



Auditing Activities in Public Enterprises

- An Empirical Approach

By Chaya Withanawasam

In the present era where fiscal and monetary discipline is essential for rapid economic development, auditing has become one of the main controlling mechanisms that can be used effectively in ensuring the fulfillment of objectives of the country. Therefore, the auditing activities and its reporting system plus the action taken to overcome such identified observations have to play a vital role in achieving the well known social and economic responsibility of any entity. Thus, it is necessary to have effectual auditing and reporting system, well established legal frame work and institutional set up to control the possibility of malpractices and to evaluate the achievement of objectives of any entity.

As the Code of Best Practice issued by the Department of Public Enterprises highlighted, there is a linkage between the activities of the Public Enterprises (PEs) and the economic stability which they put into words as “Corporate Governance in Public Enterprises is more urgent and more

challenging than privately owned firms. It is more urgent because Public Enterprises in Sri Lanka are often engaged in the provision of goods and services in strategic sectors of the national economy, which affect directly and indirectly the interest of a very large number of firms and households. Moreover, their performance has a direct impact on public finances and macroeconomic stability.”

In Sri Lankan context, it is noted that the auditing and its reporting system and the after checks of noted observations in the reports are most of the time limited to compliance audit and initial reporting only. Thereby adequate emphasis has not paid to check the performance side of auditing and effective reporting and after checks system. Accordingly, it has become essential to change the present system of auditing and its reporting system and introduce latest mechanisms after doing a thorough study taking countries who are practicing latest mechanisms as examples.

These weaknesses in the auditing practice of public enterprises is due to main reasons including, the major difficulty in striking the right balance between accountability and autonomy is that PEs are expected to achieve multiple, conflicting and vague objectives;

PEs are attempting to achieve economic goals in the market and to cope with all sorts of political pressures and demand to which it is exposed.

It is further noted that the political pressure made on PEs is a common practice through out the world and it should be borne in mind that the shortcomings in these auditing practice in the PEs as well as the political influence to those entities by the influential parties cannot be fully ruled out other than controlling them.

This has been nicely described by Mr Narayanaswamy of India as, "When concerning over declining auditing standards and the need for major reforms in auditing are voiced the response is predictable. Auditors, as part of the society, cannot be expected to swim against the tide of declining values, when politicians, bureaucrats, corporate executives and even religious leaders are no exceptions. Some of those mentioned above are behind bars. Clearly that is not something of the members of the learned accounting profession would want to emulate."

Recent assessment done by the World Bank about our country's situation as a report name Country Financial Accountability Assessment (CFAA) has highlighted the most of the crucial weaknesses in the PEs' audit and its reporting system.

It stated that the Parliamentary procedures adopted with regard to PEs auditing activities, in particular, the standing orders relating to Committee of Public Enterprises (COPE), are outdated, not in line with international best practices, and need reform. It is further noted, the issue of transparency of the COPE proceedings and the capacity to hold effective Committee deliberations as limited in practice.

As the final outcome after having these discussions about the performance and other aspects of PEs is that these conclusions arrived from these deliberations need to be far more effective and practical in all means. However, in most of the instances well established committee proceedings have ended up with less effective remedial action when considering the past practice of the Sri Lankan history. This is not the case with regard to practice considering the countries like United Kingdom and Australia, because the committee proceedings and set up of the follow-up activities and the openness of the traditional practice have paved the way to have

more durable and reliable and effective measures to the discussed matters.

The three paragraphs extracted from CFAA report shows the importance of having transparent and more effective COPE discussions.

-The issue of transparency of the COPE proceedings and the capacity to hold effective committee deliberations are fundamental for improving public financial accountability. Apart from the developed countries in the commonwealth, Pakistan, Nepal and some states in India has taken action to make their committee hearings transparent. However, because of the provisions in section 130 A of the Standing Orders and Section 17 of the Parliamentary Powers and Privileges Act, neither the public nor the media are allowed to witness the proceedings of COPE in Sri Lanka. The earlier practice of printing the minutes of evidence of the proceedings was abandoned over a decade ago. As a result, currently, the public has no access to the examinations of COPE, and remains largely ignorant of these deliberations.

-Lack of transparency and the absence of an audience lessens the incentives for the members to be presented at the COPE and COPA meetings. In fact, there are numerous instances where scheduled committee meetings had to be cancelled because of lack of quorum. This also adds to the backlog of audit reports to be reviewed by the committees. Consequently, there is a tendency to bunch reviews.

-Further, when proceedings are held in camera, there is an impact on the quality of debate and discussions. In the absence of an audience and public pressure, there may not be any motivation for the committee members to be adequately prepared to engage in qualitative performance issue of government expenditure. The media and the public will continue to remain ignorant of how Parliament extracts accountability for the use of public funds, and thus, unable to exert any pressure on the members to voice their concerns in Parliament.

When the COPE examines the operations and financial aspects of the PEs, it should be a well constructive one without having any party politics and also any personnel issues into the discussion. Current practice is to examine the entities after going through the note prepared by the Auditor General and the Department of Public Enterprises. Those notes are not received in advance and even if they are received in advance, they do not go through it until the last moment other than few exceptional cases. System needs to be changed to adopt the practice of analyzing the activities in advance with or without the help of the AGD and DPE staff. This will enable them



to have more meaningful and productive committee deliberations which will finally act as a catalyst to boost the operational efficiency and management effectiveness of the PEs. Another impediment is the knowledge of the members who are analysing and suggesting solutions to the troubles and wrong act of the PEs. Most of the time they are not having broader knowledge and experience to suggest a better and a viable solution to problems encountered. Therefore if it's possible to appoint some of the outside expertise people with sound knowledge who will be able to give practical and realistic solutions that would act as a plus point in these discussions. The latest practice of having Consultative to the COPE appointed under the Government Accountability Strengthening Programme can be treated as a new improvement to this process.

And also there is an inherited problem of rejecting most of the auditors' suggestion by the

a outdated mode. Therefore attention needs to pay in this regard as there are a handful of Accounting and Auditing related Institutions currently practicing in the country; we preserve to have more comprehensive as well as more beneficial manual to be used in the auditing activities.

For example in USA, Government Accounting Office moved into comprehensive auditing, it developed detailed guidance for its employees. It first issued a Comprehensive Audit Manual (CAM) in 1952. The manual included chapters on audit authority and responsibility; audit objectives and policies; how to perform a comprehensive audit; auditing standards; the nature of management control; and descriptions of different activities subject to audits such as procurement, property, travel, printing. GAO updated the; CAM a number of times after 1952.

Another serious concern is with regard to the

The issue of transparency of the COPE proceedings and the capacity to hold effective committee deliberations are fundamental for improving public financial accountability.

auditee institution in PEs. This is due to the fact that the negative attitudes towards the auditors finding. Especially in the PEs, when the audit is carried out by the government base audit institution, those public enterprises which are more viable to private sector practice tend to look at the auditors' suggestion with a negative way. This needs to be changed as most of the time audit is carried out based upon well accepted practice among the international audit institutions. However, auditors are also backed by a responsibility of updating their knowledge and practice with the ever changing international new pronouncements.

From the inception of these COPE discussions it is evident that the time allocated to discuss the matters pertaining to PEs are not sufficient and which in cause directly impact when controlling the PEs towards the socio economic development. As observed in the Sri Lankan context, in United States also, the problem of not having sufficient time allocated to read the reports submitted by the Government Accounting Office came into the central discussion point.

Yet another innovation needed is to have an updated manual that can be used by the auditors when they are carrying out auditing activities of the PEs. Earlier the Auditor General's Department produced a set of manual that can be used a guide and due updating had not taken place and to date these manuals are in

companies owned by the government which do not come under the scrutiny of the COPE. The Committee also noted that the subsidiary companies with 51 percent or more of Government shares and Companies incorporated under the Public Companies Act of No 23 of 1987 do not come with in the preview of the Committee; in other words, such companies are not subject to review by the Committee. This, in fact, meant that a large number of institutions in public enterprise sector do not come within the preview of the Committee, resulting in a situation where, Parliamentary scrutiny not extended to such institutions. It was recognised as a major deficiency in the whole area of Parliamentary Accountability.

So what is needed is to do the necessary changes in the present Companies Act or to the Finance Act which will enable to get the controlling power of these government owned entities. In India what they did to rectify this problem is to grant Indian Comptroller & Auditor General to conduct supplementary audit. And some researches argue that the purpose will not serve by the government owed companies if they also come under the scrutiny of the government auditing process. Because the main objective of having these companies is to gain profit by providing the same level field as their peers in the private sector. Thus, some

kind of effective mechanism is needed to take control of these government owned entities.

Most of the time the matters pertaining to the public enterprises that are going to discuss in the COPE has not made available to the Board of Directors or the Director General of such enterprises to get ready in advance. Some of the matters they came to know at the time of the meeting thereby sufficient time not made available to them to explain their remedial action or the present procedure adopted to rectify it. Especially the 14 (2)(c) report, which is the published report prepared as per the Finance Act need to be addressed by the top management of the public enterprises before going to COPE discussions, which will enable them to explain in detail the correct position. This will give a confidential level to the members of the COPE with regard to the efficiency and effectiveness of the Board of Directors and the top management of those entities. Thereby if the entity has not taken a meaningful and corrective action with Auditor General's observations, this will push the COPE members to take the next course of action and guide the management to rectify those observations with correct remedial actions.

While we have given more weight to the financial aspects in our reporting, it is worthwhile to give due regard to the VFM audit or Performance audit techniques. It is observed that the selected countries also having the practice of reporting financial and performance sides separately to the Parliament and interested parties. This has not been developed in our country and this can be treated as a most essential need in the present day auditing in the PEs. Mainly the 3 Es can be effectively checked using these new techniques.

In Britain, United States, India and Australia, the Performance audit reports are separately discussed and they are reported separately which will enable to give the correct picture with the oral and written evidences from the suspicious parties. And the follow up of the weaknesses identified will be very easy to tackle. Since the World bank is concerning with the development management, its recommendations of introducing VFM and Performance audit to the auditing practice need to give high priority.

Follow-up Reviews on Performance Audits is essential and some of the crucial recommendations are pointed down below.

- Annual work plan should includes follow up reviews designed to establish progress made in implementing recommendations raised in previous performance audits.

The performance audit policy manual includes a section about the requirements for following up on

audit reports.

There should be a scheduled programmes for specific follow up reviews to be undertaken in a given year.

At audit committee meeting attention should need to pay attention with regard to performance audit follow up activities.

As a way to improve present auditing practice through enhancing performance of good governance can be treated as a best method due to fact that it has a direct impact when public enterprises are concerned. Also the measures stated there is a positive relationship with the good governance and accountability on the PEs.

Another similar area in the auditing of PEs is the Good Governance and New Public Management Techniques. The main address made with regard to the good governance is the book produce by the Department of public Enterprises as the Hand Book on Good Governance and Accountability. This is made an immense help when carrying out the auditing and governance activities of the PEs. However, parallel to this, what is required is to amend the other circulars and rules used in the auditing to give a better and realistic picture of the entities. Presently most of the circular and rules used in auditing have not updated which cause unnecessary hassle to the auditing activities and its acceptability.

However, all these factors are depending upon the political will and its great desire paid to improve the accountability process. And there again the effective use of Parliamentary institutions depends on the quality of the member of the parliament. If the members are not with sound theoretical and professional knowledge the tendency of making the correct decision and evaluation will become very nominal. In addition the time available to discuss the matters in detail is for everybody's concern. Sometimes they tend to discuss more than 12 entities per date.

Yet another important function was to examine whether the affairs of the Public Undertakings are being managed in accordance with sound business principles and prudent commercial practices. To implement that we need to have a good data base of the updated practices of the private sector enterprises with the same field and background. The Auditor General stating that the traditional techniques could not be applied, emphasised the need for 'analytical auditing techniques based on transaction analysis, audit questionnaires and financial analysis of the information presented by the PEs.' This demonstrated the fact that the nature of the commercial Activity of the PEs demanded auditing techniques which



are different from those applied to Government Departments.

In addition auditors can use some of the features of the prevailing system like having internal audit department, corporate plan activities, audit committee meetings, control mechanisms used by Board of Directors to have a more effective control of the public money while ensuring the transparency and accountability in the public enterprises.

As mentioned above the strengthening of the internal audit activities and internal audit committee meetings are very essential as best controlling mechanisms available within those entities. Most of the time internal audit has become a place without any say and act very reluctantly and in an inefficient manner because of the undue influence made by the employees and the management in their own entity. In some cases they have not given access to the information they need to peruse and occasionally have threatened the people who work in the internal audit department.

The enactment of the Fiscal Management (Responsibility) Act No 03 of 2003 of Sri Lanka is a

unique piece of legislation which, indirectly attempts to restrict the power of elected legislature and also act as a special tool in auditing of PEs. In addition to this special Act new pronouncements are needed in the areas such as environmental and gender issues, questions of macro economic policy, scrutiny of the economic and monetary policies and provision of information technology facilities for the introduction of computer auditing.

Overall, it is prudent to have a controlling body which need to have power to check the performance carried out by the Auditor General's Department as the sole body who take care of the auditing activities other than the reporting controls carried out by the Department of Public Enterprises, Sri Lanka Accounting and Auditing Standards Monitoring Board and the ruling of the Finance Act No 38 of 1971.

It is quite evident after perusing the related details of the auditing practices in the public enterprises that lots of loopholes and weak areas are available and getting them corrected to ensure the accountability and the transparency is the biggest challenge to the controlling authorities.

The author is a fellow of the Institute of Chartered Accountants of Sri Lanka and holds a BCom (SP) from the University of Colombo and a MBA from Deakin University, Australia. Presently a Superintendent of Audit at the Auditor General's Department, Sri Lanka.

Gross Official Reserves increasing substantially in 2008

During the first few weeks of 2008, the Gross Official Reserves continued to improve and stood at US \$ 3,434 mn by 6 March 2008. Accordingly, BOP has recorded a surplus of US \$ 366 mn by that date. As per the projected level of imports for 2008, the Official Reserves were adequate to cover approximately 3.6 months of imports. The Gross Official Reserves and Balance of Payment (BOP) surplus by end 2007 were

reported to be US \$ 3,063 mn and US \$ 531 mn, respectively. The Gross Official Reserve position has increased substantially so far this year due to steady inflows of export proceeds and worker remittances, a part of which has been absorbed by the Central Bank. Therefore, the recent build-up of reserves and BOP surplus indicate improved stability and resilience of the external sector in 2008, which is reflected in the appreciation of the Sri Lankan Rupee.

Courtesy: Central Bank of Sri Lanka