

THE CYCLIC STRUCTURE OF PERFORMANCE AUDITING IN PUBLIC SECTOR

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ABSTRACT

Contemporary public management models require significant changes of the involved tools and techniques. It has switched from the analysis and processing based on historical data to methods based on correlated projections and internationally recognized rules.

The performance audit need to be integrated in management mechanisms and should be developed flexible and adaptive, to provide operative information necessary to make decisions that leads to objectives achievement. The real performance can be achieved by combining the three E's (economy, efficiency and effectiveness), only if long-term performance is provided.

The goal of this paper is to highlight specific issues of the cyclic structure of performance audit implementation in public sector.

KEYWORDS: *methodology, performance audit, public sector.*

JEL CLASSIFICATION: *G28, H83.*

1. INTRODUCTION

The modern management, responsible for the designing, substantiation and implementing of timely and qualitative decisions, that will define future evolutions at all levels, has to exploit the stock of knowledge and past experience according to the contextual differences (Androniceanu, 2003).

If the managers of private organizations firstly take into account the profit, the purpose of public management is to meet the general good in terms of profitability and efficiency.

Thus, it is considered that the main objective of the audit (Loebbecke, 2006) implemented in the public system, is to increase degree of confidence in the legality and regularity of expenditure and revenue according to the economy, efficiency and effectiveness applied to all activities.

Performance auditing deals with two questions: Has correct measures been taken? This deals with the service provider and it considers whether strategic decisions have been adequately implemented. The auditor is interested in finding out whether the management has observed the norms and requirements of the strategy defined, or acts accordingly. Has it been done as required? This is about the effectiveness and impact of the activities conducted within the organization so as to achieve the objectives set by the society. Performance auditing may reveal that one of the chosen measurements is inefficient. When conducting a performance audit and provided public accountability is totally feasible, then, the auditor must be cautious and not exceed his/her responsibilities and objectives defined and apply assessment procedures to politics.

2. LITERATURE REVIEW

Substantiation and formulation of management decisions on the improvement of organization performances impose the need for knowing the implementation stage of previous decisions, but also the functionality and/or compliance of the affected processes.

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In this context, the audit should be seen as a management support tool that allows obtaining a true view of the organization, overall or on predefined structures and processes, using appropriate techniques.

According to the studies of O'Reilly (1990), the audit is defined as a systematic process of obtaining and evaluating objectively some assertions regarding actions and events economic and not only, to assessing the degree of compliance of these assertions with the auditor's predetermined criteria, and the communication of results to interested users.

The audit represents the professional examination of information in order to expressing a responsible and independent opinion about this information having regard to the reference to a quality criterion, for increasing the information utility (Collins, G. Valin, 1996).

The audit is also considered the professional examination of information in order to expressing a responsible and independent opinion by reference to a quality standard, to investigate the functionality and suitability of a process, project or company (CECCAR, 1999). The audit is everything that a manager should do to ensure that he has a better control over situations, if he has time and if he knows how to act (Renard, 2002).

What does the human resources audit and performance audit represent? How do organizations help and what kind of implications involves performing such an audit? What is the optimum moment of performing the human resources audit, so that to generate efficiency and effectiveness for the future activities of organizations?

Therefore, here are some of the questions that frequently occur in the international specialized literature that led to the appearance and development of this relatively new field: the human resources audit. As there is not a definition unanimous accepted and recognized in the specialized literature regarding the human resources audit, each of them having as background the author's conception, the culture and the personal criterion of approach, one will try to present several definitions given by experts in this field (Marin, 2009). The aim of the performance audit is to evaluate an audited entity's performance and management in terms of economy, efficiency and effectiveness and to provide recommendations on how to improve the performance of the said entity (Daujotait & Macerinskien, 2008).

3. SPECIFIC ISSUES OF ROMANIAN PUBLIC SECTOR PERFORMANCE AUDIT

A performance audit is an audit of sound financial management, namely of the economy, efficiency and effectiveness with which the Commission and/or other audited entities have used Community funds in carrying out their responsibilities (ECA, 2006).

With regard to audit standards elaborated by the International Organization of Supreme Audit Institutions (INTOSAI, 2004), **performance auditing** stands for economy, efficiency and effectiveness:

- a) Analysis of savings in conformity with sound management principles, practices and policies;
- b) Control of efficient use of human resources, be they financial or else as well as analysis of information systems and measurement of outcome control; analysis of the procedures used by control units only to overcome identified shortcomings;
- c) Control of outcome effectiveness in terms of objectives set by the control unit as well as examination of the impact on activity expected.

At present, there is no legal definition of performance auditing. The concept is actually conceived as the criteria to be met underlying any study or analysis.

In Romania, performance auditing is based on the three internationally acknowledged „E's”:

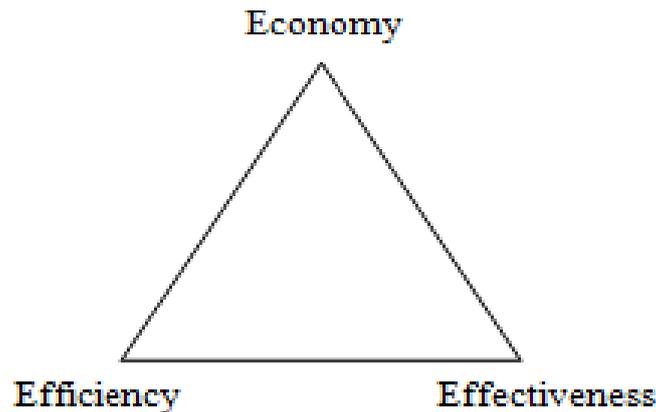


Figure 1. The three „E’s” of performance audit
Source: adapted from INTOSAI (2004)

- A. **ECONOMY** – low costs of resources used to achieve high quality of the respective activity. Economy is depicted as limit and condition, according to which, any organization from the public sector acquires material and human resources. Such an economic public organization acquires these resources in the adequate amount and quality at the lowest cost possible. In performance auditing, resources must be allocated, managed and used, economically, as cost-effectively as possible. The problem is whether the resources chosen are the most economical;
- B. **EFFICIENCY** – is defined in relation to the goods and services and the resources involved (Vasilescu, 2000). An efficient public organization will make the most of the goods and services based on the human and material resources available or will capitalize on the necessary inputs to achieve quality for the same amount of services and products. Thus, the management objective is to increase productivity while decreasing total costs. In the case of efficiency auditing, resources should be efficiently used. It presumes that the organization achieves the best outcome in terms of amount and quality. Efficiency auditing can be conducted by comparing similar activities carried out during different periods of time or by relating to specific standards. Provided complex problems and no standards available, assessments rely on the best practices already existent in the respective field of activity;
- C. **EFFECTIVENESS** – the extent to which a public organization achieves its objectives in relation to costs. Although the auditor may determine or measure effectiveness by comparing the results obtained with the objectives set, effectiveness auditing must indicate the extent to which the activities carried out have led to achieving the goals. When auditing an activity, organization or governmental program, the auditor must answer the following questions: have management objectives or the expected outcomes been achieved?; do the means involved and outcomes meet management policies and objectives?; the impact expected, is it the direct consequence of management policy?. Effectiveness assessments must ascertain whether management objectives have been achieved and whether the outcomes are due to management policies.

Does performance auditing focus only on the three E’s? Absolutely no, since the complex issue of the three E’s is largely based on the auditing objectives. Provided performance auditing aims at drawing some conclusions regarding economy and effectiveness, the auditor will also undertake an effectiveness assessment. In the case of effectiveness auditing, the auditor will also work on economy and efficiency. Thus, we can ascertain that performance measurement as compared to the objectives set, based on the three E’s, comes as a „must” for all managers at all hierarchical levels.

4. DISCUSSIONS ON THE DEVELOPMENT OF A PERFORMANCE AUDIT CYCLIC STRUCTURE

Real performance can be achieved by combining the three E's, only if long-term performance is provided. Performance assessment is based on the analysis of various indicators and these indicators are calculated according to some balances. Balances can be more or less clarifying, depending on the target in view and their type. There are three types of balances involved in the assessment process: balance sheet, economic balance, functional balance (Holder, 1998).

The aim of the performance auditing for central administration, governmental bodies and other public institutions is to provide information and recommendations regarding the way these organizational bodies require, use and justify public money, on one hand, and the ratio between money allocated and outcomes, on the other hand.

It is noteworthy that, up until now, there has been no intention of the Parliament, the only requests received by the supreme audit institution in Romania, the Court of Accounts, are concerned with legal spending of the public funds allocated to various institutions operating in this particular field of activity. Although the law stipulates efficiency control over the public funds, this particular type of control could not be conducted without an appropriate methodology. Once the law modified, clear and precise objectives have been defined regarding performance control.

Performance auditing assists the auditee in:

- ✓ building financial savings or reducing costs;
- ✓ backing-up and streamlining its management;
- ✓ providing better quality for services;
- ✓ achieving the objectives at a low cost.

In order to be in line with INTOSAI standards concerning the performance auditing process, a cyclic procedure will be implemented and, consequently, nine steps will be followed:

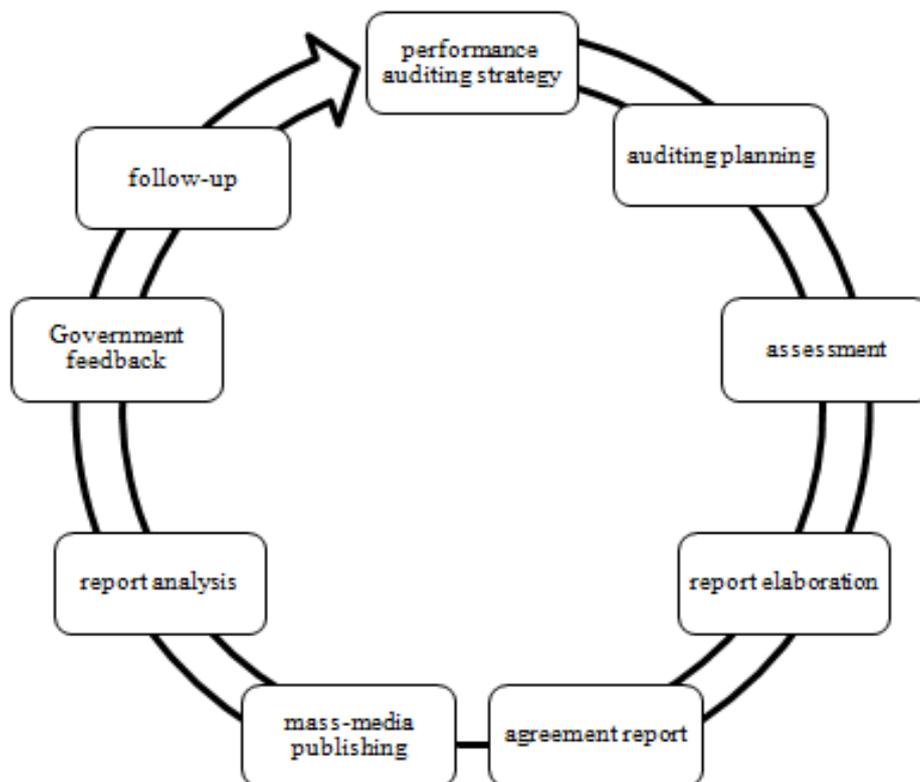


Figure 2. The cyclic structure of performance auditing

Source: adapted from INTOSAI (2004)

- 1) performance auditing strategy based on the decision making process;
- 2) auditing planning based on a thorough working program;
- 3) assessment (completion of the study) based on the auditing activity itself;
- 4) report elaboration by the auditor;
- 5) report hand-out to the auditee and agreement on findings and conclusions (acknowledgement);
- 6) publishing via mass-media;
- 7) report analysis and implementation by the auditor;
- 8) feedback from the Government regarding the recommendations mentioned in the report;
- 9) follow-up.

Concerning the Romanian economy, these steps are similarly defined, nevertheless, their content will be modified, since the Romanian manager's seriousness and sense of responsibility are not so conspicuous as with the German's. There are no managers or directors to hand in their resignation the moment the auditing report reveals bad results due to their lack of professionalism and poor management.

Strategy represents the first step of this cycle and presumes some decision making regarding the content of auditing.

This particular step is an internal assessment process of the auditing institution and it deals with areas likely to record frauds and shortcomes, management programs and initiatives in defining objectives and whether they have been achieved or not, and, finally, with those people likely to benefit from public money.

Data can be gathered from columns that identify shortcomes, from documents drafted by authorities or just from mere informal discussions.

Once the auditor has collected the information he considers necessary for the assessment, the second step of this cycle is auditing planning.

A preliminary report will be laid out to confirm the assessment of a particular activity or entity and the SAI executive board will be notified by the auditor or the auditing team about the main aspects to be addressed as well as the main possible risks, about the main methods to be used, anticipation of results, duration and necessary budget.

The key features of auditing planning are as follows:

- content and domain to be audited;
- methods to be used and necessary resources.

In fact, analysis of the content or domain to be audited is based on almost five components:

- a) in line with previous audits, the information and knowledge about the respective activity, current objectives and achievements will be consider;
- b) members of the auditing team will swap opinions concerning the most vulnerable domain, management systems and and flow of data;
- c) analysis of high risk aspects and activities, likely to pose problems, in need of solutions to achieve the defined objectives or closely related to the SAI mission;
- d) consideration of methods and techniques to be used and, if need be, a feasibility study will be conducted, performance criteria will be established so as to ensure the auditor that these criteria are relevant and fair;
- e) in case the auditing team members agree, one or more experts in the audited field will be called in in order to complete the preliminary report.

A decisive factor is the impact of the first discussions the auditing team had with the auditee, whether the management team is interested or not in the analysis proposed as well as their attitude toward sore issues.

The auditing study, to be convincing, must ensure probation of the methods and techniques to be least used by the auditor, still, and relevant data sample that will be included in the final assessment. The quality of data, performance indicators and financial information will be analized in terms of reliability necessary for the preliminary notifications. It might happen that access to company data

or events is denied since the management is reluctant to address sore issues and this requires auditor's diplomacy and determination.

Moreover, duration must also be taken into consideration and it ensures sample collection and analysis within a logical sequence of time, provided some time spent on holidays or financial reports, thus, for the auditing team this is wasted time.

Another prerequisite of performance auditing is the people involved: audit commissioner, the manager-auditee and the auditor. These people hold different functions, they are strongly committed to the auditing process, sometimes, though, they hold different views on the audit outcomes (Manole, 2010).

The audit commissioner represents the person delegated by the law to define the auditing objectives. This person is the first likely to make sure the subordinate organization is functional, competitive and efficient.

The manager-auditee is the leader or the management team whose executive activity and performance will be audited. Often, the audited manager is prone to present positive results only and disagree with all shortcomes and negative aspects of his/her activity. Thus, wider control and assessment of public organizations become a „must”, focusing on manager's activity, working system and outcomes. The auditor is the expert, the specialist, the multidisciplinary team has the necessary knowledge to assess management performance.

5. CONCLUSIONS

The management capabilities significantly increase the effectiveness of the auditing process (Ma, 2011). Managerial responsibility and the responsibility of ensuring a good management of budgetary funds involves the adoption of modern management principles, the implementation of control systems based on risk assessment, the development of clear and comprehensive rules and procedures for activities and the practice of an effective audit function. The harmonization of public institutions structures with the requirements of modern society, characterized by performance, efficiency and effectiveness contributes to the accomplishment of the public system main objective, that of to satisfy peoples requirements at the highest possible level in conditions of available resources.

The main objective of performance auditing, that is to add value and credibility to the assessment as conveyed by the audit reports, is achieved provided total freedom of auditing and observation of the following principles:

- clear objective of performance auditing;
- freedom of choice of domains to be audited;
- ex-post audit;
- fair assurance.

In addition to all this, there are specific principles that guide auditors' activity: accountability, integrity, added value as the aftermath of implementing the recommendations made by the auditing team, competence, thoroughness, determination, clear communication.

In order to successfully assess the performance of an organization in the public sector, both auditors and people in charge of training, evaluating and employing auditors will acquire and develop an additional set of skills. For an example, they will have to be capable of forming an overall impression of the organization. In this case, they are required a minimum level of management knowledge and know-how. Otherwise, it would be difficult to prove an auditor's competence to assess the general performance of the organization.

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