# PERFORMANCE AUDIT;
## Main Tool Of Measuring Efficeincy And Ensuring Accountability

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Performance Audit is assessment of overall performance of development projects and programs; an instrument to sharpen the process of accountability. In 1977 the Lima Conference of the International Organization of Supreme Audit Institutions (INTOSAI) office recognized the importance of this type of auditing. Many countries amended their Audit Acts / Rules and scope of audit was expanded to efficiency or value of money audit (Muhammad Jamil Bhatti, 2002).In traditional auditing, only financial data is used to give an opinion on financial position of an entity or project, while in performance auditing non-financial data is also taken into consideration.

That governments should apply themselves to continuously improving their performance, particularly with respect to the management of public funds and the stewardship of public assets, appears now to be a generally accepted principle of good governance. Instead of focusing on transaction, it assesses the whole project or organization (Geoffrey B. Sprinkle, 2000). Main focus of audit in performance audit is achievement of target. Even if no irregularity has been made, but the target is not achieved that entity / manager is taken to task. Economy, efficiency, effectiveness and environmental effects are assessed and accordingly general recommendations are made (Rashid Ahmed Saleh, June 2002). It is defined as "is an assessment of the activities of an organization to see if the resources are being managed with due regard for economy, efficiency and effectiveness and accountability". Right time to acquire a resource is also linked to the need to be fulfilled. The resource should be available to satisfy the need when it is required. It should neither make other resources 'wait' nor should wait for other resources. Therefore, the auditor reviews procedures to foresee demand, procurement and availability of resources.

Right place for a resource is the one where it is needed. The resources may be available where they are not needed. For example, there may be jobs which are unmanned and there may be men who do not have work. The auditor reviews the system for signaling the resource gaps. Right Cost


refers to lowest cost in the life-cycle of a resource.

Main objective of performance audit are as below:

1. To inform stake holders that how their employees / public servants obtained value for money spent out of firm's account or public exchequer and how they ensured any recovery.
2. To improve governance and encouraging better management practices in the organization, based on self-assessment.
3. Helping managers in making sound judgments.

Performance audit can be thought of as a set of systematic efforts, initiatives and processes that have a number of characteristics. It identifies performance in terms of results (outputs, outcomes, effects, impacts, etc.). It is assumed that levels of intended achievement (performance targets, service standards, etc.) are measurable. Traditional audit was checking of books but in performance audit, audit and performance are linked (Chistopher Politt & Hilka Summa, 1997).

**Approach of Auditors;** In performance audit main concern is value for money and hence an auditor interviews the executive officers, visits the field and physically verifies the facts.

Its scope is not limited to examination of financial statements, waste, extravagance, inefficiency or infectiveness, it goes beyond that and analyses causes of non-performance as well. Following are main features of performance audit;

- It is not only audit for managers but also an aid to management.
- Constraints of management or natural reasons are taken into consideration and recommendations are made on the basis of real life situation.
- Findings are quantified in terms of cash, rupee or dollar, as the case may be.
- Policies and procedures are assessed and stress is put on objectivity, with no preconceived conclusions.
- Findings and conclusions are made on verifiable facts and cooperative relationship with management (Liaqat Ali Chaudhery, 2004).


## Process of Performance Audit

Performance audit is carried out in following main stages.

1. Planning: At this stage auditors prepares for audit, studies the entity, its mandate, organization, budget, main programs, applicable laws and regulations and basic procedures of the organization. Issues of potential significance are identified to economize on cost of audit. Adequacy or inadequacy of the data lays down the audit criteria and identifies issues of potential significance. Sometimes, disagreements develop with the management regarding the appropriateness of the audit criteria. In such a situation the matter is resolved either by referring to a higher authority or by allowing the auditor to go ahead independently or simply by abandoning the effectiveness audit restricting its scope to economy and efficiency aspects only
2. Execution: The auditor examines all documents, visits fields, meets management employees and collects data. The data is analyzed in the light of rules regulations and goals. Objective, mission statement and purpose of the project / entity is examined and it is assessed that whether the goal has been obtained or otherwise or partially. Here comes the idea of value for money whether value has been obtained or not. Cost / value benefit analysis is carried various test and formulas are used

and results are obtained. At the execution stage the auditor reviews the adequacy of the management's system of effectiveness measurement. If no such system exists then the auditor develops a system of his own.

3. Reporting: Findings are tabulated, verified through statistical formulas and report preparation is started. The text of audit report gives facts, findings and recommendations. The facts relate to the background, financing, executions and operations of the program / project. The findings discuss the extent to which objectives have been achievement and at what cost, major achievements and constraints are highlighted. Recommendations part of the report gives general direction for actions. It qualifies expected savings or other benefits (Muhammad Akram Khan, 1988).

## Tools of Performance Audit

It is an ongoing monitoring and reporting of programme accomplishments, particularly progress towards pre-established goals. (US General Accounting Office, 1998). It is gives information on what management does and reports based on what programmes are achieving for citizens and at what cost. This implies agreeing on expected outcomes, measuring progress toward them and using that information to improve performance and report results (English and Linquist, 1998).

Performance audit is using performance information effectively and assessing the requisite or expected outcomes, in the light of expectations (KPMG, 1998). In performance audit all those tools are used which are commonly availed by management, for decisions making in organization.These include followings:

1. Audit command language (ACL)
2. Net present value (NPV)
3. Internal rate of return (IRR)
4. Average , Ranges, Regression analysis
5. Benefit / Cost Ratio (B/C Ratio)
6. Sensitivity test Ranking etc.

The list is exhaustive and auditor may use any tool based on his expertise and nature of the project organization. He may also use Bar chat, column chart, line graph or pie chart to show the results, both actual and expected variations may be highlighted through statistical tools. The audit report should be based on 5 C's i.e criteria, condition, cause, conclusion and corrective action (Liaqat Ali Chaudhery, 2004). Criterion explains as how the auditee action has been measured or what criterion has been involved by the management. Condition will clearly state in the findings as to what was the actual condition observed by auditor and how it differed from laid down procedure. The audit findings should identify causes for the gap between the criterion and condition. Conclusion should be based on taking into account both financial and non-financial factors. If corrective action by management has been taken then that may be identified or otherwise auditor may suggest corrective action to rectify the situation if possible.

Most notable progress in adoption of performance audit is the development of non-•'denancial audit approaches by auditors. Non-financial performance (NPI) indications are those performance indicators that are not part of organizations accounting data. NPIs are needed as financial information does not and cannot cover all aspects that influence an organization's performance (Fizza Pervez Afzal, 2004). The reinforcement, by the accounting and audit community, of the need for regular, i.e. annual, accountability reporting with a focus on results achieved, related costs, performance indicators, etc., is consistent with the performance management paradigm. It has driven the development of internal control and internal audit functions in government with an emphasis on management control frameworks, results-based budgeting, performance reporting, etc. (Christopher Pollitt and Hilka Summe, 1997). A good indication of the extent to which performance audit, and the use of performance indicators and performance measures, is increasingly rooted in the administration of governments, is the evolving role of the external/legislative auditor (Michael Barzelay, 1997). For example, Western Australia, New Zealand, Sweden, the US, England and Wales now carry out audits of performance indicators and issue opinions instead of stress on regulatory audit (Christopher Pollitt, January 2003).

**Pitfalls in Performance Audit**

Performance audit is a very good instrument of accountability and is helpful in bringing transparency and efficiency, but there are still problems, of which we must take cognizance. Inadequate indicators that do not measure what they are intended to, i.e. what evaluators would call 'poor construct validity'. This situation often arises when a performance assessment process is implemented hurriedly, under pressure, and indicators are chosen in haste or without sufficient consideration. This 'classic' pitfall is due typically to a lack of appropriate knowledge and know-how; as well, the link between activities and outcomes is usually taken for granted by those who carry out the programme and is treated as something 'obvious'. Use of performance information to ends for which it was not intended. Another important risk is goal displacement. This phenomenon occurs when performance auditor creates incentives to the detriment of the programme's relevance; and performance indicators targets overtake the programme's raison d'etre. It may fail to achieve the desired results if insufficient attention is given to the implementation process; the measurement approach reduces dynamic and complex multi-dimensional programmes to simplistic formulae and/or mechanistic linear processes; the focus of the assessment effort is on cosmetics rather than fundamentals; and, likely the surest way of producing goal displacement, there is failure to involve stakeholders and obtain buy-in. The problems associated with goal displacement can be exacerbated by what could best be called 'perverse incentives'. For example, raising the stakes associated with management increases the likelihood that people will 'work •'derst to the indicators' and produce by whatever means the required performance information (Ian C. Davies 1999). Low-probability programme technologies, i.e. 'soft' programmes such as social interventions, are particularly vulnerable to lack of attention to what is really important because it is difficult to measure. What is measured, or even measurable, often bears little resemblance to what is relevant (Perrin, 1999). Auditors are in a position to, and should, draw more on the practice's wide span of knowledge, know-how and resources to address competently both the methodological and political aspects and evaluative enterprise, especially in the context of performance management initiatives (Ian C. Davies, 1999). Auditor should make a point of telling people at the outset of any audit that he conducts that he follows two simple principles of fairness: that manager is accountable only for those things over which he has control, and he is not expected to do the impossible. Communicating these principles serves as a constructive starting point for collaborative enterprise (Pollitt, Christopher, et al, 1999). Discussing and agreeing to some rules of the game is equally important, for example: making sure there is prior agreement on the interpretation of measures and the uses of performance information; instituting a mechanism to assess the performance management initiative or process itself generating the active involvement and participation of stakeholders and ensuring transparency of process. A •'denal lesson learned is that independent input can be extremely helpful for developing an appropriate and credible performance management approach (Ian C. Davies, 1999).

Auditor independence is the most important quality for performance auditors, as it will affect the results. In performance audit, auditors should not be responsible to develop the organization's operation or correct the defects found during the audit process. Auditors are only responsible for monitoring the feedback that should be implemented by the organization (Arens, et al, 2005). Auditors have an authority to implement the feedback or correct the defects; it will create bias and reduce auditor's independence and the quality of the feedback, particularly if the auditors will perform audits again in the next period.

Sometimes performance audit may decrease the performance of a public organization. This unintended consequence appears where the expectation of performance is too high or too low (Theil and Leeuw, 2002). Development of the indicator is the most risky process in performance audit. Overvaluing or misinterpreting the performance will bring a negative feedback for the organization.

The shareholders in a private entity include those who have shares in the organization, while the stakeholders in a public organization have a wider definition as voters, tax-payers, society, parliament, and other interest groups. This shows that performance audit has more challenges in public organization than in private entities (Arens, et al,2005). In private sector, accountability is relatively limited to the management or organization and to the clients or customers. Accountability in private sector is also relatively easy to define because the value of goods in private sector is better measured. On the other hand, in accountability in public sector is more complex, because it involves multiple stakeholders (Bovens, 2005).

This shows that performance audit in public sector is more complex and broader. Public sector organization also often deals with cross cutting issues policy (Geoffrey B. Sprinkle, 2000). "Performance measures can be used to evaluate, control, budget, motivate, promote, celebrate, learn, and improve the organization's performance" (Behn, 2003). Performance audit is a comprehensive audit that audit and all aspect in organization, such as economy, efficiency and effectiveness (INTOSAI's Auditing Standards, 2004). In terms of scope, performance audit may cover all aspect in organization, but in terms of implementation, performance measurement may advance in action and timing. New Public Management (NPM) involves the transfer of knowledge and principal from private to public sector, which has proved to be more efficient; so that a corporatized public service can also be audited or measured with the similar tool applied in the private sector (Michael Barzelay, July 1997).

**Case Study:**

Government of Khyber Pakhtunkhwa province gave autonomy to four tertiary care hospitals of the province in 1999. These included Khyber Teaching Hospital (1400 beds), Hayat Abad Medical Complex (500beds), Lady Reading Hospital (1600 beds), and Ayub Teaching Hospital (600 beds). With autonomy these hospitals were

given one line budget and their management was run through Board of Governor (Management Council). Basic purpose of granting autonomy was to improve patient care and bring efficiency. It was assumed that with passage of time these hospitals would make their own revenue and government would stop budgeting them.

To asses effects of the autonomy, I undertook performance audit of Khyber Teaching Hospital. Following indicators were used.

1. Number of outdoor/indoor patients treated in a year.
2. Surgery carried out in one ward in one year.
3. Cost reduction of treatment for patients.
4. Lab tests carried out in a week on yearly basis.
5. Presence / attendance of doctors, paramedics, nurses during duty hours.
6. Bad occupancy rate of patients.

The data before autonomy and after autonomy was taken into consideration. Data for twelve years 1998 to 2009 was tabulated and comparison was made. It was observed that with the increase of population, number of patients had increased tremendously, but patient care had declined. Before autonomy attendance of employee was very good and it had declined by 30% with passage of time. New machinery had been purchased, but patients were less satisfied. Most of the tests which were supposed to be carried out in Hospital Laboratory were referred to private laboratories. Patients, who were supposed to be operated, waited for longer time. Senior doctors were least interested in patient care and they give 1-2 hours to the hospital. Number of doctors had increased many-folds, but few were present during duty hours. OPD was mostly manned by trainee doctors. There was no uniformity; in some wards OPD was for 6-days a week, while others had 1 or 2 days a week. Bad occupancy rate had declined to 65% in 2008 and 66% in 2009. In 2008 there were 65565 indoor patients and 430313 outdoor patients, but in 2009 it was 65572 and 416029 respectively. Cost per patient in 2006 was Rs.512, Rs.545 in 2007, Rs.590 in 2008 and Rs.606 in 2009. Administrative expenditure had increased but patient care had declined. Budget was 95% provided by provincial government and the hospital had failed to generate its own resources. Its own collection through various sources had increased, but due to increase in salaries it was just 5-6% of the total budget. Board of Governor (Management Council) consisted of political appointees who were more interested in promoting welfare of their voters, rather than patients care. Doctors union had become stronger and management was unable to control them, their every demand was accepted but no action could be taken against them ( Yousafzai, Muhammad Saeedullah , 2010).

It was concluded that Autonomy Act of Provincial Assembly was not fruitful and with autonomy, service of the hospital/s had deteriorated. No improvement in performance had been observed. Due to strong lobby of doctors, government could not think of abolishing autonomy. Many doctors were scions of parliamentarians, high officials and therefore no action could be taken against them, resultantly patient care suffered. Autonomy failed to bring economy, efficiency and effectiveness.

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