



Performance Auditing Guide

Office of the Auditor General
Babar Mahal, Kathmandu

June 29, 2000

Preface

This Performance Auditing Guide has been prepared in a new look on the technical assistance of the World Bank with a view to enhancing the Performance Auditing Capability of the Office of the Auditor General Nepal (OAG/N). In the past performance auditing materials acquired from various sources were compiled in 1995 on the assistance of the Bank.

Performance audit is more complex and challenging compared to the audit of compliance, as it provides appropriate recommendation for improvements after examining whether economy, efficiency and effectiveness have been maintained in the use of available resources and means. I am confident that this guide will help conduct performance audit in a simplified but effective way.

The contents of this guide include selection of issues, audit planning and acceptance, execution of audit, reporting, documentation and quality review and follow-up. This guide has experimentally been tested in the performance audit of three projects funded by the World Bank and the Asian Development Bank and updated with the feedback. The performance audit by the OAG/N will be conducted in accordance with this guide.

Efforts have been made to make the guide error free. However, OAG/N will be grateful if the user could acknowledge any error or suggestion to Performance Audit Division or Planning, Research, Methodology and Human Resource Development Division of the OAG/N.

I appreciate the World Bank for assisting OAG/N to enhance its auditing capability. Similarly I express my thanks to the Auditor General of Malaysia for sharing professional experience in making the guide meaningful. I also express my thanks to the staff involved in preparing the guide and the consultant.

Kathmandu
June 29, 2000

(Bishnu Bahadur K.C.)
Auditor General

Performance Auditing Guide

Subject

Preface

Para		Page
10 "Introduction Section"		
10.1	Performance Audit - Diagram	1
10.2	Use and Users	2
10.3	Use of Professional Judgement	2
10.4	Implementation Responsibility	2
10.5	Definition of Performance Audit	2
10.6	Need for Performance Audit	3
10.7	Performance Audit Versus Financial Audit	3
10.8	Objectives and Scope of Performance Audit	5
10.9	Audit Approaches	5
10.10	Auditing Standards	7
10.11	Performance Audit Mandate	8
10.12	Performance Audit Progress Record	8

- **Audit Tool**
 - 1 Performance Audit Progress Record Form 9

20 "Selection of Subject/Unit Section"

20.1	Need for Selection	12
20.2	Steps in Selection	12
20.3	Key Issues Criteria and Matrix of Selection	14
20.4	Common Issues in the Selection	16

- **Audit Tool**
 - 2 Selection Criteria and Matrix 17

30 "Planning Section"

30.1	Performance Audit Planning - Diagram	18
30.2	Objective	19
30.3	Policy & Procedure	19
30.4	Performance Audit Planning	19
30.5	Engagement of Personnel	20
31.1	Introduction of Overview Stage	21
31.2	Review Background Information	21
31.3	Review Operational Objectives, Strategy and Mandates	24
31.4	Sources of Overview Information	25
31.5	Determining Lines of Audit Enquiry	26
31.6	Importance of Overview Stage	26

31.7	Contents of the Overview Report	27
32.1	Introduction of Survey Stage	27
32.2	Operational Process Analysis of Key Process	28
32.3	Risk Assessment	31
32.4	Matters of Potential Significance	34
32.5	Audit Objectives	35
32.6	Audit Scope	35
32.7	Audit Criteria	36
32.8	Logistic Management	37
32.9	Audit Budget	38
32.10	Contents of the Audit Plan	38
•	Audit Tool	
3	Segment Operation Model	39
4	Information Collection Form	41
5	Process Analysis Template	58
6	Risk Assessment Process	62

40 "Audit Execution Section"

40.1	Audit Execution (Control and Performance Assessment) - Diagram	68
40.2	Policies	69
40.3	Objectives of Audit Execution	69
40.4	Control Assessment	70
40.5	Audit Programme	71
40.6	Execute Audit Test Procedures	73
40.7	Optimisation of the Control Design	74
40.8	Performance Assessment	74
40.9	Audit Evidence	75
40.10	Techniques for Gathering Audit Evidence	77
40.11	Sampling	77
40.12	Statistical Versus non Statistical Sampling	78
•	Audit Tool	
7	Audit Programme	80

50 "Reporting Section"

50.1	Reporting Procedure - Diagram	81
50.2	Subject Matters and Structure of Report - Diagram	82
50.3	Policy & Objectives	83
50.4	Types of Report	83
50.5	Contents of the Report	83
50.6	Characteristics of the Report	84
50.7	Audit Findings	85
50.8	Developing Conclusion and Recommendations	86
50.9	Reporting Activities	87
•	Audit Tool	
8	Audit Finding Form	88

60 "Documentation Section"

60.1	Policies	89
60.2	Objective of Documentation	89
60.3	Contents of Audit Work Papers	89
60.4	Characteristics of Working Papers	90
60.5	Audit File Structure	90
60.6	Completing and Reviewing Audit Files	91
• Audit Tool		
9	Audit File Documentation	92
10	Audit Review Form	93

70 "Peer Review/Post Audit Quality Review System (PAQRS) Section"

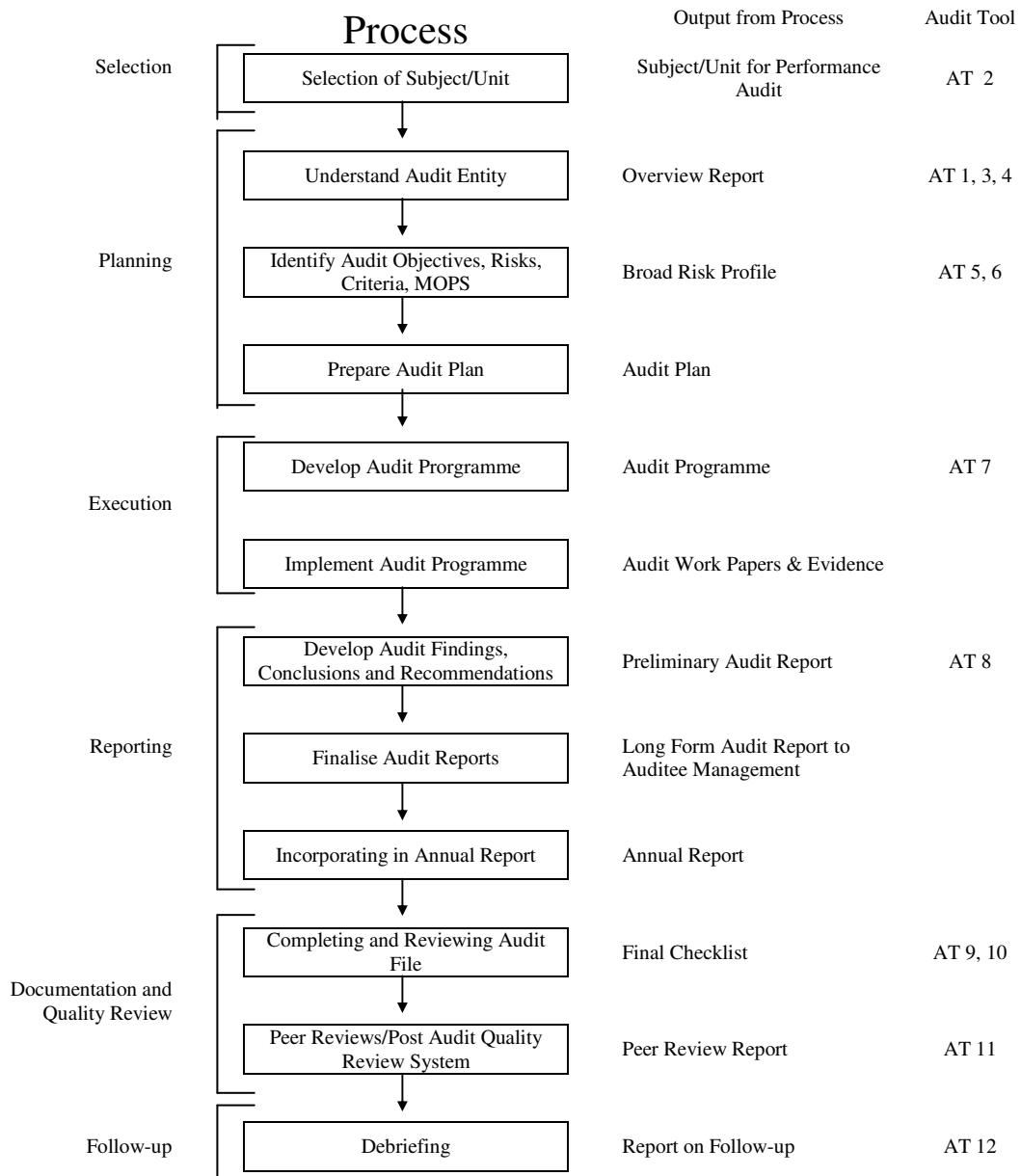
70.1	OAG Policy on Quality Control/Peer Reviews	94
70.2	INTOSAI Pronouncement on Quality Control Review	94
70.3	Objectives of Peer Review and Establishing a PAQRS	94
70.4	Overview of Peer Review/PAQRS	95
70.5	Basis of Peer Review/PAQRS	95
70.6	Conduct of the Review	96
70.7	Performing the Review	97
70.8	Conclusion and Reporting	98
• Audit Tool		
11	Performance Audit Peer Review/Post Audit Quality Review System "PAQRS" Form)	100

80 "Follow-up Section"

80.1	Policies	110
80.2	INTOSAI Pronouncement	110
80.3	Needs and Objectives of Follow-up	110
80.4	Follow-up Process at Office of the Auditor General	111
80.5	Responsibility for Implementation of Recommendations	111
80.6	Issues in Follow-up	111
80.7	Reporting Format	111
• Audit Tool		
12	Annual Report, Response and Decision of PAC	112

10 "Introduction Section"

10.1 Performance Audit - Diagram



10.2 Use and Users

10.2.1 The purpose of this Guide is to provide a framework to establish policies and provide guidance on the general principles and approaches governing a performance audit.

10.2.2 The framework applies to all performance audits undertaken by the Office of the Auditor General.

10.2.3 The policies set out and explained in this Guide, along with the other guidance provided from time to time, forms the basis for the Office of the Auditor General's approach in carrying out the performance audit engagements.

10.3 Use of Professional Judgement

It should be recognised that no guidance or policy of general application could suit all circumstances. Therefore, the auditors are required to exercise their professional judgement in using the Guide. If a particular approach, method, process, or procedures is inappropriate for a specific auditee and a more suitable and practical alternative can be used, then the alternative way should be used after obtaining the appropriate approval from the Assistant Auditor General in charge of the assignment. The approved departure should be adequately documented in the audit files.

10.4 Implementation Responsibility

10.4.1 The Assistant Auditor General - Performance Audit Division has direct management responsibility for implementing performance audit engagements, and has a coordinating role with other Assistant Auditor General to achieve a higher level of professional performance.

10.4.2 The Assistant Auditor General - Performance Audit Division is assigned to develop and recommend plans and programme for improving the efficiency and effectiveness of performance audit engagements. This includes conducting appraisals to evaluate the organisation, personnel management, objective, methods and accomplishment against policies, procedures and generally accepted standards of professional performance, and the follow-up to assure that understood and accepted recommended improvements have been accomplished.

10.5 Definition of Performance Audit

10.5.1 The concepts of “economy, efficiency and effectiveness (3Es)” are termed as follows.

- “Economy” means the acquisition of the appropriate quality and quantity of human, financial, physical and information resources at the appropriate times and at the lower cost.
- “Efficiency” means the use of human, financial, physical and information resources such that the output is maximised for any given set of resource inputs, or input is minimised for any given quantity and quality of output.

- “Effectiveness” means the achievement of the objectives or other intended effects of activities.

10.5.2 A performance audit assignment may include all/one or a combination of two aspect of “3Es”.

10.5.3 Regularity and propriety related issues which impact performance may be considered in the conduct of performance audits.

10.6 Need for Performance Audit

10.6.1 Performance audit is the outcome of the important efforts directed to improve the system of management to ensure genuine output from resources employed. The concept of performance auditing emerged in response to :

- increasing demand for information on efficiency and economy in managing resources and the effectiveness with which objectives are met;
- need to determine whether :
 - the operations of audit entities were conducted in a way that ensures the best possible use of resources or considering the 3Es;
 - officials in the public sector have met their accountability obligations;
 - reporting on performance is credible and adequate.

10.6.2 Performance audit provides the legislature and the public with an assessment whether the audited entities are achieving real value-for-money. It intends to arrive at a verifiable condition for comparing what is being done and how well it is being done with the plans, policies and standards.

10.6.3 The mere awareness that the basis for decision making is subject to scrutiny by the auditors may, by itself, compel public administrators to exercise caution and prudence in their actions.

10.7 Performance Audit Versus Financial Audit

10.7.1 Auditing is a process involving the examination of data, statements, records, operations and performance of an auditee for a stated purpose. The full scope of government auditing includes regularity and performance audit. Performance auditing goes beyond the consideration of regularity. It aims to determine to what extent the auditee has discharged its financial or other responsibilities which, imply assessment of the auditee's operation in terms of the *economy* in acquiring resources, *efficiency* in using resources and *effectiveness* in achieving objectives.

10.7.2 The major differences in the approach, scope and objectives between financial audits and performance audits are explained in the following table.

Financial Auditing	Performance Auditing
1. Uses financial data to express an opinion on financial position and compliance with existing rules and	1. Uses financial as well as non-financial data to assess economy, efficiency and effectiveness in

Financial Auditing	Performance Auditing
<p>regulations and determines whether:</p> <ul style="list-style-type: none"> • the financial statements of the auditee fairly present the financial position, reflect results of operations and cash flows or manifest changes in financial position in accordance with generally accepted accounting principles; • the auditee has complied with laws and regulations for those transactions that may have a material effect on financial statements. 	<p>the management of resources and determines whether:</p> <ul style="list-style-type: none"> • the reporting on performance fairly present the accomplishment and/or impact; • auditee is managing its resources in an economical, efficient and effective manner.
<p>2. Its objectives are:</p> <ul style="list-style-type: none"> • to obtain sufficient, competent evidential matter to enable the auditor to form and express an opinion on the auditee’s financial report; • to promote compliance with laws, regulations, agreements, directives, policies and procedures as necessitated by statutory and/or auditee requirements; • to encourage application of generally accepted accounting principles; • to establish confidence in the reliability and integrity of the financial management system and the reports generated by it. 	<p>2. Its objectives are:</p> <ul style="list-style-type: none"> • provision of a basis for improvement of public sector management of all resources; • improvement of the quality of information on the results of public sector management that is available to policy makers, legislators and the general community; • encouragement of public sector management to introduce processes for reporting on performance; • provision for more adequate accountability.
<p>3. Does not comment on the extent to which auditee is meeting target relating to output and delivery of services to the targeted groups they are serving.</p>	<p>3. Evaluates the extent to which auditee is meeting the target relating to output and delivery of services to target groups they are serving.</p>
<p>4. Does not make recommendations for improving economy, efficiency and effectiveness of programme or projects being audited.</p>	<p>4. Offers general and specific recommendations for improving economy, efficiency and effectiveness of the auditee being audited.</p>
<p>5. Concentrates attention on individual transaction to determine whether the transaction complies with laws and</p>	<p>5. Considers transaction and performance from overall accountability framework.</p>

Financial Auditing	Performance Auditing
regulations.	
6. Aims to strengthen control environment to reduce non-compliance.	6. Aims to improve overall performance capability to encourage better management of resources.
7. Regularity and propriety are major aspects.	7. Economy, efficiency and effectiveness are major aspects.

10.8 Objectives and Scope of Performance Audit

10.8.1 The objectives of performance audits are to audit the economy, efficiency and effectiveness of auditees and to evaluate the discharge of accountability and due care of probity in the use of resources.

10.8.2 Performance audits focus on one or more of following interrelated elements:

- to provide objective assessment of the extent to which the auditee is currently pursuing the 3Es;
- to identify major deficiencies in management and control practices;
- to encourage improvement in the system of performance reporting;
- to provide information and propose recommendations that can lead to better internal control and public accountability.

10.8.3 Performance auditing covers a wide variety of issues to arrive at the conclusion relating to the 3Es. It examines and evaluates the systems, procedures, operation and result related to:

- planning, budgeting, accounting and reporting systems;
- development, appraisal and utilization of resources;
- acquisition and utilization of property, equipment, plant, inventory and other assets; and
- development, production and use of information.

10.9 Audit Approaches

This appendix gives guidance both on the selection of an audit approach (es) whilst designing the audit test procedures for audit programmes as well as the implementation of the audit approaches.

The audit approach should be flexible because of the differing nature of each auditee. Different approaches may be required for different issues.

Approach?	Why?	How to implement?
Analysis of procedures/ procedure-oriented approach	<i>Process Level</i> <ul style="list-style-type: none"> • Focus on compliance with established criteria, best practices 	<ul style="list-style-type: none"> • Examine the relevant programme and activities. If control deficiencies are

Approach?	Why?	How to implement?
<p><i>Suggested stage:</i> Audit execution- assessment of control system</p>	<p>or desirable control model</p> <ul style="list-style-type: none"> • Assess the extent to which the activities, systems and procedures are well designed or implemented • Optimise the controls 	<p>significant, assess the results or outputs of the programmes, activities or concerned organisational units</p> <ul style="list-style-type: none"> • Suggested audit techniques include observation, interviews/ discussions and examination of documents
<p>Analysis of results/ result-oriented approach</p> <p><i>Suggested stage:</i> Audit execution- performance assessment</p>	<p><i>Programme/Activity Level</i></p> <ul style="list-style-type: none"> • Focus on programme outputs • Assess conformance with specific audit criteria • Identify problems with output and programme delivery <p><i>Process Level</i></p> <ul style="list-style-type: none"> • Quantify the effectiveness of activities within a process, or the outputs of a process, in achieving specific audit criteria 	<ul style="list-style-type: none"> • Examine key performance indicators in relation to identified controls for high risk areas on conformance with audit criteria • Perform substantive procedures (including analytical review) to obtain evidence on completeness, accuracy and validity of data • Suggested audit techniques include observation, interviews, examination of documents and data analysis
<p>Case study approach</p> <p><i>Suggested stage:</i> Overview/ Survey/ Audit Execution (as the case may be)</p>	<ul style="list-style-type: none"> • Represents “a method for learning about a complex instance, based on a comprehensive understanding of that instance obtained by extensive description and analysis of that instance, taken as a whole and in its context” (<i>Source:</i> The United States General Accounting Office) • Aim to understand each case studied in all relevant aspect, in answering particular 	<ul style="list-style-type: none"> • Case selection depends on the purpose of the study (i.e. sampling may not be suitable) • As far as practicable, analysis should be illustrative, exploratory and contains critical application of knowledge to findings • Some issues may require generalised findings

Approach?	Why?	How to implement?
	types of questions	
<p>Surveys</p> <p><i>Suggested stage:</i> Overview/ Survey/ Audit Execution</p>	<ul style="list-style-type: none"> • Aims to collect information from members of a population to determine the incidence, distribution and interrelation of events and conditions • Complement other audit approaches to provide a coverage of larger samples • Used for cross-section analysis (e.g. to gather information about programmes administered by a variety of agencies) 	<ul style="list-style-type: none"> • Design survey questionnaire to obtain, clarify or confirm relevant data in respect of the programme area • Allocate adequate resources to complete the project effectively. Surveys may be outsourced to outside consultants by the OAG on account of time-constraint and/or lack of expertise
<p>Use of existing data</p> <p><i>Suggested stage:</i> Overview/ Survey/ Audit Execution</p>	<ul style="list-style-type: none"> • Provides relevant information for performance audit work • Provides exploratory analysis 	<ul style="list-style-type: none"> • Used for primary data analysis involving first-hand data usage for specific purpose or secondary data analysis involving using collected data for some other purpose • Examination of variables or trend analysis (graphical, ratios, etc.)

10.10 Auditing Standards

Performance audits undertaken by the public sector auditors are conducted in accordance with auditing standards consistent with the professional standards required of private sector auditors. Ethical principles govern the auditors' professional responsibilities; independence; integrity; professional competence and due care; confidentiality; professional behaviour; and technical issues. These standards are reflected in the INTOSAI's Auditing Standards, Government Auditing Standards and the INTOSAI Code of Ethics for the public sector.

10.11 Performance Audit Mandate

The Constitution of the Kingdom of Nepal, 1990 confers on the AG the authority to audit "economy, efficiency and effectiveness" of the financial management of

the Executive, Judiciary, legislative body and all corporate bodies subject to audit by the Auditor General which go beyond the traditional framework of financial statement, regularity or compliance audit. Since the OAG has mandate to work extends into the area of value - for - money audit. The relevant constitutional and legal provisions are quoted below :

- **Article 100 (1) of the Constitution** : *The accounts of the Supreme Court, the Parliament, the Raj Parishad, the Commission for the Investigation of Abuse of Authority, the OAG, the Public Service Commission, the Election Commission, other offices of the Constitutional Bodies, the Royal Nepal Army and the Nepal Police, and all other government offices and courts shall be audited by the AG in the manner as determined by law with due consideration to the regularity, economy, efficiency, effectiveness and the propriety thereof.*
- **Section 3 of the Audit Act, 1991**: *It provides the mandate of determining the audit scope, process and duration. The OAG can decide which aspect(s) (regularity, economy, efficiency, effectiveness and propriety) would be considered while planning, executing and reporting of any audit.*
- **Section 4 and 5 of the Audit Act, 1991**: *It provides the matters to be audited considering regularity, economy, efficiency, effectiveness and propriety. Of the various matters, the following provisions relate specifically to 3Es auditing. In this context, audit is required to determine whether :*
 - *the organisation, management and job allocation of the Office are sufficient and proper and are they operating accordingly;*
 - *any function is being unnecessarily performed in duplication by any employee or agency or any essential function is being omitted;*
 - *the available resources, means and assets are properly utilized and the maintenance and preservation thereof against any loss or damage has been properly arranged;*
 - *the progress has been achieved within scheduled time and the quality and quantity of the work is satisfactory;*
 - *the objective and policy of the Office is explicit and the programme is delineated conforming to the specified objective and policy;*
 - *the programme is being implemented within the limits of approved cost estimate and the proceeds received in comparison to the cost is reasonable;*
 - *the arrangements for maintaining data relating to target, progress and cost are adequate and reliable;*

10.12 Performance Audit Progress Record

Completed works in various stage of performance audit have to be recorded and approved. Audit Tool-1 has to be applied.

Audit Tool - 1 (Performance Audit Progress Record Form)

Audit Unit

Engagement Team

Assistant Auditor General	
Audit Director	
Audit Officer	
Others	
External experts or specialists	

Parties Involved	Organisation/Person	Contact(s)
Entity subject to audit		
Experts engaged		
Financial Audit Team		

Performance Audit Progress Sign-Off	Initials and date		
	Auditor in-charge	Audit Director	AAG
Confirm that engagement team have read, are familiar with and have applied the relevant sections of the Performance Audit Guide.			
Overview stage completed in accordance with the Performance Audit Guide and lines of audit enquiry discussed with the AAG and approved.			
Survey stage completed and matters of potential significance discussed with AAG and approved in the audit plan.			
Audit execution procedures complied with and completed, salient features discussed with Audit Director and problems resolved.			
Reporting procedures complied with and completed, salient features discussed with Audit Director and problems resolved.			
Confirm that engagement is complete and report(s) and/or letter(s) may be signed.			
Working papers are completed and Performance Audit Progress Record signed off.			

Work completion procedure of Audit Officer and Director is as follows:

- **Overview and Survey Stage**

box when completed

Confirm with the AAG that findings from the selection process substantiate carrying out a performance audit.

Confirm that on completion of planning, no reasons were found not to go ahead with the audit.

Ascertain nature of letter(s) and/or report(s) required, their addressees and their purposes.

Identify need for special expertise from the OAG/N or external consultants.

Establish timetable and budget for audit.

Inform other auditors involved if reliance is going to be placed on their work.

Agree overview report with the AAG

Agree audit plan with the AAG

• **Audit Execution Stage**

✓ box when completed

Identify any relevant legislation.

Matters of potential significance agreed and discussed with audit team.

Formulate audit programme and consider review result of audit programmes used for other similar audits.

Extent of evidence gathering considered and agreed with the AAG.

Notes of all-important meetings placed on file.

Working papers complete and reviewed by the AAG.

All queries and outstanding points raised by in-charge resolved.

• **Reporting**

✓ box when completed

Reports and letters drafted in conformity with guidance contained in the Performance Audit Guide.

Confirm that audit execution procedures have included gathering evidence appropriate to the specific findings contained in the report (and, where applicable that the report has been referenced to the underlying evidence).

All outstanding audit execution procedures completed.

Comments by the audited entity on matters of substance made at meetings approved by Audit Director and confirmed to audited entity in writing or discusses as appropriate.

Report reviewed by the AAG and the DAG before final issuance.

Final Report reviewed by the AG before submitting in annual report.

20 "Selection of Subject/Unit Section"

20.1 Need for Selection

20.1.1 The selection of topic or issue is considered to be a critical task in performance auditing. The selection process provides a basis to pursue performance audit in greater detail through the preliminary identification of auditable population (the audit universe) from which the auditors make initial decisions on whether performance audit is warranted.

20.1.2 Selection of functions, activities, programme or operations of the auditee for performance audit is important for the following reasons:

- given the size, complexity and diversity of the operations of the auditee, it is normally impracticable to attempt to assess the overall performance of departments or agencies in the public sector;
- saves resources and time by concentrating on particular problematic area;
- enhances relevance of audit findings;
- timely completion and reporting facilitates initiation of corrective action.

20.1.3 Performance audit shall examine an issue or a programme that is common to or influenced by a range of departments or agencies. These performance audits have the potential to increase the relevance and scope of audit findings and recommendations in the broad area of public sector. The examples of such across the board or common issues are as follows:

- the audit of implementation of programme evaluation system,
- aspects of budgetary system, and
- project appraisal system.

20.1.4 Audit of policy or systems issue serves broad purposes rather than specific issue of a project or organisation.

20.2 Steps in Selection

20.2.1 The Central Co-ordination Unit (CCU) plays a decisive role in the selection of audit topics or issues. The Performance Audit Division provides logistic support to this unit. The Assistant Auditor General assigned to the Performance Audit Division holds the responsibility to initiate the selection process which involves a request in writing to all Operational Divisions within Office of the Auditor General to suggest/ nominate significant organisation, topics or issues considered potential for performing performance audit.

20.2.2 The request letter should seek the following information:

- name of the Programme/Project/Organisation/Activity
- year of commencement
- financial source - Donor assisted or His Majesty's Government of Nepal
- nature and brief description of activity

- location and geographical coverage (number of districts)
- name, designation and address of Chief Executive/ Programme/Administrator
- critical audit observations in previous years
- total cost of project/programme
- period to be covered by the audit
- suggested audit commencement and completion date
- major reasons for recommending the topic
- other matters of significance (media reports, public concern, requests, complaints, ect.).

20.2.3 The Performance Audit Division shall compile all the information received in the following format and shall indicate its preference or recommend the selection criteria of issues or topics to be considered for performance audit.

Compiled List of Suggested Topic or Issues Areas

Suggested Topic or Issue	Year of Establishment	Budget (RS'000)	Nature of Activities	Volume of Work	Matter of Significance

20.2.4 In compiling the listing of suggested topic, the auditor should consider preliminary issues pertaining to the broad areas of the auditee's operations, including :

- relative size of expenditures or revenues;
- trends in the authority's performance;
- comparative indicators of performance for similar organisations;
- compliance with relevant legislation;
- potential risks;
- matters of public interest;
- complexity of operations; and
- known unresolved problems from financial audits.

The CCU can request for additional topics for performance audits.

20.2.5 The CCU shall decide weightage to be applied to each topic proposed.

20.2.6 The selection matrix and criteria in the course of making decision about topic or issue for performance auditing may be developed using the Selection Matrix and Criteria for Performance Audit form provided in Audit Tool-2.

20.3 Key Issues, Criteria and Matrix of Selection

Objective assessment of factors such as risks, resource requirement, need and availability of service of independent experts within resource limitation is critical in the selection of topic or issue for performance auditing. The following aspects need to be considered by the auditor:

- *"Risk"* Assess the following risks associated with the topics or issues proposed :
 - associated challenges and probability of completing auditing in time;
 - capability of audit personnel to undertake audit;
 - potential impact of audit report; and
 - operating environment of potential organisation.

The assessment of risk generally enables the auditor to identify the expected benefits from the audit considering the resources available to undertake the audit. The auditor shall assess the risks involved in performance auditing and minimise them to an acceptable level through proper audit planning.

- *"Resource requirement"* Timely completion of audit and reporting is essential from the viewpoint of enhancing the relevance of audit findings. Therefore, it is important to consider the availability of resources including manpower, the choice of personnel and the skills they possess as well as expert or specialist, equipment and budget.
- *"Strategic plans"* All audit operations shall help achieve the objectives outlined in strategic plan of the OAG. It is essential for the CCU to consider the strategic plan of the OAG in the selection of audit topic or issue.

20.3.2 Some Example of considerable broad risk area and issues in course of recommending and selection of subjects for performance audit is given below:

Broad Risk Area	Issues
1. Human Resources	Change management Training / development Recruiting process Reward / remuneration process Industrial relations Succession planning
2. Health & Safety / Environment	Environmental planning Compliance to law / changing legislation Fire hazard Culture / commitment
3. Production	Labour shortages Physical capacity Automation Process development/ innovation
4. Logistics / Supply Chain	Inventory management Space constraints Distribution

Broad Risk Area	Issues
	Effective communication Procurement / sourcing raw materials
5. Economics factors	Foreign exchange Stock market Industry reliance Legislative changes
6. Technology	Product development R & D
7. Information Technology	Management information Changes to operations
8. Strategic development / direction	Joint ventures New markets Acquisition of opportunities Future structure
9. Financial	Production costing Working capital management Return on assets

20.3.3 There may be numerous criteria for selecting areas for a performance audit. These can be categorised as follows:

- "Impact" - Tentative judgement over the contribution or impact (improvement in service delivery system or resource management or institutional capacity building) of auditing.
- "Materiality" - Value judgement regarding the potential contribution of auditing in broader scenario of administration and/or management.
- "Risk to good audit management" - Assessment of potential risks in managing audit considering coverage, complexity of business of organisation and availability of skill and knowledge.
- "Visibility and significance" - Assessment of potential significance of audit findings in different scenarios (high or low) and visibility of impact.

20.3.4 Simple summation of scores given to overall ranking of each auditable area would not be an accurate indication, although it provides a comparative picture of priority that may be accorded. As each of these factors (20.3.3) will have a different weight, ranking remains a matter of judgment for the CCU considering risks, resource requirement and strategic focus.

20.4 Common Issues in the Selection

The common factors that affect selection process include :

- temptation to select issue that covers wide scope;
- determining the matters of potential significance;
- delineating audit scope and defining the subjects of performance audit;
- understanding cause and effect relationships; and

- foreseeing the nature and content of potential audit findings.

Audit Tool - 2 (Selection Criteria and Matrix)

This Audit Tool gives guidance on the completion of the *Selection Matrix* and how to assign ratings to determine and evaluate overall ranking of each auditable area. To be effective, the specific criteria, topics, and the resultant ratings suggested in this Audit Tool will likely need to be modified to appropriately reflect the relative significance for the topics in question. Application procedure of this Audit Tool is given below.

- **Determining Overall Significance Ratings**

After the auditor has judgementally assigned a rating to each topic, the auditor shall determine the overall significance rating by topic by totalling the individual weighted ratings across the matrix.

The weighted ratings across each column are added and recorded in the "Overall Rating by Topic" by row. These total can be helpful in determining overall public sector exposure areas.

- **Evaluating Ratings by Individual Topics**

The auditor then evaluates the overall significance rating by individual topics. This is done for each topic by row by comparing the total in the "Overall Rating by Topic" row to an appropriate scale that categorises the topics as low, moderate or high in terms of significance. Each topic will be then ranked on the basis of their merit.

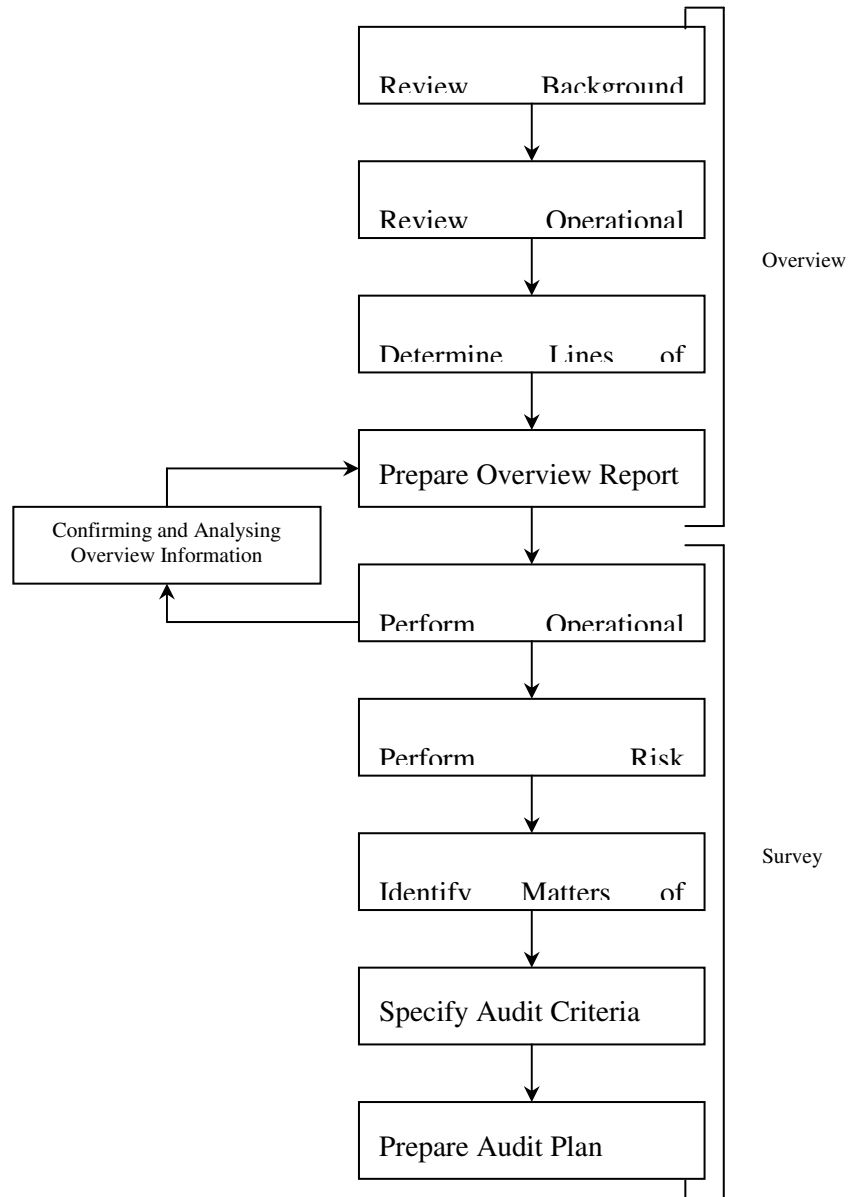
Example of Selection Matrix

Topics	Selection Criteria					Overall rating by topic	Rank (Overall rating)
	Potential Impact	Materiality	Potential Risks	Visibility			
(weighting)	(0.3)	(0.2)	(0.2)	(0.3)		1	
Topic 1	10 3	5 1	10 2	5 1.5		7.5	II
Topic 2	10 3	10 3	5 1.5	5 1.5		9	I
Topic 3	5 1.5	5 1.5	5 1.5	5 1.5		6	III
Topic 4	5 1.5	0 0	5 1.5	5 1.5		4.5	IV
Topic 5	5 1.5	5 1.5	5 1.5	0 0		4.5	IV

Note:- ● Not applicable = 0, ● Low = 2, ● Moderate = 5, ● High = 10

30 "Planning Section"

30.1 Performance Audit Planning - Diagram



30.2 Objective

The objectives of audit planning are to establish guidelines and provide guidance on the methods and process of implementing performance audits in an organised manner. Audit planning involves developing a general strategy and a detailed approach for the expected nature, timing and extent of the audit, in order for the audit to be performed effectively.

30.3 Policy & Procedure

30.3.1 The Audit Director shall be responsible for the audit planning stage and is accountable to the Assistant Auditor General. The Audit Planning shall comprise two stages overview report is prepared from overview stage and audit plan is prepared from survey stage.

The overview report and the audit plan are collectively referred to as the “planning documents”

30.3.2 The engagement personnel should possess appropriate skills and competence to properly carry out the work for which they are responsible. Because of the complexity of performance auditing, independent experts may be engaged to provide the necessary expertise in the unique and highly technical areas in respect of specific auditee culture and environment.

30.3.3 The Assistant Auditor General shall review and approve the overview report and the audit plan prior to the commencement of the audit execution stage.

30.3.4 Upon approval, the audit plan is communicated to the Performance Audit team. It is to be noted that planning is a continuous process. Changes in conditions or unexpected results of audit procedures may, if significant, result in revisions to the audit plan. Such changes or revisions in planning should be justified and documented.

30.4 Performance Audit Planning

30.4.1 The auditor should plan the audit in a manner which ensures that an audit of high quality is carried out in an economic, efficient and effective way and in a timely manner.

30.4.2 Audit planning is prepared out to determine the best way of doing the work to ensure a satisfactory and quality result. Audit scope, time, objectives and criteria are determined during the audit planning stage which ensure that major organisational activities, systems and controls are sufficiently covered by audit.

30.4.3 Audit planning is important for performance audits because of the diverse and complex nature of the methods and process of its execution. Audit planning identifies the essential elements of operation and performance. It is the best way to address the significant and high-risk issues that affect the performance of the auditee. Separate audit planning is required for each performance audit.

30.4.4 The overview report sets the broad direction for the performance audit. The survey stage provides details on the audit methodology and approach to the audit to guide the audit team throughout the audit.

30.5 Engagement of Personnel

30.5.1 "Expertise and experience" The engagement is performed and the report prepared by professionals having appropriate technical training, experience and proficiency in performance auditing and possess appropriate level of professional skills and expertise.

The introduction of Electric Data Processing (EDP) in an auditee has a significant impact on the internal control structure and procedures adopted by an auditee. In such cases, the audit team must have the EDP knowledge and expertise to conduct an audit efficiently.

30.5.2 "Training" All Officers of the Auditor General's performance audit professionals are responsible for adhering to the education and training requirements as set out by their professional bodies or the relevant manual and practice guide of Office of the Auditor General.

30.5.3 "Study" The minimum training requirement by each of the performance audit team member is to achieve 40 hours of structured learning annually. Structured learning includes attendance, either as lecturer or participant, at short courses, conferences and seminars relating to performance auditing. The minimum training requirement can also be obtained from services on a technical committee when technical materials on performance auditing is prepared by the staff member or from writing technical articles, paper or books on performance auditing.

30.5.4 "External consultants" When the work of an external consultant (independent expert or specialist) is used to support the performance audit team's findings, reasonable assurance should be obtained on the consultant's reputation for competence.

To rely on the findings of the consultant, the followings ought to be performed by the auditor.

- evaluate whether the consultant's findings are reasonable based on the auditor's knowledge of the organisation/agencies operations and knowledge of the methods, assumptions and sources of data used by the consultant;
- assess whether all relevant documentation was provided to the consultant and whether the consultant's findings are based on adequate information.

30.5.5 "Establish reliance on other auditors" The extent of reliance to be placed on other auditors should be addressed to make the best use of audit resources. Reliance on other auditors minimises duplication or overlap of work between auditors. Coordination with other auditors will also reduce the frequency and period of disruptions caused by the auditors in the audited entity.

Where reliance is placed on the work conducted by another auditor, reasonable assurance should be obtained to ensure that the work is adequate. This could be achieved either by reviewing a summary of the other auditor's procedures or reviewing sufficient working papers of the other auditor.

31.1 Introduction of Overview Stage

In this stage, all necessary information pertaining to the auditee/issue is obtained to assess the appropriateness of the topic or issue for performance audit. Based on the reviews of collected information, the appropriateness of the topic/issue will be decided whether to proceed for audit or not.

31.1.1 The objectives of the overview stage are to:

- obtain an understanding of the general factors affecting the auditee
- obtain an understanding of the auditee, its objectives and strategies
- determine the lines of audit enquiry

- gather sufficient information to decide whether the audit is warranted
- 31.1.2 The audit may not be warranted if the following reasons exist.
- the selected topics may not be of high risk
 - the outcome of the audit will not lead to increase efficiency, effectiveness or economy
 - the selected topic is not auditable due to unavailability of data, difficulty of compiling data, non-existence of measurement criteria and other factors
 - too wide in scope
- 31.1.3 The overview stage involves performing an Overview Analysis, which requires the auditor to review the background information and then the operational objectives, strategy and mandates. The Overview Analysis will enable the auditor to determine appropriate lines of audit enquiry to be pursued under the survey stage.
- 31.1.4 The information gathered during and the findings from the overview stage should be summarised in the overview report.

31.2 Review Background Information

- 31.2.1 The process of reviewing background information includes review of:
- auditee - specific information
 - industry information
 - the auditee's historical performance record
 - the Segment Operational Model, which summarises the general economic factors, the industry and specific information for the auditee
- 31.2.2 An overview team may be formed for gathering or updating background information on the auditee for use in the preparation of overview report. Financial audit team members may be called upon to provide updated information about the auditee.
- 31.2.3 The resources devoted to this process must be tailored to the current level of knowledge and potential risk assessment of the auditee. Where the auditee is well understood or there are few indications of risk, then only limited gathering may be necessary using limited resources.
- 31.2.4 Where problems arise, the Audit Director in consultation with the Assistant Auditor General should discuss with the functional responsibility leader in the auditee's department for access to the required background information. Problems in accessing information should be brought to the attention of the Audit Director immediately.
- 31.2.5 Where prior audits of the auditee has been conducted by the Office of the Auditor General, team members should ensure that they are familiar with current audit files before they begin collecting background information.
- 31.2.6 Knowledge of the auditee's operations is a major input into the development of an overview report. The performance audit team should gather sufficient auditee specific information to be aware of the risks of good management of the assigned agencies. Sufficient information should be collected to:
- develop a good understanding of the auditee - for example, its objectives, resources, activities, contracts, procedures and control environment;
 - understand how the auditee organises its operations;

- gain an understanding of the preliminary risk areas (internal and external);
- understand the auditee's view on the essential processes in achieving its objectives.

31.2.7 The auditor should obtain information on the current status of the projects as it can be useful in planning an audit. Moreover, factors that affect programme performance and accountability and matters requiring further assessment should be identified. Discussing issues that are of management's concern will help the auditor in identifying further areas that may require detailed audit work.

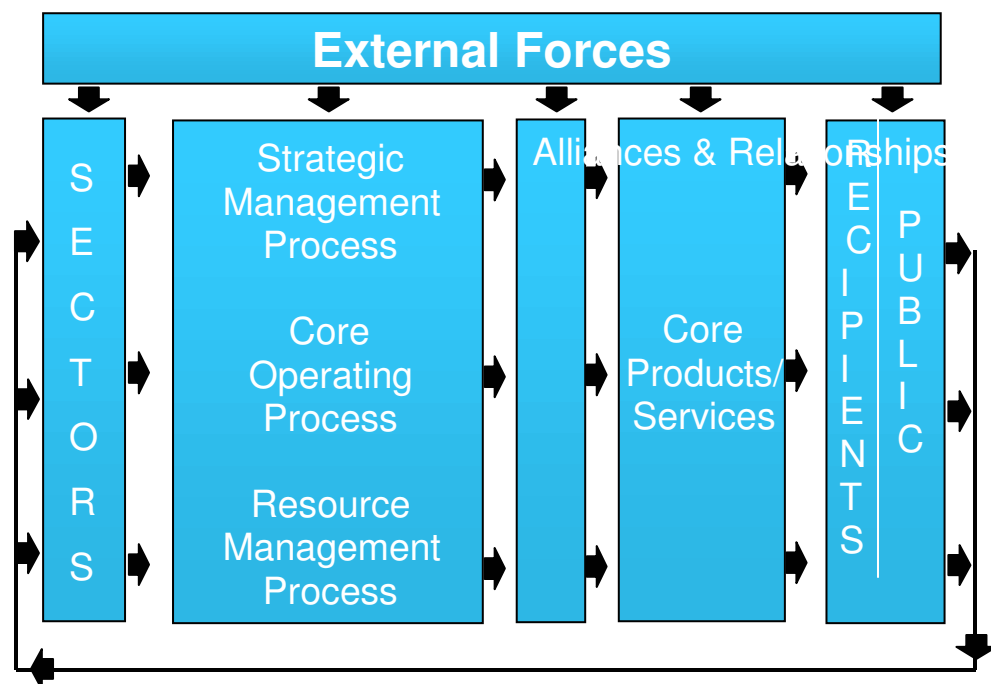
31.2.8 The auditor should review industry information to understand the structure and performance standards generally acceptable in the industry. This will assist in developing the audit criteria for the auditee in the survey stage. Industry information can be obtained from a variety of sources such as :

- online review
- periodicals
- trade associations
- industry analysis
- magazines and newspaper
- national and industries statistics

31.2.9 The auditor should review the auditee's historical performance over the last 3 to 5 years in order to obtain understanding of:

- auditee's capability to achieve its objectives as indicated by recent performance;
- past projects in strategic initiatives as an indication of management views on priorities;
- historical performance providing clues to management's philosophies on trade-off between long and short term objectives;
- how management measures and monitors performance;
- the auditee's current position in the industry.

31.2.10 Given diagram describes the auditee level components of the Segment Operational Model that is evaluated during the overview stage. Its knowledge helps to understand the auditee's operations. Audit Tool-3 provides details on the Segment Operational Model.



31.2.11 To perform effective performance audit, the audit team needs to understand how the auditee responds to external forces (or the environment). The information gathered on the environment the auditee operates in will help develop the Segment Operational Model. The components of the Segment Operational Model are :

Component	Description
External forces	Current factors, pressures and influences that may keep the auditee from achieving its strategic objectives
Sector	Major segments and sectors in which the auditee operates
Strategic management process	Key elements of the strategic management process
Core operational processes	Basic value chain of recipient/customer requirements, as typically represented by core operational processes at the auditee level
Resource management processes	Resource management processes specific to the auditee
Alliances and relationships	Role that alliances play in the industry
Core products and services	Characteristics of the major product lines/services
Recipients/Public	Recipients/Publics requirements

The component structure of the Model represents a format for capturing information about the auditee’s operations. As the auditor accumulates the information about the auditee’s environment, industry, organisational structure, and strategy, the auditor records that information in the Model. The Model represents a high level assessment of the relative strength of the control environment, both at the auditee and process levels. The results of that analysis will assist the auditor to understand the controls and identify key operational processes that require additional analysis at the survey stage.

31.3 Review of Operational Objectives, Strategy and Mandates

31.3.1 Once a basic understanding of the auditee’s past and present operations/ services is in place, the auditor begins to gain insight into where the auditee is going. The auditee’s objectives and strategy will describe the directions the auditee is taking to achieve the

auditee’s objectives and goals. Understanding the auditee’s direction helps the auditor focus the performance audit activities on the most significant areas of the auditee.

31.3.2 When identifying the auditee’s objectives, the following three broad categories of objectives should be considered:

Category	Description
Operational	Operational objectives relate to the effective and efficient use of auditee’s resources, and include performance and profitability goals (if applicable).
Financial reporting	Financial reporting objectives relate to the preparation of reliable financial statements and related disclosures.
Compliance	Compliance objectives relate to the auditee’s compliance with: <ul style="list-style-type: none"> • established controls, • policies and procedures, • applicable laws and regulations • contracts and agreements

31.3.3 The auditor should understand the goals, objectives and strategy of the auditee as it would quantify the level of performance intended or desired by the auditee and how they intend to achieve this level. This also steers the focus of the performance audit activities to the most significant parts of the auditee. Moreover, the goals and objectives can be used by the auditor as a criteria for assessing programme performance. The auditor will also be better able to assess the operations as to whether it is achieving its objectives and also the level of efficiency and effectiveness. Understanding the auditee’s strategy also enables the auditor to identify risk and focus efforts on areas of greatest operational risks.

31.3.4 Information on organisational structure, major responsibility centres or organisational components, their roles and responsibilities, and how they relate to programme and activities, can help in understanding the lines of accountability.

31.3.5 It is necessary to gather information on auditee's mandate for operation as well as its relevant rules and regulations. It enables the auditor to confirm illegal transactions or business of auditee in course of achieving objectives. Such information will aid the auditor to:

- examine the relationship between services provided and the authority for doing so
- specify audit criteria - mandate, rules, laws or regulations may describe level of service that programme are legally required to provide

31.4 Sources of Overview Information

31.4.1 Sources of information include the following:

- relevant legislation, regulations and publications

- site visits and observations of programme operations
- auditee's policies and procedures manual
- organisation chart
- project appraisal/feasibility study
- public accounts, departmental and agency annual reports
- previous audit files and reports
- participating in an auditee's orientation/subject matter training course (if any)
- media coverage and external reports
- agency periodic plan
- the OAG documentation on the auditee
- library of the OAG and auditee
- minutes of relevant parliamentary committee
- formal reports prepared by central agencies, in-house task forces or outside consultants on the operations of the auditee
- photographs or other visual aids taken or prepared by the auditors or obtained from the department and other sources
- management meeting minutes
- interviews with senior personnel of agencies involved in the execution of the project
- interview with senior personnel of central co-ordinating agency

31.4.2 Director has to insure that required information is collected for preparation of overview report.

31.5 Determining Lines of Audit Enquiry

31.5.1 Having reviewed the auditee's industry, objectives, strategies and operational environment during the overview stage, the auditor is in a position to look at those processes, where the auditee is experiencing significant operational risk. The following should be determined to facilitate audit planning at the survey stage:

- audit focus
- audit approach
- lines of audit enquiry

31.5.2 Lines of audit enquiry are matters or areas selected for in-depth analysis at the survey stage.

31.6 Importance of Overview Stage

31.6.1 The importance of the overview stage is listed below:-

- helps orient the auditor as to the various activities that are carried out within the auditee being audited;
- helps the auditor to determine the existence of high risk areas within the operational processes of the auditee.
- helps define the tentative purpose, objective and scope based on the reasons for conducting the audit and what the audit is expected to achieve;
- the appropriate lines of audit enquiry are decided upon;
- the audit team can organise and co-ordinate its efforts to ensure will be effective and efficient execution of survey;

- enables the AAG to make decisions on proposed lines of audit enquiry and budget for the survey stage;
- it provides information which recommends either terminating or continuing the audit.

31.6.2 The overview stage provides the auditor with an understanding of the auditee, sufficient to make preliminary decision about breadth and depth of the audit and the proposed approach.

31.7 Contents of the Overview Report

- background information
- policy
- laws
- objectives and target
- financial review
- operational status of project/programme
- segment operational model
- audit objectives
- scope of audit
- lines of audit inquiry
- personnel engagement
- recommendation whether to continue or terminating the audit.

32.1 Introduction of Survey Stage

Collection of detail information on appropriate topic/subject for the performance audit, risks assessment and development of audit planning are completed in this stage.

32.1.1 The objectives of the survey stage are to:

- specify lines of audit enquiry to determine what areas will be examined in detail
- gaining a deeper understanding of the auditee's key processes, the operational risks and key controls
- confirm the matters of potential significance, audit scope and audit criteria
- developing an audit plan

32.1.2 Audit Tool - 4 provide the guidance to obtain necessary information of an auditee. These information are equally valuable to prepare the planning document and provide input for developing findings.

32.2 Operational Process - Analysis of Key Process

32.2.1 During the overview stage, the auditor performs an Overview Analysis to gain an understanding of the auditee. The lines of audit enquiry are determined which serve to :

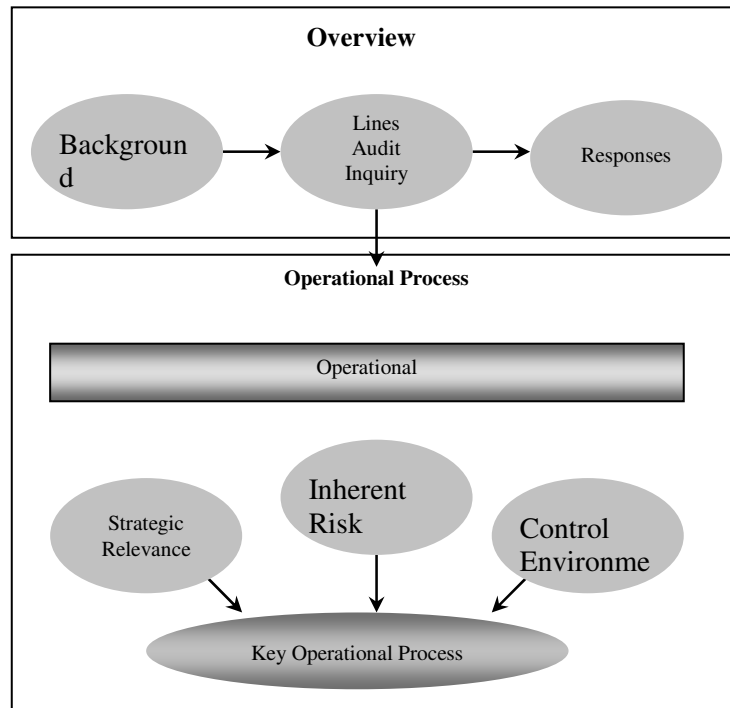
- focus the audit work at the process level; and

- identify those processes in which further analysis may be required during Operational Process Analysis in the survey stage.

Operational Process Analysis involves identifying and gaining an understanding of the auditee’s key processes, the operational risks produced by those processes and how the auditee mitigates risk.

When the auditor understands the characteristics of processes that contain significant operational risks, he is able to better understanding the potential impact of those risks on the financial statements, key operations and processes.

32.2.2 The diagram below illustrates the relationship between the Overview Analysis and the Operational Process Analysis.



32.2.3 Having reviewed the auditee’s industry and operational environment and the auditee’s strategy during overview stage and having identified the lines of audit inquiry, the auditors are now in a position to look at those processes where the auditee is experiencing significant operational risk.

By gaining a deeper understanding of the operational risk in these key operational processes, the auditor is able to learn where the auditee may be exposed to the risks of material operating weaknesses and financial misstatements.

32.2.4 The scope of Operational Process Analysis is based on the auditors’ assessment about the operational risks of each process and may vary from process to process. The depth of the analysis depends on :

- how critical the process objectives are in achieving the auditee’s strategic objectives;
- the auditor’s assessment of the auditee’s strategic operational risks, including:
 - their impact on the business processes; and
 - the implications for our audit approach;

- regulatory and/or management mandates; and
- the degree and number of centralized support processes utilized by the auditee, and their significance to the other components of the auditee’s audit universe.

32.2.5 The results of the work done during Operational Process Analysis contributes to the audit by :

- identifying operational risks to be considered in terms of audit implications;
- helping the auditor to understand how the results of the process are reflected in the overall operating results;
- helping to identify the audit universe and eventually finalising the audit plan;
- helping to identify performance improvement opportunities and the level of risk which management is likely to accept to achieve the enhancements;
- summarising the understanding of the auditee’s operations in the Segment Operational Model for discussion with management; and
- summarising the auditee’s perspective on operational risks for discussion with management.

32.2.6 The table below lists the activities performed and the typical work products that are produced during Operational Process Analysis.

Activity	Work Product
Identify key operational process	Updated memorandum on overview stage
Assess key operational process	Process Analysis Results using the Process Analysis Template (Audit Tool : AT5)
Review (discussion) findings and conclusions with management	<ul style="list-style-type: none"> • Preliminary risk profile • Audit plan

32.2.7 A key operational process is one in which the auditor believes significant operational risks reside, based upon the auditor’s understanding of strategic relevance, inherent risk and control environment. The auditor focuses his work on the audit implications of the operational risks identified in key operational processes. All core and resource management processes as identified in the Segment Operational Model are not necessarily key operational processes.

32.2.8 It is important that the auditor selects key business processes from the auditee’s perspective. The auditor performs this selection to give the audit team a starting point for discussion with management regarding those processes that are key to successful operations.

32.2.9 In order to identify process risks and controls effectively, the auditor must first gain a deeper understanding of the key operational processes. This effort involves:

- identifying process objectives,
- identifying the flow of work within the process, and
- understanding the effectiveness of the process management.

- 32.2.10 In many instances, the auditee is not aligned by process. Therefore, in order to gain an understanding of the processes in place, the auditor identifies the functions that significantly impact the process activities and discuss their roles with the respective functional owners.
- 32.2.11 The operational and programme delivery systems comprise key business processes the auditee uses to produce and deliver products and services to its clients. An understanding of these systems is critical for identifying economy and efficiency matters, and determining the focus for effectiveness measurement.
- 32.2.12 The concluding activity of Operational Process Analysis is to review the preliminary findings and conclusions with the auditee's management. This review includes :
- preparing the audit team and the auditee for the discussion;
 - confirming the findings and conclusions with the auditee's management;
 - discussing audit issues with the auditee's management; and
 - documenting observations and modifications resulting from the review.
- 32.2.13 The auditor bases his analysis of key operational processes, operational risks and controls on the auditee's perspective. Once the auditor understands how the auditee deals with Process-level Operational risk, he is in a position to evaluate the true scope and effectiveness of its risk management approach. This evaluation is completed during Risk Assessment process where inherent risk levels and preliminary assessments on control effectiveness are carried out.
- 32.2.14 Audit Tool-5 provides the Process Analysis Template which could be used as a tool in documenting the Operational Process Analysis of key processes.

32.3 Risk Assessment

- 32.3.1 So far in the audit methodology, the auditor has analyzed the auditee's operations from management's perspective. This has allowed the auditor to maximize his/her leverage from the auditee's knowledge of its operations.
- Now the auditor should step back and objectively evaluate the completeness and quality of the auditee's perceptions of strategic risk and process risk, which cumulatively comprise the auditee's operational risk. This will include conducting workshops or interviews with the appropriate level of management in the audited entity.
- 32.3.2 The purpose of the risk assessment phase is to :
- assess and minimise audit risk by focusing the audit on high risk areas;
 - determine the completeness of management's perceptions, assumptions, and judgements about operational risks and controls;
 - develop and document the auditor's risk assessments, considering both, management's risk perspective and the auditors' own objective risk perspectives;
 - apply management's understanding of existing controls to the updated understanding of risks;
 - start to evaluate the impact of economic value; and
 - perform a preliminary control assessment.
- 32.3.3 Risks are events that threaten the assets and earnings of, or the essential services provided by the auditee. In essence, a risk is anything which has the potential to prevent the auditee from achieving its objectives.

32.3.4 The evaluation of operational risk by the auditor serves to minimise the *audit risk* for the performance audits. Audit risks is the probability or risk that the auditor will arrive at an inaccurate audit conclusion by :

- failing to detect significant weakness that exist in an auditee although such weaknesses exist; or
- concluding that a significant weakness exist when it does not.

32.3.5 The auditor should consider the audit risks by addressing the *inherent risk* and the resultant *residual risk*, as explained below:

- "inherent risk" it is a measure of the auditor's expectation of risk before considering the effectiveness of internal controls.
- "residual risk" it is the level of risk that remains after taking into account the mitigating effect of related controls.

These risks are evaluated by the auditor during the planning process under the risk assessment phase.

32.3.6 The auditor performs the risk assessment portion of the methodology by using his understanding of the auditee's operations and related operational risks and controls to make an informed assessment of the :

- risk of significant operating errors;
- weaknesses;
- risk of misstatements, errors or fraud; and
- appropriateness of the control in relation to a cost/benefit consideration.

This would enable the audit team to focus their efforts and resources on areas which present significant risks to the attainment of management's objectives.

32.3.7 The control environment is the entire system of policies, methods and procedures that is instituted to manage and control an auditee. Management is responsible for establishing a control environment appropriate to the risks the auditee faces.

32.3.8 The identification of inherent risk, the associated controls and residual risk can be performed by using either one of or more of the following methods :

- workshop approach
- interview approach
- case study approach

The workshops are typically facilitated and conducted by the auditor for a group of auditee personnel to determine whether management's views on the completeness of strategic and process risks as well as significance of these risks in relation to its each individual process. The size of the group will be dependent on the auditor's judgement and prior facilitation experience to ensure that an effective workshop is conducted. For smaller groups, interviews can be held with people within the auditee in assessing operational risks.

32.3.9 Alternatively, the auditor could perform risk assessment by obtaining and understanding up-to-date information concerning policies and administration procedures, significant programme accountability relationships, internal management of performance

measurement/reporting systems, and planning and budgeting systems in use. The auditor should validate the results of risk assessment with the appropriate auditee personnel.

32.3.10 The usage of methods vary significantly in regard to their complexity and level of sophistication. Uses of appropriate risk assessment method/tool on each particular engagement should be matched basically with the auditee's needs and level of sophistication, so that it could help substantiate their needs to the best extent. Regardless of the risk assessment method or tool used the auditor considers the potential impact of the identified risk on the ongoing economic value of the auditee.

32.3.11 Once the inherent risks have been determined, the controls that manage the exposure coming from each risk must be determined. Typically, the controls for each key risk are divided into three areas as follows:

- primary controls (preventive);
- secondary controls (detective);
- mitigating controls.

Primary controls are preventive in nature and are designed to prevent error or fraud from occurring. Secondary controls are similar to detective controls and are designed to identify or detect when an error or fraud has already occurred. Mitigating controls are controls in other areas that alleviate, or mitigate, the risk exposure.

32.3.12 If the primary and secondary controls are considered weak, then the mitigating controls may make the situation at least tolerable. If the primary control is adequate and is working effectively, the auditor should consider recommending that having a secondary control may be inefficient and result in over-control.

32.3.13 The identification of risks and controls has a significant impact on the audit approach. For example , if management :

- fails to identify a significant risk or does not adequately consider risks, it is unlikely to have established control activities to manage those risks; or
- does not consider environmental changes effectively, the control activities in place may no longer be adequate or appropriate.

32.3.14 At the completion of the risk assessment process, a risk profile will be prepared for each segment of the auditee's operations. The auditor should discuss the risk profile with management and validate the assumptions on the auditor's assessment on strategic and process risks.

32.3.15 Upon determining the inherent risk rating, the auditor needs to determine the degree to which the control mitigates the identified risk (assuming the control is operating as intended). The auditor draws conclusion on the residual risk levels after consultation with management and decide whether they are acceptable in the context of the operational objectives. The objective is not to eliminate all residual risk but rather to ensure that residual risk is maintained at an acceptable level in a cost effective manner.

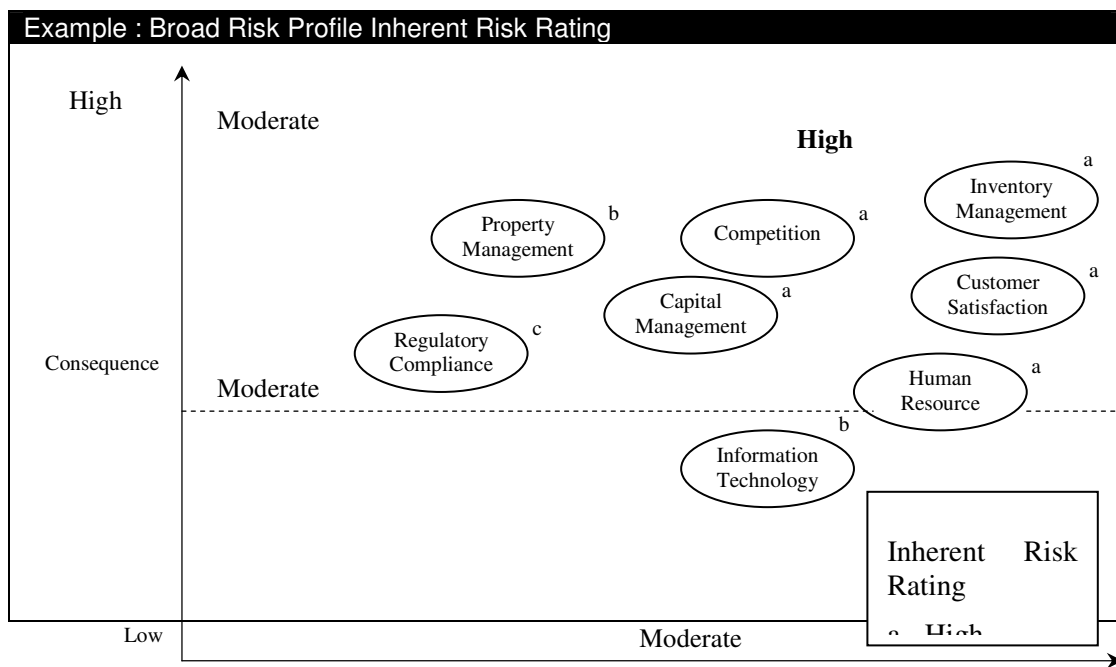
32.3.16 If it is acceptable, then tests are designed to ensure that the controls are, in fact, working as designed. If it is not, then the auditor would have to decide whether to continue with detail audit work.

32.3.17 Where the residual risk level is not acceptable, the auditor has to consider the control effectiveness of the control design to decide whether detail audit work is warranted. In

situations where control effectiveness is weak, the auditor has no reason to perform testing (because the controls do not effectively manage the risk exposure) and the concern needs to be raised with management at this point. Recommendations should be made for strengthening the controls to a level where the residual risk is acceptable. Where controls are either satisfactory or contain some weaknesses, the auditor may use his judgment to pursue an in-depth audit by identifying the MOPS, specifying the audit scope and the audit criteria.

32.3.18 The audit criteria is established for the specific MOPS which warrants detail audit testing. The auditor should identify suitable KPIs to measure the extent where audit criteria is achieved. There would normally be a direct link between the audit criteria and the KPIs. If the KPIs cannot be identified during risk assessment, then the auditor should report the absence of knowledge on the auditee’s performance and apply professional judgement either to perform a procedure-oriented analysis.

32.3.19 The following diagram illustrates the outputs of each operational process directed towards the potential risks.



32.3.20 The risk assessment process is illustrated in detail in Audit Tool-6 under “Overview of Risk Assessment Process”. It also provides details on how to conduct the workshops/interviews. Once the key risks have been determined, the controls that manage the exposure coming from each risk must be determined. Typically, there is more than one control for key risk areas.

32.4 Matters of Potential Significance (“MOPS”)

- 32.4.1 The MOPS are identified and assessed for the purpose of determining the scope of the audit examination. the MOPS stem from the risks identified during the risk assessment stage.
- 32.4.2 Audit Tool - 5 & 6 should be used for identifying the MOPS. The risks which do not reside at the accepted level from the viewpoint of auditor should also be incorporated in the MOPS.
- 32.4.3 The inherent risk is identified and the control effectiveness is assessed during the risk assessment process. The residual risk is determined based on the inherent risk and control effectiveness levels.
- 32.4.4 Based on the significance of residual risk levels, the auditor can decide which areas would require further detailed audit work to be performed.
- 32.4.5 The identification of the MOPS follows from the auditor's decision that an in-depth audit is warranted and an audit is likely to result in significant findings and recommendations.

32.5 Audit Objectives

- 32.5.1 Audit objectives relate to why the audit is being conducted and are based on the audit mandate. For example, an audit objective may be to assess whether there were any aspects of project management within a particular agency which could be undertaken in a more efficient and effective manner.
- 32.5.2 Audit objectives should be established or assessed by the auditor with a view to defining an audit which has the potential to improve public administration. Performance audits should therefore not only warn against defective practices but also identify and promulgate good practice.
- 32.5.3 One way of facilitating an analysis of economy, efficiency and administrative effectiveness is to view public sector activities in relation to the following :
- the programme objectives, which should be clear enough to identify the desired outcomes;
 - the financial, human, physical and information resource inputs used;
 - the processes or activities by which the inputs are converted into outputs;
 - the goods, services or other results which constitute the output of the programme; and
 - the actual impacts or outcomes, both intentional and unintentional.
- 32.5.4 Given the size, complexity and diversity of their operations, it is normally impracticable to attempt to assess the overall performance of departments or agencies in any meaningful way. Consequently, performance audits are usually directed towards specific functions, activities, programme or operations of the auditee's organisation.

32.6 Audit Scope

- 32.6.1 Once the MOPS are identified, the auditor should determine or assess the audit scope. The audit scope is:
- that part of the organisation, programme, activity or function to be examined;
 - the matters subject to the audit;
 - the time period of the audit.

32.6.2 The scope of an audit and the audit objectives determine the procedures that will be required during the conduct of an audit, the resources needed and the matters that will be reported. The auditor should use his professional judgement to establish the audit scope in specific terms, for example, to focus only on the two most significant programmes of the auditee for a specified time.

32.6.3 The auditor establishes the audit scope based on information obtained throughout the planning process. The scope of audit should be explicitly stated in the audit plan to document decisions made on resource requirements and the general approach to the audit.

32.7 Audit Criteria

32.7.1 Audit criteria can be defined as reasonable and attainable standards of performance and control against which the adequacy of systems and practices and the extent of economy, efficiency and effectiveness of operations, programme, or activities can be assessed. They reflect a normative control model for the subject matter under review. They represent good practice - a reasonable and informed person's expectation of "what should be". When they are compared with what actually exists, audit findings are generated. Meeting or exceeding the criteria might indicate "better practice", while failing to meet criteria would indicate that improvements can be made. Where possible it is preferable to identify the nature of such improvements or even how they might be achieved.

32.7.2 Criteria can perform a series of important roles to assist the conduct of a performance audit. They :

- form a common basis for communication within the audit team and with the OAG's management concerning the nature of the audit;
- form a basis for communication with the auditee's management in that the audit team will often solicit the auditee's management understanding of and concurrence with the criteria and eventual acceptance of audit findings in light of those criteria;
- link the objectives to the audit programme carried out during the implementation phase;
- form a basis for the data collection phase of the audit, and the identification of key performance indicators to provide a basis on which to build and monitor procedures for the collection of audit evidence; and
- provide the basis for audit findings, helping to add form and structure to observations.

32.7.3 The degree to which criteria are successful in serving these uses is often determined by their level of detail and the form they take. General audit criteria is acquired or developed during the overview stage. With the identification of the MOPS, the criteria is usually expanded and made more specific. By the end of the risk assessment, the criteria should be sufficiently detailed and specific to give clear guidance for the execution stage of the audit. In particular specific audit programme is developed to test the criteria. It is unrealistic to expect that activities, systems or levels of performance in economy, efficiency and effectiveness areas will always fully meet the criteria. Satisfactory performance does not mean perfect performance but is based on what a reasonable person would expect, taking into account the auditee's circumstances.

32.7.4 The auditor can develop suitable audit criteria by looking at the following sources:

- criteria used previously in similar audits conducted by the OAG,
- criteria used in similar audits conducted by other audit institution abroad,

- general criteria developed by the OAG,
- criteria published by other supreme audit institutions,
- performance standards used by the auditee, or previous parliamentary or other official inquiries,
- performance standards used by entities that are similar to the auditee, that is, organisations carrying out similar activities or having similar programme clients both local and abroad,
- performance standards used by professional organisations and standard-setting bodies,
- subject matter literature, and
- general management literature.

32.7.5 These sources provide a basis for the development of criteria for the audit, but may require interpretation and modification to ensure their relevance.

32.7.6 Criteria must be realistic and take into account the context of the auditee. Some key criteria relate directly to the auditee itself, for example :

- enabling and related legislation;
- auditee's operating and procedures manuals; and
- central auditee's policies, standards, directives and guidelines.

32.8 Logistic Management

32.8.1 Having identified the MOPS and planned the audit focus to gather audit evidence, the auditor should consider the logistical aspects of how the audit team may efficiently perform these tasks. As part of planning, the auditor looks at what resources the audit team require as well as when and where the audit team needs them.

32.8.2 In considering the resources required for the audit, the auditor looks at :

- staffing and other resources required for the engagement, including specialists;
- other auditors involved;
- the availability of computers and the planned use of Computer-Assisted Audit Techniques;
- the planned timing of the audit work;
- the location of the audit work;
- communication links such as telephones, facsimile and transportation links;
- the preparation of time cost budgets.

32.8.3 Planning the logistical aspects of the audit generally requires close co-ordination with the auditee. The auditor usually arranges meetings with management and the auditee's staff to discuss matters such as :

- timing of the audit and locations to be visited;
- schedules and information to be prepared by the auditee's staff;
- the involvement of specialists;
- other auditee's service issues, including management's expectations.

32.9 Audit Budget

- 32.9.1 The details of audit budget depend upon the complexity of the audit. The budget is developed based on an estimation of time required for each task to be performed.
- 32.9.2 The audit team comprises individuals with varying seniority and experience. The determination of the size and quality of staff required on each particular audit depends on the complexity and extent of the audit work expected.
- 32.9.3 Time and cost savings may be achieved by having auditee personnel prepare information for the use of the auditor, for example, the information requested under *PAG - Audit Tool : AT3*. In addition, auditee personnel are also needed by the auditor to obtain access to client facilities, records and documents.

32.10 Contents of the Audit Plan

The contents of the audit plan should include the followings:

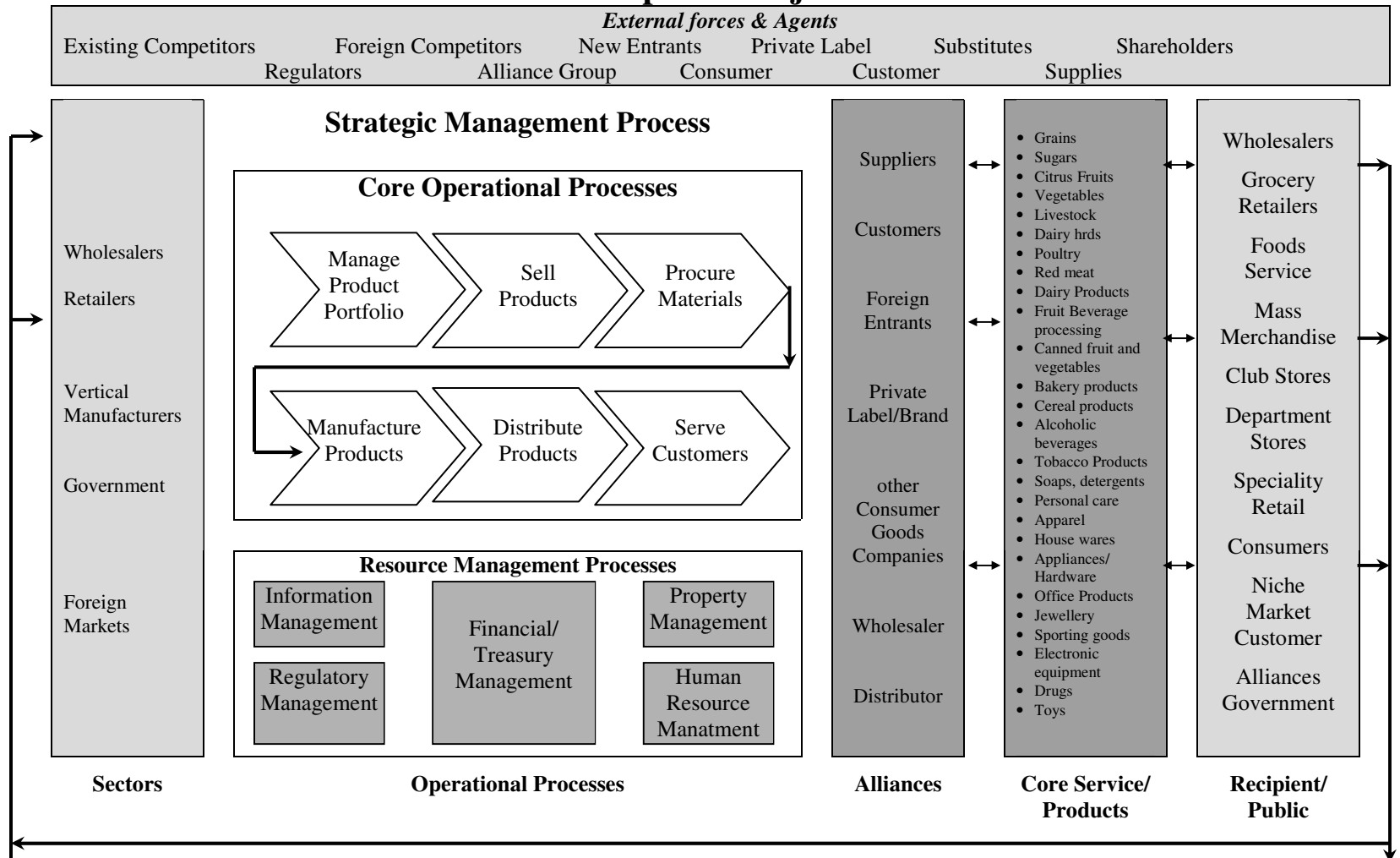
- audit objectives for each MOPS
- audit criteria to be used for each audit objective
- audit scope
- approach to audit with details on nature, extent and timing of testing required
- resources needed for the examination and reporting phases - identify and allocate resource requirements, including specialists where necessary
- manpower for the completion of the audit
- estimated working man-days of engaged manpower by level/skill or type.
- detailed time and work schedule.

Audit Tool - 3 (Segment Operational Model)

As shown on the next page, the entity Segment Operational Model is used to describe the interlinking activities carried out within an entity, the external forces that bear upon the entity, and the operational relationships with persons outside the entity. The items in the entity-level process model include the following components:

- External forces and agents are those factors, pressures and forces from outside the entity that often are threats to the attainment of the entity's objectives.
- Sectors are the segments of an industry that are applicable to the entity. Formats identify the design and location of the facilities where public goods and services are provided free-of-charge (i.e. markets for goods and services do not exist)..
- The strategic management process is the process that :
 - develops the entity's mission,
 - defines the entity's objectives,
 - identifies the risks that threaten attainment of the objectives,
 - manages the risks by establishing processes, and
 - monitors progress toward meeting the objectives.
- Core operational processes are the processes that develop, produce, sell and distribute an entity's products or services. These processes do not follow traditional organisational or functional lines, but reflect the grouping of related operational activities.
- Resource management processes are operational processes that provide appropriate resources to the other operational processes.
- Alliances are the types of relationships with third parties that entities in the industry may establish to
 - attain objectives
 - expand opportunities, and
 - reduce or transfer risk.
- Core products and services are the major products and services typically offered by entities within the industry.
- Recipients/Public are the major types of recipients/public within the markets in the industry that entities may choose to focus on.

Example of Project



Audit Tool - 4 (Information Collection Form)

1. *Strategic overview - history and background*

Objective: Gain an understanding of the entity’s history and strategic position

Potential risks

Recommended personnel to interview

- Past growth constraints
- Unfocused management objectives
- Diminishing organic growth rate
- Unfocused acquisition strategy
- Abnormal historical perspective

- Chairman/President
- Functional responsibility leaders
- Other members of senior management

Activities	Completed By & Date	File ref.	Comments
Enquire and consider organisational Structure and manpower management			
Enquire into and consider key factors behind past success or failure			
Enquire into capacity and plans for future strategic development			
Enquire about and address project/management objectives			
Enquire about pending or recently completed regulatory or other enquiries or proceedings and consider implications			

2. Entity overview - management

Objective : Consider management’s strengths and weaknesses

Potential risks

Recommended personnel to interview

- Management ineffectiveness
- No succession planning
- Over/under compensated management
- High attrition rate
- Inadequate attention to career development
- Poor reputation

- Personnel Director
- Chairman/President
- Chief Financial Officer
- Other members of senior management

Activities	Completed By & Date	File ref.	Comments
Enquire about performance criteria and address effectiveness in meeting criteria			
Enquire if incentives are consistent with the entity’s core values and whether pay and promotion are based heavily on achievement of short term performance targets			
Enquire if employees at the right level are given the authority to correct problems and make improvements, and do they have the appropriate level of competence and clear boundaries to their authority			
Consider dependence of entity’s performance on key management			
Enquire about the key responsibility centres in the entity			
Enquire about the roles and responsibilities of each individual centre			
Enquire if senior management have established clear boundaries of acceptable behaviours and limits			
Enquire about management succession plans			
Enquire about management development programmes			
Review management turnover			
Consider management's morale			
Consider if remuneration packages are competitive with similar entities			
Enquire about recent or proposed changes in employment terms and service agreements (including pension arrangements and other benefits)			
Enquire into management's operational ethics			

3. Feasibility of Projects – Project Appraisal

Objective : Gain an understanding about the feasibility of the project

Potential risks

Recommended personnel to interview

- | | |
|--|---|
| <ul style="list-style-type: none"> <input type="checkbox"/> Feasibility study not carried out <input type="checkbox"/> Study does not cover all aspects (e.g. Economics, Technology, Social, Environment) <input type="checkbox"/> Information/Statistics used are inaccurate <input type="checkbox"/> Lack of linkage with periodic plan and long term policy | <ul style="list-style-type: none"> <input type="checkbox"/> Project Manager <input type="checkbox"/> Chief of planning division of Ministry |
|--|---|

Activities	Completed By & Date	File ref.	Comments
Collect approved feasibility study			
Inquire and consider sources of information/statistics used in feasibility study			
Inquire and consider about financial aspects of project			
Test the source reliability of statistics			

4. Entity overview - structure and logic of major programmes

Objective : Gain an understanding of the entity’s major programmes’ structure

Potential risks

Recommended personnel to interview

- | | |
|---|---|
| <input type="checkbox"/> Programme objectives may not be clearly defined | <input type="checkbox"/> Product development director/manager |
| <input type="checkbox"/> There may not be a link between objectives and outputs | <input type="checkbox"/> Chief Financial Officer |
| | <input type="checkbox"/> Chairman/President |

Activities	Completed By & Date	File ref.	Comments
Enquire if the objectives of the programme are clearly defined			
What are the intended results and effect			
Enquire about the current outputs and intended outputs of the entity and how these outputs contribute towards the objective of the programmes			
Enquire about the needs of the clients and whether this is being met			
Enquire about organisations in the same or similar industry			

5. Entity overview - operational factors

Objective : Gain an understanding of the key operational factors affecting entity's performance

Potential risks

Recommended personnel to interview

- | | |
|---|---|
| <input type="checkbox"/> Inefficient plant and production processes | <input type="checkbox"/> Chairman/President |
| <input type="checkbox"/> Constraints on productive capacity | <input type="checkbox"/> Functional head(s) of major production and engineering department(s) |
| <input type="checkbox"/> Problems with client order/shipments | <input type="checkbox"/> Order Entry/Customer Service Manager |
| <input type="checkbox"/> Inaccurate product costing | <input type="checkbox"/> Production or Control Manager, Master Scheduler, QA Manager |
| <input type="checkbox"/> Inappropriate facility size, condition or location | |
| <input type="checkbox"/> Problems with production scheduling or control | |
| <input type="checkbox"/> Poor supplier or subcontractor management | |
| <input type="checkbox"/> Health and safety problems | |
| <input type="checkbox"/> Quality control problems | |

Activities	Completed By & Date	File ref.	Comments
Address whether plant capacity is in line with operational strategy and enquire about surplus/constraints			
Enquire about availability of alternative production facilities			
Consider the effectiveness of the manufacturing information systems as related to production needs			
Enquire about inventory costing methods and obsolescence reserves			
Consider the adequacy of inventory control procedures and inventory levels			
Enquire about any restrictions on supply of raw materials or essential services			
Enquire about the methodology used to develop and maintain labour, material and overhead standards			
Enquire about quality reporting systems in use			
Investigate the material handling and distribution systems			

6. Entity overview - research and development (R&D)

Objective : Gain an understanding of the extent of R&D resources and success or failure of prior R&D efforts

Potential risks

Recommended personnel to interview

- | | |
|---|--|
| <input type="checkbox"/> Reduced R&D efforts | <input type="checkbox"/> R&D Director |
| <input type="checkbox"/> Unfocused or (non-existent) R&D strategy | <input type="checkbox"/> Engineering Officer |
| <input type="checkbox"/> Inadequate resources committed to R&D | <input type="checkbox"/> Chairman/President |
| <input type="checkbox"/> Poor management of R&D efforts | |

Activities	Completed By & Date	File ref.	Comments
Analyse R&D expenditure as a percentage of income/other performance measurements			
Compare R&D expenditures to competitors and industry averages			
Consider how R&D efforts are managed and measured			
Obtain details of the experience of research staff			
Enquire about the adequacy of R&D facilities and equipment			
Enquire about the security and ownership of proprietary rights			
Enquire about in-house vs contracted R&D			

7. Accounting and information systems – management control systems

Objective : Analyse the effectiveness of the systems for the management and control of the programmes

Potential risks Recommended personnel to interview

- | | |
|--|--|
| <input type="checkbox"/> Autocratic chief executive | <input type="checkbox"/> Chairman/President |
| <input type="checkbox"/> Complex structure | <input type="checkbox"/> Chief Financial Officer |
| <input type="checkbox"/> Lack of attention to operational planning | <input type="checkbox"/> Senior accounting personnel |
| <input type="checkbox"/> Emphasis on achieving targets and forecasts | <input type="checkbox"/> Auditors |
| <input type="checkbox"/> Weak management reporting framework | |
| <input type="checkbox"/> Aggressive attitude towards financial reporting | |
| <input type="checkbox"/> Poor budgetary control | |
| <input type="checkbox"/> No effective code of corporate conduct | |

Activities	Completed By & Date	File ref.	Comments
Enquire about the procedures used by the Board or governing members to ensure the effective management and control of the operational activities, including delegated responsibilities and evidencing of control procedures			
Enquire about and address the division of responsibility amongst Board or governing members			
Consider the quality, reliability and timeliness of the information used by senior management to exercise managerial control			
Enquire about operational planning procedures, including financial planning and forecasting procedures, and consider adequacy to meet the present and future needs of the operation			
Enquire about budgetary control procedures and consider appropriateness of budget holders' responsibilities, quality of variance analysis and adequacy of review procedures			
Address information regarding the overall control consciousness of management			

8. Accounting and information systems – internal control structure

Objective : Gain a general understanding of the internal control environment and consider its strengths and weaknesses

Potential risks

Recommended personnel to interview

- | | |
|--|--|
| <input type="checkbox"/> Unreliable financial statements | <input type="checkbox"/> Chief Financial Officer |
| <input type="checkbox"/> Control procedures not followed | <input type="checkbox"/> Controller |
| <input type="checkbox"/> Understaffing/staff reductions | <input type="checkbox"/> Accounting personnel |
| <input type="checkbox"/> Inadequate treasury/foreign exchange management systems | <input type="checkbox"/> Treasurer |
| <input type="checkbox"/> Management override of internal controls | <input type="checkbox"/> Auditors |
| <input type="checkbox"/> High personnel turnover | |
| <input type="checkbox"/> Failure to implement management letter recommendations | |

Activities	Completed By & Date	File ref.	Comments
Address the quality of accounting systems and internal controls in operation and the resultant quality of the accounting records			
Investigate the methodology used to prepare financial statements			
Review organisation chart and consider whether this is conducive to effective control			
Review accounting manual and consider whether the procedures and controls as they operate in practice are in accordance with the manual			
Consider the competence of the entity's accounting personnel			
Enquire about issues arising from internal audit reports and auditor's management letters and establish if recommendations have been implemented			
Enquire about treasury management systems and consider adequacy to control cash and treasury instruments			
Enquire about foreign exchange management systems and consider adequacy to mitigate exposure to foreign exchange risks			
Enquire if there are appropriate process and procedures in place to monitor changes in legislation and ensure continued compliance			

9. Accounting and information systems - information technology (IT)

Objective : Analyse the effectiveness of the IT environment

Potential risks

Recommended personnel to interview

- | | |
|--|---|
| <ul style="list-style-type: none"> <input type="checkbox"/> Compatibility with environment <input type="checkbox"/> Restrictive covenants in current leases and licenses <input type="checkbox"/> Considerable customised applications <input type="checkbox"/> Reliance on outside programming assistance <input type="checkbox"/> Condition of equipment <input type="checkbox"/> Human resources: skills, tenure and organisation <input type="checkbox"/> Restrictive covenants in software contracts for transfer of software licenses <input type="checkbox"/> Inadequate capacity | <ul style="list-style-type: none"> <input type="checkbox"/> IT managers (operations, applications, support) <input type="checkbox"/> Key IT personnel (managers, co-ordinators, administrators) |
|--|---|

Activities	Completed By & Date	File ref.	Comments
Address the IT control environment and consider adequacy to meet present and future needs of the operation			
Consider user's satisfaction levels			
Develop analysis of past and future IT investments from budget and cost information. Compare entity's investment levels to industry standards			
Address adequacy of back-up facilities			

10. Accounting and information systems - accounting policies

Objective : Consider the nature of accounting policies and procedures

Potential risks

Recommended personnel to interview

- Aggressive accounting policies
- Changes to accounting policies or bases

- Chief Financial Officer
- Controller
- Selected accounting staff
- Auditor

Activities	Completed By & Date	File ref.	Comments
Consider whether accounting policies are in line with local GAAP and with normal industry practice			
Consider whether accounting policies have been consistently applied and investigate recent or contemplated changes in accounting principles, procedures or accounting estimates			
Consider process by which significant accounting estimates are agreed and their impact on the financial statements (reserves, allowances, accruals etc)			
Consider treatment of unusual, non-recurring and/or extraordinary items			
Consider deferred income or expenditures			
Consider nature of recurring adjustments			

11. Programme Performance - General

Objective: Gain an understanding of the methods used by the entity to achieve targeted performance

Potential risks

Recommended personnel to interview

Performance below targeted levels

Credit Manager

Chief Financial Officer

Activities	Completed By & Date	File ref.	Comments
Enquire about the standards or measures used to assess performance, how the standards were established and whether these standards can be adopted as audit criteria			
Enquire about how the results/performance are measured using the given standards/measures			
Enquire about the procedures used by management to monitor the performance. Also enquire about which aspects of performance is monitored			
Analyse output by value and units, obtain explanations for trends and consider implications for future trading			
Compare actual output with budgeted output by product line and obtain explanations for significant variances			
Enquire about terms of royalty or licensing agreements and consider impact on future output			
Enquire about and consider the adequacy of the provision for losses on uncompleted contracts			
Enquire about effect of rebate and/or other promotional programs and the costs related to such programs			
Consider the effects of refunds, credit notes and discounts on sales (where output is not free)			
Enquire about significant sales cancellations/returns and consider frequency			
Enquire about recurring customer complaints and lost customers and consider trends			
Review significant agreements for key provisions, including onerous contracts			
Enquire about product return policies and practice			
Enquire about strategic and product direction			
Enquire about other sources of revenue (eg scrap sales)			

12. Purchases and supplies - cost of goods

Objective : Gain an understanding of the significant cost of goods

Potential risks

Recommended personnel to interview

- | | |
|---|---|
| <ul style="list-style-type: none"> <input type="checkbox"/> Sourcing constraints <input type="checkbox"/> Onerous contractual arrangements <input type="checkbox"/> Cost saving measures taken which may not be sustainable <input type="checkbox"/> Insecure sources of supply <input type="checkbox"/> Vulnerability to rising input costs <input type="checkbox"/> Cost accounting inconsistencies | <ul style="list-style-type: none"> <input type="checkbox"/> Chief Financial Officer <input type="checkbox"/> Controller <input type="checkbox"/> Purchasing/Materials Manager <input type="checkbox"/> Director of Operations/Manufacturing |
|---|---|

Activities	Completed By & Date	File ref.	Comments
Investigate cost of goods by product and cost component, obtain explanations for trends and consider implications for future			
Enquire about and consider sourcing criteria and procedures			
Interview major suppliers			
Consider vulnerability to supply shortages and the adequacy of alternative suppliers (for example in the event of failure of a key supplier)			
Enquire about and consider frequency of standard cost updates and procedures for calculating and analysing variances			
Enquire about and consider causes of significant manufacturing variances and specific strategies adopted to reduce such variances			
Enquire about and consider cost saving opportunities			
Enquire about any long-term supply contracts and consider implications (eg vulnerability to onerous contracts, removal of contractual arrangements)			
Consider the extent of subcontracting arrangements for intermediate suppliers			
Review exposure to input price fluctuations and how this is managed			

13. Asset management - property, plant and equipment

Objective: Enquire about significant individual assets comprising property, plant and equipment

Potential risks

Recommended personnel to interview

- | | |
|---|--|
| <input type="checkbox"/> Poor condition of assets | <input type="checkbox"/> Production Manager |
| <input type="checkbox"/> Significant commitments or projects requiring significant cash outflow | <input type="checkbox"/> Chief Financial Officer |
| <input type="checkbox"/> Capacity constraints and bottlenecks | <input type="checkbox"/> Controller |
| <input type="checkbox"/> Inadequate maintenance and repair | |
| <input type="checkbox"/> Obsolete machinery and equipment | |
| <input type="checkbox"/> Idle facilities | |

Activities	Completed By & Date	File ref.	Comments
Tour facility to gain general impression of layout, condition, potential for expansion			
Enquire about assets not in service or under-utilised			
Consider the terms of leased property including options for renewal, lease classification, potential impact of renewal terms, unusual covenants and restrictions on use			
Enquire about planned or deferred capital asset additions or repairs and consider adequacy, including impact of technological change			
Review adequacy of maintenance procedures and consider expenditure involved			
Address degree of automation in relation to rest of industry			
Enquire about compliance with environmental and safety requirements			
Enquire into the procedures by which the physical existence of tangible fixed assets is safeguarded			

14. Asset management - inventory

Objective: Gain an understanding of inventory quantities

Potential risks

Recommended personnel to interview

- | | |
|--|---|
| <ul style="list-style-type: none"> <input type="checkbox"/> Inadequate reserves for obsolete, damaged, or slow-moving inventory <input type="checkbox"/> Dependence on few suppliers for raw materials <input type="checkbox"/> Lack of inventory control <input type="checkbox"/> Shrinkage <input type="checkbox"/> Unfavourable supply contracts | <ul style="list-style-type: none"> <input type="checkbox"/> Chief Financial Officer <input type="checkbox"/> Controller |
|--|---|

Activities	Completed By & Date	File ref.	Comments
Analyse inventory by product, calculate inventory turnover ratio and enquire about significant trends and fluctuations			
Review ageing profile and enquire about slow-moving, obsolete and excess inventory and enquire about the nature and adequacy of provisions and net realisable value adjustments			
Enquire about and consider adequacy of procedures used to determine obsolete inventory			
Enquire about timing and extent of physical inventory procedures			

15. Risk management - commitments, contingencies and litigation

Objective: Consider significant commitments and contingencies

- | | |
|---|---|
| Potential risks | Recommended personnel to interview |
| <input type="checkbox"/> Self-insurance
<input type="checkbox"/> Unfunded pension
<input type="checkbox"/> Past losses
<input type="checkbox"/> Major litigation
<input type="checkbox"/> Repairs | <input type="checkbox"/> Chief Financial Officer
<input type="checkbox"/> Controller
<input type="checkbox"/> Legal counsel |

Activities	Completed By & Date	File ref.	Comments
Obtain details of contractual commitments and economic obligations such as leases, union contracts, purchase or sale commitments			
Enquire as to the nature of outstanding or threatened litigation			
Enquire into entity's litigation history			
Consider if adequate financing exists to satisfy commitments			
Obtain details of and consider effect of non cancellable revenue commitments			
Discuss significant findings in regulatory reports with management and enquire about fines or other restrictions			

16. Risk management - employee benefits

Objective: Gain an understanding of the entity’s benefits programme and address the impact on the accounts

Potential risks

Recommended personnel to interview

- Unfunded pension liabilities
- Post retirement benefits

- Chief Financial Officer
- Director of Human Resources
- Manager of Employee Benefits

Activities	Completed By & Date	File ref.	Comments
Enquire about types of plans			
Enquire about risks associated with the acquisition of the plans			
Enquire about post-retirement benefits and the impact on reserves			
Enquire into benefit related liabilities not recorded on the entity’s books			
Consider the effect of entity’s benefit plans on the client's accounts			
Consider the effect on client's accounts of any over/underfunding			

17. Risk management - environmental overview

Objective: Gain an understanding of the environmental risk and sensitivity and management procedures to mitigate risk

Potential risks

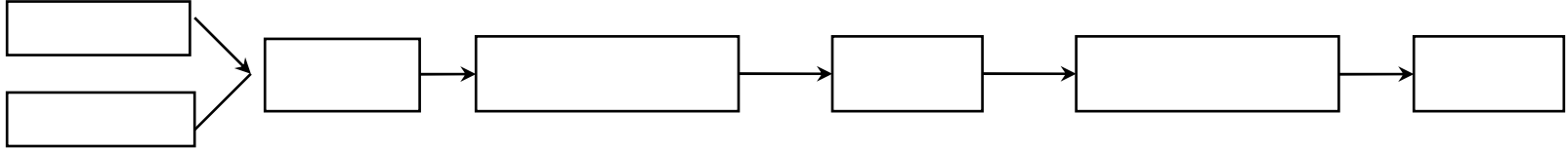
Recommended personnel to interview

- | | |
|---|--|
| <input type="checkbox"/> Unaccrued, under accrued liabilities | <input type="checkbox"/> Environmental Officer |
| <input type="checkbox"/> Capital expenditures not included in forecasts | <input type="checkbox"/> Plant manager |
| <input type="checkbox"/> Changing/new regulations | <input type="checkbox"/> Chief Financial Officer |
| <input type="checkbox"/> Inadequate knowledge of risks/costs | <input type="checkbox"/> Legal Counsel |
| <input type="checkbox"/> Poor structure/controls | |

Activities	Completed By & Date	File ref.	Comments
Interview management or outside consultants about technical issues and the probability, timing and magnitude of cash flow, financial reporting and tax impacts of environmental issues			
Review correspondence files with regulators and related documentation			
Address adequacy of entity's environmental controls			
Carry out site visits as appropriate			
Consider risk level and the need for technical specialist help			
Enquire if the entity has procedures in place to manage health and safety concerns			

Audit Tool - 5 (Process Analysis Template)

- The components of the process analysis template is explained below :-

Process Objectives	The objectives of the process are statements that define the direction needing to be taken with respect to the process. Objectives often relate to items such as recipients/customers satisfaction, efficient use of resources and compliance with applicable regulations.
Inputs	The inputs to a process represent the elements, materials, resources, or information needed to complete the activities in the process.
Activities	<p>The activities are those actions or sub-processes that together produce the outputs of the process. For some processes, arrows are omitted due to the nonsequential nature of the activities.</p>  <pre> graph LR I1[] --> A1[] I2[] --> A1 A1 --> A2[] A2 --> A3[] A3 --> A4[] A4 --> A5[] </pre>
Outputs	The outputs represent the end result of the process - the product, deliverable, information or resource that is produced.
Systems	The systems are collections of resources designed to accomplish process objectives. Information systems produce reports containing operational, financial and compliance related information that make it possible to run and control the process.

<p>Classes of Transactions</p>	<p>The classes of transactions are data and information that are related to the process for use in one or more reports to management or third parties. The classes of transactions, which are broken down into routine and nonroutine transactions and accounting estimates, provide a linkage from the process to the audit procedures.</p>
<p>Risks Which Threaten Objectives</p> <p>A process's risks are the risks which may threaten the attainment of the process's objectives.</p>	<p>Controls Linked to Risks</p> <p>Controls are the policies and procedures, which may or may not be put in place, that provide assurance that the risks are reduced to a level acceptable to meet the process's objectives.</p>
<p>Critical Factors for Success (CFS)</p> <p>Critical factors for success are the prerequisites and areas of dependency for a process to be successful. the CFS may be inputs, parallel or supporting activities or aspects of an entity's philosophy or infrastructure necessary to ensure the proper delivery of the process.</p>	<p>Key Performance Indicators (KPIs) Linked to the CFS</p> <p>The KPIs are quantitative measurements, both financial and nonfinancial, of the process's ability to meet its objectives through trend analysis within an entity or benchmarking against a peer of the entity or its industry. Whilst most the KPIs can be linked to the CFS, this may not always be the case.</p>
<p>Other Symptoms of Poor Performance</p> <p>Other symptoms of poor performance represent other evidence which may exist and indicate that the process may not be operating to its most effective level.</p>	
<p>Performance Improvement Opportunities</p> <p>Performance improvement opportunities are areas for performance or process improvement. This improvement may be achieved internally by the client or through the OAG or other third-party assistance.</p>	

- An example of a completed process analysis for human resource management is shown below : -

Resource Management Process : Human Resource Management

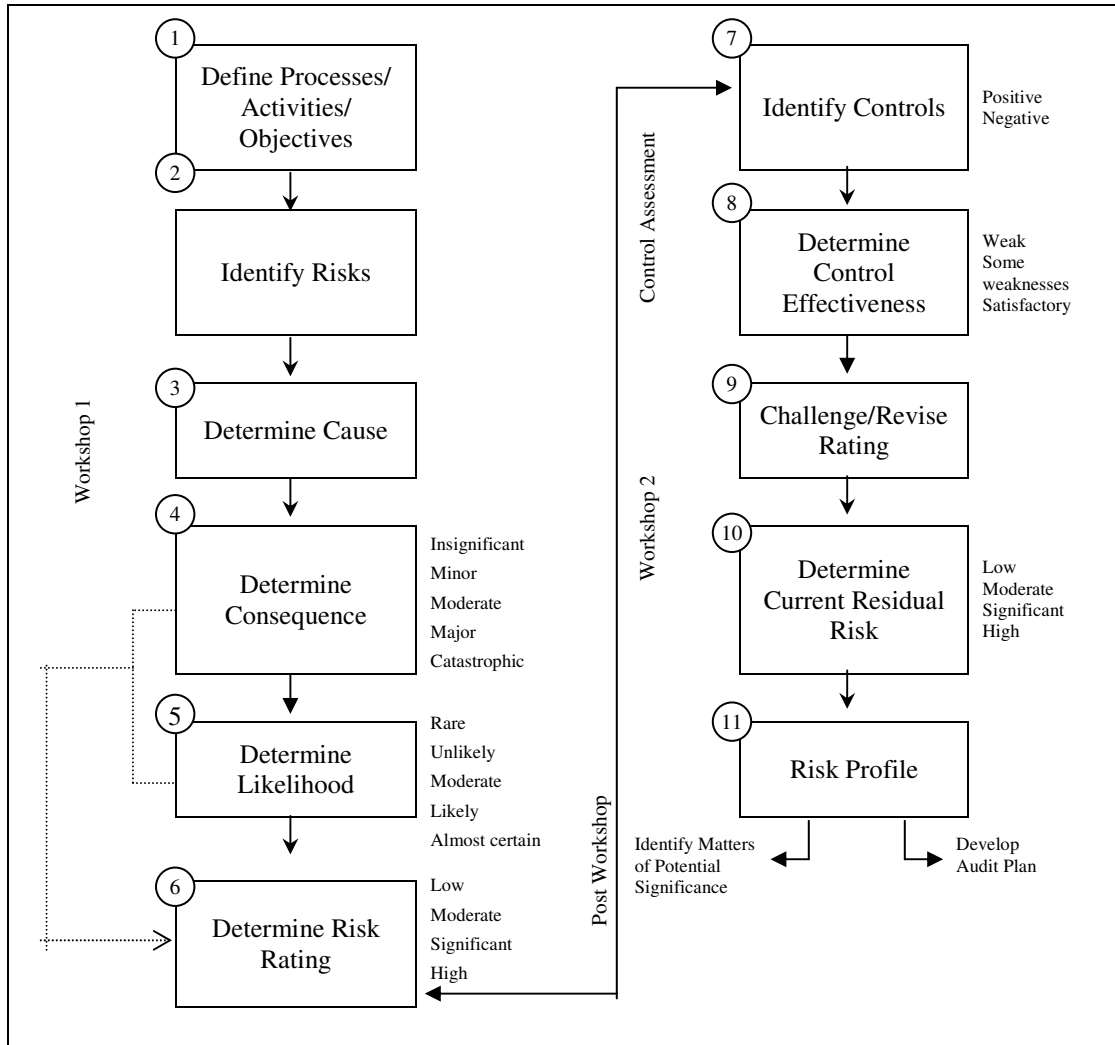
Process Objectives	<ul style="list-style-type: none"> • Attract and retain skilled and motivated work force • Control employee costs while maintaining morale and productivity • Comply with regulatory/tax filing requirements • Adherence to code of conduct
Inputs	<ul style="list-style-type: none"> • Strategic plan • Operating plan • Resource requests • Employee regulations • Tax regulations • Union contracts • Industry statistics and market data • Training goals/requests • Personnel feedback
Activities	<pre> graph LR A[Develop & maintain human resources] --> B[Establish and maintain compensation & benefits policies and programs] B --> C[Identify resource requirements] C --> D[Recruitment and hiring] D --> E[Provide training and development] E --> F[Provide performance reviews and counselling] F --> G[Perform compensation and benefits administration] G --> H[Monitor union contracts and grievances] </pre>
Outputs	<ul style="list-style-type: none"> • Regulatory filings • Compensation and benefits policies and administration • Personnel files • Tax filings • Human resource policies/procedures • Training programmes • Performance reviews • Payroll and benefits disbursements • Staffing and cost data
Systems	<ul style="list-style-type: none"> • Human resource management • Compensation and benefits • Tax system • Regulatory systems • Cash disbursements/payables systems • Employee self-service systems

Classes of Transactions	Routine <ul style="list-style-type: none"> • Payroll and benefit expenses • Payroll related accruals • Training expenses 	Nonroutine <ul style="list-style-type: none"> • Pensions • Other post retirement benefits • Post employment benefits • Incentive compensation accruals 	Accounting Estimates <ul style="list-style-type: none"> • Self-insured medical • Self-insured workers' compensation • Self-insured general liability claims
Risks Which Threaten Objectives <ul style="list-style-type: none"> • High level of staff turnover • Poorly motivated staff • Non-compliance with regulations (tax, labour, etc.) • Lack of personnel with skill sets needed • Noncompetitive compensation packages 		Controls Linked to Risks <ul style="list-style-type: none"> ⇒ Conduct employee surveys with follow up on results; implement growth and opportunity plans for employees ⇒ Compare incentive pay to performance; conduct employee surveys with follow up on results; monitor labour relations and establish employee grievance committees ⇒ Regulatory monitoring ⇒ Establish formal hiring criteria; develop and implement effective training programs ⇒ Compare salary costs to industry norms; compare incentive pay to performance 	
Critical Factors for Success <ul style="list-style-type: none"> • Commitment to training and development • Retention of key personnel • Maintain competitive compensation/benefit packages • Optimise employee utilisation and productivity • Employee commitment to customers • Optimise human resource administration efficiency 		KPIs Linked to CFS <ul style="list-style-type: none"> ⇒ Training hours per employee; training costs per employee ⇒ Employee turnover ⇒ Employee turnover; compensation/benefit levels compared to the industry ⇒ Sales per employee; payroll to sales ⇒ Customer complaint percentage; customer surveys/focus groups ⇒ Human resource employees/total employees; human resource department costs to sales 	
Other Symptoms of Poor Performance	<ul style="list-style-type: none"> • Poor internal communication • Fines and penalties for untimely, inaccurate tax and regulatory filings 	<ul style="list-style-type: none"> • High level of absenteeism • Inconsistent employee management 	<ul style="list-style-type: none"> • Low productivity • High level of customer complaints
Performance Improvement Opportunities	<ul style="list-style-type: none"> • Incentive/Compensation consulting • Managed health care studies 	<ul style="list-style-type: none"> • Claims systems reviews • Retirement plan reviews 	<ul style="list-style-type: none"> • Human resource department reengineering • Human resource benchmarking

Audit Tool - 6 (Risk Assessment Process)

Risks are events that threaten the assets and earnings of, or the essential services provided by, the entity. In essence, a risk is anything which has the potential to prevent the entity from achieving its objectives.

Risk Assessment Process - manpower management diagram:



An effective risk assessment process must be based on the following core elements :

- the identification of each operational risk;
- the measurement of the identified risks in terms of magnitude and frequency of occurrence;
- the control or the way the risk is managed in line with the needs of the entity's policies and strategies.

Step 1. Define Processes/ Activities/ Objectives

It is useful in the risk identification phase to have some assurance that all of the key risks have been raised. The approach achieves this by first identifying the key processes and activities and objectives of each operational unit.

The information is then used as a guide or “map” in the workshop session and in the preparation by operational unit management prior to the workshop in thinking about the key risks.

Example:	
Process:	Activities:
Human Resource Management	<ul style="list-style-type: none">• Recruitment• Training• Performance Appraisal• Counselling

Conduct Workshop - 1

The workshop requires the participation of key managers in the entity. It should run for approximately 2 hours and should be facilitated by at least an Audit Director. We may also use one-on-one interviews with management and/or staff where it is considered more appropriate than the workshop approach.

Step 2. Identify Risks

Participants identify the key operational risks associated with the processes within their business area. They also nominate the person or persons responsible for managing each risk area.

Step 3. Determine Cause

Participants identify the situation(s) or cause(s) which could result in the risk event occurring.

The main causes of the risk are then utilised to determine within which broad risk category the risk should be recorded.

Example:
One of the risks identified may be the loss of key personnel. Causes may include : <ul style="list-style-type: none">• uncompetitive remuneration;• poaching by competitors;• poor training and development;• poor working conditions; and/ or• perceived lack of career opportunities After reviewing the main causes, the risk would be included in the Human Resources broad risk category.

Step 4. Determine Consequence

Participants are asked to describe the consequences associated with each risk.

Example:
The following consequences may be identified as flowing from the risk of the loss of key personnel : <ul style="list-style-type: none">• recruitment costs;• production interruption;• training costs;• loss of morale; and/ or• reputation damage

Consequence are categorised as follows:

- Catastrophic : A disaster with potential to lead to collapse of the operations.
- Major : A critical event which with proper management can be endured
- Moderate : A significant event which can be managed under normal circumstances
- Minor : An event, the consequences of which can be absorbed but management effort is required to minimise the impact
- Insignificant : An event, the impact of which can be absorbed through normal activity.

Step 5. Determine Likelihood

Participants are asked to assign a likelihood rating (i.e. how likely is it that the entity will be exposed to each risk?). Consideration is given to:

- the anticipated frequency of the event occurring;
- the working environment;
- the procedures and skills currently in place;
- staff commitment, morale and attitude; and
- history of previous events.

The likelihood ratings use are:

- Almost Certain
- Likely
- Moderate
- Unlikely
- Rare

Given format has to be used to write matters relating step 2 - 5 (Workshop one)

Risk Description	Causes (Describe)	Consequence (Describe)	Consequence Rating	Likelihood Rating
Loss of key personnel (example only)	<ul style="list-style-type: none"> - uncompetitive remuneration - poaching by competitors - poor training and development - perceived end of career opportunities 	<ul style="list-style-type: none"> - business interruptions - increase cost of recruitment and re-training - loss of morale - damage to reputation - loss of customers 	Moderate	Likely

Step 6. Determine Inherent Risk Rating

On the basis of consequence and likelihood ratings identified the inherent risk rating for each risk can be determined by using following table

Likelihood	Consequences				
	Insignificant	Minor	Moderate	Major	Catastrophic
Almost Certain	Significant	Significant	High	High	High
Likely	Moderate	Significant	Significant	High	High
Moderate	Low	Moderate	Significant	High	High
Unlikely	Low	Low	Moderate	Significant	High
Rare	Low	Low	Moderate	Significant	Significant

Auditor should prepare a list of inherent risk rating in the format given below.

S. No.	Risk	Likelihood	Consequence	Risk rating

Step 7. Identify Controls

At the end of the first workshop (Step 6) the risks identified will be allocated between the responsible managers to enable pre-work on the effectiveness of controls in relation to the risks identified. The information collected during the first workshop will be collated and provided in the following workshop. All managers will be provided with the *risk records* for each risk for which they have identified as the responsible manager.

The managers are asked to review the positive and negative control considerations in determining the control effectiveness rating as follows:

Example:	
Risk of loss of key personnel :	
Positives	Negatives
<ul style="list-style-type: none"> • awareness of market remuneration levels • regular remuneration reviews • well developed training program 	<ul style="list-style-type: none"> • poor succession planning • lack of career development program

Step 8. Determine Control Effectiveness

Once the key controls have been identified, an assessment of the effectiveness is made. The following ratings are used:

Satisfactory:	Controls are strong and operating properly, providing a reasonable level of assurance that objectives are being achieved.
Some Weaknesses:	Some control weaknesses/ inefficiencies have been identified. Although these are not considered to present a serious risk exposure, improvements are required to provide reasonable assurance that objectives will be achieved.
Weak:	Controls do not meet an acceptable standard, as many weaknesses/ inefficiencies exist. Controls do not provide reasonable assurance that objectives will be achieved.

Conduct Workshop 2

Step 9. Revise Risk Ratings

During the second workshop, the management team is given the opportunity to discuss and challenge the rating proposed as a result of the work undertaken prior to the workshop. Changes to ratings may result.

Step 10. Determine Current Residual Risk Rating

The residual risk represents the risk, which remains *after* considering the controls in place to mitigate the risk. The following table illustrates the approach for determining this rating:

Risk Rating	Control Effectiveness		
	Satisfactory	Some Weaknesses	Weak
High	Significant	High	High
Significant	Moderate	Significant	High
Moderate	Moderate	Moderate	Significant
Low	Low	Low	Moderate

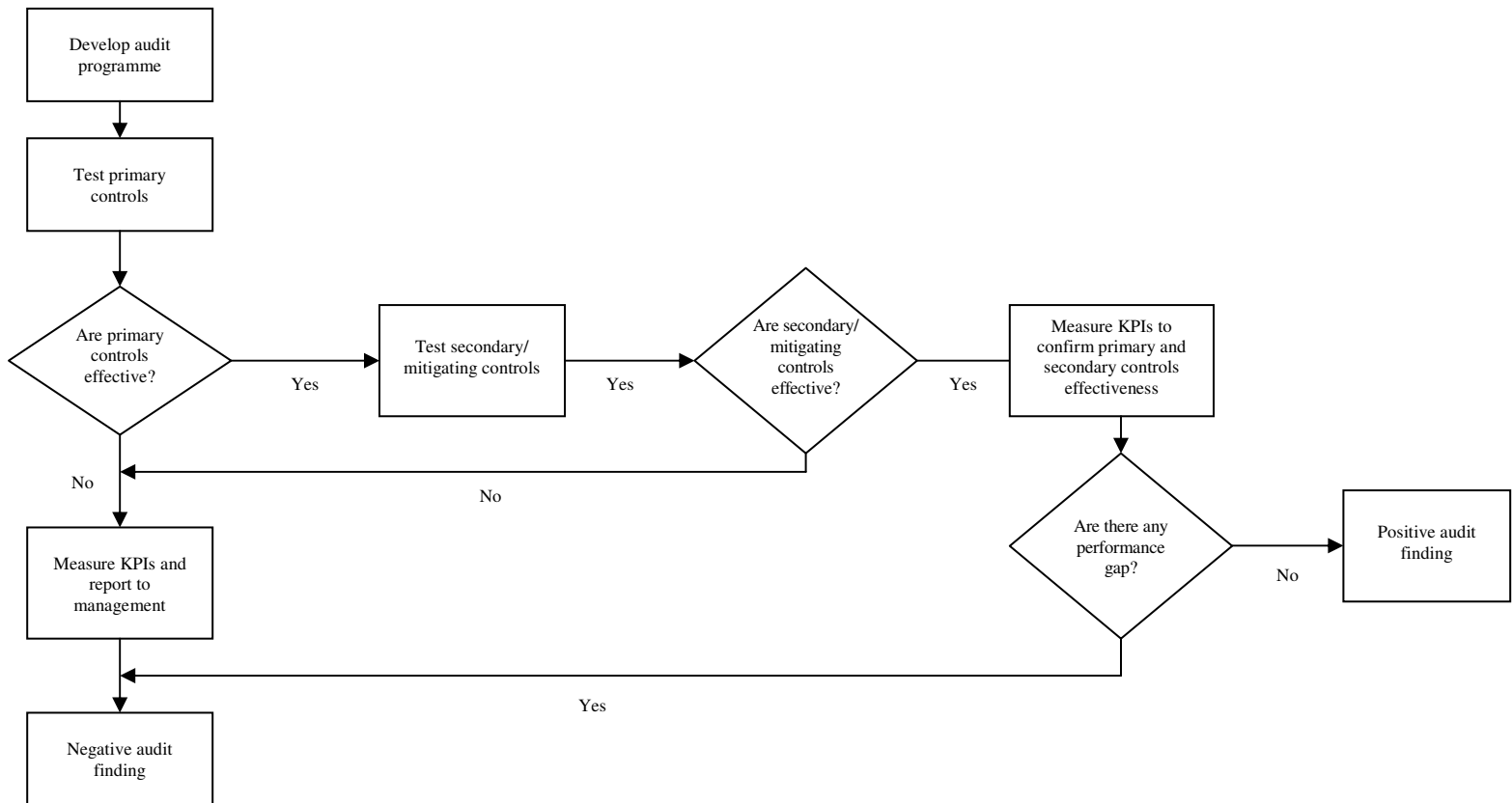
Step 11. Risk Profile and Matters of Potential Significant

At the completion of the risk assessment process, the risk records and residual risk ratings will be confirmed by the management team. A risk profile will be prepared. The following table illustrates the outputs (at the summary level) or confirmation on the degree of residual risk.

S. No.	Risk	Inherent Risk rating	Control effectiveness	Residual risk rating

At the completion of this risk assessment process, the management team then must consider the residual risk levels and decide whether they are acceptable in the context of the entity’s objectives. The objective is not to eliminate all residual risk but rather to ensure that residual risk is maintained at an acceptable level in a cost-effective manner. On the basis of residual risk rating Matters of Potential Significance have to be identified.

40.1 Audit Execution (Control and Performance Assessment) - Diagram



40.2 Policies

The significant policies in respect of audit execution are as follows:

- financial audits and performance audits should be carried out by separate teams. However, the performance and financial audits may be carried out concurrently.
- audit programme should be reviewed and approved by the AAG
- changes and the reasons for the changes in audit programme subsequent to approval by the AAG should be documented and approved by the AAG
- existing standard audit programme may be used where appropriate
- audit execution should involve the collection and documentation of relevant and reliable evidence based on audit programme
- audit evidence should be sufficient to support audit findings, conclusions and recommendations

40.3 Objectives of Audit Execution

40.3.1 Develop audit programme to translate the audit plan into detailed audit procedures to minimise audit risks;

40.3.2 Achieve audit objectives by gathering and evaluating information to compare actual practices against audit criteria, and to obtain relevant, reliable, sufficient, objective and timely evidence to substantiate any conclusions and recommendations to be reported;

40.3.3 Consider the underlying cause and effect where significant deviations from audit criteria are identified;

40.3.4 Develop conclusions and formulate recommendations which are well researched, practical and cost-effective.

The broad objectives are supplemented by detailed objectives at the beginning of the section on Control Assessment and Performance Assessment.

- Control assessment essentially represents the *qualitative* assessment of the overall effectiveness of each control in meeting management's objectives. Performance assessment involves a *quantitative* assessment of the effectiveness of activities within a process, or the outputs of a process, in achieving management's objectives.
- Performance audits should be carried out by combining both control and performance assessments to provide a comprehensive analysis of the auditee's performance. This is based on the assumption that the auditee, or part of the auditee being audited, can be thought of as a system of elements dynamically related to achieve a purpose.
- The issues identified from the control and performance assessments are indicative of potential problems or opportunities which should be reported upon. The auditor should develop appropriate recommendation for each issue noted after reaching a conclusion based on the audit findings.

40.4 Control Assessment

40.4.1 Control assessment involves the following key stages:

- develop audit programmes by designing audit procedures and tests;
- execute audit test procedures and apply audit sampling to determine whether the controls are operating as intended;
- assess the control environment and optimise the controls

40.4.2 The objectives of control assessment are to :

- design, perform and review appropriate control test procedures;
- determine if the controls provide reasonable assurance that management's objectives will be met
- identify potentially excessive and/or ineffective controls
- identify and evaluate residual risks; and
- design and perform additional test of significant residual risk if applicable

40.4.3 The purpose of assessing control effectiveness is to perform a qualitative assessment of the overall effectiveness of each control in helping the auditee meet management's objectives.

40.4.4 The findings from the review should be compared to the audit criteria.

40.4.5 The qualitative assessment is typically carried out using an analysis of procedural approach (see *PAG - Audit Tool : AT9*). This involves testing procedures against established criteria, best practices or a desirable control model. Recommendations are made by the auditor where controls are either deficient or ineffective.

40.4.6 The auditor examines the results or outputs of the programme, activities or organisational units concerned to determine the significance of control deficiencies. In this way, the likely causes and effects can be identified and assessed. In instances where it was found that the auditee had no KPIs to measure achievement, then the auditor could report the absence of knowledge about performance, rather from attempting work which may or may not answer the question.

40.4.7 Control assessment should focus on the performance audit areas instead of financial audits. However, the internal control review findings from the financial audit should be reviewed to avoid duplication in carrying out performance auditing. For this purpose, auditors should be able to differentiate between financial and performance audit objectives.

40.5 Audit Programme

40.5.1 The main reasons for using audit programme are to :

- establish a clear relationship between audit objectives, audit methodology, and the anticipated field work to accomplish those objectives
- identify and document the procedures to be performed, before commencement of testing
- facilitate delegation, supervision and review
- ensure that all planned procedures are performed
- document performance of procedures executed
- document the application of audit sampling to provide sufficient audit evidence

40.5.2 The audit programme working documents should describe the nature, timing and extent of planned audit procedures required to implement the audit plan. The audit programme

essentially translates the audit plan into detailed audit procedures designed to satisfy detailed audit objectives. The audit programme should be revised as necessary during the course of the audit.

40.5.3 An audit programme will set forth and specify the following:

- audit sub-objectives concerning efficient, economical or effective operations
- audit criteria to be applied
- the specific tasks to be performed during the field work to determine whether audit criteria are met by the audited entity
- evidence to be collected, including audit sampling
- procedures/techniques for collecting the evidence
- who is to perform the tasks, how, when and where they will be performed
- special instructions if necessary

40.5.4 The following steps have to be carried out in order to design the audit programme:

- review risk analysis results in order to decide which significant risks and related controls warrant further testing. Further testing may be appropriate for:
 - client processes that are heavily relied upon in meeting management and performance audit objectives
 - areas where significant residual risk remains
- determine performance audit objectives
- design audit procedures to meet objectives

40.5.5 An audit objective is based on the audit mandate. It represents a goal defined by the auditor for the purpose of efficiently gathering audit evidence regarding the effective operation of a control. The audit programmes should set out the audit objectives which generally parallel the intention of specific controls designed to obtain desired results.

40.5.6 During the risk assessment, the auditor decides whether the residual risk is acceptable. Audit tests referred to the audit programmes are designed taking into account the residual risk levels to obtain appropriate evidence to meet the audit objectives.

40.5.7 The table below identifies exemplary situations where controls will need to be tested.

Inherent Risk	Control Effectiveness	Residual risk	Testing
High	Satisfactory	Significant	Yes
Low	Satisfactory	Low	No
High	Weak	High	No

The extent of audit testing should be efficiently focused on the areas where important potential risks exist as well as controls are deemed adequate. The auditor should not be testing controls which are deemed inadequate. The auditor has to make careful trade-offs on the extent of testing to make efficient and effective use of available resources and to minimise audit risks.

40.5.8 The performance audit objectives can be stated in more specific terms (i.e. as sub-sets of the above-mentioned performance audit objectives) to address the specific risks and controls we are evaluating. For example, rather than listing “Cost Minimisation” as the

- objective of the audit programme, we may list specific performance objective such as “to achieve target cost” and/or “to strengthen relationship with suppliers”.
- 40.5.9 Carrying out the tests as per the audit procedures will help the auditor determine whether each of the audit objective was met. The test design should allow the auditors to assess the actual operating effectiveness of the controls.
- 40.5.10 Whenever possible, the auditor should design audit procedures so as to include the analytical procedures instead of detailed test of controls (compliance testing procedures). Greater efficiency can be obtained covering the entire population rather than just a portion. An efficient and effective approach involves only testing to the extent necessary to form a valid conclusion on the control structure.
- 40.5.11 In some cases, testing of controls may be necessary to obtain sufficient audit evidence to satisfy certain audit objectives. These include:
- regulatory compliance; or
 - policy and procedure compliance.
- 40.5.12 Other matters that should be considered in the design of audit programme are :
- size of task
 - geographic dispersions
 - audit environment
 - the components of the system to be audited
 - whether only broad issues have been identified or specific criteria available
 - based on resources and other known constraints, select an approach that will best help achieve objectives
 - identify the universe that needs to be reviewed
 - select the appropriate sample
 - a precise description of data that is needed, where it can be obtained, and the reliability of the data
 - if the data necessary to conduct the audits has not been compiled, surveys, case reviews, or other means can be used to collect the appropriate data
 - whether it is necessary to visit the auditees’ field offices, regional programme sites, or recipient household during the field work
 - depending on the nature and complexity of the auditee, the definition of certain terms may need to be agreed upon to avoid misunderstanding later in the engagement
 - based on the professional proficiency of the collective staff, the audit may require special skills such as electronic data processing, engineering, legal, or other specialist.
 - when and in what sequence during the engagement should various audit procedures be performed
 - what type of recommendations will be expected to result from the engagement and in what level of detail
- 40.5.13 The above considerations enable the auditor to develop audit programme containing procedures which are:
- linked to audit objectives, that is they enable relevant evidence to be collected;
 - clearly stated and include sufficient detail to enable them to be readily understood by the audit team;

- logically organised to enable audit testing to be performed as efficiently as possible; and
 - methodologically efficient in collecting sufficient evidence and avoid over-auditing.
- 40.5.14 The format of the audit programme should be standardised. Programme should be designed to include the identification of causes and effects of problems or weaknesses. An example of it is provided in Audit Tool : AT7.

40.6 Execute Audit Test Procedures

- 40.6.1 Once the audit programmes are drawn up, fieldwork can proceed. The process of executing the procedures to test the controls and measuring control effectiveness involves gathering audit evidence in order to develop audit findings. This enables conclusions and recommendations to be formulated.
- 40.6.2 Audit fieldwork involves a combination of a procedure-oriented and a result-oriented approach to performance auditing. Either audit approach may be used during performance audit but whenever appropriate, both audit approaches should be executed together as they are complementary.
- 40.6.3 During the survey stage, the controls are identified as primary, secondary and mitigating. In testing these controls, the auditor seek to:
- obtain evidence on whether the controls operated as documented in the survey stage; and
 - confirm whether the controls functioned effectively throughout the period of intended reliance.

40.7 Optimisation of the Control Design

- 40.7.1 Upon the validation and testing of controls, the auditor should evaluate the control design and effectiveness of the controls.
- 40.7.2 Controls should be optimised as some auditees may have implemented controls which result in accepting a greater degree of risk than the auditee desires. Conversely, controls may be excessive, reducing residual risk more than desired. Implementing and maintaining excessive controls generally involves high operating costs and may limit the financial benefits of taking appropriate risks.

40.8 Performance Assessment

- 40.8.1 Apart from reviewing internal controls, the auditor should also assess the performance of the auditee. The assessment includes both financial and non-financial performance analyses.
- 40.8.2 The primary objectives of business unit for performance analysis are to :
- compare the auditee's process' or current performance to that of prior periods or peer groups to identify potential problems and/or opportunities;
 - understand the cause-and-effect relationships between financial and non-financial measures; and
 - provide insight to the auditee/ process on the effectiveness of its measurement and monitoring systems.

- 40.8.3 The performance assessment is carried out by measuring the key performance indicators identified during the survey stage. The key performance indicators measure how well a process is performing and confirm the effectiveness of primary, secondary and mitigating controls. Performance gaps exist where the key performance indicators fall short of the specified goals and should they exist, the auditor should consider reporting their findings together with any related deficiency in controls procedures to management.
- 40.8.4 Some of the tools that can be used to measure financial performance are :
- financial ratio analysis - involves comparison of financial ratios for a single period or multiple periods.
 - analysis of cash flows - carried out to assess the implications on long term solvency and to understand the relationship over time between net income and cash flow from operations.
 - return on investment analysis - a primary measure of economic performance by providing an indication of the auditee's ability to earn a satisfactory return on capital employed.
- 40.8.5 The public sector organisations generally do not employ resources to generate profits, although some are engaged in commercial activities and are required to achieve profit targets. Consequently, the use of financial performance measures need to coincide with entities where financial statements provide an account of the overall performance in terms of objectives.
- 40.8.6 The auditor should also analyse the auditee's performance by analysing the following :
- resource management performance - this includes management of human resources, information and technology. The objectives and the key performance indicators need to be identified for each of the above processes. For example, one of the objectives of human resources management is employee's productivity and key performance indicator could be revenue per employee. The auditor will need to assess how well this resource is being managed based on its key performance indicators.
 - process performance - this includes process time, process cost and process quality. This need to be compared against the criteria identified to assess if the process performance can be improved.

40.9 Audit Evidence

- 40.9.1 Audit evidence is information collected and used to support audit findings. Such evidence forms the basis of audit conclusions and recommendations and is a central concern from the planning to the completion of the audit.
- 40.9.2 The audit fieldwork involves gathering evidence in accordance with the audit plan prepared during the survey stage and the audit programme that were developed. The evidence gathered is analysed and used to determine if the audit criteria is met. The evidence gathered should meet the following criteria :
- "Sufficient" sufficiency relates to the weight each piece of evidence plays in influencing the auditors' mind concerning the conclusion to the audit objective. Sufficient information should be gathered so that a reasonable person would agree with the audit conclusion. The risk, materiality and sensitivity of the matter to be

reported on and the cost of obtaining the evidence will determine how much evidence is sufficient.

- "Competent" competency of evidence relates to the reliability placed on the source of information used as evidence. The competency influences the persuasiveness of the evidence. The following can be used in judging the competence of evidence:
 - evidence obtained from a third party is more reliable than evidence obtained from the audited entity itself
 - evidence developed under a good system of internal control is more reliable than that obtained where such controls are weak or non-existent
 - evidence obtained directly (e.g. through physical examination, observation and inspection) is more reliable as compared to evidence obtained indirectly
 - original documents are more reliable than copies
 - testimonial evidence is more reliable where persons may speak freely compared to situations where they are intimidated
 - testimonial evidence obtained from a person who is unbiased and has complete knowledge in the relevant area is more reliable as compared to a person who is biased and has only partial knowledge
- "Relevant" the evidence should have a logical and sensible relationship to the criteria in order to provide a reasonable basis for the auditors findings. It should also be relevant to the subject and period of time encompassed by the audit.

40.9.3 The evidence gathered should help the auditor in providing the following in the audit report :

- *criteria* - reasonable and attainable standards of performance in terms of economy, efficiency and effectiveness, where the activities are assessed
- *condition* - situation that exists
- *cause* - causes of management/employee action that took place to carry out or not carry out according to the appropriate performance indicator
- *consequence* - results attained when management/employees carry out actions based on improper standards and those actions are measured against opposite standards

40.9.4 Adequate documentation of evidence is important as it will :

- confirm and support the auditor's opinion and reports
- increase the efficiency and effectiveness of the audit
- serve as a source of information for preparing reports or answering any enquiries from the audited entity or from any other party
- serve as evidence of the auditor's compliance with auditing standards
- facilitate planning and supervision
- help to ensure that delegated work has been satisfactorily performed
- provide evidence of work done for the future

40.10 Techniques for Gathering Audit Evidence

40.10.1 "Analysis" visually or electronically identifies what is the same and what is different between two or more documents, tangible items or data. Analytical evidence should be derived by experts/people who are knowledgeable about the matters analysed and have the ability to make logical inferences and value judgements from the data collected.

- 40.10.2 "Structured interviews/questioning" means seeking appropriate information of knowledgeable persons inside or outside the auditee. In the context of test of controls, auditor should ask knowledgeable client/personnel for information, listen to and consider their responses, ask follow-up questions and corroborate information, as appropriate.
- 40.10.3 "Observations" means looking at a process or procedure being performed by others. It provides evidence for that point in time and by themselves, which cannot be used to draw conclusions about matters that have occurred over a period of time.
- 40.10.4 "Physical examination" is an inspection of a tangible item, usually other than a document, such as an item of equipment
- 40.10.5 "Examining records/documentation" is reading records or documents either visually or electronically. Unlike observation, we do not need to be present at the time a process or procedure is performed to obtain audit evidence. Examples of records/documentation are correspondences, memorandum, minutes, reports, etc.
- 40.10.6 "Replication" is walking through or repeating operational steps. For example, to check the accuracy of efficiency measures, the auditor may replicate procedures used to measure efficiency. Replication can help the auditor confirm or deny the system or some part of it works as claimed.
- 40.10.7 "Confirmation" is a response, ordinarily in writing, to an enquiry, also ordinarily in writing, to corroborate information. It can be used to verify that an asset or liability exists or to verify that procedures of the audited organisation
- 40.10.8 "Conducting system tests" involves audit programme set out the assignments and test to be performed. In general, testing involves applying a given auditing procedures to some items within a group. The purpose of testing is to gather appropriate audit evidence on the effective functioning of key systems, controls and results identified by the auditor in the survey stage. This type of testing gives the auditor the necessary degree of assurance that specified audit criteria are, or are not, being met.

40.11 Sampling

- 40.11.1 If possible, the entire population should be analysed. Where this is not practicable, sampling techniques should be used.
- 40.11.2 Audit sampling is an application of an audit procedure to less than 100% of the items within a population, for instance an account balance, class of transactions, distribution of provinces, etc. for the purpose of evaluating some characteristics of the balance, class or instances.
- 40.11.3 The objective of doing audit sampling is to reach a conclusion about a set of entire data, even though there are limitations when considering the completeness or understatement of a population.
- 40.11.4 The following conditions must be met to constitute audit sampling :
- less than 100% of the population must be examined;
 - sample results must be projected as population characteristics, i.e. sampling is to be representative;

- projected sample results must be compared to an existing auditee's determined account to determine whether to accept or reject the auditee's balance, or the projected sample results must be used to assess control risk.

40.12 Statistical Versus non Statistical Sampling

Two general overall approaches to audit sampling exist: *statistical* and *non statistical* sampling. Either approach, when properly applied, can provide sufficient competent evidential matter.

40.12.1 Statistical sampling - Statistical sampling is the use of a sampling plan in such a way that the laws of probability can be used to make statements or generalisations about a population. A statistical sampling approach must meet both the following conditions:

- the sample, which is projected as a population characteristic, must have a known probability of selection (that is, the sample must be expected to be representative);
- the sample results must be quantitatively or mathematically evaluated.

Statistical sampling, when applicable, adds precision to the process for selecting the sample and to the process for evaluating the results of tests conducted with the sample. Ordinarily, the sample sizes are selected using available sampling software or the application of other Computer Aided Audit Techniques.

40.12.2 Non statistical sampling - Non statistical sampling is the determination of sample size or the selection of the sampled items using judgmental reasoning rather than probability concepts. If a sample that is projected to the population or generalised as a population characteristic does not meet both the requirements for statistical sampling, it is, by definition, a non statistical sample.

Ordinarily, the sample sizes are selected on a haphazard basis based entirely on the auditor's judgement without any special reason for including or excluding a given item from the sample. For example, the auditor may select a random sample of items where the monetary unit is above, say Rs. 1 million to reach a conclusion on the population examined.

40.12.3 The size of the sample is generally affected by the level of assurance required to place reliance on internal controls. Sample sizes generally depend on materiality or precision, the nature and reliability of the data, the degree of confidence desired and the degree of non compliance with acceptable criteria.

Audit Tool - 7 (Work Programme)

Audit Entity	Audit Year
--------------	------------

Matter of Potential Significance.....

Objective of audit execution

S. No.	Description	Sample size where applicable	W.P. Ref	Completed by and Date

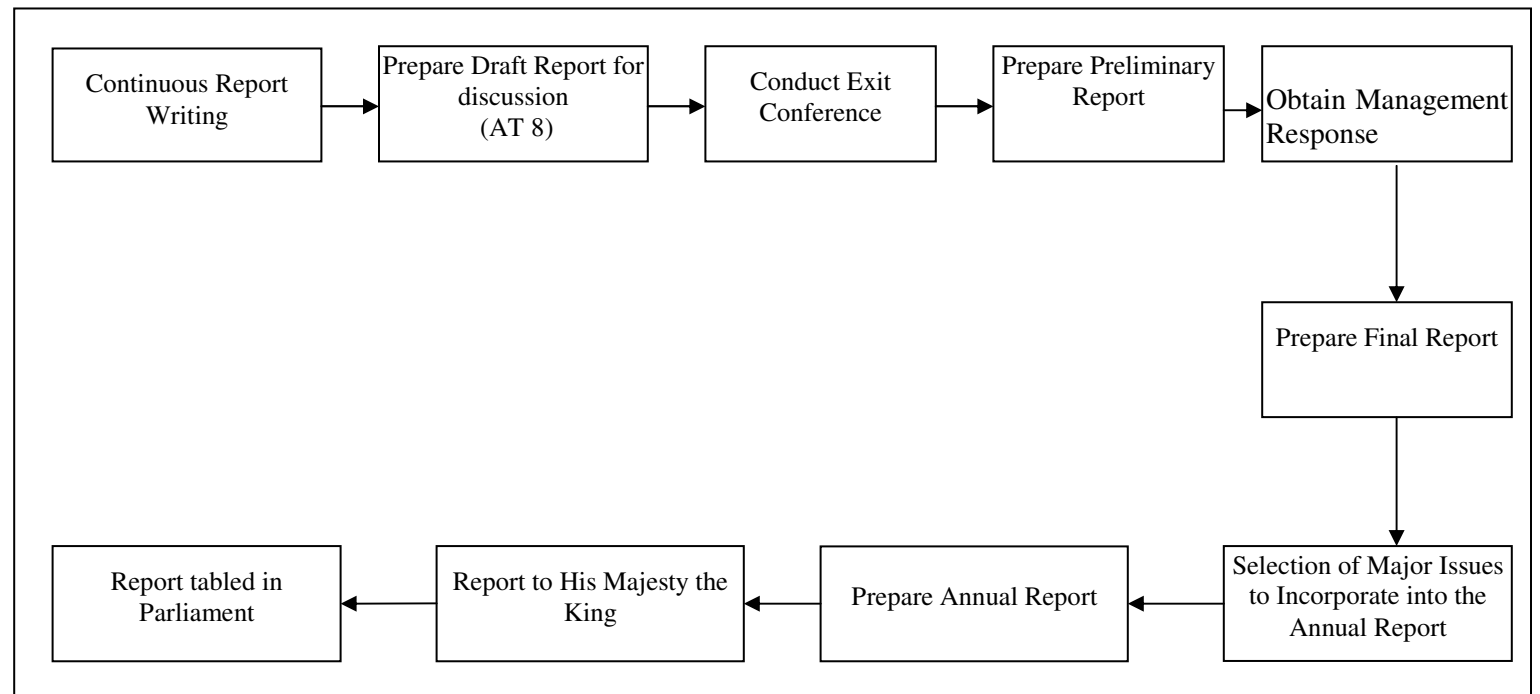
Prepared by
Audit Officer

Forwarded by
Audit Director

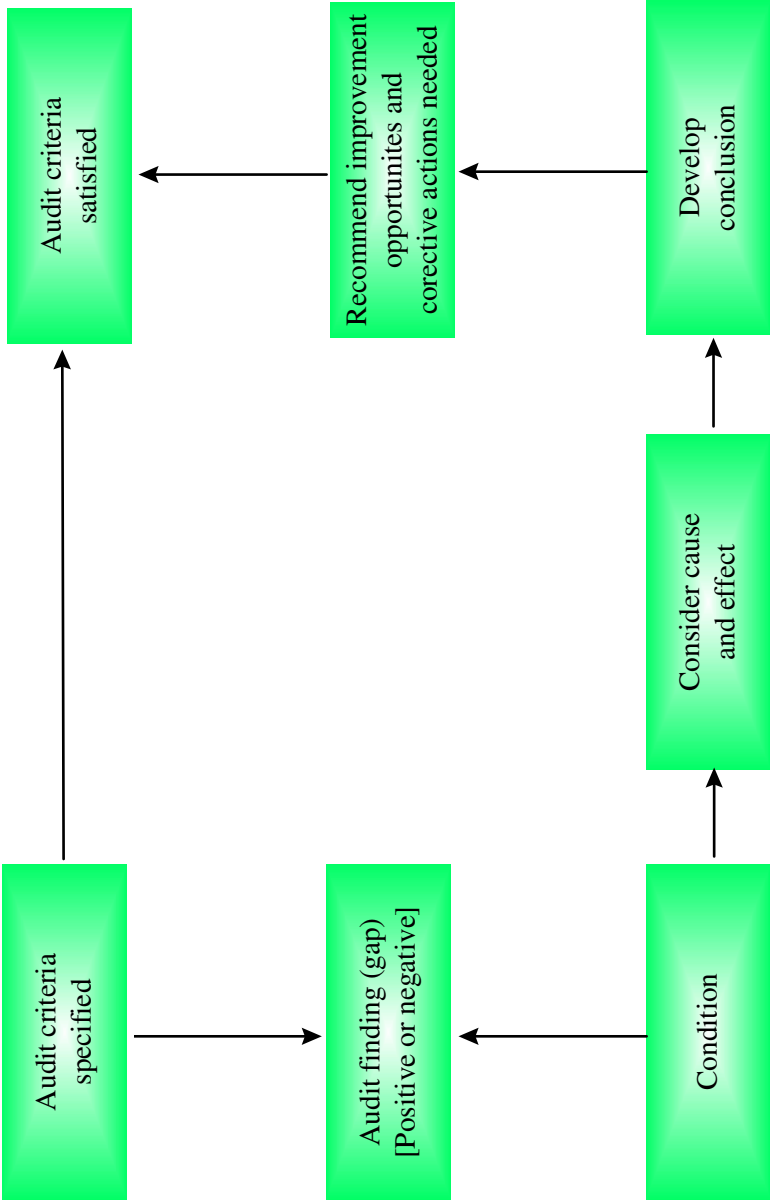
Approved by
Assistant Auditor General

50 "Reporting Section"

50.1 Reporting Procedure - Diagram



50.2 Subject Matter and Structure of Report - Diagram



50.3 Policy and Objectives

50.3.1 The significant policies in respect of audit reporting are as follows :

- only issues relating to performance audit and not financial audit should be included in the report.
- draft audit report should be discussed and agreed with appropriate level of management to ensure completeness and accuracy.
- prior to discussion with management, draft audit reports should be approved by the AAG.
- preliminary audit report should be issued to auditee management for their comments.
- management response should be obtained for each audit finding.
- a long form final audit report should be issued to the auditee management for corrective actions to be taken.
- only issues which are of pressing importance and urgency should be included in the report to be submitted to His Majesty the King.
- an annual report (final report) should be submitted to His Majesty the King.

50.3.2 The objectives of audit reporting are to :

- communicate audit conclusions and recommendations to the auditee management through a long-form report; and
- communicate important matters to His Majesty the King through an annual report or a special report, as appropriate.

50.4 Types of Report

50.4.1 There are mainly three types of reporting :

- long form report to the audited entity
- an annual report is to be submitted to His Majesty the King in accordance with section (6) of the Constitution of the Kingdom of Nepal and clause 8 of the Audit Act, 1991
- in the case of matters of pressing importance and urgency, the AG should not defer issuing a report until the presentation of the annual report. In these instances, a report may be submitted to His Majesty the King as appropriate

50.4.2 The report submitted to His Majesty the King has to be tabled in the Parliament and forwarded to the Public Accounts Committee for detailed deliberations.

50.5 Contents of the Report

50.5.1 "*Title*" The report should have an appropriate title in order to distinguish it from other reports.

50.5.2 "*Addressee*" The report should be addressed to His Majesty the King or the management of the auditee depending on the type of report.

50.5.3 "*Description of the auditee*" A description of the auditee will give the report user appropriate background information. The description should include organisation objectives and targets, overall organisation structure of the auditee, financial position, etc.

- 50.5.4 *"Auditing standards"* A statement regarding auditor's compliance with applicable auditing standards will provide the users with an assurance that the audit has been carried out in accordance with generally accepted audit practice.
- 50.5.5 *"Audit objectives, scope and methodology"* The objective and scope will establish the purpose and boundaries of the audit. The users should also be made aware of the methods and the extent of work carried out as well as the nature and extent of information available in order to arrive at audit findings, conclusions and recommendations.
- 50.5.6 *"Audit findings"* The audit findings should address the economy, efficiency with which resources are acquired and used and the effectiveness with which objectives are met. Each issue of audit should include the criteria, condition, cause and effect and consequence where a departure from criteria is highlighted. Reports may include constructive criticism or may make no significant criticism but give independent information, advice or assurance as to whether economy, efficiency and effectiveness are being or have been achieved.
- 50.5.7 *"Conclusions and recommendations"* The report should give conclusions to the questions posed by the audit objectives and recommendations for actions to correct problems found.
- 50.5.8 *"Management's response"* The report should include management's response to the auditor's findings, conclusions, and recommendations. Management should comment on the acceptability or otherwise of each recommendation.
- 50.5.9 *"Date of report"* The report should be dated to inform the reader that consideration has been given to the effect of events or transactions about which the auditor became aware up to that date.

50.6 Characteristics of the Report

- 50.6.1 The report should be based on facts and should include only information which is supported by audit evidence. The accuracy of the report will depend on the reliability of the evidence the auditor draws conclusions from. Accuracy of the report can be further enhanced by discussing draft reports with appropriate level of management in the audited entity.
- 50.6.2 The report should be readable, easy to understand, straightforward and concise. Terminology used should be familiar to persons whom the report is addressed to. The contents of the report should be free from vagueness and ambiguity.
- 50.6.3 Reports should be issued in a timely manner. The purpose of audit report is to ensure corrective action taken by the relevant persons in order to improve performance of the auditee being audited. If the report takes a long time in being issued, the audit recommendations may no longer be useful as the activities reported on may have been completed.
- 50.6.4 The report should be expressed in a respectful, professional and neutral tone. This would enhance the acceptability of the report and it is less likely the auditors will be perceived as biased.

50.7 Audit Findings

50.7.1 The comparison of observed conditions against audit criteria results in audit findings. Audit findings are based on the identification of performance gaps, that is where controls are deficient or ineffective in mitigating risks.

50.7.2 The issues to be reported on should be identified. Once the issues have been identified the following components can develop the audit finding.

- *"Criteria"* Criterion is reasonable and attainable standard against which to existing standards of performance is assessed. The criteria would have been identified in the planning stage of the audit.
- *"Condition"* The condition refers to what is currently being done or the current situation. The condition should be compared to the criteria to assess if the condition falls short of the criteria beyond acceptable levels. The comparison between the criteria and the condition will form the basis of the audit findings.
- *"Cause and effect"* The findings should also identify the cause and effects of the condition. Cause can be defined as the source or factor for the occurrence of an event. Identifying the cause provides information on accountability relationship and initiates measures of improvement.
- *"Consequence"* The result of an event i.e. the effect of the condition falling short of the criteria.

50.7.3 Where conditions fall short of the criteria, the reasons and the implications of this shortfall are examined. This step involves :

- examining relevant information
- defining the problem and collecting information on the causes of deficiencies
- critically evaluating the appropriateness of evidence to substantiate the findings
- collecting additional evidence on the causes and effects of deficiencies to illustrate the significance of the matter to be reported

50.7.4 It is the responsibility of the Audit Director to ensure that the reasons identified for non-adherence to the criteria and the implications are discussed with the appropriate levels of management in the audited organisation. The viewpoint of management must be given due consideration before the reporting phase of the audit begins.

50.8 Developing Conclusions and Recommendations

50.8.1 From the assessment of the audit findings and their possible causes and effects, the auditor draws conclusions. Tentative findings and conclusions should be tested against accumulated evidence and discussed with the auditee to get valuable input and to validate both correctness and completeness.

50.8.2 Recommendations should be developed where unfavourable findings are made and significant adverse effects have been identified. High-quality recommendations highlight the problems in need of action and the corrective action needed to achieve desired results. The following questions should be considered in developing recommendations:

- is it clear why a change is needed, why current conditions should not be allowed to continue and what the root cause of the problem is?
- does the recommendation include specific actions that should be taken and results that should be achieved?

- is the recommendation convincing?
 - will it correct the root cause of the problem?
 - have alternatives been adequately considered?
 - is the recommendation feasible and cost-effective?
 - is it clear who should take the corrective action?
- 50.8.3 Recommendation should be given to enable the auditee to rectify the weaknesses reported. Auditor's recommendation should contain actions to be taken and results that should be achieved.
- 50.8.4 Whenever possible, positive audit observations should be reported to provide a fair and balanced report. This acknowledges the auditee's efforts and provides maximum leverage and value on the audit work done.
- 50.8.5 The Assistant Auditor General is responsible to ensure that all recommendations are well researched, practical and cost-effective. The recommendations should also be consistent with those made by the Office of the Auditor General in similar situations either in the past or elsewhere in government. If they are inconsistent, the reasons must be documented.
- 50.8.6 The Office of the Auditor General should promote continuous report writing, which involves developing the main components of the audit report at the planning stage and periodically revising the draft report throughout the conduct of the audit. This approach allows the auditor to concentrate on the results of the audit, determined at the planning stage; fine-tuning the audit report and promoting the report's credibility, thus moderating the potential for management to disagree with the report contents.

50.9 Reporting Activities

- 50.9.1 Throughout the course of the audit work, there may be a need for audit issue papers to identify and discuss major issues that have emerged. They serve to communicate audit findings and recommendations to management and integrate prompt feedback for preliminary issues. Form to write audit finding is given in Audit Tool-8.
- 50.9.2 This is carried out mainly to validate the accuracy and completeness of information included in the draft report. A draft copy of the report, incorporating the criteria, condition, cause and effect and consequences, conclusions and recommendations in the audit issue papers, should be reviewed by the Audit Director and the Assistant Auditor General before being presented to the appropriate level of management a few days prior to the exit conference. Management therefore is given the opportunity of studying the report prior to discussing it with the auditors.
- 50.9.3 Based on the exit conference, a preliminary audit report is prepared and reviewed by the Audit Director and the Assistant Auditor General. Finally, the Deputy Auditor General reviews, challenges, approves and signs off the report ensuring that the Office of the Auditor General standards are met.
- 50.9.4 The preliminary report should be forwarded to the Secretary and entities or projects of His Majesty's Government or to the Chairman of the Board of Directors for autonomous bodies. Copies of the report should also be forwarded to concerned departments and project manager or In-charge. It should be communicated to the responsible party that the

response should be received in writing within 35 days. In the event this is not the case, the issues will be incorporated into the annual report as it is, with mention that no response has been received. The response should address the issues raised in the audit report and include specific action plans with regards to implementing corrective action.

- 50.9.5 The auditor should review each response received to determine that timely corrective action and adequate detail have been provided for each finding of the report.
- 50.9.6 The management responses are incorporated into the final audit report which is issued to the auditee management for corrective actions after tabulation final report on parliament. The follow-up process on the OAG's findings and recommendations is detailed in Section 80.
- 50.9.7 The Audit Director shall review the audit files again to ensure that the evidence, working papers and other documents are sufficient to support the final report.
- 50.9.8 Once the management comments are analysed, the more important issues should be identified to be included in the annual report. The annual report should have clarity and focus on the subject matter. The names of persons and institutions involved in transactions should not be mentioned in the annual report. The AG reviews, challenges, approves and signs-off the report ensuring that the OAG standards are met.

Audit Tool - 8 (Audit Finding Form)

1. Matters of Potential Significance _____
2. Audit work paper reference _____
3. Discussion date _____
4. Criteria, condition, cause and consequence

5. Conclusion and Recommendation (include benefit)

6. Comment of auditee management (name, date and comments)_____

7. Explain cause if not included in preliminary report

Prepared & recommended by
Audit Officer

Reviewed by
Audit Director

Approved by
Assistant Auditor General

60 Documentation Section

60.1 Policies

The significant policies in respect of Audit Documentation are as follows:

- the Audit Director should ensure that audit files exist, contain appropriate and sufficient evidence, are complete and easily retrievable.
- all working papers are confidential documents belonging to the OAG. Audited organisations and the public have no right of access to the OAG's working papers.
- audit staff should not disclose information gathered during the audit to third parties.
- audit files support reports issued.

60.2 Objectives of Documentation

The objectives of Audit Documentation are to

- provide evidence to support the auditor's report
- aid in the auditors in planning, conducting and supervising the audit
- provide evidence of a quality conduct of the audit and the quality of the reported results

60.3 Contents of Audit Work Papers

Audit working papers should contain the following :

- basis and extent of planning
- the objective, scope and methodology, including any sampling criteria used
- documentation of work performed to support significant conclusions and judgements. These include audit programmes, schedules supporting information contained in the audit report, third party confirmation, reliance placed on the work of other auditors, other evidence contributing to auditors findings, etc.
- evidence of supervisory work performed
- draft reports
- details of discussion with management
- management responses
- copies of photographs that form part of the audit evidence

The ultimate test on audit working papers is to ensure whether they contain appropriate and sufficient evidences and are complete enough to withstand knowledgeable scrutiny.

60.4 Characteristics of Working Papers

Audit working papers should exhibit the following characteristics:

- completeness and accuracy - to show the nature and extent of audit work performed and to provide proper support for contents of the audit report
- clarity and conciseness without requiring supplementary oral support. The legend to tick marks or other symbols used to document performance of audit tests should be explained.
- ease of preparation
- legibility and neatness with adequate space for additional data, notes and comments
- relevance - should contain information that is important and useful with respect to the objectives established for the examination
- organisation - files should be systematically organised, indexed and cross referenced
- ease of review

60.5 Audit File Structure

60.5.1 Information gathered should be separated between two audit files, namely the current audit file and the permanent audit file.

60.5.2 The permanent audit file consists of information of a permanent nature. The information contained here will be useful when conducting financial audit of the same auditee or when conducting performance audit in a different area of the same auditee.

60.5.3 Some examples of main file documents are as follows:

- Policy
- Laws/Rules - legal framework
- Organisational Structure
- Details of closely related entity and programme.
- Project Memorandum/Appraisal
- Resource Management (Agreement of Loan/Grant)
- Project Documents
- Mid-term and other evaluation
- Target and Achievement
- Major Audit Findings of Previous years, which were incorporated into the Annual Report
- Decisions of Public Accounts Committee
- Cuttings of Matters of Public Concern Published in Magazines/Newspapers
- Other Relevant Documents and Statements (Useful for more than one Fiscal Year)

60.5.4 The structure and contents of the current audit file is illustrated in Audit Tool-9.

60.6 Completing and Reviewing Audit Files

60.6.1 The overall review process should be done by the Assistant Auditor General, to ensure that all conclusions made are consistent with each other, are relevant, logical, constructive and supportive.

Working papers should be prepared in sufficient detail to enable an experienced auditor with no previous connection with the audit to ascertain what work has been performed to support the findings and conclusions.

60.6.2 Review form is given in Audit Tool-10.

Audit Tool - 9 (Audit File Documentation)

Topic	Index
Overview Stage	A
Performance Audit Progress Record Firm (AT1)	A1
Basic Information	A2
Overview Report	A3
Sources of Overview Report	A4
Review of Internal Audit Report	A5
Other Working Papers	A6
Survey Stage	B
Information Collection (AT4)	B1
Process Analysis (AT5)	B2
Risk Assessment (AT6)	B3
Audit Planning	B4
Other Working Papers	B5
Audit Execution Stage	C to X
Segregate audit areas in accordance with Matters of Potential Significance and name each area with a different index (C....D....X) then Structure in the following manner : <ul style="list-style-type: none"> ● Audit programme (AT7) ● Working Paper 	
Reporting Stage	Y
Audit Findings (AT8)	Y1
Draft Report (Preliminary)	Y2
Preliminary Report	Y3
Management Response	Y4
Draft Report (Final)	Y5
Final Report	Y6
Other Documents	Y7
Review/Follow-up Stage	Z
<i>Audit Review Form (AT10)</i>	Z1
<i>Peer Review/PAQRS Form (AT11)</i>	Z2
<i>Follow-up Report (AT12)</i>	Z3
<i>Other Documents</i>	Z4

Audit Tool - 10 (Audit Review Form)

Audit Entity

Audit Year

S.No.	Subject Matter	Yes/No/NA	Comments
1.	Do the working papers contain sufficient evidence on the following: - Audit plan/ approach - Detailed audit programme - Evidence/ initial of staff performing work - Evidence/ initial of Supervisor/Director reviewing work - Documentation of findings, conclusions and recommendations.		
2.	Has management agreed to our pre-determined audit criteria? Have disagreements been resolved?		
3.	Have we identified and documented the controls which are: - effective - ineffective - excessive (from a cost/benefit perspective)		
4.	Have we identified and documented operational and other potential improvement opportunities by performing appropriate operational measurement activities?		
5.	Have we communicated all matters included in the Report and performance improvement opportunities to management?		
6.	Has management reviewed and commented on the Report and have disagreements with the audit findings and recommendations been analysed?		
7.	Have all critical judgements, including management's response on contentious findings been appropriately and comprehensively documented in the working papers?		
8.	Are the recommendations well researched, practical and cost-effective?		
9.	Are we satisfied that all elements of the Performance Audit have been satisfactorily completed in accordance with the legislative mandate and applicable auditing standards?		

Prepared and Recommended by
 Audit Director

Reviewed by
 Assistant Auditor General

70 "Peer Reviews/Post Audit Quality Review System (PAQRS) Section"

70.1 OAG Policy on Quality Control /Peer Review

The OAG policy provides that, to ensure the maintenance of the highest quality of auditing services to its clients, a system of quality control policies and procedures are established. It includes a review of general quality control considerations and review of selected individual performance audit engagements.

70.2 INTOSAI Pronouncement on Quality Control Review

70.2.1 The twelfth Congress of the INTOSAI (Sydney 1986) has recommended that the objective of quality assurance programmes of an audit institution is to satisfy its top management that:

- the audit work has been carried out to appropriate standards;
- the output has been presented in a satisfactory manner; and
- the work in general meets the legitimate needs and interests of the audited body and other users of output, including Parliamentary and supervisory authorities on the political level, the media and the public at large.

70.2.2 In addition, the Intosai Auditing Standards state that the Supreme Audit Institutions ("SAI") should establish systems and procedures to:

- confirm that integral quality assurance processes have operated satisfactorily;
- ensure the quality of audit report; and
- secure improvements and avoid repetition of weaknesses.

70.3 Objectives of Peer Reviews and Establishing a PAQRS

- evaluate quality of performance on engagements
- provide reasonable assurance that the work performed confirm to the generally accepted government auditing and accounting standards and the OAG's laid down policies and procedures
- provide reasonable assurance that adequate work has been performed to support the reports issued and that the underlying working papers provide sufficient evidence of this
- evaluate the performance of individual audit team or staff in relation to understanding and implementation of the OAG's policies and guidelines and to facilitate the process of educating the value of complying with such policies and guidelines
- corroborate the implementation and effectiveness of action plans for correcting deficiencies
- identify significant deficiencies in operations and quality assurance procedures

- provide constructive recommendation for improving the efficiency and effectiveness of the OAG's PAQRS and enhancing service and satisfaction to the audited entity.

70.4 Overview of Peer Review PAQRS

70.4.1 Across the globe, government and industrial and commercial enterprises are trying to embrace corporate governance- Good Business Practices- with transparency. As a result of corporate governance and good business practices- management expects that their auditors will also provide good quality and value added services and, therefore, contribute to corporate governance. This is achieved by conducting "Peer Reviews" or implementing the PAQRS, a concept which is being widely recognized as the tool to assess and improve the quality of audit service.

70.4.2 The OAG has the responsibility of providing high quality (reliable, relevant and sufficient) information to its auditee. For this, it needs to establish its own quality review system to ensure best product that meets the information needs of its audit entities and offers opinions and recommendations that are professionally sound and relevant. It involves evaluating the effectiveness of the systems and controls used during the audit process, to determine whether the audit work was conducted in a professional manner and reports were prepared and distributed in accordance with the OAG strategy and policy.

70.5 Basis of Peer Review/PAQRS

Peer Review programmes and the PAQRS are based on the following considerations on the part of the reviewer :

- *"Independence Integrity and Objectivity"* The Peer Review team should maintain independence, perform all responsibilities with integrity and maintain objectivity in performing the review. The review team needs to be impartial, it should recognise an obligation for fairness, and intellectual honesty and it should be free from any conflict of interest.
- *"Competence"* A Peer Review should only be carried out by a team possessing full knowledge of the Performance Auditing Guide, current government auditing and accounting standards, an understanding of the Office of the Auditor General's staff profile and the procedures related to its management and supervision.
- *"Due Professional Care"* Peer Reviews are sensitive and confidential in nature. The peer review team needs to take due professional care in carrying out the review.
- *"High Standards of Review Administration"* To gain the maximum outcome of the reviews, it should be carried out under certain specific administrative standards supervised by Quality Control Committee.

- 70.6 Conduct of the Review
- 70.6.1 As Office of the Auditor General is an independent constitutional body, no outside authority is authorised to supervise its work and monitor its performance. The in-house team of Office of the Auditor General shall carry out the peer review. The members of the team shall be drawn from different divisions of Office of the Auditor General.
- 70.6.2 The review shall cover the overall quality and technical standards and also selected audit engagements to ensure that specified professional standards are actually followed.
- 70.6.3 The Auditor General shall constitute a Quality Control Committee to develop and maintain policies and procedures. This committee will provide reasonable assurance so as to the quality of performance auditing services and that it is rendered in compliance with this Guide, government auditing and accounting standards and such further audit guidelines as are established by Office of the Auditor General from time to time.
- 70.6.4 The chairperson and the members of the committee shall be designated by the AG which may include Deputy Auditor General, selected Assistant Auditors General and Audit Directors. The committee shall have a maximum of five members.
- 70.6.5 Responsibility of Quality Control Committee shall include but not be limited to:
- select audit engagements to be reviewed
 - designate an individual or a team to be responsible for the review of general quality control policies and also the individual audit engagements
 - approve questionnaires/checklists prepared for the review and to prepare necessary instructions for conducting the review
 - supervise and monitor the review assignment
 - prepare summarized results for presentation to the AG and the follow-up suggestions for improvement which should include whether, in the opinion of the Committee :
 - the review programme met the review objectives and was carried out in a manner consistent with the OAG policies;
 - the review conducted have been appropriately documented;
 - the review report fairly reflects the review results; and
 - the indicated follow-up actions to be taken appear appropriate in the circumstances.
- 70.6.6 The report should also contain:
- details of timing of the review and the names of review team members
 - a description of the scope of the review (general approach, extent of coverage of the general quality control aspects and the description of individual audit engagement)

- 70.6.7 At least 10% of the Performance Audit engagement should be reviewed each year. However, not more than 10% of the relevant engagement hours should be spent on peer review work.
- 70.6.8 The sample of individual engagements selected must be sufficient to constitute a representative sample of all performance audit engagements conducted by the OAG, and should include:
- engagement of every Assistant Auditor General/Director and, to the extent practicable, every audit in-charge being reviewed at least once every 3 years;
 - large and complex engagements, as well as a sample of smaller engagements;
 - engagements in specialized sectors, e.g., public health, education, rural housing, must be covered.
 - new engagements; and
 - special studies/engagements e.g., clients where budgetary involvement is insignificant but is a matter of public concern should be covered.
- 70.6.9 Consideration should be given to biasing the sample towards the review of those audited entities which the Assistant Auditor General of Performance Audit Division regards as having critical significance.

70.7 Performing the Review

- 70.7.1 The review shall be conducted in the following steps:
- *"Planning"* The planning process involves the following :
 - A detailed planning for conducting the review in an organised manner is essential. A team with the right mix of people shall be formed and a team leader from amongst them chosen. The team should then plan for the review considering the nature of the review, inherent risk in the assignment, best practices available for the assignment, etc.
 - Every review team member should have questionnaires or checklists for use both in the review of general quality control policies and procedures and also in the review of individual audit engagements consistent with guidelines given in this Guide. Audit Tool -11 is referred to facilitated review team or member for developing questionnaire or checklist.
 - *"Reviewing"* The review of the specified engagements should be carried out in accordance with the detailed checklists prepared for the review. During the review process, the deficiencies in the quality control system and its compliance would be established.
- 70.7.2 The objectives of review at the level of individual audit would normally cover:
- Audit is a specialized work that is to be performed with certain standard practice. The PAQRS assesses the performance of audit considering general practices that focuses on integrity and diligence of auditor. Following considerations for it should be in place,

- possess the technical standards and professional competence required for fulfilling their responsibilities;
 - the audit personnel are directed in the appropriate manner. It is important for completing the engagement efficiently and effectively;
 - the work is adequately supervised which involves monitoring the progress of the assignment.
- Proper documentation of evidence is very important from the viewpoint of justifying audit findings. Auditor should gather sufficient, relevant and reliable evidence that supports audit findings and index them systematically. Reviewer is required to verify whether audit findings are based on evidence that is sufficient, relevant and reliable. Performance audit demands several evidences that support findings.
 - Audit plan is the major guiding force in performance auditing. Auditors are required to follow audit plan. The PAQRS focuses on adherence to the audit plan. Any deviation from audit plan has to be properly justified and approved by appropriate authority.
 - The office has introduced strategic and auditee level planning. Strategic plan outlines the issue areas of concern. Audit operation divisions are required to plan their work considering strategic focus of the SAI. The PAQRS also attempts to appraise the relation between auditee level and strategic planning.
 - Quality of report (presentation method, style and relevance) is always a matter of high concern to the Office of the Auditor General. The report should address the following issues :
 - Use of non-technical terms, conciseness, clarity of message, etc. Matters of non-compliance with laws, regulations and management policies should be clearly spelt out;
 - Facts and figures carefully verified with evidence;
 - Preliminary report generally issued within three weeks of completion of audit. Delays, if any, properly justified and approved by the AAG;
 - Audit findings are presented in a courteous manner. It should not reflect any kind of emotion and antagonizing expression.

70.8 Conclusion and Reporting

70.8.1 The primary objective of the review is to formulate recommendations which address the cause of any shortcoming in quality to ensure that appropriate corrective action is taken. The objective is achieved through the process of concluding the review. The findings of the review should be formally tabulated and communicated by way of a report.

70.8.2 The following factors should be considered in concluding the review :

- at the end of the review visit, the reviewers should prepare an overall summary report for the AAG responsible for the audit.

- the reviewer's report on individual engagement should be discussed with the relevant Audit Director and the summary report with the AAG - PAD prior to finalisation.
- upon completion of the review, every team should submit a report to the chairperson of the QCC. This report should be consistent with the format included in the Quality Control Audit Tool. This report contains :
 - the representation by the review team in-charge that the review was conducted with the OAG's policies as set forth in this guide
 - the more prevalent findings from the review, material queries raised and responses and related recommendations for follow-up consideration
- information about the scope and extent of the reviews, including but not limited to :
 - details of timing of the review and the names of review team members
 - a description of the scope of the review (general approach, extent of coverage of the general quality control aspects and the description of individual audit engagement)
 - time spent on engagement reviews and on the review of general quality control aspects
 - name and designations of reviewers involved including professional specialists from outside the SAI
- the reviewer may highlight other pertinent issues that may be of interest to all other Audit Divisions.

70.8.3 An overall grade should be given to the sections reviewed to summarise the conclusion of the review. The gradings used are either “Satisfactory” (1a) or “Satisfactory - but needs improvement (1b)” or “Unsatisfactory” (2). When grading individual components of the questionnaire these terms should be used in a common way. When it comes to the overall evaluation, the definition of “Satisfactory” is :

“This rating indicates that, although there may be some relatively trivial negative answers to the individual checklist questions, the reviewer believes that the work performed supports the audit report delivered to the auditee, the advice or the opinion given and the workpapers include all appropriate documentation with only trivial exceptions.”

The definition of “Satisfactory-but needs improvement” (equivalent to, say, a “weak pass”) is:

“This rating indicates that the work performed supports the audit report delivered to the auditee and the advice or the opinion given, but in the reviewer’s opinion, at the most a moderate number of improvements are needed to comply with relevant detailed (but not fundamental) aspects of the Performance Auditing Guide and/or local professional requirements.”

Where these gradings are not justified, the grading must be “Unsatisfactory”.

70.8.4 A Performance Audit Peer Review/PAQRS Form is provided in Audit Tool-11

Audit Tool - 11 (Performance Audit Peer Review/Post Audit Quality Review System “PAQRS” Form)

- General Information

<i>Name & Address of Audit Topic :</i>	
<i>Year of commencement :</i>	
<i>Project Location :</i>	
<i>Total cost of project :</i>	
<i>Expenditure till audited year :</i>	
<i>Overview report approved at :</i>	
<i>Audit Planning approved at :</i>	
<i>Audit Execution period :</i>	
<i>Audit Team :</i>	<i>Audit Director :</i> Audit Officer (s) : Auditor (s) :
<i>Meeting with Management, date, subject and involvement :</i>	
<i>Date of preliminary report issued :</i>	
<i>Date of response received from Management :</i>	

• **Overall Evaluation**

Reviewers Evaluation	Grading
<p>“This rating indicates that, although there may be some relatively trivial negative answers to the individual checklist questions, the reviewer believes that the work performed supports the product delivered to the auditee, the advice or the opinion given and the workpapers include all appropriate documentation with only trivial exceptions.”</p>	<p>Satisfactory</p>
<p>“This rating indicates that the work performed supports the product delivered to the client and the advice or the opinion given, but in the reviewer’s opinion, at the most a moderate number of improvements are needed to comply with relevant detailed (but not fundamental) aspects of the PAG” and/or local professional requirements</p>	<p>Satisfactory - but needs emprovement.</p>
<p>Where these gradings are not justified, the grading must be “Unsatisfactory”.</p>	<p>Unsatisfactory</p>

- Strengths & weaknesses

Strengths

**Reasons why components of the engagement have been graded
'unsatisfactory'**

**Reasons why components of the engagement have been graded 'satisfactory
- but needs improvement'**

- **Recommendations for Improvement (Items recommended to be referred to in Management Report)**

Reviewer Comment(s)	AAG's Comment(s)

- **Opinion and Direction**

Deputy Auditor General's Opinion
Direction of Auditor General

• Detailed Valuation Statement

S.No.	Title	Subject/Area of Review	Grading
1.	Selection Process	Was the initial decision made on whether performance audit is warranted subjected to a formal selection process in accordance with the PAG.	
2.	Scope of engagement	Was the scope of the engagement adequately defined and discussed with the auditee to ensure that what was essential was covered but unnecessary work was avoided?	
3.	Independence	If potential independence or conflict of interest issues were present, were they effectively dealt with (for example, a separate performance audit team is utilised)	
4.	Planning	Do the work papers document effective planning of the assignment? Consider: <ul style="list-style-type: none"> • understanding of the auditee's industry and operations, and the requirements of the engagement; • adequacy of the AAG / Audit Director involvement; • early identification and involvement of concurring reviewer AAG; • adequacy of specialist involvement; • instructions to other offices; • statutory and regulatory conditions; and • nature and extent of the work to be carried out. 	
5.	Performance audit planning	Have appropriate overview report and survey plans developed (as applicable) setting out the performance audit objectives, priorities, resources and timing and areas to be covered, and have these been approved by the AAG? Consider: <ul style="list-style-type: none"> • strategic analysis in understanding the auditee's operations, objectives and strategies; • operational process analysis in understanding the auditee's processes and factors that drive operations performance; • risk assessments in identifying the auditee's operational risks and evaluating the design and operating effectiveness of controls; and • use of appropriate agency, auditee and external industry and operational information to make informed assessments. 	
6.	Auditee's approval	Has there been adequate consultation with the	

		auditee to ensure that the planned strategy, key performance indicators and specific areas of work have been properly identified, prioritised and approved by the auditee?	
7.	Engagement personnel	Did the engagement personnel (as a team) have the experience and training necessary for this engagement?	
8.	Performance against work plan	Was the work that was planned actually implemented and documented and, if not, appropriate explanations given?	
9.	Auditee communication	Were communications with the auditee (oral and written) well documented and do they guard against misunderstanding (for example, making sure that there are notes of conversations, making use of draft stamps, supporting oral advice properly, etc)?	
10.	Changes in circumstances	Did the engagement team react to changes in circumstances as the work progressed and appropriately modified the strategic and annual plans, and were these approved by the AAG?	
11.	Scope of procedures	Were the audit criteria of each specific area of work identified?	
12.	MOPS	Were the MOPS identified appropriate, the audit objectives set as the MOPS and the audit scope appropriately?	
13.	Extent of procedures	Were the decisions on the extent of work and adequacy of checking procedures appropriate? Consider: <ul style="list-style-type: none"> • the MOPS identified; • extent of evidence gathering considered (for example, observation and enquiry, sample testing, etc); and • individual work programmes tailored and used. 	
14.	Oral communications	Were all meetings and interviews adequately recorded?	
15.	Representation	Where necessary, were appropriate representations obtained?	
16.	Documentation	Do the working papers indicate that the detailed procedures have been conducted in accordance with the agreed terms and documented approach and, where applicable, stated the OAG policies and procedures and that appropriate findings and recommendations have been reached?	
17.	Findings and recommendations	Were the findings and recommendations drawn from the fieldwork appropriately documented and supported by the work undertaken? Consider:	

		<ul style="list-style-type: none"> • procedures performed are appropriate given the nature of the auditee and scope of the engagement; • specific procedures requested by auditee properly performed; • appropriate checklists and aide memoirs used where available; • appropriate evidence obtained for the MOPS; • appropriate procedures undertaken to confirm that third parties (eg. other experts) are reputable and suitably qualified. 	
18.	Final report	Were the findings and recommendations drawn from the fieldwork appropriately incorporated in the final report? Are the reasons for not reporting any points adequately documented?	
19.	Final report- documentation	Is information in the final report traceable to supporting working papers?	
20.	Audit Director's supervision and review	Was the level and timing of Audit Director's supervision and review and the documentation thereof, appropriate?	
21.	Review queries	Were review queries and matters raised for attention during the engagement addressed, resolved, adequately documented and queries / review notes removed from the files?	
22.	AAG/Audit Director involvement	Do the time records and other documentation reflect adequate and timely involvement of the AAG/Audit Director? Is the level of the AAG and Audit Director involvement consistent with that indicated in the audit plan?	
23.	Review of fieldwork	Was the approach to, and depth of, the review of the field work by the AAG and Audit Director satisfactory?	
24.	Consultation	Has there been adequate and timely consultation with other AAGs and Audit Directors in relation to significant issues and were the results of such consultations adequately documented and considered?	
25.	Scope of work	Does the wording of the report clearly indicate the extent and scope of the work undertaken by the OAG/Nepal?	
26.	Source of data	Does the report clearly indicate the source of any financial data or information contained therein and the extent to which it can be relied upon given the extent and scope of work undertaken by the OAG/Nepal?	
27.	Findings and recommendations	Are the findings and recommendations expressed in the report appropriate given the extent and	

		scope of the OAG/N's work, especially where a limited investigation has been undertaken?	
28.	Reporting to parliament	Are reports issued to the Parliament highlighting all significant findings and recommendations?	
29.	Report issuance	Was the report issued on a timely basis, and issued in draft to the relevant auditee management for review and discussion in relation to factual content and to evaluate the findings and recommendations, and was this adequately documented?	
30.	Efficiency	<p>What is your overall evaluation of the efficiency with which this engagement was conducted?</p> <p>Consider:</p> <ul style="list-style-type: none"> • Planning <ul style="list-style-type: none"> • in accordance with the PAG; • the DAG and the AAG involved; • Audit Director involved; • risk focused; • performed early enough; and • involvement of specialists. • Staffing <ul style="list-style-type: none"> • engagement hours spread throughout the engagement; and • specialists involved where necessary. • Documentation <ul style="list-style-type: none"> • photocopies of needless information; • non-critical areas with minimal documentation; and • restricted to 'what we did', 'what we found' and 'what we recommended'. • Performance <ul style="list-style-type: none"> • reports drafted early in engagement and reporting issues resolved early; and • the AAG and Audit Officer reviews interactive. 	
31.	Scope of procedures	<p>Was the scope of procedures performed adequate?</p> <p>Consider:</p> <ul style="list-style-type: none"> • The scope of our procedures performed shall be adequate to support our findings and recommendations. • Matters that are integral to the conduct of the engagement shall be included in the working papers. 	
32.	Report	Was the report issued appropriate under the circumstances?	
33.	Overall Evaluation	In your opinion, was the overall quality of professional performance on this engagement adequate?	

		<p><u>Points to consider:</u> The evaluation ratings and criteria for the overall evaluation are as follows:</p> <p>1a - Satisfactory</p> <ul style="list-style-type: none"> • This rating indicates that although there may be some individual questions answered as "1b" or "2", the reviewer believes that the working papers support the report issued and include all appropriate documentation with only minor exceptions. <p>1b - Satisfactory - but Needs Improvement</p> <ul style="list-style-type: none"> • The reviewer can conclude, based on the working papers, and, to a limited extent, on supplementary explanations, that the work performed is adequate to support the report issued in all material aspects, but either or both of the following conditions apply: <ul style="list-style-type: none"> • Additional procedures should have been performed; or • Additional documentation needs to be added to the working papers with respect to procedures or other significant matters. <p>2 – Unsatisfactory</p> <ul style="list-style-type: none"> • One or more of the following three conditions exist: <ul style="list-style-type: none"> • the report is materially deficient, or the wrong report was issued; • significant procedures, which are required by firm policy have been omitted; and/or • the reviewer is unable to reach a conclusion as to the appropriateness of the report due to material inadequacies in the work and/or documentation of procedures or other significant matters. 	
--	--	--	--

80 "Follow-up Section"

80.1 Policies

The significant policies in respect of audit debriefing are as follows:

- the Office of the Auditor General should adopt proper, prompt and adequate follow-up programme on the implementation of its audit findings.
- a systematic review should be carried out by the Office of the Auditor General on the action taken by the management of an auditee on the recommendations/audit observations made by Office of the Auditor General or Public Accounts Committee ("PAC") of the Parliament;
- an assessment should be made by the Office of the Auditor General on the management action in correcting the problems that led to the recommendation or audit observation; and
- the OAG should report on results of follow-up reviews to the Parliament and/or management, as appropriate.

80.2 INTOSAI Pronouncement

The INTOSAI has not made any specific pronouncement on follow-up of audit findings and recommendations. However, the Lima declaration has made the following recommendations on "Environment of SAI findings":

- the audited organisations shall comment on the findings of the Supreme Audit Institution within a period of time established generally by law, or specifically by the Supreme Audit Institution, and shall indicate the measures taken as a result of the audit findings.
- to the extent the findings of the Supreme Audit Institution are not delivered as legally valid and enforceable judgment, the Supreme Audit Institution shall be empowered to approach the authority which is responsible for taking the necessary measures and require the accountable party to accept responsibility.

80.3 Needs and Objectives of Follow-up

80.3.1 Follow-up is an important and final stage of performance audit process, i.e. planning, execution, reporting and follow-up. It is the obligation of the OAG to carry out follow-up of the actions taken on the conclusions and recommendations of the audit.

80.3.2 The objectives of follow-up are :

- to report on the progress made by the auditee in taking corrective action against audit findings and observations.
- to discharge the OAG's public accountability to the Parliament which has the legitimate interest in reviewing the management actions taken or improvements made after the delivery of its judgment, directives and recommendations.
- to provide feedback for self-assessment of the opinion, conclusion and recommendation of the audit. (Such self-assessment support quality improvement)
- to remind the auditee to initiate corrective actions and demonstrate improvements.

80.4 Follow-up Process in the Office of the Auditor General

- 80.4.1 The OAG makes the follow-up on its findings and recommendations in two stages, i.e. one after the submission of preliminary report to the auditee and another after the deliberation of the PAC on final audit report.
- 80.4.2 The auditee is required to make a written response to the OAG on the findings and recommendations presented in its preliminary report within 35 days of its submission. The concerned AAG shall designate a competent officer to review the management response and also to examine the additional evidence, if any, produced in support of its response. The reviewers shall make a review note for the AAG who after being satisfied that the management has satisfactorily addressed the issue shall authorise to delete the audit findings and update audit working papers accordingly.
- 80.4.3 The PAC is parliamentary authority to review audit report submitted by the AG, hold discussions with the management of the auditee, examine all relevant facts and figures submitted subsequent to audit report and make deliberations on audit findings and recommend corrective actions. The OAG has the responsibility of reviewing the actions taken on the PAC's directives and recommendations and report progress to the Parliament.

80.5 Responsibility for Implementation of Recommendations

The auditee is responsible to make written response on the audit findings and recommendations to the PAC with a copy to the OAG. The deliberations and recommendations delivered by the PAC are legally valid and enforceable judgment on the management of the auditee.

80.6 Issues in Follow-up

The major problem regarding effective follow-up is the resources that are required for it to be truly authoritative. To determine whether management has, in fact, followed audit recommendations and instituted procedures that will overcome the weaknesses identified in the audit might, in some instances, require almost as much effort as did the original audit. As a result most audit organisations rely heavily on declarations from management, supplemented where possible by specific-checks undertaken during financial audits. In such situation, the auditor may select sample cases to provide judgment on the sufficiency of actions taken and improvements observed.

80.7 Reporting Format

Audit Tool-12 is provided for review, monitor and report follow-up actions :

Audit Tool - 12 (Annual Report, Response & Decision of the PAC)

Name of the Audit Entity :

Report year :

Audit Officer :

Audit Director :

Date of deliberation held in Public Account Committee :

Public Account Committee's report reference and date:

Ref. No.	Summary of Audit Observations	Audit Entity Response	Directions and recommendations of the PAC	Auditor's remark

Audit Officer

Audit Director