

A. Institutional Framework for Public Sector Auditing

26. Effective scrutiny by the legislature to ensure effective implementation of fiscal and expenditure policies needs comprehensive and competent external audits that are underpinned by International Standards on Auditing.⁸ The environment for an effective supreme audit institution requires a comprehensive approach to public financial management. Supreme audit institutions are not stand-alone institutions. They are part of a PFM architecture that includes budgeting, accounting, internal control, audit and legislative oversight, and appropriate government response. Improving the way the SAI functions is integral to providing information for improving the overall PFM system. All of these requirements are supported by the INTOSAI and IFAC standards. These should be utilized by the Comptroller and Auditor General.

27. The diagnostic questionnaires collected information describing current arrangements and the apparent gaps in the country for the following areas:

- Institutional framework for the supreme audit institution,
- Process for setting auditing standards,
- Use of code of ethics or conduct,
- Arrangements to ensure accountability in the supreme audit institution,
- Arrangements to ensure independence,
- Arrangements to ensure adequate skills and qualifications for the auditors,
- Arrangement for providing training,
- Arrangements to ensure a desired level of competence for the auditors,
- Arrangements for quality assurance.

Those areas with significant scope for improvement are discussed below.

(1) Institutional Framework

28. **A National Audit Act providing a better statutory framework in accord with INTOSAI auditing standards would be needed for a modern audit function.** The Constitution establishes the Comptroller and Auditor General. Annex C gives the relevant extracts from Part VIII of the Constitution

⁸ *Scope, quality, and follow-up of external audit is performance indicator No. 26 in the PFM performance measurement framework supported by the Bank and other development agencies.*



relating to the Comptroller and Auditor General. The CAG Additional (Functions) Act 1974 and the CAG (Additional Functions) (Amendment) Act 1975 provide for the Comptroller and Auditor General to certify appropriation and finance accounts, and audit the accounts of statutory public authorities. The Comptroller and Auditor General is appointed by the President for a term of five years or until the appointee attains the age of sixty-five, whichever is earlier. The Bangladesh Supreme Audit Institution is seeking to enhance its independence by having improved legislative authority for its personnel policies and funding arrangements. Both of these measures would significantly enhance independence. The Bangladesh Supreme Audit Institution is currently under-resourced for conducting the level and extent of auditing to meet its statutory obligations. Although the diagnostic questionnaire did not assess this issue, any resource problems will only be exacerbated as the Bangladesh Supreme Audit Institution endeavors to audit all of the entities under its mandate, and to appropriately respond to the challenges of improved financial reporting over coming years. More efficient auditing processes can alleviate the problem.

29. **A new National Audit Act should contain an adequate Offences Clause.** Full cooperation by auditees and ethical behavior by auditors are essential for effective audit. Current legislation is inadequate to respond to significant lack of cooperation. A culture of impunity must be strictly guarded against.

(2) Setting Auditing Standards

30. **The new National Audit Act should adopt International Standards on Auditing.** The CAG has adopted INTOSAI Auditing Standards. These standards are too general for adequate guidance. The International Standards on Auditing are needed for effective guidance for the audit staff to improve the audit work. The IFAC International Audit and Assurance Standards Board (IAASB) is progressively rolling out International Standards on Auditing. INTOSAI is moving from maintaining its own auditing standards toward supporting IAASB in the development of its auditing standards, especially so that the IAASB Auditing Standards appropriately reflect the interests of the international public sector audit community.

31. International Standards on Auditing represent best international practices for the auditing profession, particularly in areas of fundamental auditing practice such as:

- audit evidence,
- documentation,
- audit materiality,
- fraud,
- audit errors,
- audit opinions,
- audit planning,
- control environment assessments, and
- supervising the work of audit staff.

32. The Comptroller and Auditor General has decided that Bangladesh can benefit from adopting the INTOSAI Auditing Standards as the core of its own auditing standards, as these are internationally

recognized, credible and readily available. However, it is generally recognized that INTOSAI Auditing Standards need the underpinning support of the more detailed International Standards on Auditing. With the decision by INTOSAI to adopt ISA and to prepare public sector practice notes where necessary to support each ISA, the way is open for Bangladesh to use the more comprehensive ISA to guide its work. This is quite appropriate as Bangladesh is a member of INTOSAI and its regional group, the Asian Organization of Supreme Audit Institutions (ASOSAI).

(3) Ensuring Independence

33. **A new National Audit Act is needed to provide effective independence.** Some of the core principles of SAI independence that were set out by INTOSAI are only partially, if at all, met by the current legislative and administrative framework:

- financial and managerial autonomy and the availability of appropriate human, material, and monetary resources;
- independence of the SAI Heads, including security of tenure and legal immunity in the normal discharge of their duties;
- sufficiently broad mandate and full discretion in the discharge of SAI functions; and the freedom to decide on the content and timing of their reports, and to publish and disseminate them; and
- existence of effective follow-up mechanisms on SAI recommendations.

34. **More statutorily independent arrangements for staffing and for establishing the budget should be put in place by legislation.** The CAG officers and staff are under the administrative control of the Finance Division of the Ministry of Finance, which controls the appointment, promotion, and disciplinary action for the CAG employees. The CAG independence as upheld in the Constitution has been jeopardized by this practice. The CAG should be separated from the executive branch of the government and be attached with the Parliament. The Comptroller and Auditor General should be vested with more financial powers. Also in practice the annual budget of the audit department needs to be placed and approved by the Ministry of Finance, like other ministries. The more preferable arrangement, is for budget approval to involve a Parliamentary Committee considering the CAG budget and audit plans prior to approval by the Parliament.

35. **A more open appointment process for the post of Comptroller and Auditor General, which addresses term of service and ranking status, is preferred by modern audit legislation.** The Comptroller and Auditor General is appointed from among senior officers of the Audit and Accounts Cadre. The Comptroller and Auditor General is appointed by the President for a term of five years or until the appointee attains the age of sixty-five, whichever is earlier. Canada and the United States provide for 10-year terms to professionally qualified persons. In Bangladesh, the current practice of a CAG tenure of five years does not provide a long enough term to initiate and implement reforms. In the Bangladesh Warrant of Precedence, the Comptroller and Auditor General is ranked sixteenth, which is below the rank of Cabinet Secretary. In many countries, including Canada, this position is of an equivalent rank to that of a minister or a federal justice. Model legislation for an audit office prepared in the United Kingdom recommends the same status of chief justice.⁹

⁹ *A Model National Audit Office Act. The Association of Chartered Certified Accountants, London, 2004.*

36. Legislation should provide an environment in which resources are adequate for the full regularity and performance audit mandate. The Comptroller and Auditor General enjoys full power to conduct audits and prepare reports. However available capacity is such that the office mainly conducts regularity and compliance audits. In this type of audit, vouchers and records of the financial transactions of public officials or organizations are verified one by one. A more explicit authority for the full range of current and prospective types of audit conducted by INTOSAI members would be more appropriate in authorizing functions and funding. The scope of the CAG audit is narrowly focused. Supreme audit institutions normally conduct audits on the overall financial management performance issues of state bodies.

37. Legislation should provide an environment in which the Comptroller and Auditor General is free to arrange for appropriate involvement with the media on audit reports. In Bangladesh, the audit report is never discussed with the media, unlike the practice in other countries. The Legislature's Public Accounts Committee (PAC) discusses the report but the press or media are not invited. Some public sector rules have been cited as restricting civil servants from making comments to the press. The model legislation reads, "The Auditor General or his/her authorized staff may provide comments and interviews to the press or other media on the subject of any published audit reports."¹⁰ This communication may need to be in Bangla, the national language.

38. Improved PAC and departmental administrative processes are needed for following up audit reports.¹¹ There is an enormous backlog by the Public Accounts Committee in hearing the audit objections. To some degree, improved audit methodology and report writing skills will help, but the fundamental processes for scrutiny need reform. Audit Committees and corporate governance arrangements for departments and agencies need to be reformed along with improvements to the audit processes. Better protocols may be useful between the Comptroller and Auditor General and departments to ensure that access to the relevant records for auditors is made easy, and disruption to departments is kept at a minimum. In addition, better protocols would help ensure that draft audit reports are reviewed quickly by departments for accuracy and fairness and that the CAG and departments, as far as possible, reach agreement on reports before they are made public. Similar protocols are needed between Parliament and the CAG covering, for example, how audit reports will be handled.

(4) Qualifications and Skills of the Auditors

39. When recruiting, qualifications should include an accounting degree for all appointees. The current recruitment criteria for financial auditors in the CAG Office do not give sufficient attention to accounting qualifications. As a result there is too much pressure on government training institutions to provide specialist knowledge. This has not been effective. Since there is a comprehensive tertiary education sector in Bangladesh, which includes accounting, as well as a professional accounting body, these resources should be used. A PAC survey found that both professional qualifications and training programs were ways of improving auditors' competence.¹²

¹⁰ *A Model National Audit Office Act. The Association of Chartered Certified Accountants, London, 2004.*

¹¹ *Legislative scrutiny of external audit reports is performance indicator No. 28 in the PFM performance measurement framework supported by the Bank and other development agencies.*

¹² *Chowdhury, Innes, Kouhy, 2005. "The Public Sector Audit Expectations Gap in Bangladesh. Managerial Auditing Journal Vol. 20 No. 8, page 900.*

(5) Training

40. **The CAG Office should operate a continuing professional development program for the professional personnel.** Improved facilities are needed and the adequacy of proposals in the Financial Management Reform Project should be reviewed.

(6) Auditor Competence

41. **It is necessary to strengthen the technical and professional competence of the CAG Office and improve its operational capacity to produce and disseminate quality audit reports that meet international standards and serve the need of the stakeholders.** The CAG Office has historically concentrated mainly on the compliance audits needed to support proper execution of the budget. It now needs to improve resources and training to build in-house capacity for financial, performance, forensic, environmental, and information technology audits. The CAG Office needs to create a core group of professional accountants for the certification of public accounts. Substantially enhanced technology support is needed both in hardware and software terms. Attention needs to be paid to ethical behavior. A 2005 study of PAC expectations found that PAC members saw room for improvement in the ethical standards of the CAG auditors.¹³

(7) Quality Assurance

42. **Improved structures and indexing of more comprehensive audit working papers would help audit supervisors to ensure that audits meet specified standards of quality.** The Comptroller and Auditor General periodically issues directions to the Audit Directorates for quality assurance, mentioning supervision, review, and other requirements of the audit standards. The Bangladesh Audit Standards cover audit planning, compliance with laws, internal control, audit evidence, and others which are being followed by the Audit Directorates. Findings, conclusions, and recommendations have been given importance, taking into consideration the materiality and significance of the audit findings. But due to lack of trained personnel and inadequate training facilities, the audit standards cannot be implemented properly, and audit working papers do not come up to the standards required. A robust quality assurance regime needs to be in place and operating effectively. Such a scheme should ensure that audit reports are systematically reviewed for quality by line managers before being released. There should be a subsequent internal independent review process, operating on a sample basis, to ensure that the work of all auditors is reviewed on a regular basis. Such a system can be further enhanced through the use of external reviewers.

B. Auditing Standards as Practiced

43. The diagnostic questionnaires have collected information about the current arrangements for the audit methodology and the apparent gaps in the country in the following areas:

- audit planning,
- audit supervision,

¹³ Chowdhury, Innes, Kouhy. 2005. "The Public Sector Audit Expectations Gap in Bangladesh. *Managerial Auditing Journal* Vol. 20 No. 8, page 900.



- reviewing internal controls,
- reviewing compliance with laws,
- ensuring adequate audit evidence is collected,
- analyzing whether the financial statements accord with accounting standards,
- preparing audit opinions,
- reporting on fraud, and
- reporting on compliance.

Out of this exercise came recommended activities that will help bring local standards in line with international standards.

(1) Audit Planning

44. **In the final results of an audit, the company's chief executive should be accountable for the fiscal and expenditure policies and their implementation.** Consultations between the auditor and the senior management of the auditee are helpful at the planning stage to provide senior level focus. Engagement with the auditors and their results is likely to assist with implementation of audit findings. More consultation is needed.

45. **The new audit methodology manual should introduce more comprehensive planning requirements based on the specific objectives of the audits.** The current introduction of improved audit methods under the Financial Management Reform Project will make the audit process more meaningful. The present process appears to be driven by the 'necessity of issuing reports' and is not having enough impact on (a) strengthening internal control, and (b) dealing with the malpractices. Generally the planning for compliance audit that is focused on assessing regularity needs to be more systematic when conclusions are drawn about the relative frequency of errors or the correctness of an overall figure for expenditure.

(2) Audit Supervision

46. **A more comprehensively structured working paper system is needed for the audit to attain the normal audit objectives regarding the validity of transactions.** Current supervision is hampered by inadequate working paper systems and an outdated audit methodology.

(3) Reviewing Internal Management Control Procedures

47. **Introduce a modern audit manual that includes the audit risk model.** Bangladesh has had some earlier projects to develop its auditing methods with the assistance of specialist consultants and supreme audit institutions in other countries. However, it is apparent that there is a lack of an adequate audit methodology. This manifests itself in a number of ways: It is not clear what kind of audit opinion is being sought. There is insufficient assessment of audit risk and the appropriate level and extent of audit responses necessary in order to address those risks. Also, there is no concept of audit confidence—the confidence level that is implicit in the audit opinion and that underpins the level and extent of audit testing required in order to express that opinion.

48. **An audit methodology should clearly outline the following points:**

- the audit confidence level;
- the requirements for audit planning, audit work papers, and audit reporting;
- how audit materiality is determined and what is an acceptable level of audit risk and confidence;
- how to develop an appropriate mix of audit work to address the audit risks.

The audit should be completed by a process which provides a method for summarizing audit errors and evaluating them against audit materiality.

(4) Audit Evidence

49. **The audit methodology and necessary supporting working papers should be more precisely defined in a manual of procedures.** Audit evidence is crucial to an effective audit and currently is poorly documented, filed, and referenced. The technical assistance under the Financial Management Reform Project is aimed at improving this.

(5) Analyzing Financial Statements

50. **Audit testing needs to be more directed toward forming an audit opinion.** There is a need to expand testing to undertake full financial attest audits covering all financial assertions. A financial audit should result in an audit opinion being expressed on the complete set of financial statements rather than solely an identification of the deficiencies found in the transactions scrutinized. Audit reports currently reflect the scope of the work undertaken in the audit. The audit report is heavily compliance based, identifying regulatory breaches in the compilation of the financial reports. Reports focus on discrepancies found and regulatory breaches. There is little systems work and control testing. Thus, recommendations for systems or control improvements do not appear. Although significant deficiencies are noted, the underlying causes of these deficiencies are not explored so that the remedies can be recommended. Such audit reports do not give much assurance.

(6) Reporting on Financial Statements

51. **Audits of State-owned enterprises need to improve their impact.** Independent chartered accounting firms examined the audit reports of 9 state-owned enterprises and reviewed the audit reports of the Commercial Audit (CA) Department of the CAG that had been submitted to Parliament. The following problems emerged in the reviewed reports:

■ **Delayed issuance**

The table shows typical delays:

Ministry	Year	Issue date
Industries	2001/2	January 2004
Energy and MR Division	2000/1	April 2003
Finance Division	1999/0	January 2002
Civil Aviation & Tourism	2000/1	April 2003

■ **Long outstanding audit objections**

The reports below refer to unresolved audit objections, dating as far back as 1973-74 in the case of Finance Division.

Ministry	Period	Audit objections		
		Total	Resolved	Unresolved
Industries	1971/72 to 2000/01	351	7	344
Energy and MR Division	1985/86 to 1999/2000	82	1	81
Finance Division	1973/74 to 1998/99	367	04	363
Civil Aviation & Tourism	1981/82 to 1999/2000	83	0	83

■ **Late preparation of independent audited accounts**

The relevant Ordinance or Memorandum and Articles of Association sets a time limit for submission of annual audited accounts, but this is not being complied with by many enterprises as per the table below.

Ministry	Number of CA audit reports required	Number of CA audit reports not received
Energy and MR Division	62	27
Finance Division	36	31
Civil Aviation & Tourism	17	14
Civil Aviation & Tourism	2000/1	April 2003

■ **Lack of response by auditees/ministries**

SOEs do not respond to the audit queries.

■ **Need for technically qualified audit staff**

All the SOEs are of a specialized nature and the quality of the audit work would be considerably improved if technically qualified personnel were made part of the audit team, or provide training to the CAG auditors. The latter approach would also require the CAG auditors to be grouped by industry specialization.

■ **Need for more revenue audit**

The CAG audit is limited to expenditures and does not include audit of the sales and revenue cycle. Given the importance of the revenue cycle of the public utilities revenue should be in the scope of audit work.

52. **The requirements of ISA 700, The Auditor’s Reports on Financial Statements, for the form of the audit opinion should be adopted in full.** The audit scope and audit opinion paragraphs for the Consolidated Financial Statements 2004 do not contain the degree of detail set by ISA 700 in paragraphs 12 to 15. This creates doubts as to the auditing standards used for the work. It also does not categorically state whether the audit provides a reasonable basis for the opinion, and if the audit was planned and performed to obtain reasonable assurance about whether the financial statements are free of material misstatement. The scope statement notes the limitations of staff, other resources, and time available. This would normally be read by a user of the accounts as an indication that the audit opinion on the accounts is thereby qualified although this is not clearly stated in the opinion paragraph.

(7) Reporting on Fraud

53. **There is a need for forensic audit training.** Much of the audit reporting seems to relate to fraudulent behavior. The Bangladesh Supreme Audit Institution does not focus on fraud in a sufficiently systematic way. The International Standards on Auditing provide guidance for the auditor on tests for fraud. ISA 240, The Auditor’s Responsibility to Consider Fraud and Error in an Audit of Financial Statements, requires the auditor to perform procedures to obtain information that is used to identify the risks of material misstatement due to fraud. In addition, it requires the auditor to evaluate the design of the entity’s related controls, including relevant control activities, and determine whether they have been implemented. The ISA 240 also requires the auditor to inform the auditee’s management and its Board of any fraud and of the failure in its internal control that led to the fraud. The auditor’s report should identify the action that the entity is taking about the fraud. A PAC study found that both the CAG auditors and the PAC members agreed that the audits did not confirm that no material fraud exists¹⁴

(8) Reporting on Compliance

54. **Improve the effectiveness of the audit report by more efficient action on enforcement of corporate governance requirements through the Public Accounts Committee and agency audit committees.** Under the present process, the CAG submits a yearly report to the President. The Public Accounts Committee of the Parliament calls the auditee/ministry for response to the unresolved audit findings. To reduce the number of unresolved audit objections to be submitted to the President, it would be helpful if the CAG could work with the Establishment Division to identify measurable violations and introduce financial and administrative penalties that can be used to correct the violation and reduce repetition. The PAC survey found that CAG reports could be improved in terms of communicating clear objectives, addressing more relevant problems, making more effective recommendations, and involving more extensive audit work. The CAG Office and Public Accounts Committee should review current reporting arrangements, including consideration of the legal requirements governing reporting. It may be possible for the CAG to produce a more balanced portfolio of reports during the year and/or only bring to the attention of the PAC major concerns which can not be dealt with at the departmental level or which appear to have system-wide implications. This process could involve staff retraining. The staff would need to shift from a focus on identifying cases when rules have not been followed correctly, to suggesting ways in which control systems can be affordably strengthened, thus reducing the risks of errors – accidental or deliberate.

¹⁴ Chowdhury, Innes, Kouhy, 2005. “The Public Sector Audit Expectations Gap in Bangladesh. *Managerial Auditing Journal* Vol. 20 No. 8.

