

Is Auditor-General the Ally of the Parliament and the People?

*Mohd Azmi Nias Ahmad
Faculty of Accountancy
Universiti Teknologi MARA (UiTM), Malaysia
Email: azminias@pahang.edu.my*

ABSTRACT

This paper outlines the scope of the auditor-general's activities. It can be concluded that the activities can be divided into the three categories, financial statement audit, compliance audit and performance audit. Auditor-General's authority to undertake examinations of the government agencies should be maintained and the Auditor-General is expected to offer recommendations for improvement not only regarding accounts and records, but in relations to management efficiency, economy and effectiveness. Four states of Audited Financial Report were reviewed in order to determine whether the Auditor-General is "the ally of the parliament and the people".

Keywords: *Public Sector Auditor, financial statement audit, compliance audit and performance audit*

Introduction

Public funds are the revenues and expenditures that public sector organizations collect and spend on behalf of the public. In democratic society, every citizen has the right to know how public funds are spent in order to ensure that the money has been spent in such an effective and efficient manner and of the public interest.

Since the accountability and transparency of each transaction are the centre issues of public sector financial management, and becoming crucial especially in the rapid growth of information technology, the role of Auditor-General is to ensure that the public sector money be monitored and managed ethically and responsibly. Regarding the role of the Auditor-General (and National Audit Department in general), the Australian National Audit Office (ANAO) has claimed itself as “*the ally of the parliament and the people*” and the same is apparently believed by all public sector audit departments. However, the statement is only true of those which do broad scope audits embracing efficiency and effectiveness as well as compliance. Thus, this paper aims to study and analyze whether the above statement is true and relevant to Malaysian public sector auditing.

Background

Public Sector Audit

In the public sector, audit activities are described as a comprehensive audit, which encompasses regularity in auditing and auditing performance. Audits of governmental organizations are premised largely on the concept that the official and employees who manage public funds are accountable to the public. The public sector is claimed to be diverse and complex and range from local, state and federal government (Golightlyd 2000). Therefore, accountability in the public sector is relatively more complex than the private sector, primarily due to the different environment in which the public sector entities operate. Elements of accountability are the core differences between government and private or profit oriented organization. Accountability is regarded as the cornerstone of all financial reporting in government, which requires the government to answer to the citizens’ justification of the raising of public resources and the purpose for which they are used. The demand for accountability may induce the auditor to ensure that the government administrator, as well as the public, received greater assurance and additional disclosures. Thus, government accountability should be as good as or better than the accountability of large corporation law (Milley and Read 2000).

Another distinguishing factor is the scope of audits of the government, by public sector external auditors which are broader, normally encompassing reporting on internal control and on compliance with law

and regulations, as well as attesting to financial report. Although they use the same technique and processes in performing their audits, the emphasis of public sector auditing is different to that of private sector auditing whether, compliance, performance or financial statement oriented. This is due to the overriding criterion of accountability in the public sector, which has been discussed above.

The public sector auditing put much emphasis on three types of auditing, which are financial statement audit, performance audit and compliance audit. In fact, those are three types of auditing procedure carried out by Malaysia National Audit Department (NAD) as prescribed in section 6(a) to section 6(f) of the Audit Act 1957. The following is the description of the area of interest performed by each audit.

Financial Statement Audit

The objective of the financial statement audit is to express opinion on the financial statements of all government controlled entities under examination, which the Auditor-General is responsible for (Gill & Cosserat 1999). According to Audit Act 1957, the purpose of financial statement audit is to give an opinion whether financial statement shows a true and fair view of the financial position. The Auditor-General is also required to disclose any non-compliance to the specified acts or orders by the entities.

Performance Audit

Performance audit according to Gill and Cosserat (1999), is defined as an independent, objective and systematic examination of the management of an organization, program or function. It is based on two important principles of management, that is:

- i. Public fund must be used in the best possible way. Decision made must be legal and ethical and result in economical, efficient and effective public service.
- ii. Officials and employees who manage public funds are accountable to the public for prudent and effective management of resources entrusted to them.

The objective of performance audit of the public sector entity is to provide assurance on the efficiency and effectiveness of that entity's

administration. In Malaysia, the requirement of performance audit on public sector entity is specified under section 6(e) of the Audit Act, 1957. The act state that the purpose of the performance audit is to determine whether the objective of the programs or activities are achieved and whether the implementation of the programs and activities is carried out on economical, efficient and effective manner.

Compliance Audit

The purpose of compliance audit is to determine whether an entity has complied with specific laws and regulations (Arens and Loebbecke 1991). According to section 6(f) of the Malaysia Audit Act 1957, NAD is responsible to conduct compliance audit which includes the inspection and evaluation on activities of public sector entities to determine whether laws and regulations are fully complied.

Structure of Public Sector Audit in Malaysia

Appointment of Auditor-General

The auditor-general is an independent officer of parliament who audits and report to parliament on the activities and performance of performance of government agencies, authorities, companies and their controlled entities (Gill et al. 1999). Article 105(1) of Federal Constitution prescribes that there shall be an Auditor-General, who is appointed by Yang di Pertuan Agong on the advice of Prime Minister and after consultation with the Conference of Rulers. Further, Article 105(2) of the same constitution prescribes that the Auditor-General shall be eligible for re-appointment but shall not eligible to accept any appointment in the service of the Federation or State at the same time. The purpose of the article is to avoid any conflict of interest to arise while the Auditor-General conducting his duties.

Independence of Auditor-General

The following shows the position of the Auditor-General under the Federal Constitution.

The figure shows that the Auditor-General, should be as independent as the legislative, executive or judiciary. Thus, in the performance of his statutory duties, he is not subjected to the authority of any minister or

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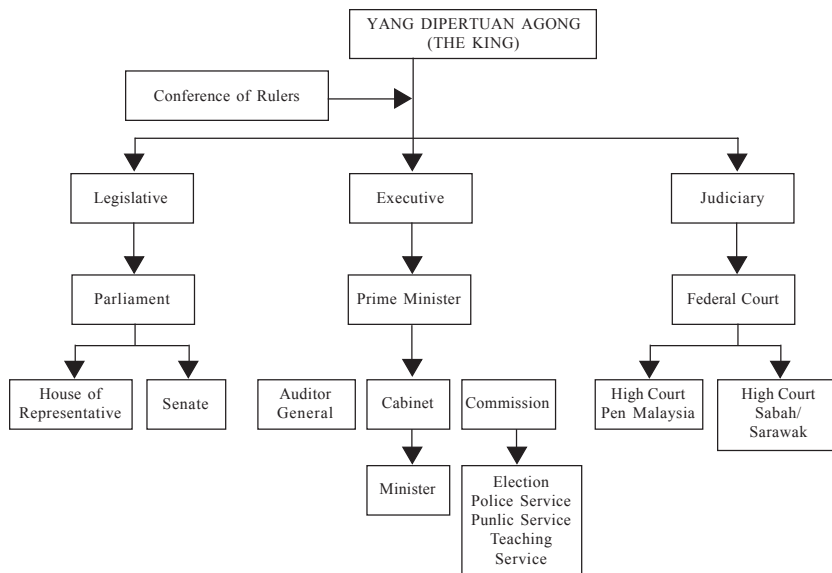


Fig. 1: Organization Structure of Malaysian Government
Source: The National Audit Department web site

executive body. This enables him to carry out his statutory duties according to the requirements of the law and without interference, fear or favor. Adequate safeguards have been provided in the Federal Constitution and the Audit Act to ensure his independence. This technical independence is reinforced by the Audit Act 1957 which allows the Auditor-General to carry out the audit in such manner as he may deems fit. In addition, Article 109 of the Federal Constitution states that the Auditor-General is not subjected to the jurisdiction of the Public Services Commission. The office of the Auditor-General though part of administrative setup, is independent from the executive branch of the Government. The Auditor-General's independence is further guaranteed by the provision in the Constitution for the appointment, remuneration and security of tenure of the office.

To further assists him in discharging his duties independently, section 8 of the Audit Act 1957 supersedes any secrecy provision contained in other laws except to the extent any such other laws (except to the extent any such other laws) specifically excludes the operation of Section 8, Audit Act 1957. The staff of the Audit Department in discharging the audit on behalf of the Auditor-General is protected by the statutory powers provided to the Auditor-General by legislation.

The Audit Act 1957 also grants the Auditor-General adequate powers to obtain explanations and information from persons and get access to all documents and records including those classified as secrets, to enable him to discharge his duties. He is allowed to delegate his powers and may authorize any person he deems competent to conduct an audit on his behalf and under his direction. Where the audit department lacks certain specialized knowledge, the Auditor-General can authorize a competent person from outside the government to assist him in carrying out such specialized audit work. This is to ensure the quality of audit is not compromised due to lack of competent staff.

Responsibility and Accountability

Sections 9(1) and 9(2) of the Audit Act 1957 and Articles 106(1) and 106 (2) of the Federal Constitution states that the Auditor-General primary responsibility is to audit and certify the appropriation and other accounts of the Government and to report the result of his examination to the Yang di-Pertuan Agong, state Sultans or Yang di Pertua Negeri who will cause it to be laid in the Parliament or State Legislatures. A copy of those reports shall be transmitted by the Auditor-General to the Minister, who shall cause the statement and report to be published if the Dewan Rakyat be not then sitting.

Besides the annual report, the Auditor-General may also at any time submit a report to the King or ruler of the States upon urgent matters arising in the course of discharging his duties (section 9(4), Audit Act 1957). Matters reported to the Federal and State Legislatures are considered by the respective Public Account Committees who may make recommendations in a formal report to the Federal or State Legislature concerned.

On the audit of the accounts of any other authorities, bodies or fund, the Auditor General is required to submit a certificate and observations to the head of the Authority or Body and a copy thereof to the Minister of Finance or the Chief Minister responsible for the Authority or Body (section 9(7), Audit Act 1957).

The provision of Federal Constitution and the Audit Act 1957 prescribed that the Auditor-General is responsible for enhancing the standard of public accountability by reporting and providing an assurance to Parliament and State Legislatures through timely and accurate reporting on the Public accounts and the proper management of resources.

The following figure shows the graphical representation of the relationship between the audit and accountability processes in Malaysia.

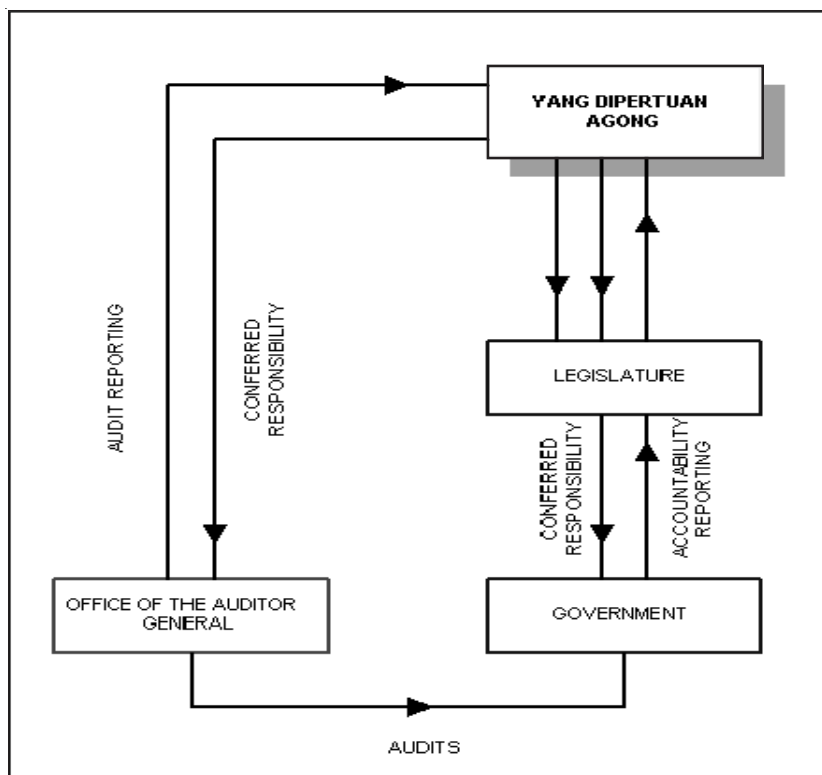


Fig. 2: Audit and Accountability Processes
Source: The National Audit Department web site

The Role of Public Accounts Committee Audit

The Public Accounts Committee (PAC) is appointed by the House of Representative (Dewan Rakyat) at the beginning of each Session. It comprises members drawn from the major parties represented in Parliament. The work of the PAC depends to a large extent on the nature and scope of audit and the reports of the Auditor-General in so far as they identify the issues relating to control and management of public finance. The PAC has no executive powers. The PAC's functions have been defined as being a Parliamentary process of control with a view to:

- i. ensure that money is spent according to the purposes and programmes as approved in the Government Budget;

- ii. see that public officials exercise due economy and efficiency in spending;
- iii. maintain high standards of public accountability in all financial matters.

The main objective of the PAC is to ensure that there is a proper accountability of funds by public officials. The PAC would examine reports of the Auditor-General pertaining to instances of expenditures overrun authorized limits, moneys appropriated not spent in accordance with approved rules and regulations and as to whether programs are achieving their objectives and whether 'value for money' is being obtained in government spending.

Findings and Discussion

This study examined the Auditor-General's report an opinion on the four financial reports of the state selected, Johor, Negri Sembilan, Malacca and Terengganu. The following discussion will be based on the financial statement audit, compliance audit and performance audit conducted by the Auditor-General on the audit of the four states financial reports.

Financial Statement Audit

It is mandatory for the Auditor-General to conduct the financial statement audit to certify the financial statements of the federation, states and other public authorities as may be provided by law. Briefly, the Auditor-General should express his opinion on the financial statements, disclose any non-compliance relating to the specified law and order and report an exception on any limitation and shortcoming of the financial statements. In fact, there are many comments made by the Auditor-General on improper accounting records, omission and misstatement and non-compliance to the specified law and order in the four states financial reports.

Some of the findings on the performance of financial statement audit by Auditor-General on the four states financial reports are summarized in the following table.

Compliance Audit

Federal Constitution, Article 105, under Audit Act 1957, Subsection 6(f), states that the department is responsible to conduct compliance audit

Table 1: Comments, Advice, and Issues Raised by the Auditor-General in Performing Financial Statement

Comments, advice, and issues in financial statement
<p>The accounts balance which cannot be confirmed:</p> <ol style="list-style-type: none">i. Johor – 91 accounts amounting RM215.76 millionii. Malacca – 121 accounts amounting RM133.38 million. In addition, there is misstatement of account balances amounting RM376,748.iii. Terengganu – 6 accounts amounting RM80.35 millioniv. Negri Sembilan – 22 accounts amounting RM4.91 million and deposit in bank amounting RM8.54 million. <p>Among the reasons are the list of individual account balances has not been provided for verification and incomplete bank reconciliation.</p>
<p>Receive of revenue amounting RM32.18 million has not been disclosed in any accounts (Johor).</p> <p>Investment by the state Head Minister Corporation in five subsidiaries from 1986 to 1994, which amounting RM46.11 million has not been disclosed in the Memorandum Account (Terengganu).</p>
<p>The diminution in value of the balance of State Trust Fund amounting RM121.52 million has not been provided (Johor).</p>

which includes the inspection and evaluation on activities of ministries, department or agencies to determine whether laws and regulation are fully complied. The review on the four states financial reports found that the Auditor-General has fulfilled his duty in conducting the compliance audit and gave the necessary comments and advice. The following table summarized some of our findings on the performance of compliance audit by Auditor-General on the four states financial reports.

Performance Audit

Federal Constitution, Article 105, and section 6(e) of the Audit Act 1957, stated that the performance audit involves studies and evaluation of specified programs or activities of ministries, department and government agencies. This is to determine whether the objectives of the programs or activities

Table 2: Comments, Advice, and Issues Raised by the Auditor-General in Performing Compliance Audit

Comments, advice, and issues in performing compliance audit
Reduction in timber premium revenue due to improper control and management in awarding the timber area (Johor)
The disposal of 43.752 hectares of land at an undervalue price of RM2.8 million instead of RM3.4 million as per market value, due to violation of the law and finance procedure (Malacca)
Unauthorized usage of the government vehicles for personal purpose (Terengganu).

are achieved and whether the implementation of the programs and activities was carried out in an economical, efficient and effective manner. This act is designed to ensure that public resources have been managed and utilized economically and efficiently so as to achieve the objectives set. The review on the four states financial reports found that the Auditor-General has fulfilled his duty in conducting the performance audit and gave the necessary comments and advice. The following table summarized some of our findings on the performance audit conducted by the Auditor-General on the four states financial reports.

Table 3: Comments, Advice, and Issues Raised by the Auditor-General in Conducting Performance Audit

Comments, advice, and issues in performing compliance audit
The state government loss RM2.41 million due to the delay in granting the ownership to the landlord (Negeri Sembilan)
Business license revenue of RM7.27 million was not collected by the state government (Malacca)
Weaknesses in the financial management especially relating to expenditure and payment, revenue and loan (all the four states under review).

Issues Relating to the Financial Statement, Compliance and Performance Audit

The findings above show that the Auditor-General has fulfilled his duties in conducting the financial statement audit, compliance audit and performance audit. However, two issues arise, which might affect the accountability of the Auditor-General.

- i. It was found that some of the comments given by the Auditor-General are not detailed enough. For example, in the case where the timber area has been granted with non-compliance to the specified law, the Auditor-General did not disclose the reasons for non-compliance; is it because of negligence or fraud? Another example is the recurring problems on the weaknesses of the states financial management where he cannot confirm the accounts balance, which involves million of Ringgit Malaysia in value. In my opinion, he should explain the reasons of the inability of the related entities to adhere to his advice; is it because of negligence, misconduct by the government servant itself or because of the interference of the politician?
- ii. Most of the comments made by the Auditor-General are made on the financial statement audit. For example, out of nine comments on financial statement of Malacca, seven of them are related to the financial statement audit. In my opinion, to enhance the accountability of the Auditor-General, the emphasis of public sector auditing should be put on performance and compliance auditing. The demand for accountability may force the Auditor-General to ensure that the government administration as well as the public receives greater assurance and additional disclosure. Auditing in the public sector may requires investigating a fraud at some stage (Buttery 1989), which could be done by conducting more performance and compliance audit.

Other Issues and Arguments

The independence of the Auditor-General

The method of appointment of the Auditor-General as prescribed in Article 105(1), Federal Constitution could raise the issue of independence. In my opinion, Yang di-Pertuan Agong should be given

full authority, after consultation with the Conference of Rulers, to appoint the Auditor-General without any advice from the Prime Minister. The advice may become an instruction if the power of Prime Minister is greater than Yang di Pertuan Agong, and this could lead to the appointment of Auditor-General, which may act on the interest of the government rather than in the interest of the public. Rutherford (1983) claimed that the Auditor-General seem to have close relationship with the politician and it raises the issue whether they conducted the performance audit accordingly or just fulfill the requirements without in-depths audit.

Role of the Public Audit Committee (PAC)

The accountability of the Auditor-General should not limit until the submission of the audited report to Yang di Pertuan Agong, but also to ensure that the information will reach the public. Thus, one of the means to enhance accountability of the public sector financial reporting is to widen the role of PAC by giving them the authority to forward to the public immediately, any significant comments or issues raised by the Auditor-General.

Conclusion

The discussion of this paper is focused mainly on the issue of accountability, which is the main concern of the citizens regarding the public sector audit. Accountability requires the government to answer to the citizen the justification of raising public resources and the purpose of which they are use. The issue of accountability in public sector leads in the study on the problem statement of “the ally of the parliament and the people”. The finding reveals that the Auditor-General has fulfilled his duties in conducting the financial statement audit, performance audit and compliance audit. However, there is still room for improvement that should be done by the Auditor General and National Audit department, in order to claim themselves as the “ally of the parliament and the people”. The most important issue is lack of emphasis on performance and compliance audit, which is the prerequisite to claim on such statement. Another issue is the independence of the Auditor-General, the comments of the Auditor-General which are not detailed enough and the role of Public Account Committee.

There is many rooms for improvement for Public Sector Audit. Rice (1999), suggests that, “There is need for change in work patterns and skills in new philosophies. The introduction of out-sourcing, changes to reporting rules, increase accountability and risk management and the trend towards privatizing and corporatization of government utilities are revolutionizing the public sector”. She believes that one of the effects of fundamental change in the public sector is a convergence of the boundaries that once portray the public and private sector. In my opinion, this initiative supports moves to ensure best practice in government and introduces a new level of quality assurance. More than ever before, employees in the public sector must be able to think analytically and strategically and they must have strong finance and management skills.

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