Lumpp signed cooperation protocol between the Turkish Court of Accounts (TCA) and the Office of the United Nations High Commissioner for Refugees in Turkey regarding the audit of funds given to public administrations by UNHCR on 17.04.2019.



The background features a light blue gradient. In the top-left corner, there are overlapping diagonal bands of red, orange, and yellow. In the bottom-right corner, there are overlapping diagonal bands of purple and blue. Thin, dark grey lines intersect diagonally across the page, creating a sense of depth and structure.

# Articles & Research Papers from Member SAls





## Sustaining reform in Supreme Audit Institutions

**Hasan Masud**

Director General Quality Assurance, Inspection and Monitoring Wing, Department of the Auditor General of Pakistan



People around the world now expect governments to manage their financial resources in a prudent and cost-effective way. Governments collect revenues, largely through taxation, and in return are expected to deliver in social sectors like education, health, infrastructure and social transfers for the benefit of current and future generations.

Financial management lies at the core of operations and activities of the public sector. Since public sector is the largest spender and employer in almost every developing country and it sets the policy agenda for the rest of the economy. Unfortunately, the approach to mobilizing and managing public finance in most developing countries has been met with challenges such as corruption, misapplication and misappropriation of funds, over-spending and lack of compliance with existing legislative frameworks. In that context an effective office of the Auditor General producing quality audit reporting is the key to successful accountability in the country.

Reforming the Public Sector is perhaps one of the most overworked clichés in Supreme Audit Institutions (SAIs) today. Everyone wants change but hardly anyone is willing to give a thought to the how part of the process. The SAI office and its auditors must be honest, efficient, rule bound and use cutting edge technologies. Yet how this is to be done is a challenge. There are many examples of reform implementation failures all around us.

Development thinkers are now talking about 'techniques of successful failure' that make reform extremely difficult to implement. It is argued that more often development schemes in developing countries are examples of what is described as isomorphic mimicry. The concept of mimicry in natural sciences is widely known as many animals use camouflage techniques to survive. For instance, the 'scarlet kingsnake has the same yellow, red, and black banded coloration of the deadly poisonous eastern coral snake, but without the bother of actually having venom'. Similarly, in the world of policy formulation and implementation we have many examples where excellent

laws are available on the statute book without any actual implementation. Just like the scarlet kingsnake they have the stripes but not the venom of the eastern coral snake. In such an environment how do we reform where failures galore and isomorphic mimicry is a real threat. Working on grand reform proposals seldom give us the desired results. The focus of an auditor in a developing country should be on scoring small victories. Reform is an incremental process needing small steps and teamwork. Focusing on solving local problems that are debated, defined and refined by local people in an ongoing process should be the first step. These small steps will be taken by empowering people giving real results by finding real solutions to real problems.

The idea that an all-powerful top leader would quick fix a situation needs a reality check. Reform is hard work which requires leaders to be consistent and adaptive. It also means we will face setbacks but that should help us to course correct and adapt. We move from one problem to the next with grit. We aim for small victories instead of grand solutions. These small victories enable us to stay motivated and stay the course. Therefore focus area of any reform effort in the SAIs should be:

- Development is about problem solving instead of predetermined solutions.
- Leadership is not a single all powerful sovereign but instead a series of authorizers who work like an orchestra.
- We move in step wise iterative process where we experiment, learn and adapt.

What is important is that we need to identify whether our aim is make a substantive, procedural or a maintenance contribution. The policy focus of developing country auditors should be on making a substantive contribution by:

- Constructing, communicating problems
- Coming up with reform ideas
- Reviewing implementation'

The presumption that replacing the old system would improve performance delivery automatically is flawed.

This often creates a patchwork and the resulting system lacks efficiency of the new system and responsiveness of the old system. Reform has to be seen as an on-going process and not a one-time magic prescription to end all problems.

SAls today operate in a world where there is an ever rising tide of expectations for transparency and accountability. The rise of social media, globalization and information technology revolution has changed the whole debate on accountability issues. In this environment it is only logical if citizens of a country expect better reporting from the national SAI. In that regard improving Quality Management framework in an SAI is the key to the process of responding to public expectation.

SAls must act on a timely basis and ensure no backlogs or delays are created so as to provide basis for accountability

by the Public Accounts Committee (PAC). This will also ensure that cases on which urgent action is required are not delayed. Quality Management of Audit cannot be seen as isolated process performed at the end of the audit cycle. Instead it has to be seen as a dynamic process aimed at responding to the ever changing demands of our societies.

The presumption that simply replacing the old system in one go would improve performance delivery automatically is flawed. This often creates a patchwork and the resulting system lacks efficiency of the new system and responsiveness of the old system. Reform has to be seen as an on-going process and not a one-time magic prescription to end all problems. Improving SAI's Quality Management needs public sector auditors to focus on the reforming the old while staying in step with the latest trends in the field.

# Accountability In Question: A Critical Review Of Public Accountability

**Dr. Murat İNCE**

Principal Auditor

Turkish Court of Accounts



As a critical rhetoric term accountability poses a per se signifier to describe the radical differences between traditional understanding of government and new public management. No doubt that the shift from traditional understanding of government to new public management manifests itself best in the rising public awareness of average people to hold the performers accountable. In fact, the term "public accountability" paraphrases this paradigmatic and unresolved change in the modern public administration still mediating between representative democracy and participatory democracy.

There is a very robust understanding of public accountability both in technical and ethical terms, which endeavours to consider accountability like a magic show and to smooth away all the malfunctions in governmental performance. This article intends to evaluate and criticize this late modern conception of accountability through depicting the fragile and fragmented contents of the term and questioning the controversial relationships between bureaucracy and democracy as well.

In evaluating the modern concept of accountability, one should bear the following questions in mind: How can we explain the ambiguousness embedded in the concept of accountability? Is there any essential relationship between accountability and democracy? What should our choice be when there comes out a concrete contradiction between efficiency and democracy? Is it rational to vote for democracy at the expense of accountability? Should we conceive accountability as a well-designed system to improve productivity, effectiveness and efficiency or in contrast, as a simple and limited moral conduct to be pursued by both the accounter and the accountable? And yet; what can be done against the post-political implications of the notion of accountability?

## 1. Definitions Of Accountability

As a complex term, which is now a commonplace of the public administration literature, "public accountability" is one of those golden concepts that no one can be against because it conveys an image of transparency, trustworthiness, fidelity, justice and democratic consciousness. Although the term "accountability" has leapt to prominence in the last three decades, it seems that unlike other core democratic values, such as freedom, justice and equality, accountability has not yet had time to accumulate a substantial tradition of academic analysis. "Many authors have been writing about accountability in a variety of contexts, political, legal and commercial, but there has been little agreement, or even common ground of disagreement, over the general nature of accountability or its various mechanisms" (Mulgan, 2003:IX).

Central to all definitions of accountability is the idea that one person or institution is obliged to give an account of his, her, or its activities to another (Jenkins, 2007). Accountability can be concisely defined as "the obligation to explain and justify conduct". This definition implies "a relationship between an actor, the account or, and a forum, the account holder or accountee" (Bovens, 2007:450; Stewart, 1984). The most basic form of accountability in the public sector is the hierarchical Westminster system of government whereby: a) public servants are accountable to ministers; b) ministers are accountable to parliament; and c) parliament is accountable to the people (Fuller and Roffey, 1993:12). Mulgan defines accountability as "the obligation to be called to account" (2003:1). According to Day and Klein, accountability means "the responsibility of one party, the accountability holder, to justify its actions to another, the accountability holder, according to a pre-existing set of rules, standards or expectations" (1987:32). Another definition of accountability draws on result-oriented content of the term and describes it as "a relationship based on obligations to demonstrate, review, and take responsibility for performance, both the results

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*Available at: <https://www.sayistay.gov.tr/tr/Upload/95906369/files/dergi/pdf/110m7.pdf>*

achieved in light of agreed expectations and the means used."

Today it is almost impossible to understand accountability apart from its close relations with democratic governance and democratic participation. The term, which was first introduced as an instrument to enhance the effectiveness and efficiency of public governance, has gradually become a goal in itself, an icon for good governance, first in the USA, but increasingly also in the EU. Many developing countries consider accountability as an indispensable instrument to provide a democratic means to monitor and control government conduct, for also preventing the development of concentrations of power, and yet to enhance the learning capacity and effectiveness of public administration.

As the size and functions demanded of government have expanded through time, the demands for government to be kept accountable have become progressively more sophisticated. As a result of this complexity, many scholars began to consider accountability as a highly vague term to meet the emergent needs of modern states. Some speak of interlinked networks of accountability and overarching accountability burden of the modern governance while others argue that the application of accountability in the public sector is both complex and contestable, given the complexities of government and its accompanying multifaceted accountability dimensions and relationships.

## 2. Accountability And New Public Management

The adoption of New Public Management (NPM) by an increasing number of countries worldwide is described as one of the most striking international trends in public administration. Within the scope of government and governance, as part of NPM, the concepts of new governance, market-based governance, and good governance have replaced the traditional concepts of government and governance. The shift from traditional understanding of government to new public management manifests itself best in the rising public awareness of average people to hold the performers accountable. In fact, the term "public accountability" paraphrases this paradigmatic change in all aspects (Ince and Taner, 2017:3).

NPM is a new paradigm for public sector. As the inspiring spirit of the late modern states, the notion of NPM has been deeply influenced by neo-liberal

conception of public management frameworks and from 1980s onwards many governments became committed to reducing the proportion of national income devoted to public expenditure, and the range of functions undertaken by government. Within the scope of government and governance, as part of NPM, the concepts of new governance, market-based governance, and good governance have replaced the traditional concepts of government and governance. In public administrations, implementations of new public management such as liberalizations, administration by proxy, deregulations, outsourcing, and public-private partnerships, privatization and contracting-out have been globally acknowledged (Farazmand, 2006: 352).

Various models of new public policies (NPAs) have been introduced and implemented to challenge the new efficiency and accountability problems in the world. Behind the idea of these NPA models there exists one crucial notion which encapsulates and legitimizes various implementations: the notion of minimal, efficient and regulative state (Osborne and Gaebler, 1993:321-331). Some critics of these NPAs insistently maintain that minimization and privatization policies do not necessarily produce higher efficiency; that the policy of sweeping public-private/corporate sector transformation only benefits corporate globalizers; and that these policies are indeed a threat for "democracy" and democratic rights of citizens because they undermine the sovereignty of nation states (Farazmand, 1999, 2001, 2010; Korten, 2001; Waldo 1992; Woods 2006).

## 3. Accountability, Bureaucracy and Democracy

Accountability is normally considered as a critical element of democratic public administration. However, it is a crucial question to ask whether there exists an inevitable relation between accountability and democracy. Some scholars are of the opinion that we are not sure whether an ideal praxis of accountability is best achieved through a centralised concentration of control or through dispersed power and delegated responsibilities. A state having a historically well-established and sound bureaucratic system, depending on a robust and well-defined accountability framework does really need to be called as democracy? In fact, this question is closely related with a more general question, that's, whether a strong and well-designed bureaucratic establishment is compatible with the essential pillars of democracy.

As a Weberian rationalization instrument, bureaucracy served much for the rationalization and modernisation process of the state, both emerging as a threat for democracy and so as an applicable instrument for democratic questioning as well. Perhaps, we do not really have to mention a deep contradiction between democracy and bureaucracy. Eliminating the imbalances between the two, why might it not be a reconciliation to speak of in order to tackle the philosophical dilemma between Reason and Freedom in the guises of bureaucracy and democracy? Aspiring to this critical thesis Farazmand argues that although there are certain contradictions in the relationship between the two phenomena, in fact democracy and bureaucracy are reconcilable. "The political dilemma of democracy and bureaucracy has always confronted politicians and scholars with major choices to make—dismantling bureaucracy means chaos and disorder, and dismantling democracy means rule by bureaucratic officialdom. A balance must be maintained between the two, as there is no other alternative" (Farazmand, 2010:256).

### 3. Critical Review Of Accountability

As the state is centralized, it becomes less challenging to design accountability relations depending on the well-defined lines of authorities and well-designed regulative framework. However, when the state becomes more scattered and wide-ranging, the accountability becomes more ambiguous and slippery as a guideline to be pursued effectively in all levels of authorities. Modern state, parallel to the ever-changing global trends, is undergoing a very rapid institutional settlement especially derived from the undermining and dynamic effects of private sector experiences. Today, to some extent, we have to call modern public administration or (so to say "new public management") as a sort of public entrepreneurship on the way to evolve eventually into a private one.

Doubtlessly, today's multiple networks of public accountability are the result of a lengthy history in which we have learned through the polity how to control personal and organisational frailties as public power and public resources are utilised for political purposes. To some scholars, we are witnessing an accountability crisis nowadays. For example, Dowdle (2006:26) suggests that claims of accountability crisis will continue in the twenty first century, "simply

because there is a foundational contradiction between our innate desire to trust others and the innate limits in our capacities to trust others."

In line with the new public management frameworks, new methods of accountability schemes are being introduced. Within this concept, opponents of innovative ways of increasing accountability often argue that efforts to improve accountability often put nongovernment actors in prominent roles, having a damaging potential to undermine the proper development of state capacity. Jenkins argues that structural transformations in the nature of governance—including the privatization of some state functions—have blurred lines of accountability, making it difficult to establish which actors hold ultimate responsibility for certain types of policies or services. "The ongoing process of globalization has introduced a range of new power-holders—such as multinational corporations and transnational social movements—that slip through the jurisdictional cracks separating national authorities, yet whose actions have a profound impact on people's lives. The influence exercised over economic policy in poor countries by such multilateral institutions as the World Bank, the International Monetary Fund, and the World Trade Organization has also reduced the autonomy of many governments, making domestic democratic accountability even more elusive" (Jenkins, 2007:137). It should be also emphasized that we are living in an increasingly internationalised world in which many privately owned commercial companies exercise more power than some individual nation states. "Indeed, in modern democracies, the problem of regulating large, multinational companies and holding them to account for breaches of laws and regulations is often even more pressing than the control of government power.

This rationale for accountability, the need to keep powerful institutions from harming the interests of the public, clearly extends across all sectors of society and is not confined simply to the government sector. The extent of this justification, however, is more circumscribed, being restricted to the prevention of harm and not encompassing, like the principle of ownership, a general right to determine overall purposes and objectives" (Mulgan, 2003:13-14).



In one respect, the instrumental and ethical perceptions of accountability are deeply in conflict with one another in today's modern governance debates. This conflict is primarily concerned with the questions of whether the accountability should be conceived as a well-designed system to improve productivity, effectiveness and efficiency or whether it refers to a moral conduct to be pursued by both the accounter and the accountable.

The worldwide movement in favour of increased accountability reflects a growing democratic assertiveness in the world. As a result of this, we witness an increased community participation in today's policymaking processes. This fact brings additional burdens and aporias on the issue of accountability. As Edwards puts it; "important accountability issues arise as more non-government players are involved in the policy development process (2003:15). It is evident that the wide range of collaborative government / partnership arrangements (the model of PPP "public-private partnership" constitutes only a small portion of this) in modern public administration made accountability relationships more ambiguous and complex than ever. Collaborative partnerships normally involve both governmental and non-governmental agents in delivering services and policy-making.

As mentioned above, collaborative and complex arrangements in governments have stimulated the need for developing more detailed and complex accountability schemes. Depending on this, some argue that modern governments should persistently strive for finding the new ways of holding accountability parallel to the ever-changing needs of modern societies. In order to overcome the undermining impact of a certain weakening in the performance of state apparatus, we should maintain a critical grasp of the notion of accountability. For example, accountability should not be considered as a simple substitutory instrument for poor performance. As Jenkins underlines it; "Substituting non state actors when state capacity is weak may be tempting, but it is shortsighted: bypassing poorly functioning state institutions can lead to further atrophy of official organs" (Jenkins, 2007:176).

Another critical aspect with regard to accountability is the paradox between "accountability and efficiency". We must admit that there is not any automatic relationship between accountability and efficiency. It is apparent that the extended range of accountability

mechanisms does not lead to a satisfying "state of accountability". Although the number and scope of NPM-inspired accountability arrangements have grown considerably in all over the world, many scholars are deeply suspicious about concurrent and compatible achievement of accountability and efficiency goals.

Behn labels it as a "trade-off between accountability and efficiency" (Behn, 2001). According to Hodge and Coghill (2007), it is a paradox that in the midst of deregulating government operations, there is a tendency to strengthen public accountability mechanisms. Some others underline the fact that public accountability is losing ground, in fact is being sacrificed in the name of public sector efficiency (Flinders, 2001; Mulgan, 2003). Cendon argues that there is today a real flourishing of instruments of supervision and control of administrative performance and that society is more and more aware of the relevance of this control, in order to assure the maximum efficiency of public administration. It is also pointed that we live today in an "audit society". However according to Cendon; "The consequences of the realisation of democratic accountability do not have a concrete legal profile and they depend on the character of the control and of the social pressure that public administration has to undergo." (Cendon, 2000:45).

### Conclusion

We observe that as the size and functions demanded of modern government have expanded through time, the demands for government to be kept accountable have become progressively more sophisticated. Today, one can hardly come across any term more stimulating than accountability revealing both the idealistic expectations and technical requirements of democratic governance. Having a consolidated image of transparency, trustworthiness, fidelity, justice and democratic consciousness the notion of accountability manifests a very strong discursive temptation to be "ever more democratic" in our modern public administration. Touching on the undecidable core of democracy, Derrida (1994) uses the term "democracy to come" in order to demonstrate the ever-idealistic/never-ending content of the term in philosophical terms. In his understanding, democracy never comes; it is always on the way to come. Perhaps it is meaningful to apply this insight to the notion of public accountability and conclude that public accountability is never performed at all; it is always on the way to be performed.

We should bear in mind that the uncertainty or the ambiguousness implied here is not a sort of transitory disfunction to be overcome by long-run persistent commitments; on the contrary, it is the main feature, which essentially and ineradicably identifies accountability itself.

Although accountability is fully considered as a critical element of democratic public administration, it is a crucial question to ask whether there exists an inevitable relation between accountability and democracy. In fact, we are not sure whether an ideal praxis of accountability is best achieved through a centralised concentration of control or through dispersed power and delegated responsibilities. Accountability has the potential to serve for both democracy and bureaucracy at the expense of each

other.

We are living in an increasingly internationalised world in which many privately owned commercial companies or supra-national organizations such as World Bank or IMF exercise more power than some individual nation states. On the one hand, we should be alert to the post-political implications of the notion of accountability as a whole. And on the other hand, we should avoid discussing accountability issues apart from the determining factors of ever-existent political power relations. As a last word; we should always keep in mind that the paradoxes of accountability extend its performative spirit much farther than expected and it is just this distance that makes accountability both elusive and tempting.

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# Developing a Framework for Outsourcing Audit in a Supreme Audit Institution

**Dr. Iram A. Khan**

Deputy Auditor General (Policy), Department of the Auditor General of Pakistan



## Introduction

In today's fast changing world, the functions and roles of SAIs have evolved along with changes in governance patterns. The SAIs once used to espouse only one primary function of audit: verification of the accuracy and completeness of accounts and giving assurance that all expenditures and disbursements were authorized, vouched and correctly classified. Now, they have moved to a new audit approach that aims to add value to public resources. They are now increasingly and proactively engaged with governments in improving the ways public resources are managed.

This new ambition brings forth the role of an SAI outside the confines of narrowly focused regulatory and compliance audit. It accentuates the proactive role of an SAI in taking up audit assignments that offer considered opinions on the value that public sector entities add to the society they serve or in the field of forensic or environmental audit (for example) where there is need for collecting and testing evidence/data for which the public sector audit does not have adequate knowledge or expertise. This paper argues that it is only in rare situations that an SAI should outsource its work.

## Need for outsourcing

The SAIs have in the past outsourced different types of audit assignments to private sector professionals /consultants. From the experience of SAIs, the following reasons for outsourcing audit work can be identified:

- a) Skills currently unavailable within the SAI;
- b) Need for specialized or professional skills;
- c) Need for independent research or assessment;
- d) Shortage of staff, or
- e) Seasonal work.

It is pertinent to note that the Australian National Audit

Office has even outsourced work relating to the audit of financial statements, which should be a routine work for an SAI. This shows that the option for outsourcing is not limited to some specialised audit activity alone.

## Typology of outsourcing work

It is important to understand that the private sector professionals or consultants who may be outsourced audit work fall in either of the three broad categories outlined below: Category – I Includes high level professionals who would advise an SAI about planning audit in a specialized area through brief advisory intervention. They are not directly involved in the execution or follow-up phase of audit. Category – II Includes mid-level professionals who would be part of an audit team in the execution phase of audit in an advisory capacity. Category – III Includes individuals with specialization and experience who would be assigned specialized audits as and when required. They would plan and execute an assigned audit activity independently. The typology above shows that in the first two categories, the role of a consultant is partial in nature, with the public sector auditor taking the lead in audit activity. It is in the third category that an SAI, being unable to handle the work of audit on its own and relying on the assistance of professionals from the private sector, is forced to outsource it entirely.

## Pros and cons of outsourcing

There are certain benefits and risks for outsourcing audit work to the private sector. The benefits are:

- a) Staff augmentation to provide additional skills or resources in the short term that an SAI does not have or does have the capacity to develop internally;
- b) Long term comprehensive capacity building program;
- c) Sharing private sector training resources (trainers, materials and facilities) where the private sector has expertise that will be useful

He can be reached at: [iram.khan@fulbrightmail.org](mailto:iram.khan@fulbrightmail.org).

to an SAI, such as generally accepted accounting and auditing standards, SAP operations, internal auditing, and auditing in an Information Systems environment;

- d) Transfer of knowledge through the inclusion of private sector auditors in SAI teams and secondment of the SAI auditors to private sector firms for exposure to audit practices and methodologies as well as through interaction on more informal basis;
- e) Ongoing professional development such as seminars, retreats, study tours, research and so on in collaboration with private sector counterparts; and,
- f) Integration of professional qualifications by developing a body of knowledge, a curriculum, and a training and evaluation mechanism to prepare public sector auditors for certification.

#### The risks identified are:

- a) The hiring of private sector firms requires additional funding, depending on the extent of their use. The demand for additional resources raises questions about the sustainability and cost-effectiveness of this exercise.
- b) The private sector auditors may supplant the work already being undertaken by public sector auditors.
- c) Excessive reliance on consultants may actually kill the capacity of the host SAI rather than build upon it.

The pros and cons identified above clearly indicate that outsourcing should not be pursued as an independent goal in itself, but as a potential input to an integrated plan for enhancing the mandate and activities of an SAI. The use of private sector consultants is therefore also predicated on the HR strategy being pursued by an SAI. In any case, they should be used very selectively and as circumstances permit.

A careful analysis shows that these risks arise due to thoughtless and unplanned use/employment of consultants in an organization. If the objective of hiring private sector consultants is to build the capacity of an organization, rather than spending donor money to

show the extent of disbursement and progress in a project, the gains from employing consultants will be sustainable and the risks of killing the capacity of an organization will be minimized. However, the issue is that in case of a donor funded project, it is mostly the donor that drives its substance and pace. The result is that reliance on readily available resource (private sector consultants) may become a hindrance in the capacity enhancement of an SAI.

Here it will be useful to cite the example of World Bank funded project PIFRA (Project to Improve Financial Reporting and Auditing) in SAI Pakistan, where the project could become sustainable only when the project team took a strong and decisive decision to internalise the technical knowledge and expertise of private sector IT consultants by establishing a PIFRA Resource Centre and by recruiting and building a team in-house.

Another example can be given of BMB consultants from the Netherlands, who developed Performance Audit Guidelines for different sectors in SAI Pakistan. They also conducted large number of trainings and transferred knowledge to public sector auditors. It is this internalisation of knowledge that today SAI Pakistan is at the forefront of Performance Audit and has been regularly conducting national and international training courses in this area every year.

#### A new paradigm for outsourcing

In today's complex world, specialised audit assignments require the presence of multi-disciplinary teams that not only understand audit requirements but can also give input of scientific and technical nature. In order to build these teams and to overcome the risks identified with respect to outsourcing, this paper proposes the creation of "Knowledge Groups" as a means to internalise knowledge and expertise in the SAIs.

These collaborative Groups will comprise stalwarts of the SAI, subject specialists from academia, practitioners as well as private sector consultants. In case an expert in the field is not available in an SAI, rather than hiring a private consultant, it will be preferable to provide adequate training to a public sector auditor, who can lead the knowledge group proactively. The services of a private sector consultant may be employed in extreme and rare cases.

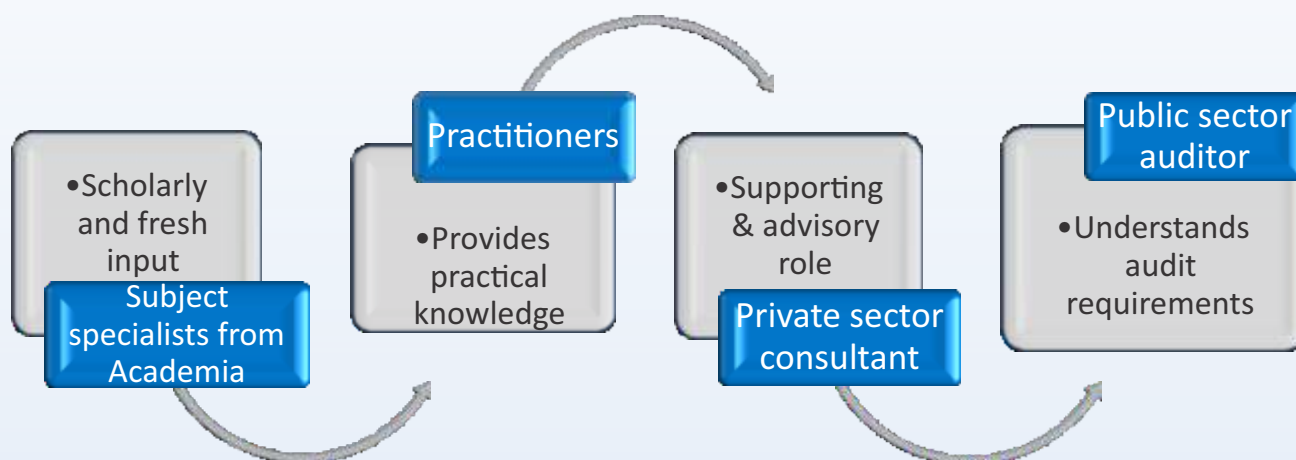
Effort should also be made to capitalise on the expertise of other public sector organizations that can provide technical input. In case of Environmental Audit

of tanneries, SAI Pakistan has used the services of Pakistan Council of Research in Water Resources, a public sector organization, for testing water samples and reporting the extent of contamination in underground water. However, we may need technical input from a consultant regarding safe leather tanning processes or treatment of residual waste water etc. Retired or serving professionals in the field may also be co-opted during the course of audit.

A synergy of resources and expertise in Knowledge Groups will create a conducive environment for public sector audit, which will not only mitigate the above-mentioned risks associated with the hiring of private

sector consultants but will also build the capacity of an SAI. This conceptualisation has been depicted in the figure below. In other words, instead of outsourcing the entire work to consultants, the SAI should work in Public Private Partnership mode, where the public sector auditor takes the lead, and the private sector is given a supportive or advisory role. By actively involving the academia and practitioners with public sector auditors, it is ensured that scholarly and fresh input is available for developing standards and guidelines that will be applied in the field. Creation of Knowledge Groups will ensure that the capacity of public sector auditors is enhanced and they remain motivated.

Figure 1: Creation of Synergy through Knowledge Groups



### Conclusion

The discussion above shows that Knowledge Groups can go a long way in facilitating, integrating and enhancing the pace of learning in an SAI. Private sector professionals may be co-opted only when technical expertise in a certain area is not available either in the SAI or any other public sector organisation. However, their role should at best be advisory and supportive in nature. The policy direction and need identification

must come from the public sector auditor, who should have a proactive role in the development of guidelines or setting the course of audit. The creation of synergetic Knowledge Groups provides framework in public private partnership mode for benefiting from the knowledge, expertise and experience existing outside the SAI. It provides necessary support to a public sector auditor and builds his capacity till such time he is able to work independently.

# Performance audit as a contributor to change and improvement in Public Administration

**Muhammad Afnan Alam**

Director International Relations & Coordination Wing,  
Department of the Auditor General of Pakistan



## Abstract

The last 30 years of the New Public Management 'regime' in many western countries have resulted in increased use of audit and other control mechanisms. These mechanisms are supposed to contribute both to accountability and improvement. In this article, theories of evaluation and organizational learning are used to understand how the dynamics of control affect change processes.

## Keywords

accountability, control, evaluation for accountability, improvement, organizational learning, Supreme Audit Institutions

## Introduction

Over the past 30 to 40 years, western societies have increasingly modernized in line with New Public Management (NPM) doctrines. The NPM 'regime' has involved increased delegation, which in turn has resulted in greater use of audit and control mechanisms. In his much-quoted book, *The Audit Society, Power* (1997) nevertheless claims that controls or audits are just rituals of verification with the purpose of assurance, but without real effect (see also Behn, 2001). The impact of audits is a contested issue. Some researchers claim that control can work against improvement, whereas others argue that control enhances trust and performance (Furubo, 2011; Möllering, 2006). Trust reduces transaction costs and thereby increases efficiency and performance (Fukuyama, 2014). The actual outcomes are nevertheless likely to depend on the way controls are implemented (Ossege, 2012).

The Supreme Audit Institutions (SAIs) in most countries have become a key part of the institutional framework (Pollitt & Summa, 1997), and increasingly become active in examining performance of public sector administrations (Talbot and Wiggan, 2010). This performance movements have resulted of more use of audit as a mechanism of improving accountability and control (Hood, 1991; Power, 2003a). The theme

emerged is that performance audit has become an important tool to assess whether the economy, efficiency and effectiveness of the use of public money have been met. This is usually conducted by team of expert auditors based on special are criteria of measurement and evaluation (Kells, 2011; Waring & Morgan, 2007; Intosai, 2004).

In practice, the SAIs considered how particular methods might help identify savings in public administrations, help make recommendations to improve performance and accountability, help assess performance and produce relevant information for decision makers in public organizations (Lonsdale, 2000). They also set up performance indicators and a set of targets that should be met by the audited entities in order to prove that public resources are managed properly. Thus, the success or otherwise of audited entities in performance audit would be confirmed by the ability to produce evidence on whether performance indicators have been met (Bawole & Ibrahim, 2016). As a rule, auditors examine these evidences to establish whether public administrations' targets have been met, identify any shortcomings and then write their reports based on the findings. The focus of their reports is usually on the management of service or the implementation of public programs (Keen, 1999). Their reports, in most countries, are presented in the Parliament to enhance accountability in public administrations (Nutley, Levitt, Solesbury, & Martin, 2012; Pollitt et al., 1999).

## Research on the impact of performance auditing

There are few empirical studies focused on the actual outcomes of performance audits. In a review of existing research on the subject, only 14 studies pertaining to state audit were found

(Van Looke and Put, 2011). Like the present study, many of these studies are based on the perceptions of those audited. A recent study (Reichborn-Kjennerud, 2013a) found that performance



audits were perceived as useful by the auditees in the Norwegian context. The author suggests that the extent to which the auditees considered the reports useful depended on their appraisal of the quality of the report and of the SAI as an institution.

It also depended on perception of the extent to which auditees' comments were taken into account during the process, and on the changes that actually ensued after the performance audit. In another article Reichborn-Kjennerud and Johnsen (2015) demonstrated how holding auditees to account contributed to actual changes in the audited entities. These results are not reflected in research on the Estonian SAI, however, where the auditees did not perceive performance audit reports as useful (Raudla et al., 2015). And Morin's recent qualitative research similarly indicated that the impact of the French SAI is weak, its audits contributing more to window dressing than to real influence (Morin, 2016). In the Danish context, Justesen and Skærbek (2010) looked into how accountability mechanisms contributed to the impact of audits, suggesting that they represent forceful mechanisms that induce organizations to implement change. All in all, this indicates that the impact of SAIs is likely to vary according to context.

Morin (2004, 2008) has conducted several studies on performance audit, both qualitative and quantitative. From her quantitative research, she concludes that auditors have a certain impact, one aspect of this being that they influence the auditees' management practices and their perceptions of usefulness. In later qualitative studies, she problematizes the double role played by auditors as both controllers and management consultants. She also discusses the challenges faced by audit institutions in adopting new evaluation methodologies in performance audits (Morin, 2010, 2016). In a qualitative study, Alwardat (2010) suggests that the utility of performance audits – as perceived by the auditees – depends on their expectations, their view of the auditors' expertise, the materiality of the auditors' findings, and the truth and fairness of the reports.

Several authors problematize the independent role of auditors as constituting an obstacle to impact. Being involved with the auditees, which would otherwise enhance impact, may interfere with the auditors' independent role (Reichborn-Kjennerud and Johnsen, 2011; Vanlandingham, 2011).

Other contributions have explored questions of

accountability and the reactions of auditees to audits (Reichborn-Kjennerud, 2013b, 2014a, 2014b). These studies suggest that performance audits have greatest impact:

- i. when civil servants consider the reports to be of a high standard,
- ii. when they have some influence over the process, and
- iii. when they agree to the SAI's approach

Furthermore, auditees will tend to make concrete changes when they are held to account politically and when media and interest groups use the reports. However, knowledge about what types of change occur as a result of performance audits is lacking. More than two decades ago, Pollitt et al. (1999) mapped and analysed SAI performance audits in five different countries, but few studies have investigated the actual content of performance audits (Grönlund et al., 2011) and what contributions to change are instigated by the reports.

### **SAIs as a contributor to improve in public administration**

The SAI is one of the most important control institutions in a country, investigating whether the public administration use their resources economically, efficiently and effectively. According to its own standards, an SAI's primary task is control. A secondary task, however, is to contribute to improvements in the audited public organizations (Lonsdale and Bechberger, 2011). In their form and purpose, performance audits resemble accountability evaluations in that their purpose is to hold the public administration to account for their use of resources. Both evaluations and performance audits are conducted to assure the efficient and effective use of public funds (Pollitt et al., 1999).

The SAI's methods of control are: financial auditing, corporate control and performance auditing. Financial auditing involves verification of the accuracy of financial information. Corporate controls are carried out in order to assess whether the state's interests in companies have been managed in accordance with the decisions and intentions of the Norwegian Parliament. The mandate for performance audit is to establish whether public policies, programmes, projects or organizations have operated with due regard to economy, efficiency, effectiveness and good

management practice (Lonsdale, 2000; Pollitt et al., 1999).

The SAI's logic is broadly based on an instrumental, purposive rationality. SAIs expect ministries to improve following detected deviance from audit criteria. Although this expectation can be questioned (Hollnagel et al., 2007), the urge to improve based on relevant information is an established assumption in classical management theory and in scientific management (Christensen et al., 2004; Morin, 2008; Taylor, 1967; Weber and Andreski, 1983). This assumption is also present in the performance control system in Norway, labelled 'Management by Objectives and Results', which was introduced on a general basis in national public administration from 2001 (Læg Reid et al., 2006).

### Theoretical approach

#### *Similarities and differences between audit and evaluation*

SAIs are not organized in any direct hierarchical relationship to other public sector organizations, nor do they have formal sanctioning power. They do have indirect power, because Parliament may use the SAI's assessments to sanction ministries (Bovens, 2007) (see examples above). SAIs that issue publicly available reports can also influence their environment through media attention paid to these reports. Potentially, interest groups and different types of Non-Governmental Organizations (NGOs) may also make use of the reports for advocacy purposes (Noussi, 2012). Nevertheless, in order to have an impact, predominantly SAIs, like other evaluation researchers and consultants, must convince auditees of the validity of their assessments.

One important goal for SAIs is to contribute to improvement, notably through performance audits. When SAIs identify deficiencies in the audited organizations, they expect that the auditees will use the relevant information to make improvements (Riksrevisjonen, 2005). This may also apply to programme evaluations when the aim is to hold the evaluated agency to account. A good example of this is the evaluation of development aid, where the aim is to investigate whether the funding has been used as intended (Armytage, 2011). Performance audit nevertheless differs from programme evaluation in that it is part of an institutionalized arrangement, and carries the latent threat that Parliament is entitled to use the report for accountability purposes.

### Performance audit and organizational learning

Different types of control produce different types of organizational learning. In the rational instrumental perspective, two different types of learning can be identified: single- and double-loop learning (Argyris, 1999). In cases when an auditor's logic focuses on compliance, this will lead to single-loop learning; whereas a logic focusing on explaining and understanding performance has the potential to lead to double-loop learning (Reichborn-Kjennerud and Vrangbæk, 2016). Single-loop learning involves repeated attempts to solve the same problem without any attempt to change the overall problem-solving systems or their goals, whereas double-loop learning helps to reset, change and redefine the systems and goals that define how problems are to be solved.

From a rational instrumental perspective, there is one aspect of organizational learning that has not been adequately addressed: namely, situations where there is a lack of will to implement recommended changes. This can occur if potential changes threaten particular groups' interests, or if they work contrary to political agendas (Bringselius, 2013; Reichborn-Kjennerud, 2014a). In such cases, the audited entities can make symbolic changes instead of real changes that improve systems and practices.

Even in cases where the SAI's recommendations are highly relevant, there may be political reasons for auditees not to make real changes. We therefore expect disagreement with audit assessments to be an important reason why change does not occur (Brunsson and Olsen, 1997; March and Olsen, 1989); otherwise we would expect improvements. These insights about limitations to organizational learning come from the cultural-institutional perspective (Christensen et al., 2004), where learning is considered to be a socially constructed rather than technical process.

Learning can be both positive and negative. If there is a positive and significant correlation between the auditees' perception of usefulness and their opinions about the report, the performance audit could lead to positive learning by making them reflect on their current practices.

However, if the auditees' assessments of the performance audit reports point to lack of compliance with these systems, single-loop learning may occur.

One branch of the organizational learning literature

looks into what kinds of intervention are likely to be effective in enhancing organizational learning. Many scholars hold that changes in structures and rules in an organization can bring about desired changes in behavior (Argyris, 1999: 34). Control systems can, on the other hand, also lead to dysfunctional behavior that hinders improvement. Cyert and March (1963) showed how control systems led to conflicts between rule setters and rule followers. Internal power games, for example between leaders of different subunits, can undermine efforts to measure performance and improve organizational efficiency and effectiveness. Often, there are gaps between the intended use of systems to improve organizational performance – such as new formal structures, information systems and procedures – and their implementation and actual use (Argyris, 1999: 51).

### **The link between deliberation and action**

Fundamental to theories of action are peoples' reasoning processes. Communication and deliberation are links to action and can explain change dynamics (Schmidt, 2008). The goal both for performance audit and programme evaluation is to provide objective information on the functioning of political programmes and institutions. Such information can be regarded as a kind of deliberation. Background ideational abilities guide actors' thinking and change will not take place until these ideas are expressed (Argyris, 1999; Bourdieu, 1977; Searle, 1995). If auditees perceive performance audit reports as useful, they may be persuaded to change their systems and practices (Argyris, 1999: 67). Based on this, we would expect changes to occur if reports are persuasive to the auditees and if the auditees buy into the arguments made by the SAIs. The extent to which auditees will actually make the changes that they promise will nevertheless vary with context.

### **Audit frameworks and methods**

Even though programme evaluation reports, as well as performance audit reports, differ in important ways in their institutional set-ups, they both face challenges in addressing funders' (in this case Parliament's) need for information about accountability. One challenge that is well documented in research on performance measurement has to do with problems of measurement (Crawford et al., 2004; Van Thiel and Leeuw, 2002). Another challenge is methodological, and is linked to Logical Frame Analysis (LFA) evaluations. LFA breaks down the logic of a project into a 'chain of causality'. 'Inputs' are invested to facilitate certain predefined tasks in order to produce results.

These results are, in turn, expected to have desirable 'effects' on society.

Discussions of the LFA illustrate how difficult it is to identify causality between political interventions and the changes observed (Crawford et al., 2004). The rise of LFA in ex post evaluation can also be seen as part of 'the audit explosion' that prioritizes external checks using easily quantifiable measures (Gasper, 2000; Power, 1997: 288). In stark contrast to the positivism of the LFA methodology, we find Guba and Lincoln's (1989) constructivist 'fourth generation evaluation', also termed 'action research'. This type of evaluation is participatory and involves the evaluated party in the evaluation process. The bodies under scrutiny are regarded as collaborators rather than subjects to be investigated.

Assuming this role is difficult for SAIs because they must safeguard their independence and role as watchdogs of public resources (Reichborn-Kjennerud and Johnsen, 2011). Still, some SAIs have recognized the need to be more open and responsive and experiment with new methods (Van der Knaap, 2004). When measuring results there is a risk that only what can easily be measured is measured and that what actually matters in the policy area is overlooked. Another challenge is the tendency of the LFA to develop into a 'lock frame', where evaluators are insensitive to change and stick to their initial model. Another problem linked to the LFA model is that it is preoccupied, as is performance audit, with checking whether predefined goals are attained – whereas the most important results were often not preplanned and therefore initially not formulated as goals or reported on during implementation. Because of these weaknesses, Gasper (2000) argues that the LFA model is more suited to planning and communication purposes than ex-post evaluation. In his view, LFAs can lead to dangerous simplifications that can easily be misused and are liable to block rather than aid learning.

### **Variations in the Impact of Performance Audits**

Although performance audits are intended to contribute to improving the operations of the audited entities (Reichborn-Kjennerud, 2015), their effectiveness as an instrument to control and to improve public administration should not be taken for granted (Morin, 2001). Performance audits should produce actions. We will look at impact as the capacity to produce these actions, either by changes in the



practices of the auditee (usually measured by the implementation of recommendations) or by influencing the political debate (usually measured by the amount of attention gained in Parliament; Lonsdale, 2000). As a result of increasing interest in the impact of performance auditing, academics have looked at it from different perspectives (Van Looke & Put, 2011).

Some authors focus on its effects at the macro-level, analyzing its impact in terms of fiscal policy, government effectiveness, and capital productivity (Blume & Voigt, 2007; Schelker, 2008). At the microlevel, a common measure of this impact has been the recommendations implemented (Alon, 2007; Brown & Craft, 1980; Hatherly & Parker, 1988; Johnston, 1988; Milgrom & Schwartz, 2008). Pollitt et al. (1999) find that the proportion of recommendations of performance audit reports implemented is the most common measure of effect used by the UK National Audit Office, the Swedish Riksrevisionsverket (RRV), and the Dutch Algemene Rekenkamer (AR). Similarly, Van Looke and Put (2011) indicate that the European Court of Auditors found that the most commonly used indicator of the impact of performance audits is the recommendations implemented or accepted. Morin (2001, 2004, 2008) and Reichborn-Kjennerud (2013, 2014, 2015) measure the impact of performance audits based on the opinions of the auditees and on their contribution to the public debate. Performance audits, like many public sector reforms, are often criticized for not leading to action (Bouckaert & Peters, 2002; Streib & Poister, 1999; Torres, Pina, & Yetano, 2011). The challenge that audit institutions must overcome is the lack of implementation of their recommendations (van Zyl, Ramkumar, & de Rencio, 2009).

To interpret the adoption (real and rhetorical) and adaptation of public sector initiatives, institutional theory has been extensively used by academics in recent years (Johnsen, 2005; Pina, Torres, & Yetano, 2009; Ribeiro & Scapens, 2006). This theory is mostly concerned with the diffusion and spread of organizational models within a given organizational environment and with understanding organizations within larger social and cultural systems (DiMaggio & Powell, 1983; Oliver, 1991). It assumes that a common way of gaining legitimacy is an alignment with rationalized institutional myths (Meyer & Rowan, 1977). Isomorphism, a concept embedded in institutional theory, can be used to predict that audit institutions would adopt performance audit as a "symbol" of efficiency and modernity.

This prediction seems to be confirmed by the international diffusion of performance auditing. This adoption of internationally recognized "good practices" often creates a gap between rhetoric and reality (Pina et al., 2009). This gap or decoupling from the expected objectives is underpinned by the historical and sociological approaches of new institutionalism which suggests that the functioning and performance of institutions are historically and culturally embedded. Thus, it can be expected that performance audit may be a rhetorical instrument, in some cases, rather than a vehicle for change.

The variety of practices of performance audits (Shand & Arnberg, 1996; Tillema & ter Bogt, 2010) suggests that there is not only a dichotomy of rhetorical versus instrumental implementation (Burns & Scapens, 2000; Siti-Nabiha & Scapens, 2005) but also different ways of introducing performance audits that lead to action. The concept of logic4 could explain variations in the impact of performance audits. Lounsbury (2008) argued that the study of variations in practice should be focused on the primacy of culture, rather than relying on mimesis (Lounsbury, 2008; Lounsbury & Ventresca, 2002). The socio-cultural contexts of organizations facilitate cognitive, normative, and regulative pressures that fundamentally shape organizational behavior (Scott, 2008). As a result, pressures of the institutional environment for the introduction of performance mechanisms may result in different configurations of the "same" reform. This approach implies substituting the idea of "diffusion as imitation," which involves the spread of a certain model to a number of passive recipients (Campbell, 2004), by the organizational adoption of reforms carried out by intelligent, performance-oriented managers who are conditioned by the cultural context.

Institutional environments are influenced by multiple and competing logics (Friedland & Alford, 1991; Lounsbury, 2007), which, as shown by Lounsbury (2007), explain the various configurations of performance audit, "the variations on a theme" (Hood, 1995). The New Public Management (NPM) promoted a performance logic, or managerial logic (Reichborn-Kjennerud, 2014), that became embedded with other logics, rooted in geographical and cultural differences and broader belief systems. The logic based on culture explains variations in practice and provides legitimacy to specific actions and solutions (Friedland & Alford, 1991; Lounsbury, 2007). Pollitt et al. (1999) argued that performance audit was more fruitfully adopted by countries with a common law tradition than by those

with a strong administrative tradition.

Different logics, like different public administration styles, lead to different approaches to performance audits that affect their impact and effectiveness. The national context of public administrations is frequently used to explain variations in public sector reforms (Dunleavy & Hood, 1994; Kickert, 1997, 2005; Pina et al., 2009; Pollitt & Bouckaert, 2011). The public administration style is an institutional logic, represented by the organizational and administrative culture, historical background, and legal structural elements (Pina et al., 2009), which is usually shared by a group of countries. A managerial logic is associated with Anglo-American countries while a state law logic is associated with Continental European countries (Reichborn-Kjennerud, 2014). The Anglo-American countries seem closer to performance-driven ideas, such as performance audits, while Continental European countries have been structurally and culturally less hospitable to this kind of reforms (Pina et al., 2009; Pollitt & Bouckaert, 2011). However, Continental European countries have also responded to environmental pressures for improving public services by developing their own mix of reforms (Pollitt & Bouckaert, 2011).

Anglo-American countries were more active in introducing performance budgeting, full accrual accounting, and performance measures. Audits were divided into financial-compliance audits and performance audits (Pollitt & Bouckaert, 2011). Nordic countries have followed a similar model of public sector reforms; Sweden was considered a leader in the diffusion and implementation of effectiveness audits (Pollitt et al., 1999). Continental European countries aimed to modernize their traditional bureaucracy by making it more professional, efficient, and citizen friendly, but they considered traditional bureaucracy had virtues that should be preserved (probity, predictability, continuity, close attention to the law). Administrative practice, in Continental Europe, is still marked by an overriding legalistic philosophy where civil servants require specific legal training (Jann, 2003; Ongaro, 2008). The differences in public administration logic are expected to affect the diffusion of Performance Audits (PA).

### Conclusion

This article has investigated the content of performance audits, and linked different types of content to the auditees' reactions, their perceptions of the reports' usefulness, and accounts of

actual changes made in their organizations. Our contribution demonstrates empirically that the auditees actually take the results from performance audits into account (like other forms of evaluation which produce information that feeds into policymaking) and typically regard them as useful. The article contributes to the literature on the impact both of evaluation and performance audits as well as the literature on knowledge utilization and policymaking (Wittrock, 1982). The necessary, but not sufficient, condition for performance audits to generate impact is the legal framework. The absence of legal requirements shows a lack of political will that leads to shortages of resources with which to carry out performance audits. The sufficient condition is the implementation of the recommendations. Otherwise, performance audits become a source of waste and the resources used could be better used for other purposes.

Some financial reforms, especially those related to the budget, accounting, and performance measures, condition the role of performance audits and their consequences. In the UK-Nordic group, the audited entities have cost indicators, performance measures and defined objectives. All this information allows the SAls to carry out economy, efficiency, and effectiveness audits more easily. In the Germanic group, it is more frequent to find cost indicators than performance measures, which explains why the activity in performance audits of the SAls is focused on economy topics.

There is no single way to obtain impacts from performance audits. Institutional theory and the concept of logics/public administration styles help us to understand variations in the practice of performance audits. The Anglo-American model is not the only approach in the EU to carrying out performance audits and implementing recommendations, although it is still the model of reference in many cases. Actions are taken, in the Anglo-American environment, through the direct implementation of the audit recommendations by the audited entities—which requires follow-up processes—and, in the case of Germanic countries, through parliamentary action. Performance auditing usually involves the collaboration of the private sector because both the UK-Nordic and the Germanic groups use external support.

The legal training of civil servants in Continental Europe seems to affect the level of contracting out. Future studies could analyze the savings achieved by these recommendations to conclude whether performance audits are cost-effective. This study considers only one source of variation (Power, 2003) in performance audit practice, that is, the influence of

logics/public administration styles. The configuration of audit institutions as Offices or Courts is a variable that may condition performance audit developments, in this study this effect is embedded in the concept of public administration style rather than studied in isolation. Future studies could analyze this effect in isolation as done previously by Noussi (2012).

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## How has the New Audit Methodology helped SAI Pakistan conduct efficient and effective audits?

**Aamir Fayyaz**

Director HRM

Office of the Auditor General of Pakistan



This article is about SAI Pakistan's incremental implementation of a new risk based audit methodology for conducting efficient and effective audits. An SAI should lead by example and before it comments on the efficiency and effectiveness of client entities in the public sector, it needs to plan and perform efficient and effective audits in the first place. SAI Pakistan has precisely done that in the current decade using the new audit methodology that it adopted under a World Bank funded project-PIFRA that aimed at improvement in Pakistan's public sector accounting and auditing regimes. The new audit methodology is being used at the macro level to select high risk entities for inclusion in annual audit plans of the SAI's two and a half dozen audit directorates and then at the micro level, for planning and performing individual audits of selected organizations. The flagship tool of the new audit methodology is the Financial Audit Manual which is the first in the series of documents that has supported the SAI achieve its mandate by optimally utilizing the limited resources.

This is work in progress and ,as an extension of the earlier reforms, the SAI is currently in the mid of implementing an AMIS- Audit Management Information System- to automate its business processes under another World Bank funded Program for Results (P for R) since 2017.

### How did it work?

Department of the Auditor-General of Pakistan, being the Supreme Audit Institution, derives its mandate from the Constitution which is the highest law of the land. Mandate includes regularity and performance audit in line with ISSAI framework. The Constitution does not recognize any exception to this mandate which covers federal, provincial and district governments. All government ministries, divisions, attached departments, subordinate offices, and autonomous / semi-autonomous organizations, foreign funded projects etc are part of the mandate. Some key statistics of the SAI for the last three years are in Table below:

Description	2015-16	2016-17	2017-18
Total Budget (PKR Millions)	3802	4209	4463
Budget meant for employees(PKR Millions)	2663	2891	3114
Pensioners related (PKR Millions)	94	119	119
<b>Total entities in jurisdiction</b>	<b>47000</b>		
Entities audited	8746	8746	9193
Employees	5387	5392	5407
Amount recovered effected from Government entities (PKR Millions)	80,964	88,569	127,279

A total of some 47,000 clients comprise the SAI mandate! This by all means is a huge responsibility that has been assigned to the Department by the Constitution and amply reflects the trust that the framers of the Constitution had on the audit institution. Correspondingly, the SAI has some two and

half dozen specialized directorates across country to carry out this rather daunting mandate. As we know, resources have always been limited. Out of total budget allocation of 5,365 million rupees for the current financial year 2019-20,71% is meant for employee and pensioners' related

<sup>1</sup>Project to Improve Financial Reporting & Auditing. This was closed in 2015

<sup>2</sup>WB: Report No: 121796-PK, see para 47 (DLI 6)

<sup>3</sup>International Standards of Supreme Audit Institutions, issued by INTOSAI

<sup>4</sup>Annual Reports of the Department of Auditor General of Pakistan for the respective years

expenses. One thing is as clear as daylight that SAI does not have the requisite resources to audit all 47000 organizations every year. During audit year 2017-18, audit of 9193 entities was conducted and actual audit coverage resultantly is just about 20%.

Our basic question is this? If for a given year, the SAI can conduct audit of just 9,000 entities, out of 47,000 entities, then what is the criteria for selection of these 9K entities? Our second related question is: what do we do when we actually audit these 9K entities? Putting it in another way, what is our audit methodology at the macro and micro levels? How do we satisfy ourselves and our stakeholders that, on both these levels, we are focusing on areas of greatest materiality, significance and risk?

Struggling for answers, SAI Pakistan adopted the risk based audit methodology a decade ago. Its incremental implementation has significantly improved several key performance indicators as can be witnessed in World Bank's Public Financial Management and Accountability Assessments of Federal government of Pakistan in 2012 compared with similar assessment of 2009 and 2007.

### What are the key instruments?

**FAM:** One of the key instruments of this new audit methodology was commissioning of a Financial Audit Manual (FAM). This was developed for the SAI by Cowater International, a management consulting firm based in Canada. SAI made FAM compulsory for financial attest and compliance with authority audits in 2006. This was done to address the questions highlighted above and to bridge the gap between what we are supposed to audit (47K entities) and what we actually can and do audit (9K entities). The Manual is the embodiment of an audit methodology in vogue in the financial and compliance auditing around the globe. FAM comprises a series of documents. Firstly, there are two volumes covering the theoretical framework and the auditor's working paper kits respectively. The former gives concepts, standards, auditing techniques whereas the latter comprise four working files. These are known as Permanent, Planning, Execution, & Evaluation and Reporting files. These provide assistance to the audit teams when they plan, execute, evaluate and report the results of an individual audit and systematically document these as

well. Secondly, there are twenty sector specific Audit Guidelines addressing individual requirements of some of the individual directorates that I mentioned earlier.

**Macro and Micro level planning:** Using FAM, the individual directorates plan their audit assignments at macro and micro levels: Level –I: Prepare risk based annual audit plan i.e. what to audit in a year? How do we select 9 K entities out of 47 K entities? Each of these directorates prepare their Annual Audit Plans where in they define the basis of selection of organizations for audit in a year. Several factors are kept in view for selecting and ignoring organizations. This provides a near scientific basis of selection of organizations, against pre-determined benchmarks. These benchmarks are not static and continue to change on yearly basis. Sometimes a Scoring System is used which rank the organizations against quantitative materiality (e.g. large expenditures or revenues), relevance of the organization to the Sustainable Development Goals, sensitive issues for public, media visibility of organizations, development projects, public private partnerships, etc. Sometimes instead of scoring system, set of issues are identified at the SAI level and then selection of an organizations is made which may involve more than one directorate. Level: II- The methodology now works its way up to help prepare individual audit plans for the selected organizations i.e. focusing on what to audit in a particular government entity? Take, for illustration purposes, SAI Pakistan's one Audit Directorate 'Provincial Audit Directorate'. The SAI has given it mandate to audit some 3K provincial government entities. Using methodology of level-I, "Provincial Audit Directorate" has selected 500 entities out of 3 K. Now audit teams will be assigned audit of these entities.

**Desk auditing and using ACL:** As per tradition, audit will be conducted at the premises of these entities. SAI's risk based audit methodology however does not allow audit teams 'go out' unless they have performed Desk Audit and only where they have done the following activities under close supervision of senior audit managers.

» Developed a fuller understanding of the entity and then documented this understanding in the Permanent and Planning Files of the selected organizations. For the time being (as AMIS is not

<sup>5</sup>USD 34 Million @ 1 USD=155 PKR

<sup>6</sup>Information is from respective year's Annual Report of DAGP. Available at [www.agp.gov.pk](http://www.agp.gov.pk)

<sup>7</sup>WB: Report No. 69185-PK, See para 3.145.

<sup>8</sup>WB: Report No. 39761-PK, see para 3.6.1

<sup>9</sup>The original version was revised in 2012 to incorporate the full ISSAI framework, all four levels, adopted by the SAI in 2010.

available) this work is done manually or these files are typed and stored as MS Word files in the computers.

» Analyzed available data using a licensed software Audit Command Language (ACL) which increases the effectiveness of audit as auditors already have a fair idea of what to examine when they are out in field. This considerably reduces person- hours allocated to audits resulting in economic and efficient audit.

» Determined sample size and made its selection using approved sampling methods only and using ACL. Earlier this was not the case and auditors used to draw sample manually when they were actually in the premises of the audit entity. Now they convey the sample before-hand to client so that the record is available to them on their very first day. This also reduces level of effort on the part of audit teams.

### Conclusion

SAI Pakistan has been entrusted with huge mandate to conduct audit of some 47K public sector entities. Adoption of the risk based audit methodology has paid dividends in the form of increased efficiency and

effectiveness. Coverage may be just about 20% but, thanks to the methodology, only high materiality and high risk organizations and issues are selected. In the audit year 2018-19, SAI recovered from government departments 91.5 billion Pakistan Rupees utilizing its scarce budget of just 5.596 billion Pakistan Rupees. Thus it paid back to the government over Rs16 for every single rupee spent on it. Similarly, because of strong desk audit and focus on high risk and high value transactions, the SAI has improved its reporting to the legislature and for the past many years, audit reports are being presented within 8 months of the close of preceding financial year. The on-going efforts for automation of audit business processes will further contribute to SAI efficiency and effectiveness. Additionally, efficiencies gained in the regularity audit exercise are being utilized by the SAI in creating more space for increasing the number of performance and specialized audit assignments relating to education, health, environment, social safety, information technology. This trend is expected to establish and strengthen the bond between the citizens and the SAI which in turn will lead to more effective audits.

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<sup>10</sup>SAIs audit year is from July to June

<sup>11</sup>Permanent and planning Files are part of Audit Working Paper Kit

<sup>12</sup><https://www.urdupoint.com/en/business/agp-recovers-over-rs91-billion-from-various-g-664518.html>



## Use of Big Data in TCA Audit with respect to the Municipalities

**Mr. Umutcan METİN**

Auditor

Turkish Court of Accounts (TCA)



### 1. CONCEPT OF BIG DATA

As a concept, which was first used in 1990s but gained popularity in 2000s, big data refer to data that are meaningless when they are used alone but make sense when they are combined, are called as 5 (V) and have features of variety, velocity, volume, veracity and value. Use of big data has increased in many fields from astronomy to genetics and from private sector to public sector since 2011, and they came into use in many fields.

Data can be defined as unprocessed information, which does not make sense alone but needs to be associated, grouped, interpreted, and analyzed for forming the basis for information.

Big data are data collections that are obtained from traditional and digital sources and require analysis and examination.

Today big data are used in a variety of scientific fields, economy, audit, health, communication and education and progress every passing day. These developments certainly change depending on the technological tools and data production ways of these tools.

Big data can also be defined as data sets and analytic techniques that require complex and developed data storage, management, analysis and visualisation technologies, cannot be stored in a data warehouse, are variable and continuously flow. They need qualified technology and analytic methods and stand out with their features of volume, variety, velocity, veracity and value.

### 2. CHARACTERISTICS OF BIG DATA

While big data were previously referred to as 3V, it has come to be known as 5V with the addition of new features in recent years.

These crucial features of big data, which are referred to as 5V, are explained in detail as follows:

**1-Volume:** Volume refers to the size of structured or unstructured data in huge amounts. In other words, big data emerges when data sets that cannot be analyzed by using database management systems or traditional software programs are combined. About 10% of big data consist of structured data while 90% are unstructured data.

Examples for unstructured data include:

Data obtained from social media, data obtained through telephone services, electronic mails, web sites accessed, videos watched, audio tracks listened etc.

The volume of big data obtained by big companies, public institutions and states is measured in petabyte. A petabyte is equal to about 10<sup>15</sup> byte (character) information. This shows us that warehouses where these data are kept accommodate data stored in 1 million and even 10–20 million personal computers.

**2-Variety:** This characteristic shows that big data are data which are not uniform, are in different sizes, can be obtained from internal and external sources and also that a part of these data are structured while the vast majority are not structured. For instance, these are data concerning the tendencies of people concerning their expenditures, their hobbies, socio-cultural relations and financial and non-financial areas.

**3-Velocity:** The velocity of big data can be defined as the fact that new data are generated from the existing ones in a constant manner and useful outputs are obtained by processing these data.

**4-Veracity:** As mentioned previously, while big data had features referred to as 3V when it first emerged, it came to be known as 4V with the addition of the feature of Veracity. In short, Veracity is the fourth characteristic that big data acquired.

The data to be used should be orderly, safe, verifiable and reliable data. Only under these conditions, big

data can bring great benefits to the users.

**5-Value:** This fifth feature refers to the value creation power that the institutions benefiting from big data gain owing to the use of big data. It is of great importance that the beneficiaries of big data can reach the desired outcomes in an easy and efficient manner. This is because of the fact that the obtained value increases benefits and also creates new opportunities.

### 3. Importance of Big Data in Audit

As audit has a great importance in all parts of the life, it is of paramount importance in the public sector. In particular, the audit of budget, which is crucial for the power of the purse, is conducted by the Turkish Court of Accounts (TCA) in Turkey.

TCA audit is highly important so that public funds are properly used and public revenues are obtained completely and in a timely manner. TCA, which conducts audit on the public institutions and entities in Turkey, benefits from the advanced technology and uses technology for conducting its audit more efficiently in line with its vision.

As a result of digital revolution, E-State Project was launched in Turkey in 2006. With the implementation of E-State by the public institutions in Turkey, their data have become accessible and processable in the electronic environments. This development provides the TCA with the necessary convenience and data for the analysis of big data.

We have stated that the complete development and generalisation of the concept of big data, which emerged as a result of the developments in the 1990s, date back to the years after 2010. Right at this point, the TCA closely followed these developments, formed a dedicated audit group and started to conduct big data analyses. The TCA obtains data for such analyses both from internal and external sources.

As of the end of 2018, Turkey is a big country with a population of 82.003.882 persons, and its 2019 budget has 961.000.000€ as expenditure and 880.400.000€ as revenue. As it is expected, in a country like Turkey which has a large population and budget, the audit of public institutions is of great importance.

How can the audits be conducted more effectively in a country with such a large population and budget?

The answer to this question is having well-trained auditors and benefiting from technology by closely

following the advancing technology.

### 4. Use of Big Data in the TCA

Owing to the technological developments and TCA's future vision, in addition to the applications such as ACL and Access used by the auditors in the analysis of data, a special Data Analysis Group consisting of auditors experienced in Information Technologies was established in the TCA in June 2017.

The mission of this data analysis group is as follows:

Developing a methodology for the use of computer-assisted audit systems and making the implementation of computer-assisted audit techniques in audits widespread.

Within the framework of this mission, the Data Analysis Group fulfills the following tasks:

- 1) Determining the activities required for conducting computer-assisted audits;
- 2) Creating risk scenarios which might help risk assessment among municipalities;
- 3) Conducting audits by using accounting data;
- 4) Creating scenarios with the aim of controlling wage calculation systems in the electronic environment;
- 5) Performing financial statement analyses;
- 6) Facilitating the access of auditors to data through their works;
- 7) Conducting data confirmation controls.

Accounting audits and data confirmation works assist audits by determining inconsistent account areas by controlling the consistency of the data related to the accounts. In this way, debt-receivable relation within the accounting system is reviewed and whether accounts not included in the account plants have been used is controlled. 104 accounting analyses were determined for the conduct of these works.

With the control of wage accounts, whether there are extra payments or inconsistencies in personnel payments and whether extraordinary transactions have been carried out are checked, and the results are shared with the auditors auditing the relevant entity. 71 payroll analyses were determined for the conduct of these works.

To this end, the group conducts works for determining

the definitions of data sets and format and presentation form of the data sets required.

Group uses VERA "Turkish Court of Accounts Data Analysis and Business Intelligence System". Although this system is a central and web-based system, it is open to the use of all auditors. Thanks to this system, collection and analysis of big data are possible.

Group uses risk assessment system and analysis scenarios, as well. 114 risk scenarios were determined to be used in this analysis. Thanks to these scenarios, the TCA management can determine the municipalities to be covered by the audit and the audit strategy to be used. After the works are conducted for the entities that are planned to be included in the audit, risky areas determined in the municipalities covered by the audit plan are taken into account by the auditors in the audit planning and execution phases. Data provided for the audit are also reviewed in accordance with the pre-determined parameters. In addition to this assurance, auditors themselves can do research, as well.

This special data analysis group established within the TCA enables auditors to conduct audits by benefiting from big data and can lead other auditors with its works. Furthermore, this group makes risk analysis through the analysis of the obtained data, and this analysis can be used in the determination of the entities to be included in the audit scope.

Apart from these, a system called "BVAS" was developed to ensure the transfer of the data of municipalities. This system was activated in 2017, and

the data of more than 1250 municipalities were safely uploaded in this system until 2018.

## 5. Conclusion

It is beyond doubt that the use of innovations brought by technology in the audit makes audit work easier and more efficient. As a result, the use of big data has become an indispensable area for the TCA, and thanks to big data, risk-driven audits are carried out by directing the auditors to risky areas.

### For instance, in the future;

In the municipality audits, auditors can conduct compliance audit on the status of those working in the entity for benefiting from the family allowance by reaching the Social Security Institution data for these persons. In this way, public loss can also be detected if there are employees benefiting from family allowances despite the fact that their spouses are employed. Apart from this, if there are employees in the worker cadre benefiting from education or child allowances, whether they are benefiting from these allowances properly will be easily checked in the future. Furthermore, for those who reside within the service areas of the municipality and enjoy property tax exemption, whether they have properties registered to their names in the land register and whether they enjoy exemption in a rightful manner can be checked, and public loss can be determined.

As can be clearly seen from the examples, audits that would consume too much time of the auditors can be conducted in an easier manner through the use of big data analyses.

## Assessment of Internal Control Systems

**Ms. Vildan KARABOĞA**

Senior Auditor

Turkish Court of Accounts (TCA)



Assessment of the internal control system is one of the major tasks of supreme audit institutions (SAIs) and contributes to the effectiveness of the audit activity. International standards on auditing state that the internal control systems of entities should be recognized so that the environment in which the entity operates is understood and thus, risks affecting or having the potential to affect the entity are determined.

### What is Internal Control?

Following the significant changes in the public financial management and control in recent years, a transition from central controls to internal control has taken place. COSO (The Committee on Sponsoring Organisations of the Treadway Commission) developed the internal control understanding, which was used first by the private sector and then was adopted by the public sector as a managerial tool. Therefore, the internal control model is known as COSO model. COSO model is an internal control model accepted and implemented by the European Union and the International Organisation of Supreme Audit Institutions (INTOSAI). COSO developed the internal control concept, and internal control was divided into components.

Based on the COSO definition, internal control is a process conducted by the board of directors, management and other personnel of an entity and designed to provide reasonable assurance on the achievement of targets related to the operations conducted, reporting and compliance. Internal control is a managerial tool for the realisation of the objectives of the entity. It aims the achievement of the objectives related to the operations conducted, reporting and compliance. All decisions and actions taken by the entities with the aim of achieving their targets and objectives constitute internal control. Internal control is a process and also a tool used for achieving the objectives. Internal control refers to a process in which not only the policy makers but also all the personnel from senior executives to the lower level employees

take part. Internal control can provide the senior management and board of directors of an entity with reasonable assurance but cannot give absolute assurance.

In the COSO model, internal control consists of five components. These are control environment, risk assessment, control activities, information and communication, and monitoring.

### Why is Understanding the Internal Control Systems Important in the Audits of the SAIs?

Supreme audit is an activity regulated by international standards. Achieving standardisation at the international level is of great importance for the quality and standardisation of audit. The standards on auditing adopted by INTOSAI emphasizes the importance of understanding the internal control system. INTOSAI prepared and published the International Standards of Supreme Audit Institutions (ISSAIs) for the use of all member SAIs in the planning, execution and completion of the audit process. ISSAI 100 addresses the "Fundamental Principles of Public Sector Auditing", ISSAI 200 addresses the "Fundamental Principles of Financial Auditing", ISSAI 1315 is titled "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment" and ISSAI 1610 addresses the issue of "Using the Work of Internal Auditors" in detail.

Both ISSAI 100 on the Fundamental Principles of Public Sector Auditing and ISSAI 200 on the Fundamental Principles of Financial Auditing state that it is necessary to obtain information about the audited entity and examine its objectives, activities, environment in which it operates and internal controls, financial and other systems and work processes in detail in the public sector audit and in financial audits, in particular.

Understanding the entity and its environment ensures that the auditor plans and executes the audit in an effective manner.



Risks that an entity faces are evaluated after information is obtained about the entity and internal controls are evaluated in detail. The reaction of the management to the risks determined and the implementation and design of the internal controls to address these risks become important. It is stated in the standards that the control environment should be understood to evaluate internal controls and to this end, practices of the audited entity with respect to integrity and ethical values, competency of the personnel and commitment of the management to the targets, participation of those responsible for management, philosophy and working style of the management, organisational structure, existence and level of internal audit activities, authorities and responsibilities should be determined and human resources policies and practices should be examined.

ISSAI 1315 on Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment aims at determining and assessing the material misstatement risks resulting from fraud and error at the level of financial tables and statements through the understanding of its environment and internal control conditions and in this way, designing and implementing actions to be taken against material misstatement risks assessed in terms of impact. ISSAI 1315 defines internal control as a process designed, implemented and maintained by those responsible for management, executives and other personnel with the aim of providing reasonable assurance about the achievement of objectives related to the financial reporting reliability of an entity, effectiveness and efficiency of its operations as well as their compliance with the relevant legal and administrative regulations. In this standard, how an auditor obtains information about internal control and assesses each component of internal control is explained in detail. Making an examination on the basis of the five components of internal control provides auditors with a useful framework for the assessment on how different aspects of internal control affect audit. Understanding the control environment is important to assess whether this component forms a proper basis for the other components of internal control and other components are weakened by the weaknesses in the control environment. With risk assessment, risks that the entity may face and actions taken by the entity for preventing these risks are examined. In terms of information and communication, information is obtained about the information system concerning financial reporting in the entity, duties and responsibilities of the entity

regarding financial reporting as well as how the entity informs important issues about financial reporting. Control activities need to be examined to assess material misstatement risks at the level of statement and to design additional audit procedures for preventing the risks assessed. Within the scope of the monitoring component; activities for the regular monitoring of internal controls, the nature of the responsibilities related to the internal control function in case of the existence of internal control activities, whether the internal control function complies with the organisation structure of the entity and the activities conducted or to be conducted by the internal audit function are examined. Also, ISSAI 1610 addresses how to use the works of internal auditors in detail.

### **Activities Conducted for Understanding the Internal Control System in the Regularity Audits Performed in Turkey**

In Turkey, the main law regulating the public financial management system is the Law no. 5018 on Public Financial Management and Control, which entered into force in 2006. This Law determined the fundamental principles of public financial management. Law no. 5018 contains detailed provisions on the objective, structure and functioning of internal control with the aim of ensuring that internal control systems compliant with these provisions are established in the public entities. Public Internal Control Standards were prepared to determine the main rules that the entities need to consider in the establishment, monitoring and assessment of the internal control systems. Public entities are responsible for establishing and implementing the internal control systems in line with these arrangements.

In our country, the TCA assesses the financial management and internal control systems of the entities through the regularity audits performed in line with the TCA Law no. 6085. At the planning phase of the audit, audited entities are understood and internal control systems are examined. Understanding the audited entity is the main and most important phase of the audit process. Achievement of the audit target depends on the results to be obtained in the planning phase. Audit process is designed on the basis of the conclusion reached with the examination of the internal controls. In regularity audits, reasonable assurance is obtained about the financial reports, statements, accounts and transactions of the entity by assessing internal controls and examining accounts

If it is concluded that internal controls are reliable, it is assumed that internal controls give reasonable assurance, and financial confirmation assurance is obtained by examining accounts and transactions. When assurance is obtained from internal controls, works to be done to obtain financial confirmation assurance decrease. In case that sufficient assurance cannot be obtained from internal controls, a higher number of accounts and transactions are examined to obtain financial confirmation assurance.

Auditors obtain information about the internal controls of the entity through the procedures carried out during the audit as well as the internal control system assessment form. With the understanding of the internal control, risks that may prevent the entity from achieving its objectives are specified, and areas to be focused during the audit are determined. The procedures in the phase of understanding the entity are assessed by examining the environment, information system, internal control system, internal audit activities and information systems controls of the entity.

Furthermore, a more detailed examination is conducted within the framework of questions prepared on the basis of five components of internal

control through the internal control system assessment forms. The form shows the results of the assessment conducted by the auditors based on the information obtained from the examinations made in and discussions held with the entity. Answers given by the auditor to the questions in the form lead to a conclusion about the effectiveness of the internal control system in the public entity. Also, a total score is obtained for each entity by giving scores between 1 and 5 to the answers given to the questions in the form. It is possible to have an idea about the actions taken by an entity for the development of internal control on the basis of the progress of these scores by years. This scoring also allows a comparison between the entities.

The TCA audit has a key role in the establishment of an effective internal control system consistent with the criteria envisaged in the legislation in the public entities. In the detailed assessments and audits conducted by the TCA, findings are obtained with respect to the establishment and effectiveness of the internal control system; deficiencies, if there are any, are revealed; and counselling activities are carried out with a focus on these areas and entities. Also, a great importance is attached to good practice examples, and activities for making such practices widespread are carried out.

<sup>1</sup>COSO-(2013), *Internal control Integrated framework*

<sup>2</sup>IN TOSAI, ISSAI 100 *Fundamental Principles of Public Sector Auditing*, ISSAI 200 *Fundamental Principles of Financial Auditing*, [www.issai.org](http://www.issai.org)

<sup>3</sup>INTOSAI, ISSAI 1315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, [www.issai.org](http://www.issai.org)

<sup>4</sup>INTOSAI, ISSAI 1610 *Using the Work of Internal Auditors*, [www.issai.org](http://www.issai.org)

# Municipal Corporations and Supreme Audit Institutions: Practices in the World and Turkey

**Mr. Atila KILIÇARSLAN**

Senior Auditor

Turkish Court of Accounts (TCA)



## 1. The Situation Of Municipal Corporations In The World

The European Charter of Local Self-Government, which was adopted by the European Union and took effect in 1998, aims at providing the local governments with stronger and more democratic structures. Envisaging the reinforcement of local government as a requirement of identifying the demands of the people electing the local government more closely, the European Charter of Local Self-Government was adopted by Turkey, as well, and put into effect on 01.04.1993. In this document, Local Self-Governments are defined as governments granted the right and authority to arrange and manage a significant portion of public works under their responsibilities and in line with the interests of the local population within the limits determined by laws.

European Union (EU) took further measures to ensure the implementation of the principle of decentralisation. The implementation of this principle required strengthening municipal corporations along with municipalities. This is because of the fact that the hierarchical effect of the central government on the municipalities is higher than its effect on the municipal corporations.

In general, in Turkey, what determines the line between the Turkish Court of Accounts (TCA) and the public entities is the concept of expediency. While the TCA audits whether the public entities in Turkey deliver their services in accordance with laws, it cannot assess whether these services are necessary or not. In this respect, the EU acts in parallel to the practice in Turkey and has refrained from determining general principles and rules in terms of the municipal corporations that the

Member States use in the delivery of local services. In this case, each EU Member State adopted different practices in terms of their attitudes to the municipal corporations within the framework of their financial structures, experience and views. While some Member States (like the Netherlands, Hungary) behaved timid for the establishment of municipal corporations, a large number of municipal corporations have been established in countries like Germany and France.

The number of municipal corporations was highly limited in Turkey in the past, but every municipality (including district municipalities) established a company as per the Decree Law no. 696 (publicly known as the subcontractor law) and now countless municipal corporations operate in the commercial arena. These different practices have impact on the audit of municipal corporations, as well.

In some Member States, municipal corporations are audited by the commissions/committees established by the municipalities to which the corporations are affiliated while local audit committees audit the municipal corporations in some countries. Apart from this, in some other countries like Germany, municipal corporations are audited by the SAI just like in Turkey. Finally, in some countries, local audit offices are established, and municipal corporations are audited by these offices.

The following table shows the audit procedures applied to the municipal corporations in some EU Member States (Hasan ÖZÇELİK; Doctoral Dissertation: Municipal Corporations in the European Union and Turkey: A Study on the Municipal Corporations of İstanbul Metropolitan Municipality).

<b>Countries</b>	<b>Type of Audit on Municipal Corporations</b>
<b>Austria</b>	Management control by the local government and the charter of the Union may permit the right to veto or approve for local government ( personnel management)
<b>Belgium</b>	Post-action control of the local government (budget, decision making) Audit control at federal levels
<b>Czechia</b>	State control for some public services
<b>Denmark</b>	Control by the local government Legal control of the Ministry of Industry for the companies within the scope of the Law no. 384  Legal control of the Ministry of Interior for the companies within the scope of the non-written local government laws or the Law no.383.
<b>Estonia</b>	Supervisory committee consisting of the municipality councillor State Audit Office (financial control over property and aids) The approval of the municipal council is needed for important decisions.
<b>Finland</b>	Special power to regulate for some activities; for energy, state control in the electricity market
<b>France</b>	Control by the local government Post-execution control by the state representative (SAI)
<b>Germany</b>	Control by the local government and upon request, control by the local audit authority (local government control with respect to the efficiency of the representatives in the corporations), (SAI).
<b>Greece</b>	Local government budget audit State legal control (Ministry of Trade)
<b>Hungary</b>	Municipality control committee consisting of the municipal councillors Municipality finance committee and other possible special committees based on the decision of the municipal council
<b>Ireland</b>	Ministry of Environment Local government General Auditor Monitoring committees within the framework of the National Development Plan authority with respect to the national and local public services



<b>Italy</b>	Control over the activities of the corporations by a special regulatory In recent years, regulatory authorities for the gas and electricity sectors (the same for the two sectors)
<b>Latvia</b>	Annual reports approved by the local government audit committee (not mandatory) Control of the state audit office
<b>Lithuania</b>	Municipality control authority for a company the total capital of which is owned by the municipality (100%) State control authority for municipal corporations and mixed capital companies
<b>The Netherlands</b>	Control by the National Audit Commission for companies owned by the local governments and the State Auditors one third of whom are appointed by the local government
<b>Poland</b>	National control office
<b>Portugal</b>	Approval of the local government is required for all main decisions of the corporations (budgets, management report, loans etc.)
<b>Slovakia</b>	Prior approval of the municipal council is required for all important decisions
<b>Slovenia</b>	Local control committee appointed by the municipal council Court of Auditors
<b>Spain</b>	Approval of the local government is required for the estimated budgets and budget expenditures Control over the accounts of the corporations by the National Audit Commission
<b>Sweden</b>	Control by the local government Control by the citizens The principle of free access to the administrative documents of corporations (Law no. 1980 on Official Secret), Ombudsman
<b>United Kingdom</b>	Control over the loans of the corporations under state control by the State Control by the local government auditors

On the other hand, there is no uniformity among the EU Member States in terms of the legal status of municipal corporations. Municipal corporations carry out their activities as legal entities operating in accordance with the provisions of the commercial code fully independent from the municipalities in some countries as in the case of Turkey while they operate as a subsidiary/affiliate like an organ of the administration in some countries.

## 1. Status of Municipal Corporations In Turkey

### 2.1. The Need to Establish Municipal Corporations

As entities using public resources, the municipalities have to operate under the rules of law that are stricter than the rules that bind the private law legal entities. For example, while a company can act quite freely in recruiting personnel, the municipalities are obliged to comply with the Civil Servant Law no.657 and other personnel legislation in recruiting personnel. Of course, this obligation requires more procedures (written exam, oral exam etc.) and, while people discuss whether it has faults or not, these procedures cause public entities to spend more time and effort while implementing their activities. Due to many such reasons, municipalities that use public resources become inclined to establish corporations. We can list those reasons as follows:

- To be able to move more freely in resource utilization.
- To be able to move more freely in employment policy.
- To ensure that public resources are used more effectively and efficiently by ensuring flexibility and rapidity in activities.
- To avoid the TCA audits etc., which are considered a control power on decentralization.
- To benefit from the experiences of workers that gained important experiences in the private sector.
- To be able to act more quickly in the procurement of goods, services and construction works.
- To avoid the strict attitude of the personnel laws in terminating personnel.

- To decrease the cost of produced goods and services to gain competitive power in the free market.
- Corporations can make a profit and transfer it to the municipalities.
- To create synergy with the people residing within municipal borders by bringing other local resources and municipal resources together,
- To ensure that the products produced intensively by the private sector and needed by the whole public (milk, bread etc.) are delivered to the public more economically.

### 2.2. Establishing Municipal Corporations

In Turkey, the legislation that allows for the establishment of municipal corporations consists of the Municipal Law no.5393 covering the duties, authorities and responsibilities of municipalities and the Metropolitan Municipality Law no.5216. Both laws state that municipalities can establish corporations in their own duty and service areas according to the procedures specified in the relevant legislation.

Here, the most significant issue is that the municipalities are allowed to establish corporations that operate in "their own duty areas". The duty areas of municipalities are defined clearly in their relevant laws, and the basic characteristic of these duties is that they aim to meet the common local needs. TCA audits regarding the municipal corporations found that one municipal corporation made expenditure to carry out helicopter taxi activity. While one might think that the Commercial Law does not prevent municipal corporations, which operate as private law legal entities, from carrying out air transportation in addition to bus, tramway and metro as means of passenger transportation, it is clear that passenger transportation with a high-cost means of

transportation such as helicopters does not meet a common need. Consequently, the main purpose of the corporations established by municipalities should be to meet the common local needs within municipal borders.

Turkey has a very interesting practice regarding the ownership of corporations by municipalities. The main law on the establishment of municipal corporations is Article 26 of Law no.4046 on Privatization Practices. According to this law, establishment of corporations by municipalities or their contributions to the capital of corporations that exist or will be established is subject to the permission of the President of Republic. That means if a municipality wants to establish a corporation or become partners with one by contributing to the capital; it has to get a permission from the President of Republic.

Not let us talk about the interesting practice mentioned in the above paragraph: In one of its decisions, the Council of State decided that when a company was donated to the municipality and thus, the municipality operated under Turkish Commercial Law as the owner of the relevant corporation, this was not illegal. That means, if a person establishes a corporation and then grants it to a municipality, the municipality will be the owner of this corporation and can operate in the commercial area. While the relevant decision of the Council of State broke the system stipulated by Law no.4046 and created a loophole, it was born in the legal realm and has been practiced since the date of this decision. In this scope, either the condition of getting a permission from the President of Republic in Law no.4046 should be revoked or a new law should forbid municipalities from acquiring corporations through grants.

## 2. TCA AUDIT OF MUNICIPAL CORPORATIONS IN TURKEY

The purpose of Law no.5018 on Public Financial Management and Control, which entered into force in 2003 is to regulate structure and functioning of the public financial management, preparation and implementation of the public budgets, accounting and reporting of all financial transactions, and financial control in line with the policies and objectives covered in the development plans and programs, in order to ensure accountability, transparency and the effective, economic and efficient collection and utilization of public resources.

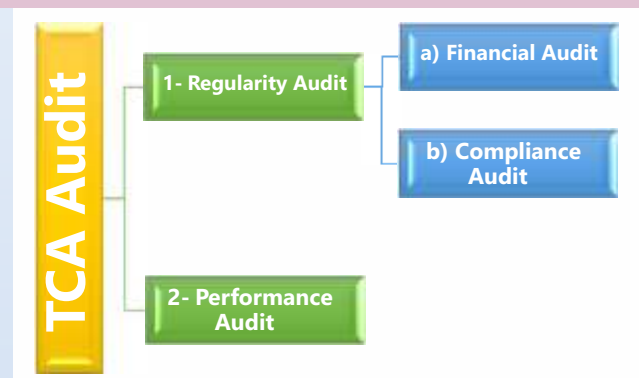
The most important tool used by this Law no.5018 to achieve this purpose is "external audit", which is

expressed in Article 68 of this law. According to this, the purpose of the ex-post external audit to be performed by the TCA is to audit the financial activities, decisions and transactions of management in terms of their compliance with the laws, institutional goals, objectives and plans, and to report their results to the Parliament within the framework of the accountability of public administrations within the scope of general government.

Here, it is first necessary to specify the public administrations within the scope of general government. Such public administrations were specified in paragraph (a) of Article 3 of Law no.5018, and local administrations were included in the scope of general government. In this framework, it is clear that the external audit of the local administrations shall be performed by the TCA. However, how about the municipal corporations? Will the external audit of those corporations be performed? If so, how will the methodology be?

### According to Law no.5018, external audit is performed by;

- a) Performing financial audit on the reliability and accuracy of financial statements, and determining whether the financial transactions related to revenues, expenditures and assets of public administrations comply with the laws and other legal arrangements, on the basis of public administrations' accounts and relevant documents,
  - b) Determining whether the public resources are used in an effective, economic and efficient way measuring the activity results and evaluating them as to their performance.
- The following table indicates the schema of external audits.



As the above table indicates, if an administration is subject to TCA audit, it goes through the following

audits, bar the exceptions, and the audits will result in the preparation of reports stipulated by the TCA Law no. 6085. However, there will be exceptions as indicated.

In the light of this perspective, for the audit of municipal corporations, first, we need to consider whether they fall under the scope of the TCA audit.

According to the general perspective of INTOSAI Auditing Standards, the SAIs have the legal infrastructure to audit all public funds.

Based on this framework, it is necessary to evaluate the limits of the audit area of the TCA. Article 4 of TCA Law no.6085 specifies the audit areas of the TCA very extensively. According to this, the TCA has the authority to audit the local administrations including municipalities and all types of administrations, organizations, institutions, associations, enterprises and companies affiliated to or founded or partnered

by these administrations directly or indirectly.

With the enforcement of TCA Law no.6085, municipal corporations became subject to the TCA audit, and they were audit in 2014 for the first time. In this framework, the TCA performed financial audits of 59 municipal corporations from 2014 to 2017. Before Law no.6085, municipal corporations were not audited by the TCA. These corporations were audited by the private sector just like other companies and by those companies in the framework of the authority of the Ministry of Customs and Commerce to audit other companies.

We screened the findings included in the financial audit reports written by the TCA after the financial audit of municipal corporations. The following table lists some of the finding titles.:

Making retrospective journal entries
Differences between 2014 Closing Records and 2015 Opening Records
Bouncing checks
No provision was made for the amounts recorded in the account of 128 Doubtful Receivables
Receivables, which were finalized by court decisions, were not recorded as collections
The stocks were not included in the financial statements with their real values because stock recording system was not in order
The account of 193 Pre-paid Taxes and Reserves had remaining receivables
The amounts, which were given as business advances, did not have provisions
The corporation paid %18 VAT instead of 1% for the helicopter rented for the helicopter taxi activity
There were amounts, which were not recorded in 245 Affiliated Partnership
Values belonging to 288 Fixtures were not included in the financial statements
The rented immovable properties were followed in the account of 252 Buildings just like the owned tangible assets
No amortization was reserved although the corporation procured fixtures
There were incomplete records in the account of 252 Buildings
Current Activity Expenses were recognized in the account of 280 Expenses for Following Years
Social security premiums, which were not paid yet, were monitored in the account of 280 Expenses For Following Years

Using bank credits without receiving the decision of the Municipal Council
Since the legal obligations of the corporations, such as taxes, duties and charges were not paid on time, there was an unnecessary increase in general management expenses
Not using the accounts of 372 Provisions For Employee Termination Benefits and 472 Provisions For Employee Termination Benefits
The need to increase the equity capital of the corporation
The expense record was not made for the rent that the entity should pay for the carpark building
The relatives of the personnel benefited free-of-charge from the in-city transportation services
Borrowing contrary to the Municipal Law no.5393
Not declaring bankruptcy although the corporation was heavily in debt
Not taking the necessary legal precautions although two third of corporation capital was lost due to losses
The contracts regarding the renting of places that belonged to public hospitals included clauses that were contrary to legislation
The corporation procured various assets without bidding although they were not included in the exceptions in paragraph (g) of Article 3 of Public Procurement Law no.4734
Immovable properties were rented without bidding
Electronic fee collection system of the corporation had internal control weaknesses
Cash and in kind donations were made to the associations
Propellers and engines of the newly-procured air vehicles were changed shortly after starting to use them
Attendance fee was paid to the corporation's board members contrary to the decision of the general council
More than one social houses were sold to the same person

As the above table indicates, the financial audit findings detected and reported by the TCA after auditing the municipal corporations were wide ranging and not limited to accounting errors. While assessing whether the financial statements of municipal corporations give a true and fair view, the

auditors evaluated the personnel legislation, procurement legislation and other legislative provisions. I.e. while drawing the framework of the financial audit of municipal corporations, the audit of financial statements was interpreted and implemented broadly.



## Governance Related Issues of Stated-Owned Enterprises in Pakistan

**Faisal Saeed Cheema**

Director General, Defence Services Audit,  
Department of the Auditor General of Pakistan



### Introduction

SOEs constitute a significant share of Pakistan's economy, contributing about 10 percent of Gross Domestic Product. According to the Ministry of Finance, Government of Pakistan, there are around 200 organizations in Pakistan, which are performing either quasi or fully commercial functions. SOEs exist in many forms such as an autonomous body, attached departments, corporations, and public sector companies under companies' ordinance, 1984. The rationale for the creation of such SOEs was to improve service delivery and fill the investment gaps in the public sector. However, it has been observed that most of the SOEs in Pakistan are making losses and creating a burden on the fiscal exchequer and affecting the overall economic growth in the country. In financial year 2016-17, according to International Monetary Fund (IMF), the combined accumulated losses of Public Sector Enterprises in Pakistan including Pakistan International Airlines (PIA), Pakistan Steel Mills (PSM), Power sector and others have exceeded Rs. 1.2 trillion or 4 per cent of the GDP. The cumulative losses suffered by the PSC's during the last five years (2013-18) comes to Rs. 3.746 trillion.

Successive governments in Pakistan have been attempting to address financial losses of SOEs through subsidies and bailout packages. Most of the literature witnessed the poor performance of SOEs in Pakistan due to poor governance. There are host of structural

and procedural governance issues faced by these SOEs. However, this paper analyses the corporate governance issues of SOEs and its impact on performance and service delivery.

### Statement of the Problem

The existing literature and debate on the performance of SOEs suggest that there are host of factors leading to poor governance of SOEs such as lack of legislative and regulatory frameworks, poor accountability mechanism, deficient human resource, absence or weak internal controls, and lack of central performance assessment process. However, the most critical governance problems are resulted due to inactive or deficient Board of Directors (BODs) of SOEs. Therefore, it is imperative to examine the role of BODs in depth and find solutions for a useful role of BoDs to improve corporate governance of SOEs in Pakistan.

Review of the literature

A study on corporate governance of SOEs indicates the issues related to SOEs performance. These issues come from various sources, including the need to enhance their competitiveness and that of the economy as a whole, especially in countries where SOEs are major players; to provide essential infrastructure, financial, and other services to businesses and consumers more efficiently and cost-effectively; to reduce their fiscal burden and fiscal risk; and to enhance the transparency and accountability of the use of scarce public funds. A

<sup>1</sup> The Author wrote this article as part of the requirement of Senior Management Course at the National School of Public Policy, Pakistan

<sup>2</sup> Asian Development Bank, "Report and Recommendations of the President to the Board of Directors", (Manila: Asian Development Bank, 2014), p.1

<sup>3</sup> Ministry of Finance, Government of Pakistan. "State Owned Enterprises Performance Review." Islamabad, 2014-15. [http://www.finance.gov.pk/publications/State\\_Owned\\_Entities\\_FY\\_2014\\_15.pdf](http://www.finance.gov.pk/publications/State_Owned_Entities_FY_2014_15.pdf) (accessed 22 March, 2018)

<sup>4</sup> "Public Sector Companies losses Swells to Rs. 1.2 Trillion", The News, Rawalpindi, March 20, 2018

<sup>5</sup> Bilal Hussain, "Public Sector Units Suffer Hefty Rs. 3.74 trillion loss over five years, The Express Tribune, May 16, 2018, [www.tribune.com](http://www.tribune.com) (accessed on May 16, 2018)

<sup>6</sup> Ishrat Hussain, "Governing the Ungovernable." Karachi: Oxford University Press, 2018. 443-453.

<sup>7</sup> Asad Ali Shah, the former Advisor on Finance to Chief Minister Sindh, Pakistan has defined "Corporate Governance is the system and processes by which the entities are controlled, directed, and held accountable to enhance the performance and sustainable shareholder value", Asad Ali Shah, "State Owned Entities & Privatization Process in Pakistan" (Lecture, National Institute of Management, Islamabad, 15 March, 2018)

long history of efforts at reform shows that the key to better SOE performance is better governance.

The weak corporate governance will continue to pose challenges regarding transparency, lack of clarity of roles, political interference and ineffective oversight by the BODs that create difficulties for the SOEs to operate efficiently and vibrantly. BODs remains the governing body responsible for overall governance of the SOE under the law, however, the immense authority of line ministries and other public office holders, drawn from the government, hinders the BODs in exercising effective oversight role, carry out strategic planning and hold CEO and management accountable as they are often directly appointed by the government instead of BODs.

There is sufficient institutional framework of Corporate Governance in Pakistan and it has developed good corporate governance laws but poor implementation of these laws together with political instability adversely affect corporate governance in the country.

There is no clear theoretical case either for or against SOEs. Undoubtedly many SOEs are inefficient, dynamic, and corrupt. However, there is no clear, systematic evidence that SOEs are burdens on the economy. Furthermore, there is a certain degree of

“selection bias” in the empirical materials relating to SOEs in the sense that poorly performing SOEs tend to be discussed more. It is natural that people talk more about problem cases, but this gives the wrong impression of the prevalence of inadequate SOE performance.

### Rationale of SOEs- International Perspective

The global financial crisis of 2008 proved a significant setback to the privatization process that was initiated in many countries during the 1990s. The global public debts were enhanced much fold as a result of this crisis. A new debate on the effective public financial management and corporate governance of the SOEs came to the limelight. One of the major lessons of the financial crisis was to improve corporate governance of the SOEs to ensure better financial management. The outcomes of an international survey found that SOEs account for about 80% of the market capitalization in China, 35% percent in Brazil and 60 % in Russia. State-owned enterprises (SOEs) are now responsible for approximately one-fifth of global stock market value. The form and structure of SOEs, however, varies in different countries in terms of their ownership structures. There are broadly three models of state ownership of SOEs which are explained below:-

**Table. 1 Models of State ownership of SOEs**

Decentralized Model	Dual Model	Centralized
Line ministries responsible (e.g., Pakistan)	Line ministries & another ministry, usually MOF (e.g., Turkey, Mexico)	Three broad types: - Advisory bodies (e.g., Norway, Sweden, New Zealand, India, S.A.)
i. Line ministries have historical experience, sector/company knowledge	* A hybrid between decentralized and centralized model	- Ownership agencies within the government structure (e.g. France, Indonesia, China)
ii. However, many limitations - Conflicts between ownership, policy-making and regulatory function	- Provides checks and balances - Promotes technical and financial oversight	- Holding companies (e.g. Malaysia, Singapore, Hungary, Gulf countries)
iii. Fragmentation of ownership - Insufficient “ownership” capacity	* Limitations: - MOF focused more on financial and budgetary matters - Lack of capacity to be an advocate for reform - Numerous other bodies continue to be involved	* Benefits: - Separates and strengthens the ownership function and ensures consistent implementation
iv. Lack of adequate oversight and accountability of sector as a whole		- Concentrates scarce skills and resources - Helps drive reform

<sup>8</sup> *State-Owned Enterprises: A Toolkit.* 2014

<<http://documents.worldbank.org/curated/en/228331468169750340/pdf/913470PUB097810B00PUBLIC00100602014.pdf> (accessed on April 10, 2018)

<sup>9</sup> Muhammad Naveed Iftikhar, “State-Owned Enterprises in Pakistan: The Need for Corporate Governance and Private Investment.” Policy Research Institute of Market Economy, (August 2015).

<sup>10</sup> Attiya Y. Javaid and Robina Iqbal, “Corporate Governance in Pakistan: Corporate Valuation, Ownership and Financing.” PIDE Working Paper, Islamabad: Pakistan Institute of Development Economics, 2010. p.16.

<sup>11</sup> Joon-Chang, Ha, “State-Owned Enterprise Reform”, National Development Strategies Policy Notes. United Nations Department for Economic and Social Affairs, 2007. pp. 7-8.

Source: Sunita Kikeri, "Global Trends and Developments in SOEs Corporate Governance", a paper presented at the World Bank workshop on corporate governance of SOEs held in Turkey, June 10, 2014

Organization of Economic Cooperation Development

(OECD) and the World Bank have produced guidelines of corporate governance of SOEs. The fundamental purpose of these guidelines is to ensure transparency, accountability, and effectiveness of SOEs. The comparative analysis of the OECD and the World Bank guidelines on SOEs is given in the following table: -

**Table 2: Guidelines on Corporate Governance**

Decentralized Model	The World Bank Guidelines
<ol style="list-style-type: none"> <li>1. Ensure a level-playing field with the private sector</li> <li>2. Reinforce the ownership function within the state administration</li> <li>3. Provide equitable treatment of minority shareholders</li> <li>4. Improve transparency of SOEs' objectives and performance</li> <li>5. Improve stakeholder relationship</li> <li>6. Strengthen and empower SOE boards</li> </ol>	<ol style="list-style-type: none"> <li>1. Sound legal and regulatory framework</li> <li>2. Professionalized state ownership</li> <li>3. Good Board and management practices</li> <li>4. Robust Regime of disclosure and transparency</li> <li>5. Shareholder/stakeholder treatment</li> </ol>

Source: Constructed by the author from the OECD and the World Bank documents

The careful examination of OECD and the World Bank guidelines reveal that many principles are in common like ownership function, improved transparency, strong regulatory framework and robust board management practices. Both these organizations have accessed the degree of compliance of these corporate principles in many countries. For instance, various countries like Finland, Hungary, Namibia, Philippines, Poland, and Romania have ownership legislation. Whereas countries like Bhutan, Finland, Norway, Sweden have ownership policies. Similarly, Egypt, Germany, India, Kenya, Malawi, Malaysia, Mozambique, Mauritius, Morocco, Peru, Poland, Seychelles, South Africa have developed corporate governance codes/guidelines.

#### The Board Composition, Role and Independence

The BODs play a crucial role in the governance and management of SOEs. SOE board approves strategy and monitors management of the organization. The Boards also set strategic direction and take major decisions. The boards also appoint and oversee management of the SOEs. OECD defines the following responsibilities of the boards of SOEs:-

- I. The board should have a clear mandate and ultimate responsibility for the company's

performance

- ii. The board acts according to objectives set by the ownership entity. It has the power to appoint and remove the CEO.
- iii. The board is composed so that it can exercise objective, independent judgement.
- iv. The Boards should have employee representation.
- v. Specialised board committees should be considered.
- vi. Annual board evaluation should be published.
- vii. Monitor the effectiveness of the company's governance
- viii. Select, monitor and, if necessary, replace executives
- ix. Align remuneration with the longer-term interest of the company
- x. Ensure formal and transparent board nomination practice
- xi. Monitor potential conflicts of interest in the organization

It is common practice globally that capital market listing rules and company bylaws require utilities to have a Board of Directors for the issuance of bonds or shares. Board members play the primary role of ensuring that all the management of the company act

<sup>12</sup> "The Company that Ruled the Waves", *Economist*, Dec. 17, 2011,

< <https://www.economist.com/node/21541753> > (accessed on April 17, 2018)

<sup>13</sup> Sunita Kikeri, "Global Trends and Developments in SOE Corporate Governance", a paper presented at the World Bank workshop on corporate governance of SOEs held in Turkey, June 10, 2014

<sup>14</sup> "OECD Guidelines on Corporate Governance of State-Owned Enterprises", (2015 Edition),

< <http://www.oecd.org/corporate/guidelines-corporate-governance-SOEs.htm> > (accessed on April 17, 2018)

<sup>15</sup> "Corporate Governance", The World Bank,

< <http://www.worldbank.org/en/topic/financialsector/brief/corporate-governance> > (accessed on April 17, 2018)

in the interests of the shareholders, through monitoring and an advisory role. The Boards formulated through the certain regulations about some directors for the company, their types of independent directors, executive, and non-executive members as well as required skills of the appointees. Corporate governance regulations have specific requirements like frequency of meetings of the Board. According to corporate governance rules, there should be Board committees. Appointment of highly qualified professional meeting certain criteria are also the requirement to fulfill the corporate governance rules. The appraisal of the BoDs performance is also an essential aspect of it.

Many politicians and public officials in developing countries have used SOEs to provide gifts (transport, housing), Board membership, jobs for themselves relatives and supporters, and in some cases even procurement kickbacks. A particular problem that seems to be emerging in developing countries is the excessive turnaround of directors which does not allow them to exercise any influence in corporate events. Policymakers in several countries have turned to independent directors as an essential element of legal and policy reforms in the field of corporate governance. In the United States, insider-dominated Boards have been rare for years. Although the New York Stock Exchange (NYSE) has required that independent directors constitute a Board majority in domestic companies only since 2004, as of 2001 approximately 75% of NYSE-listed companies already had such majorities. Under the current NYSE listing rules, the Board overall must have a majority of independent directors.

The experience of BODs of SOEs in some emerging economies is particularly enlightening. The Chinese model of appointment of independent directors to the Boards of SOEs is pre-dated the corporate scandals that led to federal-level corporate governance reforms in the United States, possibly because of the many similar scandals. In August 2001, the China Securities Regulatory Commission (CSRC) issued its Guidance Opinion on the Establishment of an Independent Director System in Listed Companies. In response to the 1997-1998 East Asian financial crisis, Korea adopted corporate governance rules in 1999, requiring "large" firms to have 50% outside directors. Smaller firms must have 25% outside directors. India's also

adopted significant governance reforms in 1999, such as Clause 49 which requires, among other things, audit committees, a minimum number of independent directors, and Chief Executive Officer (CEO)/Chief Financial Officer (CFO) certification of financial statements and internal controls.

There are four mechanisms through which BODs independence can be ensured. The first one is to tighten the standards and rules of disqualifying relationships, including current employment by the firm and dimensions of potential connectedness. Throughout the 80s and 90s, panels and "blue ribbon" committees developed influential "best practice" guidelines for relationship tests. The principles of corporate governance recommended that the Board of a public corporation "should have a majority of directors who are free of any significant relationship with the corporation's senior executives".

The second mechanism for independence is to increase penalties and incentives, such as legal liability for fiduciary duty breach, reputational sanctions, and stock-based compensation. Directors also potentially face liability under the federal securities laws for material mis-statements or omissions in a corporation's financial disclosures. A third mechanism to enhance the independence of the members of the Board of Directors is the development of intra-Board structures, such as task-specific committees and designation of a "lead director". This may enhance independence in two ways: 1) the ownership and accountability for a specific critical task may lead to greater autonomy from the CEO in performing that task, 2) the practice of acting jointly and autonomously in a targeted area may carry over to other important roles of the Board".

In a nutshell, the transformation of SOEs from a government department to the corporation under corporate governance rules and the company ordinances poses formidable challenges. At the same time, it presents several potential opportunities. Corporate Governance brings about insulation. It allows company laws to limit the right of shareholders to manage the enterprise directly. The decision-making role is delegated to the chief executive officers under the corporate rules. Overall, the management is monitored through company's BoDs. Being the shareholder of SOEs, the government has a legitimate

<sup>16</sup> Sunita Kikeri, *Op.cit.*

<sup>17</sup> *Ibid.*

<sup>18</sup> ECD (2015), *OECD Guidelines on Corporate Governance of State-Owned Enterprises*, 2015 Edition, OECD Publishing, Paris, <http://dx.doi.org/10.1787/9789264244160-en>. (accessed on April 10, 2018)



right to influence SOEs. Although, the extent of influence and the scope in practice has been excessive. It calls for some limitations. Government role should be limited to the objectivity of outcomes and regulations of the corporate laws instead of influencing and managing the management.

### Pakistan's Experiences with SOEs

Pakistan inherited 12 major SOEs in 1947. The policy and objectives of SOEs were indicated in Industrial Policy of 1948. Pakistan Industrial Development Corporation (PIDC) was established in 1952. Its charter reflected objectives of SOEs in Pakistan. During the 1950s and the 1960s, SOEs were set up in all the sectors of the economy, i.e. water and power, finance, transport, agriculture etc. A concept of "Government by the Corporation" was implicitly evolved in the 1960s. Public Corporations in Pakistan emerged as well-run entities. Following Nationalization, in early 1970s public sector expanded radically. Expanded public sector confronted challenging task for improving operational efficiencies of SOEs. A number of high-powered commissions/ committees i.e. H.U. Baig committees, Uquaili commission, etc were constituted to examine the existing system and make recommendations for improvement. In last few years, corporate governance emerged as one of the most practical models to run the SOEs particularly in the field of utility services. Today, Pakistan has SOEs in all sectors of the economy such as financial, trading,

services, transportation, and promotional and advocacy sectors.

The performance of SOEs in Pakistan is crucial for sustainable economic growth and effective service delivery. The SOEs constitute about 10 per-cent of the GDP in Pakistan and have been established in all major sectors of the economy like energy, infrastructure, and communication and, the financial sector. The underlying purpose for the creation of SOEs in Pakistan was to develop infrastructure in major areas of the economy where private sector did not have incentives for investment. However, with the passage of time, SOEs faced problems, resulted in as a burden on the economy and creating fiscal problems for the government. These SOEs have become a liability on the part of the government as it consumes major chunk of government resources in the form of subsidies and bail-out packages. According to the IMF report "the combined accumulated losses by these SOEs now exceed Rs.1.2 trillion (4 percent of the GDP) which could eventually lead to sizable demand for budgetary resources". During the tenure of Pakistan People's Party (2008-13), the performance of SOEs was not encouraging as these enterprises recorded an average loss of Rs. 400 billion annually. Besides, the SOEs have accumulated enormous domestic and external public debts during the recent years. The following table highlights the debts owned by the SOEs during the last five years.

**Table 3. Year wise Debt of Public Sector Enterprises in Pakistan (Rs in Billions )**

Year	Domestic Debt	External Debt
2013	312	183
2014	366	204
2015	459	253
2016	568	294
2017	823	284

<sup>19</sup> Benjamin E. Hermalin and Michael S Weisbach. "The effects of Board composition and direct incentives on firm performance." *Financial Management* 20 (1991), pp. 101- 112.

<sup>20</sup> Craig, G. Doidge, Andrew Karolyi, and René M. Stulz . "Why do countries matter so much for corporate governance?" *Journal of Financial Economics*, 2006.

<sup>21</sup> World Bank Group, International Bank for Reconstruction and Development,. "Corporate Governance of State-Owned Enterprises: A Toolkit." 2014 < <http://documents.worldbank.org/curated/en/228331468169750340/pdf/913470PUB097810B00PUBLIC00100602014.pdf> (accessed on April 10, 2018)

<sup>22</sup> Jay Dahya John J. McConnell, "Board Composition, Corporate Performance, and Cadbury Committee Recommendation." *Journal of Financial and Quantitative Analysis*, forthcoming, 2007.

<sup>23</sup> OECD, Policy Brief on Corporate Governance of State-Owned Enterprises in Asia: Recommendations for Reform. Paris: OECD-Asia Network on Corporate Governance of State-Owned Enterprises, OECD, 2016.

<sup>24</sup> Tamunu, M. and Tumewu, F. "Analyzing The Influence Of Price And Product Quality On Buying Decision Honda Matic Motorcycles In Manado. , Manajemen," *Jurnal Riset Ekonomi (Bisnis Dan Akuntansi)* 2(3) (2014).

<sup>25</sup> Khanna and Vagliasindi. "Overview of SOE corporate governance rules best practice and transpositions to emerging countries." 2007.

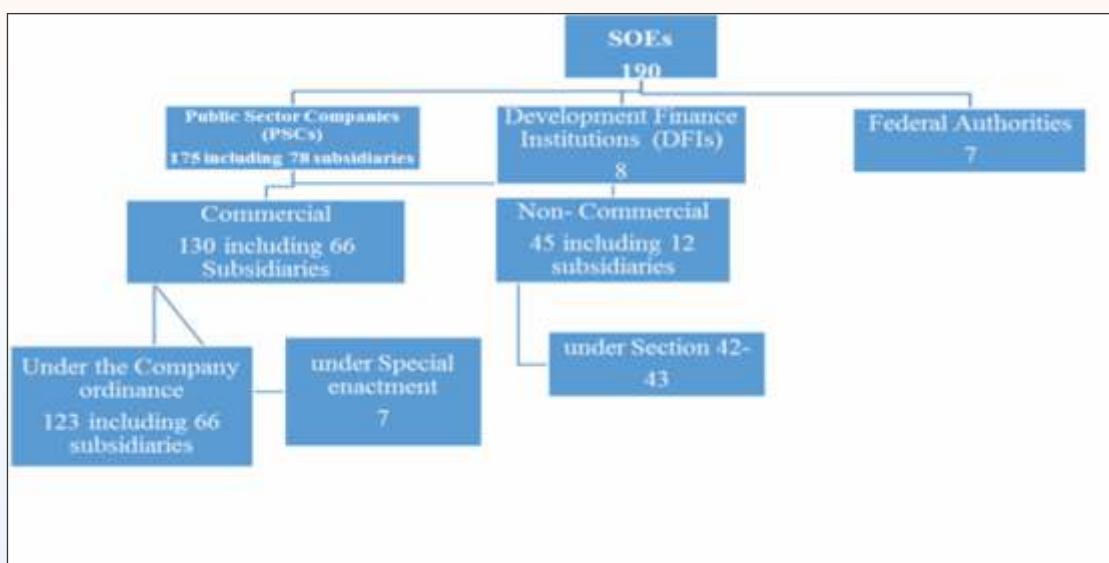


Source: State Bank of Pakistan, Annual Report, 2017  
[www.sbp.gov.pk](http://www.sbp.gov.pk)

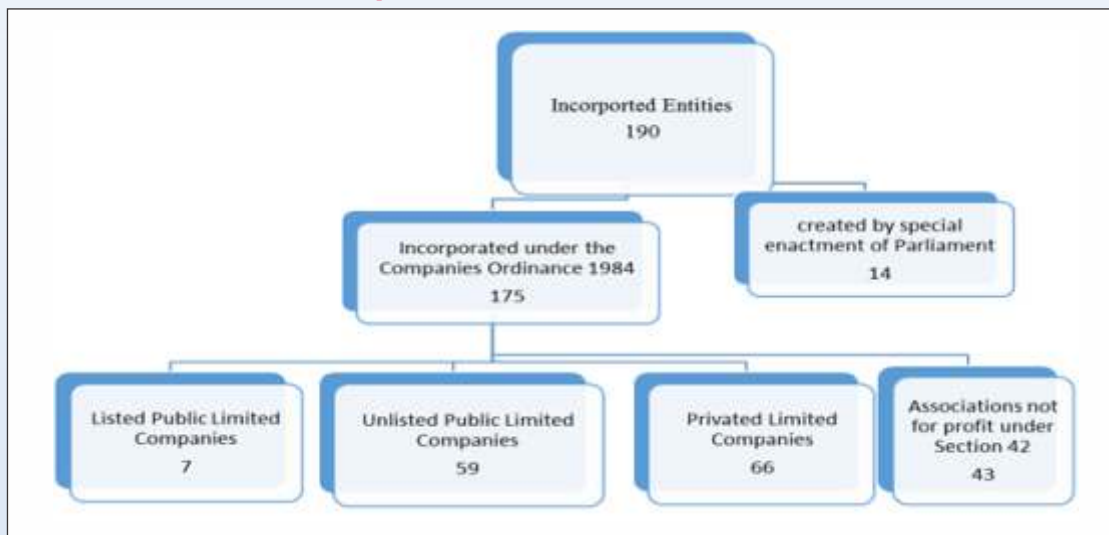
Pakistan has the heterogeneous legal structure of SOEs. At present, Pakistan has 190 SOEs in various sectors. These SOEs are categorized under Public Sector Companies, Development Finance Institution and, Federal Authorities. Out of 190 SOEs, 175 entities are incorporated under company's ordinance 1984 whereas 14 have been created under special

enactment of the parliament as autonomous bodies or attached departments. The federal and provincial authorities are not following the corporate governance rules issued by the Securities and Exchange Commission of Pakistan since these are not governed under company's ordinance 1984. The following diagrams explains the legal structure of SOEs in Pakistan.

### SOEs Classification<sup>36</sup>



### Incorporation Structure of the SOEs



Source: Ministry of Finance, Government of Pakistan, [www.finance.gov.pk](http://www.finance.gov.pk)

<sup>26</sup> "Guidelines for Introducing Independent Directors to the Board of Directors of Listed Companies", China Securities Regulatory Commission, < [http://www.csrc.gov.cn/pub/csrc\\_en/newsfacts/release/200708/t20070810\\_69191.html](http://www.csrc.gov.cn/pub/csrc_en/newsfacts/release/200708/t20070810_69191.html) > (accessed on April 17, 2018)

<sup>27</sup> Ibid

<sup>28</sup> Tamunu, M. and Tumewu, F. "Analyzing The Influence Of Price And Product Quality On Buying Decision Honda Matic Motorcycles In Manado. , Manajemem,," Jurnal Riset Ekonomi (Bisnis Dan Akuntansi) 2(3) (2014).

<sup>29</sup> Joon-Chang, Ha. "State-Owned Enterprise Reform." National Development Strategies Policy Notes. United Nations Department for Economic and Social Affairs, 2007. pp. 7-8.

<sup>30</sup> Hermlin, Benjamin E., and Michael S. Weisbach. "Endogenously chosen Boards of directors and their monitoring of the CEO ." American Economic Review 88 (1998): pp.96-118.

<sup>31</sup> Hermlin, Benjamin E., and Michael S. Weisbach. "The effects of Board composition and direct incentives on firm performance." inancial Management 20 (1991): 101- 112.

<sup>32</sup> Adams, Renee B., and Daniel Ferreira. "A Theory of Friendly Boards." Journal of Finance 62 (2006).

### The regulatory framework of SOEs in Pakistan

The regulatory framework is divided into two categories, i.e. Institutional Framework and Legislative Framework. Institutional Framework: Federal government of Pakistan holds the majority of the shares of SOEs. It is automatically responsible for their management control. There are seventeen ministries engaged in the administration of the 190 SOEs in Pakistan. Out of these entities, most of the SOEs are concentrated under three central ministries. These include Ministry of Industries & Production, Ministry of Finance, and Ministry of Water & Power. About 31 SOEs are directly controlled by the Ministry of Finance. These SOEs belong to the financial sector including Development Finance Institutions (DFIs) and Banks. The entities from 'Industrial & Engineering' sector and 'Promotional & Advocacy' sector controlled by the Ministry of Industries & Production. About 25 Public Sector Companies (PSCs) and one Federal Authority (WAPDA) are under the supervisory role of Ministry of Water and Power. These PSCs belong to 'Power' sector. These are involved in power generation, distribution and transmission, and other relevant functions. Securities and Exchange Commission of Pakistan (SECP) performs the function of regulator of Public Sector Companies (PSCs) registered under Companies Ordinance, 1984.

### Legislative Framework:

There is no specific legislation for SOEs in Pakistan. However, the SECP notified the rules for the corporate governance of public sector companies in 2013. These rules apply to all public sector companies, directly or indirectly, owned and controlled by the government. These rules were aimed at empowering the boards of PSCs and for creating greater transparency and accountability. The development of these corporate governance rules was considered as a first significant step towards the improvement in corporate governance processes of SOEs. These rules have also helped clarify roles and responsibilities of different stakeholders involved in governance and management of SOEs.

SOEs faced several governance problems regarding their structures and processes in Pakistan. These governances include, amongst many other transparency, accountability, weak performance evaluation and, insufficient or weak regulatory framework. Some of the major governance problems

of the SOEs in Pakistan are given as under:

- i. **Heterogeneous Governance Regimes.** The heterogeneous legal structures of SOEs in Pakistan weakens the regulatory framework. As stated earlier, among other things, the Corporate Governance Rules 2013 are applicable to select numbers of PSCs like Companies registered under Companies Ordinance 1984 (for and not for profits).
- ii. **Weak Boards of Directors:** The system of appointment, training, remuneration and performance evaluation of BODs of SOEs is not transparent and affects the performance of these organization. In most of the cases, BODs are appointed by the government which compromises their autonomy in decision making. The Chief executive Officers or Chairperson of SOEs are most of the time from governments sector. The SOEs also do not have a proper and regular system of training of its Board members.
- iii. **Absence of Performance Evaluation System:** The absence of performance evaluation system for the managers is frequently the major cause of inefficiencies in the SOEs and creates vagueness about their goals. A performance evaluation system, which is based on clear and quantifiable targets and linked with an incentive system minimizes vagueness and motivates managers to achieve specified performance level. Performance evaluation system was introduced in Pakistan through the "Signalling System for Public Enterprises" in 1980s but was abandoned in 2000.
- iv. **Budget Constraints:** Historically, SOEs in Pakistan faced budget constraint, compared to their private sector counterparts. It leads to non-commercial decision-making and lack of financial prudence. The successive federal government continued to provide support in the form of investments, subsidies, bailout packages, grants, guarantees and public sector loans to enable SOEs to obtain loans from commercial banks. This has resulted in fiscal challenges and exposed the government

<sup>33</sup> "State Owned Entities (SOEs) Performance Review (FY 2013-14)", Ministry of Finance, Government of Pakistan [http://www.finance.gov.pk/publications/State\\_Owned\\_Entities\\_FY\\_2013\\_14.pdf](http://www.finance.gov.pk/publications/State_Owned_Entities_FY_2013_14.pdf) (accessed on April 15, 2018)

<sup>34</sup> Khaleeq Kiani, "PML-N's unfulfilled Promises: Public sector enterprise", Dawn, April 02, 2018.

<sup>35</sup> Bilal Hussain, op.cit.

to risks of fiscal instability along with financial mismanagement in some SOEs..

- v. **Weak Compliance with Corporate Governance Rules:** Although, SECP mandated to carry out supervision and enforcement of corporate governance to ensure compliance by the SOEs. However, the compliance rate of Corporate Governance rules for the fiscal year 2015 reached the level of 37 per cent. These efforts of SECP are appreciable, but still, SECP faces challenges regarding directing the government to comply with the requirements of the rules and holding government functionaries accountable.
- vi. **Politicization:** In Pakistan, SOEs perceived as tools to achieve political objectives of the government and in some case interests of the individual's politicians. The politics of clientelism gave importance to the idea of keeping SOEs in traditional mode instead of promoting the culture for well-governed entities. This general model has allowed the political governments to influence the service delivery and employment process.

## Conclusion

SOEs in Pakistan face many governance issues and have not been to achieve the desirable results in term their contribution to economic growth and public service delivery. Rather these SOEs have proved burden on the national exchequer. The successive governments in Pakistan had to allocate major chunk of their budgetary allocations in terms of subsidies and bail out packages to finance the deficits of SOEs. Though, there is a cluster of governance problems being faced by the SOEs, yet the performance of the BODs is most significant. The investigation of the BODs of SOE's in Pakistan reveals many short comings in their structures and processes. The study could not find the sufficient evidence that corporate governance rule of the SECP were being implemented in letter and spirit in SOEs. There is no formal process of appointment, training, removal and performance evaluation of independent directors of SOEs. The lack of market-based remunerations to the board members have also compromised the quality of board members. The boards are not autonomous in taking important policy decisions.

In the case of USC, the important policy decision like

grant of subsidies on utility items is taken by the ministry of Industries and Production rather than board of directors. However, in this case the company should be adequately compensated to fulfill public service obligation which is a scarce practice. Contrary to the best practices, the CEOs of SOE's are appointed by the government and are answerable to the government rather than board members. The institutional arrangements for regulation of PSC's is also very weak and faces many challenges of implementation. The SECP is the main regulator of corporate governance of PSCs established under Companies Ordinance 1984 and have issued corporate governance rules to ensure performance, transparency, financial management, and disclosures of the SOEs. However, the compliance of SECP rules is far from satisfactory. The BoDs of IESCO and USC also suffer many compliance issues as required by the SECP corporate governance rules 2013.

## Recommendations

Based on the literature review, international best practices, and analysis of the available data, this study has developed recommendation to improve the corporate governance and performance of SOEs in Pakistan. Considering the complexity of the challenge, the study has decomposed the recommendations in short, medium and long term. While formulating the recommendations, it was considered that they should not be idealistic, and they should be well grounded in the current governance structure of the federal government. The recommendations of the study may also be helpful for the new democratic government to evolve a comprehensive reforms agenda to save the public money and to improve the service delivery by these SOEs.

### A) Short Term

I. A detailed corporate governance assessment of all the SOEs in Pakistan should be carried out by a third party. Currently there is no such assessment available to the government. The analysis of two companies i.e. USC and IESCO has revealed that there are severe loopholes in the implementation of corporate governance rules. Such a study for all SOEs can certainly help to develop a comprehensive policy response by the government.

II. The new government should immediately ensure appointment of well reputed professionals and public servants on the board of SOEs. The new boards will undertake immediate measures to reduce losses

<sup>36</sup> "State Owned Entities (SOEs) Performance Review (FY 2014-15)", Ministry of Finance, Government of Pakistan, [http://www.finance.gov.pk/publications/State\\_Owned\\_Entities\\_FY\\_2014\\_15.pdf](http://www.finance.gov.pk/publications/State_Owned_Entities_FY_2014_15.pdf) (accessed on April 16, 2018)

and to improve performance of SOEs. It is required to address the overlapping roles and responsibilities of the boards of the directors and management teams as the study found its importance in both USC and IESCO. It is needed to ensure that management team should focus only on operational matters and BoDs should limit their role to the policy decisions.

III. SECP should made the compliance report of all SOEs public in order to ensure transparency and accountability. The public disclosure of compliance will build pressure on SOEs to fulfill the requirements of corporate governance rules in letter and spirit.

IV. Training programs for executives, board members, and senior officers of line ministries should be conducted to impart them contemporary knowledge and skills of corporate governance.

V. The emoluments of senior management of SOEs should be linked to the financial viability of the SOE in order to hold them accountable and to curtail organizational losses.

## **B) Medium Term**

I. Ministry of Finance, Government of Pakistan has recently started publishing an annual report on SOEs but ex-ante goals are not agreed with the SOEs. Thus, the performance is not being reported against such goals. Each SOEs should submit its financial and service delivery goals in advance and then at the end of the year their performance should be benchmarked against those targets. This practice was pioneered by Pakistan through its Expert Advisor Cell of Ministry of Industry and Production for SOEs in the 1980s. However, this practice was abandoned in 2000. Many countries such as India, Philippines, Egypt, Venezuela and Korea adopted this practice and their SOEs performed much better after introduction of such performance agreements. This practice is now being done by Department of Public Enterprise in India, Khazna Model of Malaysia's Treasury, Tamasak Holding of Singapore and Crown Monitoring Agency in New Zealand.

II. There is a need to develop clarity on which SOEs need to be privatized. The new government should do both technical and political consultation to develop a consensus way forward in this regard. This study considers that some of the SOEs such as PIA, Pakistan Steel and other such companies either need private investment or privatization. Generally, Privatization Commission prepares this list with the approval of Council of Common Interest (CCI) but implementation has been weak in this regard.

III. The government needs to restrict its role to improve regulatory quality to attract private sector investments. The policies related to subsidies and notifying the tariff results in an inefficiency of the company performance. For a conducive environment, the government should adopt the corporate governance rules rather than deciding to serve their political interests.

IV. There is a need to develop a formal process for nomination and performance evaluation of Board members of SOEs. A pool of professionals should be developed, and board members should only be nominated from that pool by an independent commission. This will reduce discretionary practices to appoint incompetent board members by the sitting government. The record of previous performance of board members should also be developed and it should be consulted while making board nominations.

V. It is required to create a culture of corporate governance in utility companies in Pakistan. The directors should be made to realize their potential role and must hold equal responsibility and accountability as members of the board. A behavioral change amongst the stakeholders is also needed for democratic values, accomplishing harmony and good governance practices.

## **C) Long Term**

I. Most of the countries, who have managed their SOEs in better way, have introduce dedicated legislations on SOEs in order to ensure

<sup>37</sup> Pakistan Institute of Corporate Governance, "Report on the Survey on Board Practices of Public Sector Companies in Pakistan". May 2016. PP: 16

<sup>38</sup> Ibid.

<sup>39</sup> "Challenges in reforming public sector enterprises", Dawn, March 25, 2013

<sup>40</sup> Muhammad, Naveed Iftikhar, "State-Owned Enterprises (SOEs) in Pakistan: The Need for Corporate Governance and Private Investment", PRIME Institute, (Islamabad: PRIME Institute, 2015), p.28

<sup>41</sup> Istaqbal Mehdi, "Application of Performance Evaluation System and Benchmarking to Improve Operational Efficiency of Public Enterprises", ICPE Public Enterprise Half-Yearly Journal, Volume 22, Issue 1 (2016), p. 92

<sup>42</sup> Ishrat hussian, "Recent Privatizations in Pakistan and their Impact." 2009.

<sup>43</sup> Attiya Y. Javaid and Robina Iqbal, "Corporate Governance in Pakistan: Corporate Valuation, Ownership and Financing." PIDE Working Papers. Islamabad: Pakistan Institute of Development Economics, 2010. p.16.



professionalism, accountability and service delivery of SOEs. Pakistan also need to develop a unified structure of all SOEs under such legislation. Currently there are variety of governance mechanism and accountability forums for SOEs which need to integrated and unified. The SOE law should provide a broader framework for governance of SOEs. The same law should clarify roles and responsibilities of all stakeholders involved in the governance of SOEs.

II. Pakistan needs to move towards Singapore's model of Holding Company. All SOEs of Singapore are subsidiaries of its Tamasak Holding Company. Such a holding company will be led by professionals and officers of extreme integrity and dignity. This company in turn will give targets and performance benchmarks to all its subsidiaries.

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<sup>44</sup> Pakistan Institute of Corporate Governance, "Report on the Survey on Board Practices of Public Sector Companies in Pakistan". May 2016. p.19

<sup>45</sup> Istaqbal Mehdi, "Privatization-A device for reforming public enterprise sector in Pakistan." *The Pakistan Development Review*, 1999. pp 895-905.



## Public Policy Evaluation: A new Initiative by DAGP

**Muhammad Raza Shah,**

Director, Pakistan Audit & Accounts Academy,  
Department of the Auditor General of Pakistan



### Introduction:

Department of the Auditor General of Pakistan (DAGP) is the Supreme Audit Institution of Pakistan which is mandated to carry out independent and objective assessments of the governance process in the country. The DAGP conducts various types of audit including compliance audit, performance audit, financial audit and environmental audit etc. to fulfill its mandate.

DAGP has been carrying out performance audits since decades now with the aim to conduct an independent examination of government programs, projects and functions. The performance auditing by DAGP add value to public sector performance and lead to good governance in the country.

Today, there is an increased focus on the performance of governmental agencies. The administrative authorities are also increasingly concerned about the need for an independent evaluation and assessment of public policies. In response, the SAIs across the globe are engaging more and more in the field of evaluation which has emerged as a fundamental link in the accountability chain. DAGP has also recently taken a major initiative to actively participate in the international drive to develop the practice of public policy evaluation.

### Public Policy Evaluation:

A public policy evaluation is an examination aiming at assessing the utility and relevance of a public policy. It analyses its objectives, implementation, outputs, outcomes and impacts as systematically as possible, measures its performance in order to assess its utility. Evaluations serve a broader purpose as compared to performance audit, and that is to make a particular contribution to an area of public policy. Performance audit mainly assesses economy, efficiency and effectiveness up to the immediate outcome level while assessment of same up to higher outcome and global and socio-economic impact levels can be termed as evaluation.

It is crucial for the SAIs conducting evaluation not to go so far as to prescribe the policy orientation itself. The SAIs based on their conclusion and findings, should only give possible orientations for the policy and not enter into political discussions or bound the executive or legislative branches.

### Evaluation initiative by DAGP:

DAGP is an active member of INTOSAI Working Group on Evaluation of Public Policies and Programs. DAGP regularly attend the meetings of the working group and provides its input and comments on draft documents. The SAI played a very important role in finalization of INTOSAI GOV 9400 'Guidelines on Evaluation of Public Policies' which serves as guiding principles for carrying out public policy evaluations.

As part of the Work Plan 2017-19 of the INTOSAI Working Group on Evaluation of Public Policies and Programs, DAGP is in the process of carrying out public policy evaluation of health policy of the provincial government of Khyber Pakhtunkhwa (KPK) on the control and prevention of dengue fever. The report and results of the evaluation will be shared with other SAIs in the upcoming meetings of the working group.

### Topic of Evaluation:

Dengue fever is endemic in Pakistan with annual seasonal outbreaks at regular intervals. Pakistan observed outbreak of dengue fever in 2011, 2013, 2017 and recently in August 2019 the north-western province of Khyber Pakhtunkhwa (KPK) has been hit by dengue fever. Over the years the transmission of dengue fever has intensified in the country with increased incidence and geographic expansion. Since August, over 4,000 suspected patients have been treated in different hospitals of KPK province, of which around 1000 have tested positive. During the same period, a number of people have died due to dengue fever.

The KPK government has adopted a health policy and

taken measures to control the outbreak of the disease and take precautionary measures against the dengue virus. The KPK health department has also launched an awareness campaigns against the fever for implementing control and preventive measures.

#### **Evaluation by DAGP:**

DAGP is in the planning process of carrying out evaluation of the health policy of the KPK government on control and prevention of dengue fever. It is expected that carrying out the evaluation would not only be of interest to the policy makers and stakeholders in the province, but it will also help bring to the forefront the utility of this public policy and outcomes of the initiatives of the provincial government in dealing with this endemic disease.

Some important elements of the above evaluation activity by DAGP are as under:

- a) The services of medical doctors available in the department will be utilized during the assignment. Moreover, the services of academicians and experts of the field shall also be utilized on a voluntary basis.
- b) Stakeholders like local representatives, citizens and NGOs/CBOs will be involved during the evaluation process.
- c) The assignment is carried out as per the guidance contained in INTOSAI GOV 9400 'Guidelines on Evaluation of Public Policies'.
- d) Optimal combination of quantitative and qualitative methods of evaluation shall be

employed in line with the decisions taken during the annual meeting of the Working Group held in September, 2017.

- e) The team will carry out an in-depth analysis of the objectives, implementation, outputs, outcomes and impacts of the policy.

#### **Expected Outcomes:**

It is expected that the public policy evaluation will add to the learning experience and professional knowledge of DAGP as an SAI and based on the experience and lessons learnt during the assignment, DAGP will be able to take up more assignments related to the policy evaluation field in the future.

#### **Conclusion:**

Evaluation and performance auditing share similar aims, approaches, analytical methodologies and techniques. The distinguishing feature of evaluation is that it goes one step further and looks at the effectiveness of program outcomes and its utility. It is important that while carrying out evaluations, the SAIs ensure that the boundaries between evaluation of public policies and political interference should not be crossed by an evaluator under any circumstances.

With the DAGP taking lead in the field of evaluation, it is expected that the ECOSAI member SAIs will learn from the experiences of SAI Pakistan. The sharing of evaluation activities related to various fields by the SAIs at the forum of ECOSAI will certainly help in the capacity building of the SAIs in the field of evaluation will help improve the national roles of ECOSAI member SAIs in their respective jurisdictions.

## Benchmarking by Supreme Audit Institutions

### Chaudhry Nauman Zafar

Director, Special Sector Audits

Department of the Auditor General of Pakistan



#### Benchmarking

Benchmarking is a way of discovering best or most efficient performance or results being achieved (usually financially, or in any other quantifiable way) in a particular company. The benchmarking process is commonly employed either by a competitor or by a regulator. Sometimes, an entirely different industry also compares its performance against the benchmarks of other industries. This information can then be used to identify gaps in an organization's processes to achieve organizational efficiencies.

#### Problems in Benchmarking

One of the major challenges in benchmarking is data availability, quality and statistical relevance. If all data has the following characteristics, benchmarking process would almost always run smoothly: -

- Easily available
- In one central location
- Using common definitions
- Having a statistically relevant sample size

Unfortunately, having or arranging the data in such a usable form is not always easy and it takes a lot of hard work to take it to a form usable for benchmarking. For example, if we are planning to benchmark the patient management processes of five hospitals in a country, and there is no consistency in the way data is collected across these hospitals or how metrics are defined, it will be an uphill battle. In such a case, it becomes very challenging to effectively execute the benchmarking process even internally between hospitals, and more so in case of external organizations.

#### Access to Data for Benchmarking

Due to constitutional and legal mandate enjoyed by the SAI, various agencies of the government are duty-bound to provide all operational, transactional, financial and other requisitioned data to the staff of the SAI. Hence, if such data is collected in a systematic way and used with responsibility while keeping the relevant

provisions of data protection and data integrity in mind, a data repository will soon be available which will not only enable chronological comparison over the years but also enable horizontal comparisons among various similar projects executed in same year.

#### Benchmarking by SAI

In a SAI, benchmarking of procurement practices can be used to compare the prices of similar items/contracts between various functional divisions, regions, provinces, districts etc. Similarly, it can be used to compare the performances of provincial governments, or between divisions/departments of same government. To illustrate, following examples are given: -

- I. Per kilometer cost of a road in similar terrain in different provinces/districts
- ii. Cost of one ream of A4 papers
- iii. Time taken from start of bidding process to issuance of work order
- iv. Percentage of cost escalation in projects under various cost heads such as HR, cement, steel, transportation etc.
- v. Medical expense per citizen
- vi. Food expenses per soldier
- vii. Cost of cement per sq. ft. covered area of a recently completed building
- viii. Cost per student of new school building
- ix. Average area of hospital per patient etc.

The above scenarios are just examples. It is important to gather data for different or projects in the country. Over the years, a huge cache of data will be made available with the SAI which can then be used to make inferences about the reasonability of the costs incurred, the cost of providing services per client etc. Over the years, we will have a sufficiently close estimate of the average cost structure of various types of projects thus obviating the possibilities of overcharging, fraud or budget slack in provision of services by the government.

### What kind of data to be captured

To illustrate the concept, two examples are taken: -

#### 1. Audit of construction of an expressway

The first step to consider while determining the cost and related data about a project is to understand the cost drivers and the factors that can cause cost variations among different projects of similar nature. For a road, some of the factors include length, width, quality, number of bridges on the road (as bridges push the cost upwards) etc.

**The data that can be gathered for such a project is as follows: -**

- a) The cost per kilometer of the road
- b) Number of lanes in the expressway
- c) Number of toll plazas
- d) The average elevation
- e) Total length of the bridges constructed as part of the project
- f) Total no. of vehicles passing through it per day or month etc

#### 2. Value for money audit of a hospital

The following quantifiable metrics can be used for gathering data of a hospital: -

- a) No. of patients served per day
- b) Average wait time per patient
- c) Operational cost per outdoor patient
- d) Operational cost per indoor patient
- e) Number of total man-days spent by patients admitted to hospital
- f) Total value of medicines distributed to the patients

### How to use the data collected

Over the years, each SAI will amass valuable, authentic and insightful data pertaining to various necessary but routine operations of the government, especially those related to provision of the following services: -

- a) Health
- b) Education
- c) Infrastructure
- d) Social security etc.

**There are a number of ways in which the data can be used through data analysis.**

Data analysis is defined as a process of cleaning, transforming, and modeling data to discover useful information for business decision-making. The purpose of data analysis is to extract useful information from data and taking the decision based

upon the data analysis. Some mathematical analysis that can be done on the data includes: -

- Trend analysis over various years
- Variance analysis
- Time series analysis
- Correlation between two cost drivers
- Regression between dependent variables to

**make best estimate of a dependent variables (which can be cost, number of patients, number of vehicles etc.)**

Horizontal comparison with other projects of similar nature

However, in order to infer meaningful and actionable insights from the data, the data collected by the SAI should be used in conjunction with other economic variables such as: -

- Inflation/Consumer Price index
- Exchange rate movements
- Economic growth
- Human development index
- Gini coefficient etc.

The purpose of the data analysis should not be to find faults with the government policies or operations but to enable evidence based decision making so that most desirable outcome is achieved with lowest possible inputs and limited government resources are put to the best possible use.

### Benefits of data collection and analysis

Analysis of data can lead to efficiencies such as: -

- Help in calculating average cost of provision of basic services
- Better forecasting the demand for government services
- More insightful budget making
- Highlighting inefficiencies and room for cost cutting
- More timely and efficient procurements etc.

### Cost of data collection

A centralized country-wide procurement MIS will make the cost of data collection easier and affordable. However, in most countries, the government is divided into various tiers with little or no electronic data sharing.

The level of IT prevalence and advancement varies greatly for SAIs of different regions. Hence, it is up to

each SAI to decide the level of data it can record in a cost-effective manner. However, at a minimum, data related to provision of basic services for achieving SDGs, such as primary education, clean water, basic health should be recorded as these services directly impact the life of a common man of developing and least developed countries.

### **Situation In Sai Pakistan**

The SAI Pakistan does not have any system of comparing the cost of similar projects/items in different parts of the country except on occasional manual basis. It is thus both laborious and time-consuming to make any comparisons.

### **Recommendations**

**1)** The critical requirement for benchmarking is data. While there are thousands of items procured by government each year, there are only few which are significant and consume a large chunk of money. It is recommended that some data metrics should be defined for large scale development projects and compared across Pakistan. This will be immensely

useful in performance audit of various development initiatives. Within few years, we will be able to compute national, provincial averages and standard deviations, and use data analytics to make our reports more convincing and quantitative.

**2)** Recommending Adoption of e-Procurement Systems: In many auditee organizations, especially in self-accounting entities, records of major procurements are not readily made available to the audit team. Delay in provision of records leads to low level of audit assurance and a low-quality report. SAI Pakistan should vigorously advocate at different forums the use of e-procurement systems in organizations with regular procurements of repetitive nature. This will not only make procurement records easily available but also bring transparency and traceability in spending from public coffers. For example, purchase of medicines by health department is a regular feature and e-procurement can be very useful when it comes to auditing the number of dosages purchased, number of patients served etc.



## Auditing in the age of Technology

**Sheraz Manzoor Haider**

Director General Budget & Accounts,  
Office of the Auditor General of Pakistan



After the financial crisis of 2011 in USA, while experts were analyzing the financial crisis and the post-mortems were over, one big question was repeatedly asked 'where were the auditors'?. Investigations into the financial disaster showed that many of the U.S. merchant banks had blatantly misrepresented their financial positions but the auditors did not raise alarms. The audit firms defended their role by claiming that the financial statements were fine and conformed to accounting standards. The critics agreed that auditors might have applied all the required tests and reassured themselves that the figures were presented according to the standards. However, they pointed out, the audit managers seemed to be unconcerned about what was the use of employing them beyond providing reasonable. The critics were able to demonstrate that what the auditors failed to take notice of, the Wall Street analysts were able to be suspicious of. The financial crisis in USA reminded auditors that their role is about providing confidence to shareholders and other stakeholders based on trust. If audit fails to provide assurance and confidence, audit is likely to become irrelevant.

In the contemporary world, a number of key drivers are fast rendering the traditional approach to audit, in both public and private sectors, irrelevant to the requirements and expectations of clients and stakeholders. These key drivers are primarily manifested in the changes in business models ranging from innovative and technological to disruptive changes; and reflected in momentous increase in volume of data resulting from digitization of government and corporations. The challenges posed by these drivers require the auditors to justify their relevance in a changing world. Financial management gurus suggest that survival of profession of auditing lay in its ability to adapt to the changes in business models of their clients. There is a natural expectation that the role of auditors, in the presence of these significant changes, is required to correspondingly evolve. They must be able to understand growing

volume of information and use it effectively for delivering high-quality audits.

Experts suggest that use of technology in the practice of auditing is the key to enabling auditors to remain relevant, to continue servicing clients and stakeholders and to carry out high quality audits. The untapped potential of data generated by new technologies triggers the need for digitization of audit. Equipped with the technology, the auditors will keep on performing their role of providing confidence to clients and stakeholders. The fundamental elements of delivering that confidence; including independence, professional skepticism, sound judgment and courage; will remain the same. Steve Drake, Partner, Middle East Leader – Risk Assurance and Capital Markets and Accounting Advisory Services (CMAAS), PwC argues that typically, an audit has looked at historical financial statements and provided an opinion. Steve commented that 'data analytics is doing more than just change the way we will do an audit. It will change what an audit of the future will look like.' As clients adopt new technology they will be looking to wider assurance services to mitigate risks in their business, beyond the focus on historical information.

The challenges and way forward for auditors discussed in the preceding paragraphs have catalyzed a 'movement' for harnessing of IT technologies in the domain of audit. AI is fast becoming the buzzword for auditors. According to a 2017 report by Public Company Accounting Oversight Board (PCAOB), the accounting profession spends approximately \$3 billion to \$5 billion a year on technology and it is now part of the new baseline of operational costs for the major firms.

This paper purports to briefly introduce some of these revolutionary technological tools and methods which will determine the future audit. According to KPMG, Machine Learning (ML) and Deep Learning (DL) are two of the three forms of what is sometimes termed 'digital

labour', with the third being robotic process automation (RPA). On a spectrum of technological advancement, RPA is the most basic, ML is more sophisticated and DL is the most sophisticated of all.

### Artificial Intelligence (AI)

AI is an umbrella term that describes a number of technologies, like RPA, ML, Dee and a computer's ability to learn and mimic human thinking like judgment based decisions, reasoning, and cognition. AI refers to the simulation of human intelligence in machines that are programmed to think like humans and mimic their actions. In simple words, it is Cognitive Computing singularly focusing on mimicking human behavior and reasoning to solve complex problems. The term AI may be applied to any machine that demonstrates learning and problem-solving traits associated with a human mind. AI tends to be used in situations where adapting to new scenarios are important. AI seeks to train the computers to attempt to do things which at present human can do better. According to ACCA Audit and Technology Report 2019, 'AI often constitutes a combination of processing power and access to data: for instance, a computer will play a game such as chess by analysing all the possible outcomes of a move, using datasets from past games and selecting the winning option'.

AI is all geared to change the definition of reasonable assurance by focusing on a ledger in its entirety. While humans rely on judgment and random sampling, which can be time consuming and prone to missing items, AI tools have the capacity to analyze hundred percent of a dataset without 'requiring a human to create tests, write scripts, or memorize all the rules'. AI enables the analysis of entire populations of data to identify patterns or exceptions. With a view to offer risk-based assurance, transactions are marked for probes based on how they deviate from the data set. Thus unusual payments or activities that may not normally be caught by traditional testing practices are identified as probable risks. Artificial intelligence automates many tasks that were previously done manually. With the use of AI, auditors are freed from mundane tasks and can focus their time on deploying their skills, training and judgment. Auditors are free to explore and dive into details as they wish, providing a richer financial picture than ever before. AI-based systems continually learn and adapt to the data. As more information is entered and processed, 'AI analyzes secondary data and cross-correlates with the support of hundreds of variables'. Its use also reduces the amount of work. By having complete ledgers

ingested and analyzed, with little manual effort, it minimizes the need to go back-and-forth asking questions to the client. It is believed that AI, in future, will be commonly identifying anomalies based on risk rather than rules.

### ROBOTIC PROCESS AUTOMATION (RPA)

Robotic Process Automation (RPA) is software intended to automate repetitive production tasks to streamline business processes. RPA 'robots' are software routines that are more like very sophisticated Excel spreadsheet macros. Contesting for the title of the digital worker, RPA mimics human behavior to automate consistent routinized workflows in an effort to boost productivity. The rules are programmed and the bots can extract structured inputs from applications like Excel and enter them into SAP. The software works on the user interface just as a human would, seamlessly integrating with ERP and CRM systems.

ACCA's joint report with CA ANZ and KPMG Embracing robotic automation during the evolution of finance, defines RPA as a software that can be easily programmed or instructed by end users to perform high-volume, repeatable, rules-based tasks in today's world where multiple loosely integrated systems are commonplace. RPA is commonly used when the output of one financial process needs to be input into another, or where multiple sources of information need to be consulted. As a result, it is sometimes referred to as 'swivel chair automation', conjuring up the image of an employee swiveling their chair around as they consult multiple systems and re-key and check information

### Machine Learning (ml)

ML is a key subset of AI that automates analytical model building. ML uses these models to perform data analysis in order to understand patterns and make predictions. The idea of ML originated with the idea that machines could be taught to learn in ways similar to how humans learn. Where RPA uses technology to automate a process such as collecting data, ML is the science of getting computers to act without being explicitly programmed. In simple words, a computer recognizes patterns without having to be explicitly programmed. In the past decade, machine learning has given us self-driving cars, practical speech recognition, effective web search, and a vastly improved understanding of the human genome. ML uses algorithms to analyse data and make correlations and predictions (with human oversight). It is a more

'intelligent' form of technology than RPA.

According to a recent article published by CPA Journal 'machines are programmed to use an iterative approach to learn from the analyzed data, making the learning automated and continuous; as the machine is exposed to increasing amounts of data, robust patterns are recognized, and the feedback is used to alter actions. Machine learning and traditional statistical analysis are similar in many regards, but different in execution. While statistical analysis is based on probability theory and probability distributions, machine learning is designed to find the combination of mathematical equations that best predict an outcome. Thus, machine learning is well suited for a broad range of problems that involve classification, linear regression, and cluster analysis'.

In ML, algorithms acquire the knowledge or skill through experience. ML relies on big data sets to remind the data to find common patterns. ML uses statistical analyses to generate predictions or make decisions from the analysis of a large historical dataset. It has clear applications in risk management and the detection of fraud and inaccuracy by comparing historical data sets with current data, which can help with risk assessment. Or it can look forward, predicting, for example, the likely future value of an asset.

According to KPMG, ML is a vital step beyond robotics because the technology can capture data and identify correlations and patterns. 'It is also more intelligent than robotics — for example, it can locate specific line items by currency symbol and/or other keywords even if the placement varies from invoice to invoice — something robotics alone is not able to achieve. The technology can therefore be used to scan huge volumes of information'. For example, on various valuation matters, audit firms are developing applications to read bank loan agreements, leasing contracts, and other documents in order to find specific data and identify subjective areas. KPMG has developed smart audit platforms, to present their findings in powerful visualisation capabilities to organisations called a 'visual ledger'. This enhances their understanding of transaction flow and allows us to ask more precise questions on those transactions that stand out from the others.

Machine learning has the potential to disrupt nearly

every industry during the next several years, and the auditing profession is no exception. Jon Raphael, chief innovation officer at Deloitte, expects machine learning to significantly change the way audits are performed, as it enables auditors to largely "avoid the tradeoff between speed and quality"

### Deep Learning

DL means full-fledged artificial intelligence where a machine continuously integrates new information draws conclusions and absorbs the learning to enhance its cognitive abilities. DL is seen as one of the greatest potential prizes of emerging technology. With DL, the automation of some tedious and repetitive audit processes would significantly enhance audit effectiveness and efficiency. Given a sufficiently large sample of how auditors make decisions under various circumstances, a deep learning system allows auditors to automate many tasks that have traditionally been conducted manually, such as checking inventories, processing paperwork, reviewing contracts, and even drafting audit reports. The application of deep learning to improve audit efficiency and effectiveness is especially relevant to facilitating repetitive audit procedures and supporting audit judgments. Deep learning can add value for routine tasks that involve massive amounts of data and require significant effort for auditors to solve, such as text analysis, speech recognition, and parsing images and videos. It can also be used to reduce manual work by automating some substantive procedures, such as confirmation and examination. Furthermore, these competencies will allow auditors to perform tasks, such as examining all corporate contracts that are currently cost prohibitive or too complex for unaided human minds.

While full utilisation of deep learning is in the near future, KPMG is well positioned for it through KPMG Clara, which has been developed specifically to enable new technologies to be integrated, and the platform is fully scalable. According to KPMG, there are issues that will need to be resolved. For example, it will be critical to show that the algorithms and technology behind deep learning are valid and robust in order to understand and document the outcomes derived and not to be lead to 'false positives'. Regulators are actively working to keep pace with these emerging technologies. In the US, the American Institute of Certified Professional Accountants (AICPA) has published a guide to data analytics in the audit.

**Resources:**

This article is based on the concepts, knowledge and discussion points acquired/extracted from the following resources:

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# Forensic Audit in the Public Sector of Pakistan

**Mrs. Izzat Jahan**

Chief Accounts Officer, Pakistan Post

**Sharifullah Dawar**

Deputy Director FAOs

Office of the Auditor General of Pakistan



## 1. Introduction

Audit is the examination of entity's accounts by the auditors to determine if the accounts are accurate, present fair picture and give his/her independent view thereon. The Auditor's report on company's accounts provides insight to the company's management to improve the weak areas and provides the shareholders a blue print of the management's strengths and weaknesses. In the public sector, Auditor General's report is laid before the parliament in case of federal accounts and before the states/provinces in the case of states/provincial accounts wherein the spending of the public sector departments are reported to have been in accordance with applicable laws, rules and regulations and the accounts therein, maintained in accordance with the Generally Accepted Accounting Principles.

The Department of Auditor General of Pakistan has been mandated by the Parliament under Articles 169 and 170 of the Constitution to conduct compliance/financial audits of the budgets approved and allocated to different Ministries/Divisions/Attached departments and Statutory bodies in case of the federal government and provincial assemblies in case of the provincial governments with the objective to review the financial systems and transactions and ensure that the funds have been spent in a transparent manner, thereby helping the government to eradicate corruption in the country.

However, after the 18th Constitutional amendment, Article 170 was amended as Article 170(2) and the Auditor General of Pakistan was empowered to conduct audits of federal and provincial governments, as well as statutory authorities. With the arrival of statutory bodies under the audit domain, the Auditor General of Pakistan alongside traditional concept of compliance and financial auditing also initiated performance audits, special audits and special study reports on requests of the Principal Accounting Officers (PAOs) and/or directives of the Public

Accounts Committee and incumbent governments. The new auditing format stimulated the accountability mechanism and enhanced the significance of the Auditor General and reliance of the government thereon.

Meanwhile, white collar crimes infested the socio-economic fabric of the state at a steady pace and greatly perturbed the economy. The government took substantive measures to curb the menace of corruption, enhancing the role of NAB and FIA authorities but due to multiple reasons the aforementioned two investigating agencies' capacity to handle with white collar crimes came under question. Simultaneously, the Supreme Court of Pakistan began to take suo moto actions in mega corruption cases. In order to take some cases to a logical end, the Supreme Court started to rely on the audit authorities and directed the Auditor General to carry out forensic audits in a few cases dealing with public sector organizations. Thus, the role of the Audit department was further enhanced to assist the Supreme Court in their legal proceedings in corruption cases via provision of forensic audit reports.

## 2. Definition of Forensic Audit

Institute of Forensic Auditors (IFA) defines forensic investigation as "an activity that consists of gathering, verifying, processing, analyzing of and reporting on data in order to obtain facts and or evidence in a predefined context in the area of legal financial disputes, and/or regulative disputes (including fraud), and giving preventative advice". The word "forensic" is derived from the Latin word "forensis" which means forum, a public place where, in Roman times, senators and others debated and held judicial proceedings.

Forensic audit differs from other types of auditing in the sense that it involves criminal investigations and legal proceedings. Therefore, a forensic audit is carried out to prevent or detect misappropriation, corruption, bribery, extortion, fraud and embezzlement etc. and



prosecute a party thereof in the court of law.

Forensic auditors are certified public accountants who have skills both in criminology and accounting. They specialize in money trail, fraudulent and actual balance sheets and checking of overall inaccuracies in income and expenditure reports. They have a special training in forensic audit techniques, criminology and sociology and in legalities of accounting issues. They have good communication skills (verbal and written) and ability to interview and investigate the fraudster(s). They are expected to be analytical because the forensic audit reports need to be analytical, precise and very comprehensive.

### 3. Difference between Financial/Compliance Audit and Forensic Audit

Forensic audit is different from financial/compliance audit on the following grounds:

- Financial auditors review the financial statements so that they are prepared in compliance with GAAP and there is no material misstatement in the financial information. Forensic auditors are required to detect frauds and embezzlements in addition to the above job.
- Financial auditors provide a reasonable assurance that the financial statements present a true and fair view of the company's assertions. Forensic audit, however, is carried out against specific allegations of fraud or embezzlement leveled against the employees of a particular organization.
- Financial audit is conducted on the basis of the documents produced by an organization and is not necessarily legal in nature, while forensic audit is investigative, analytical and has a legal character.
- Financial audit reports are submitted to the parliament and provincial assemblies under Article 171 of the Constitution while forensic audit reports are submitted to the client and the court as legal or implicative evidence.
- Forensic audit examines the entire population to arrive at a factual position while financial audit examines a selection of a sample of total transactions on a test check basis.
- Financial audit is statutory in nature and its report is required to be prepared in accordance with the auditing standards of INTOSAI. Forensic audit is carried out by professional/certified accountants/auditors in case of private companies and can be carried out by the department of the Auditor General in case of public sector companies/ departments.

### 4. Objectives of Forensic Audit

The basic purpose of forensic audit is to

detect/prevent corruption, assets misappropriation, frauds and embezzlements so as to improve management accountability, corporate governance, audit functions and financial reporting system. Forensic auditors are mandated to bring evidences against the culprits in the court of law so that they may be prosecuted and punished. As white collar crimes are committed in a professional manner and in connivance by the perpetrators, they can be detected through forensic audit that involves investigation.

The primary motive behind white collar crimes is financial gain and lust for power; nonetheless, white collar criminals are also motivated by the following additional factors:

- They think they are professional insiders and cannot be caught.
- Everyone in the country/company is involved in making wealth and power.
- They have no regard for ethics and prevailing laws.
- They think law can be hushed up.
- They receive inducements, being in the position, to help or favor those whose interests can be served.

White collar crime is usually non-violent in nature. Such offences can be committed by an individual or by a group of conniving individuals serving the organization. Besides the insiders, there may be outsiders who may collude with the insiders to commit the offence. There is a range of white collar crimes that can be detected through forensic audit such as tax fraud, bribery, embezzlements, securities frauds and frauds in public funds etc.

### 5. Scope of Forensic Audit

Forensic audit covers a wide range of investigative activities. Apart from embezzlements and frauds, the forensic auditors also carry out investigations into disputes related to bankruptcy, business closures, and divorces. The forensic auditors provide evidence for legal proceedings in the courts; therefore, they also assist the courts as experts/ witnesses in fraud cases.

The forensic auditors conduct investigative auditing in embezzlement and fraud cases on the requests of the public and private companies and on the directives of the governments in cases of public sector departments. It is always a 'request audit'. In Pakistan, the Supreme Court of Pakistan has issued orders to the Auditor General of Pakistan to carry out forensic audits in cases of mega corruption in public sector projects

under its preview.

## 6. Process of Forensic Audit

Forensic audit investigation generally involves four major steps to be undertaken by the forensic auditors in order to gather evidence for use in the court of law against alleged fraudulent activity. Forensic auditors exercise the same steps to carry out financial audit; however, investigative techniques are used to gather relevant evidence in forensic auditing to address questions such as why the fraud was committed and for how long? How the fraud was committed and how was it concealed for such a long time? What amount was involved in the fraud? What were the motives of the fraudster and whether it involved other fraudsters or not? The audit investigators look for physical evidences at site or/and contained in documents. They also conduct interviews of the suspects before and after arrests. They determine whether the offenders have destroyed evidences or not. To actualize the process of forensic auditing and investigation, the following steps are undertaken:

i. Accepting a Forensic Audit Assignment: The conducting firm/agency needs to be sure of its ability to carry out the job on hand and have the legal mandate before accepting the assignment offered. Additionally, forensic auditors need to understand the necessary investigative techniques involved in forensic auditing. In the private sector, the firms also take business objectives into account and negotiate maximum compensation for its officials and officers involved in the forensic audit investigation.

ii. Planning of Forensic Audit: Planning is an essential requirement before undertaking any forensic activity. Forensic auditors must understand the objectives of their investigation and should plan their activities accordingly. The investigation team identifies the type of fraud committed and discerns its operational time. The team also determines the volume of fraud. They plan on how evidence can be gathered for use in court proceedings. They also work on how to report the fraud in a substantial manner and render advice in the report to prevent its recurrence in future.

iii. Evidence Collection: Evidences play a vital role in fraud and embezzlement cases that are prosecuted in the court of law. Therefore, the evidences gathered need to be concrete, substantial and exhibitable and fulfill the INTOSAI auditing standards as well as the laws of evidences. The quality of evidence is judged by the fact that it is sufficient to expose the fraudster(s), their motives for committing fraud, the scheme of

things they had planned and the losses incurred by the client/department. The evidences should be conclusive and free from gaps in the chain of custody and falsification. Moreover, the auditors must ensure that the evidences have not been tampered with or destroyed by the alleged suspect(s). The forensic auditors use Testing controls techniques to identify weaknesses and loopholes that paved the way for the identified fraud. They adopt Analytical procedure techniques through which they analyze and compare trends overtime to detect fraud. They also exercise Computer assisted audit techniques for the purposes of fraud detection where payment accounts and asset management accounts are maintained through Management Information System. Substantive techniques are used to collect evidences wherein data is reconciled, the cash available (if any) is counted and the documents are reviewed to create concrete, substantial and exhibitable evidence for the court of law. Forensic auditors also gather evidences through Interviews and discussions with employees of the organization.

iv. Reporting: After completion of forensic audit, the investigation team submits its findings along with the summary of evidences collected and conclusion drawn, and mentions the loss suffered by the client/department as a result of fraud. The auditor's report describes explicitly how the fraudulent scheme was envisaged and how the fraudsters circumvented loopholes in the internal controls, and points out the existing weaknesses in the system. The report is thoroughly supported by substantial, concrete and exhibitable evidences. It is well edited and presentable in the court of law for legal proceedings. The report gives recommendations at the end for prevention of fraud in future. Alternatively, the report is presented to the requesting client/department so that they can sue the fraudsters in the court if they so want.

v. Court Proceedings: After submission of the auditor's forensic report, the client/department may file a case against the suspected fraudster(s) who may be prosecuted in the court. As producers of the report, forensic auditors are needed to be present in court proceedings. They may be summoned to assist the judges in understanding the complex accounting issues and accounting jargons unknown to them and the prosecutors.

## 7. Impact of Forensic Audit

Forensic audit has far-reaching positive and negative impacts on the financial and corporate sectors which

are underlined below:

#### Positive impacts

- Forensic audit would instill fear in the minds of management and employees that their frauds and embezzlements would be detected; the ratio of frauds would be reduced to greater extent.
- It would enhance shareholder and investor confidence due to improvement in corporate governance.
- Outcome of proper utilization of the public sector development funds would be shown and the impact would be vividly noticed in the socio-economic indicators.
- The use of forensic auditing techniques by statutory auditors would augment their capacity and hone their skills increasing their credibility in the corporate sector.
- Role of the Auditor General (DAGP) would be enhanced. The federal and provincial governments would rely on DAGP in fraud and embezzlement detection cases. This in turn would reduce the forensic auditing costs borne by the public exchequer.
- The DAGP would help the government achieve its sustainable development goals (SDGs) by the end of 2030 by becoming a force of deterrence against corruption.

#### Negative impacts

Forensic audit poses a real threat to the confidentiality of financial information in the case of private companies. However, in case of the Auditor General of Pakistan conducting audit as statutory responsibility, the state bears the cost of forensic audits as a charged expenditure on the exchequer. There is minimal threat of any confidentiality breach of information.

As a result of detection of fraud by the forensic auditors, the management personnel may face threats and intimidation from those who are identified as suspects in the fraud/embezzlement. It can also affect the image and reputation of the company which may harm the profitability of their business.

### 8. Forensic Audit in Pakistan: Issues

As mentioned earlier, forensic audit is a new phenomenon in the public sector of Pakistan. The constitution of Pakistan provides for statutory audit of the accounts of federation, provinces and of any authority or body established by the federation and provinces. However, the Supreme Court of Pakistan assigned the job of forensic audits of e.g. Nestle to the Auditor General which set a new paradigm for his

department. Every new journey faces certain difficulties and bottlenecks in the course of its manifestation. Some of the issues facing public sector forensic audit in Pakistan are thus highlighted below:

• **Legal lacuna:** The Auditor General of Pakistan has been mandated under Article 170(2) of the Constitution, read with Sections 8 and 12 of the Auditor General's functions and powers, Ordinance 2001 to conduct statutory audit of the receipts and expenditure of the federal and provincial governments and of any authority or body established by the federal and provincial governments. The statutory audit includes compliance, financial, performance audit, special audit and special study reports. The Auditor General's department began to carry out forensic investigations in few mega projects specifically on the orders of the Supreme Court of Pakistan. Strictly speaking, this was a departure from its traditional mandate. The legal implications of the forensic investigation by the statutory auditors can better be expounded by legal experts; however, the constitutional mandate under the above mentioned Article doesn't provide for forensic audit by the AGP.

As a result of this legal lacuna, forensic investigative tasks concerning financial matters have been assigned to Federal Investigation Agency (FIA) and National Accountability Bureau (NAB) which don't have the capacity to conduct forensic investigations involving financial frauds, embezzlements, money laundering and other financial matters.

Besides, Qanun-e-Shahadat Order, 1984 has been amended in 2002 to make forensic investigation a tool of the justice system in Pakistan. Article 2(e) and (f) of the said Order says that the expression, "automated", "electronic", "information", "information system", "electronic document" and "electronic signature" etc. shall bear the meanings given in the ETO 2002. Article 30 further states that "the statements generated by automated information system may be attributed to the person exercising power or control over the said information system". This signifies that digital evidence with regard to financial matters can be produced and accepted in the court against the fraudster(s).

• **Lack of capacity of statutory auditors in Forensic investigation:** The Auditor General's department has many competent, diligent and professional auditors to conduct audit but they are not well trained in investigative skills. As the forensic audit reports have to be presented in courts as evidence and the auditors are required to assist the judges and prosecution in court proceedings, the auditors of

DAGP will require focused trainings and preparation in forensic auditing.

- Lack of integrated financial management system in the public sector: Forensic audit is, most often than not, conducted through computer software programs for which automated financial management system is required in public sector departments. In fact, most of the civil departments of the federation and provinces are linked to the SAP system but there are still a number of departmentalized accounts which are beyond the purview of SAP. Hence, forensic audit of those entities are difficult.

## 9. Recommendations

Forensic audit, though a new phenomenon in public sector auditing, is the dire need of today's Pakistan to deter the rising incidences of frauds, embezzlements and corruption in public funds and public sector companies. The initiation of forensic audit in public sector projects will instill fear in the minds of the public sector management and officials that frauds can be detected and perpetrators can be sued in the court of law. To make forensic audit a success, the following steps are proposed to be undertaken by the DAGP:

- As a matter of policy, a case may be taken up with the concerned quarters to enact law authorizing the Auditor General to conduct forensic investigation in fraud cases on the orders of the Supreme Court, the Prime Minister, and the Cabinet or on special requests of the Principal Accounting Officers (PAOs).
- Forensic audit is a specialized job. A special group of forensic auditors may be created within DAGP to carry out forensic investigations if and when required. The said group may consist of Data Analysts, Forensic Scientists and other members who have a wide experience in forensic investigation and financial matters.
- Officers chosen for forensic audit assignments may be required to go through formal training at National Forensic Science Agency, Islamabad to acquire the requisite forensic investigation skills and techniques.
- Public finance management policy is in the process of being formulated. The Auditor General of

Pakistan may offer to extend SAP system to entities which are not linked to SAP system across the country.

- The DAGP may also seek special remuneration for forensic auditors for their extensive job of investigation into fraudulent financial matters that also involve court proceedings.

And/Or

- Alternatively, given the existing laws, the Auditor General of Pakistan can continue playing an active role in the conduct of Forensic Auditing in the public sector as proposed in the following Model:

\* Since Forensic Auditing is a specialization within the field of accounting, for the Auditor General this would mean using accounting skills competently to detect fraud and embezzlement in financial statements in a focused manner.

\* Therefore, as administrative head of Pakistan Audit and Accounts Service (PAAS), the Auditor General may create a special purpose team of competent officers who excel in the knowledge of accounting (Crack Experts) and have reasonable experience.

\* He may then align NAB, FIA, and other Anticorruption agencies after formally negotiating with the heads of respective organizations mentioned above, to provide/loan our forensic experts as a member of their forensic investigative teams which would basically be headed by NAB, FIA etc. as these agencies have the legal mandate to examine criminality and prosecute the accused.

\* It is thus proposed that a forensic audit assignment may preferably be a joint venture of related agencies to achieve optimum results.

\* After due investigations the report on the evidence gathered can then be presented in different courts by the agencies mandated to do so by law, and the Auditor General's assistance in their efforts can thus be acknowledged formally without requiring the Auditor General to bear the onus of conducting the whole exercise on his own.

\* If the Auditor General so deems fit, he may present the said report in PAC for their information.

## SAI in an age of Disruptive Technologies

**Muhammad Kashif**

Director to the Auditor General of Pakistan



The world is undergoing tremendous technological changes. The governance structure is witnessing shift from its traditional ways of delivering to modern public service delivery systems. The organizational behavior has set to change to achieve its specific organizational goals. Supreme Audit Institutions need to realign their organizations with the changing environment so that they can play an effective role in promoting accountability and transparency across the executive departments.

Disruptive technologies, that include but not limited to Mobile Internet, Artificial Intelligence, Blockchain, Cyber Security, Internet of Things, Data Analytics, Cloud Storage and Renewable Energy, are reshaping the business processes at growing pace in public sector organizations. A SAI needs to identify these changes and strive for equipping itself with new capacities and technologies for combating modern challenges in Public Sector Auditing.

A Public Sector Auditor conducts three types of Public Sector Audits as recognized by ISSA-100. These audits include Financial Audit, Performance Audit and Compliance Audit and vary in terms of their purpose, methodology, scope and assessment criteria. SAI needs to develop its skills and capacity to conduct each type of audit as per modern needs. A SAI may become redundant in its contemporary environment if it does not employ modern technological techniques in its business processes and the ways to conduct audit. SAI can learn from examples of various big multinational organizations that failed to adapt the changing environments and have now become extinct. For example, Kodak dominated camera and film-maker business for over hundred years till 1990s. It did not adopt new digital technology and had to file bankruptcy in 2012. Now digital cameras are dominated by Canon and Nikon. Similarly, Borders (book-seller) replaced by Amazon and Blockbuster (video-seller) by on-demand video streaming like Netflix and Hulu Plus etc. The case of Nokia that used

to be global leader in mobile phone may be an eye-opener for the SAIs. In fact, non-adopting of new technology means extinction. A SAI needs to learn concepts of modern technologies like AI, Blockchain, Data Analytics, Cyber Security etc. to remain relevant with the growing technological trends.

Introduction of disruptive technologies into the government systems has also brought changes in control and risk environment of the business process of the entities. It becomes imperative for the Public Sector Auditor to develop understanding towards these new risks associated with the adoption of modern technologies. SAIs may give due considerations to technological mega-trends while developing their Strategic and Annual Audit Plans as per INTOSAI Standards. Understanding towards contemporary changes in risk and control environment will help Public Sector Auditor at Planning and Execution stages of various kinds of audit assignments to produce quality and relevant audit reports.

The Government of Pakistan has undergone tremendous technological changes during the last two decades. It has started e-governance, computerized its accounting system on erp SAP across the country, established ministry of IT, Pakistan Information and Technology Board and recently launched Digital Pakistan Project to digitize various sectors of economies and to take the benefits of IT revolution to its masses. Further, the project of online submission of bills to the payment and accounting system is going to bring fundamental changes in the landscape of public financial management.

SAI Pakistan, under the visionary and vibrant leadership of Mr. Javaid Jehangir, Auditor General of Pakistan, is cognizant of emerging needs in Public sector Auditing. Recently, SAI Pakistan has embarked upon project of Audit Management Information System (AMIS) to computerize its business processes



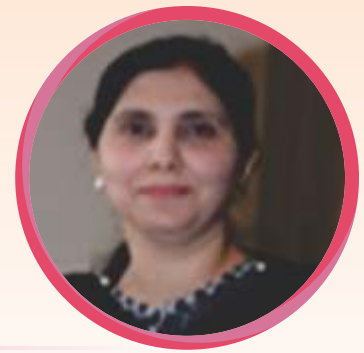
and to give quality audit reports. As part of its policy to re-align itself with the changing priorities of its stakeholders the SAI Pakistan is in process of switching to sectoral reporting instead of traditional mode of transaction reporting. Various sectoral audit offices focusing on audit of one specific area like Petroleum, Power, Water Resources and Social Safety Nets have been established in line with the expectations of the stakeholders. Though SAI Pakistan has sufficient pool of IS auditors (CISA qualifies), forensic auditors, professional accountants and holders of certifications like CISM, IPSAS, it has launched an incentivized scheme to further encourage its auditors to pursue various certifications and qualifications.

However, re-aligning of SAI with the changing technological environment cannot be achieved without capacity development of its human resources. Therefore, SAI Pakistan has developed a Continuing Professional Development Program (CPDP) as envisaged by ISSAI-100 to improve skills and capacities of the auditors. The CPD comprises of various courses as per technological environment of its stakeholders. The dynamic nature of CPD is one of the salient features that allow SAI to include new courses on disruptive technologies as adopted by the stakeholder's time to time. The SAI Pakistan believes in adopting modern technologies to remain relevant in the contemporary environment.

## Performance Audit Report -A Different Approach

**Mrs. Afshan Salman,**

DG Performance Audit Wing,  
Department of the Auditor General of Pakistan



In any of the SAI of the world reporting of the audit findings is considered as the most important part of the audit activities. It is the end result of auditors' observations. Through audit report the stakeholders i.e. legislature, public, press, investors and other institutes of accountability get to know about the health of the accounts and financial matters of public departments. . Apart from the routine annual compliance or financial audit reports each SAI also prints some performance audit reports. These reports are published on the performance of different ongoing /completed projects initiated by the government. These performance audits are conducted mainly on the basis of the routine audit plan or on the special request of the government.

### **Difference Between Performance Audit Report and Other Audit Reports**

Performance audit report is different from the other audit reports in its form and substance. It reports upon the outcomes of a project or a program against its stated objectives while keeping in view the economy, efficiency and effectiveness of its operations. In the financial and compliance with authority audit reports the findings are made against the violation of relevant accounting or financial rules but in performance auditing the auditor focuses on economy, efficiency and effectiveness in the utilization of resources, emphasizing on improving management and accountability of the managers. It is also a point of interest that many SAIs in the world have also adopted the concepts of ethics, equity and environment in addition to already focused principals of economy, efficiency and effectiveness. These principles question during the performance audit about the equal and justifiable distribution of resources and whether the measures to protect the environment during the implementation of a project have been taken?

As we find in the case of financial audit reporting the errors and omissions are found on the basis of internal record checking but in performance audit reporting is

done on the basis of both internal and external evidence. In financial and compliance audit the criteria are usually fixed accounting standards and financial rules and regulations. But in performance audit the criteria are unique in each case. It generally uses applicable rules and regulations and generally accepted management practices.

The knowledge required for financial and compliance audit is accounting and auditing but in performance audit the auditors should have the back ground knowledge of the different fields depending on the nature of the operations of the project. The team undertaking the performance audit should be the fine combination of the persons having relevant expertise and experience. In performance audit the auditor's personal interest and ability to evaluate and judge the things plays a very important in reaching towards conclusion. The methodology used in performance auditing varies from audit to audit depending upon their nature but in other forms of audit the standard methods are applied not only during the audit but also in reporting.





**ECOSAI Secretariat**

Office of the Auditor General Pakistan, Constitutional Avenue, Islamabad. 44000, Pakistan

[www.ecosai.com.pk](http://www.ecosai.com.pk)