



# AUDITING OF PUBLIC SECTOR ENTITIES

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# Introduction...



- *Auditing of public sector entities is unique in the sense that they are governed by the International Standards of Supreme Audit Institutions (ISSAIs) developed by the International Organization of Supreme Audit Institutions (INTOSAI) which has its headquarters in Vienna, Austria*
- ISSAI 100- Fundamental Principles of Public-Sector Auditing provides detailed information on: -
  - the purpose and authority of the ISSAIs;
  - the framework for public-sector auditing;
  - the elements of public-sector auditing
  - the principles to be applied in public-sector auditing

# Introduction...



- The professional standards and guidelines are essential for the credibility, quality and professionalism of public-sector auditing. ISSAIs aim to promote independent and effective auditing by the Supreme Audit Institutions(SAIS)
- The ISSAIs encompass public-sector auditing requirements at the organization level (SAI) level, while at the level of individual audits they aim to support the members of INTOSAI in the development of their own professional approach in accordance with their mandates and with national laws and regulations
- Discussion on relevant laws-which article of the CoK, 2010, PFM Act, 2012, Public Sector Accounting Standards Board (PSASB)

# Framework for Public-Sector Auditing Mandate:



- o The SAI will exercise its public-sector auditing function within a specific constitutional arrangement and by virtue of its office and mandate, which ensures sufficient independence and discretion of performing its duties
- o SAI may be mandated to perform many types of engagements on any subject of relevance to the responsibilities of management and those charged with governance and the appropriate use of public funds and assets. The extent or form of these engagements and the reporting thereon will vary according to the legislated mandate of the SAI concerned

# Public-sector Auditing and its Objectives:



- ❖ The public-sector audit environment is that in which governments and other public sector entities exercise responsibility for the use of resources derived from taxation and other sources in the delivery of services to citizens and other recipients. Public-sector auditing helps to create suitable conditions and reinforce the expectation that public-sector entities and public servants will perform their functions effectively, efficiently, ethically and in accordance with the applicable laws and regulations.
- ❖ In general, public-sector auditing can be described as a systematic process of objectively obtaining and evaluating evidence to determine whether information or actual conditions conform to established criteria. Public-sector auditing is essential in that it provides legislative and oversight bodies, those charged with governance and the general public with information and independent and objective assessments concerning the stewardship and performance of government policies, programmes or operations

# Public-sector Auditing and its Objectives:



o SAls serve this aim as important pillars of their respective national democratic systems and governance mechanisms and play an important role in enhancing public-sector administration by emphasizing the principles of transparency, accountability, governance and performance. ISSAI 20-Principles of Transparency and Accountability contain guidance in this regard

# Public-sector Auditing and its Objectives:



- ❖ All public-sector audits start from objectives, which may differ depending on the type of audit being conducted. However, all public-sector auditing contributes to good governance by:
  - i. Providing the intended users with independent, objective and reliable information, conclusions or opinions based on sufficient and appropriate evidence relating to the public-sector entities;
  - ii. Enhancing accountability and transparency, encouraging continuous improvement and sustained confidence in the appropriate use of public funds and assets and the performance of public administration;
  - iii. Reinforcing the effectiveness of those bodies within the constitutional arrangement that exercise general monitoring and corrective functions over government and those responsible for the management of publicly-funded activities
  - iv. Creating incentives for change by providing knowledge, comprehensive analysis and well-founded recommendations for improvement

In general, public-sector audits can be categorized into one or more of three main types: audits of financial statements, audits of compliance with authorities and performance audits. The objectives of any given will determine which standards apply.



# Types of Public-Sector Audits:



The three main types of public-sector audits are as follows: -

- 1. Financial Audit:** focuses on determining whether an entity's financial information is presented in accordance with the applicable financial reporting and regulatory framework. This is accomplished by obtaining sufficient and appropriate audit evidence to enable the auditor to express an opinion as to whether the financial information is free from material misstatement due to fraud

# Types of Public-Sector Audits:



**2. Performance Audit** focuses on whether interventions, programmes and institutions are performing in accordance with the principles of economy, efficiency and effectiveness and whether there is room for improvement. Performance is examined against suitable criteria and the causes of deviations from those criteria or other problems are analyzed. The aim is to answer key audit questions and to provide recommendations for improvement

# Types of Public-Sector Audits:



**3. Compliance Audit** focuses on whether a particular subject matter is in compliance with authorities identified as criteria. Compliance auditing is performed by assessing whether activities, financial transactions and information are, in all material respects, in compliance with the authorities which govern the audited entity. These authorities may include rules, laws and regulations, budgetary resolutions, policy, established codes, agreed terms or the general principles governing sound public-sector financial management and the conduct of public officials

# Continuation...



*SAIs may carry out audits or other engagements on any subject of relevance to the responsibilities of management and those charged with governance and the appropriate use of public resources. These engagements may include reporting on the quantitative outputs and outcomes of the entity's service delivery activities, sustainability reports, future resource requirements, adherence to internal control standards, real-time audits of projects or other matters. SAIs may also conduct combined audits incorporating financial, performance and/or compliance aspects*

# Elements of Public-Sector-Auditing



- ❖ *Public-sector auditing is indispensable for the public administration, as the management of public resources is a matter of trust. Responsibility for the management of public resources in line with the intended purposes is entrusted to an entity or person who acts on behalf of the public. Public-sector auditing enhances the confidence of the intended users by providing information and independent and objective assessments concerning deviations from accepted standards or principles of good governance. All public-sector audits have the same basic elements: the auditor, the responsible party, intended users (the three parties to the audit), criteria for assessing the subject matter and the resulting subject matter information*

# Elements of Public-Sector-Auditing



## ❖ The three parties:

**The Auditor:** In public-sector auditing the role of auditor is fulfilled by the Head of the SAI and by persons to whom the task of conducting the audits is delegated. The overall responsibility for public-sector auditing remains as defined by the SAI's mandate

**The Responsible Party:** In public-sector auditing the relevant responsibilities are determined by constitutional or legislative arrangement. The responsible parties may be responsible for the subject matter information, for managing the subject matter or for addressing recommendations, and may be individuals or organization

**Intended Users:** The individuals, organizations or classes thereof for whom the auditor prepares the audit report. The intended users may be legislative or oversight bodies such as the National Assembly(PAC/PIC), The National Senate and County Assemblies, those charged with governance or the general public

# Elements of Public-Sector-Auditing



## ❖ *Subject matter, criteria and subject matter information*

- ✓ Subject matter refers to the information, condition or activity that is measured or evaluated against certain criteria. It can take many forms and have different characteristics depending on the audit objective. An appropriate subject matter is identifiable and capable of consistent evaluation or measurement against the criteria, such that it can be subjected to procedures for gathering
- ✓ sufficient and appropriate audit evidence to support the audit opinion or conclusion.
- ✓ The criteria are the benchmarks used to evaluate the subject matter. Each audit should have criteria suitable to the circumstances of the audit. In determining the suitability of criteria, the auditor considers their relevance and under stability for the intended users, as well as their completeness, reliability and objectivity (neutrality, general acceptance and comparability with the criteria used in similar audits. The criteria used may depend on a range of factors, including the objectives and the type of audit. Criteria can be specific or more general and may be drawn from various sources including laws, regulations, standards, sound principles and best practices. They should be made available to the intended users to enable them to understand how the subject matter has been evaluated or measured
- ✓ Subject matter information refers to the outcome of evaluating or measuring the subject matter against the criteria. It can take many forms and have different characteristics depending on the audit objective and audit scope



# Principles of Public-Sector Auditing



1. The principles are fundamental to the conduct of an audit. Auditing is a cumulative and iterative process

Areas covered by the principles for public-sector auditing, i.e. general principles related to the audit process: -

- a) Ethics and independence: ISSAI 30 Code of Ethics and ISSAI 10 on independence
- b) Quality control: ISSAI 40 Quality control for SAI contain guidance in this respect
- c) Audit team management skills
- d) Audit risk materiality
- e) Professional judgement
- f) Due care and skepticism
- g) Documentation
- h) Communication



# Principles of Public-Sector Auditing



- 2. Auditors should maintain appropriate professional behavior** by applying professional skepticism, professional judgement and due care throughout the audit. The auditor's attitude should be characterized by professional skepticism and professional judgement. Auditors should exercise due care to ensure that their professional behavior is appropriate
- 3. Professional skepticism means maintaining professional distance** and an alert and questioning attitude when assessing the sufficiency and appropriateness of evidence obtained throughout the audit. It also entails remaining open-minded and receptive to all views and arguments. Professional judgement implies the application of collective knowledge, skills and experience to the audit process
- 4. Due care means that the auditor should plan and conduct audits** in a diligent manner. Auditor should avoid any conduct that might discredit their work

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# PUBLIC SECTOR ACCOUNTING STANDARDS BOARD (PSASB)



## Background

- Kenya adopted International Accounting Standards (IAS) in 2000 through the Institute of Certified Public Accountants of Kenya (ICPAK). These standards were however largely used by the private sector. Public Sector relied largely on accounting principles which were not standard across the sector. In 2008, the then Minister of Local Government issued a directive that all Local Authorities to adopt International Public Sector Accounting Standards (IPSAS). However, there was no clear mechanism to implement the same.
- Some public sector entities adopted IFRS while others summarized the Government Chart of Accounts. This non-uniformity made it difficult for the Auditor General to audit public sector entities as it was not clear what constituted annual financial statements.

This necessitated the harmonization of reporting in the public sector.

- ✓ The Public Sector Accounting Standards Board (PSASB) was established as part of PFM reforms in Kenya following the promulgation of the new Constitution in 2010 and the subsequent enactment of the Public Finance Management (PFM) Act in 2012.
- ✓ The PSASB is a statutory, standard setting body established under the Sections 192 to 195 of the Public Financial Management Act, 2012.

# The Mandate of the Board is to:



- ✓ *Set generally accepted accounting and financial system standards for the public sector.*
- ✓ *Develop and pronounce generally accepted internal auditing standards.*
- ✓ *Mainstreaming of best practices for good governance, internal controls and risk management in the public sector.*
- ✓ *The Board is the only standard setter of Accounting and Auditing Standards for the Public Sector in Kenya.*

# Composition of the Board:



*The Board is a representative entity and consists of nominees from:*

- ✓ *National Treasury*
- ✓ *The Controller of Budget*
- ✓ *the Intergovernmental Budget and Economic Council*
- ✓ *the Auditor General*
- ✓ *the Institute of Certified Public Accountants of Kenya*
- ✓ *the Association of Professional Societies of East Africa*
- ✓ *the Capital Markets Authority*
- ✓ *the Institute of Internal Auditors and*
- ✓ *the Institute of Certified Public Secretaries of Kenya*

# Other Key Information:



- *The PSASB through a Gazette Notice No. 1554 dated 8th August 2014, signed by the Cabinet Secretary on 8 July 2014, adopted IPSAS and IFRS for use by public sector entities.*
- *Retrospective application for the year ended June 2014 was encouraged by PSASB.*
- *The use of IFRS and IPSAS was therefore formally adopted and applied for the first year in the year ending 30 th June 2014.*
- *FY 2015/2016 is the third year of implementation of the standards that were gazetted by PSASB in 2014*
- *The National and County governments and their respective entities apply International Public Sector Accounting Standards (IPSAS) Cash based standard.*

# Other Key Information:



- *The Semi-Autonomous National County and Government Agencies apply IPSAS Accrual based standards issued by International Public Sector Accounting Standards Board (IPSAB).*
- *The State and County Corporations carrying out commercial activities apply International Financial Reporting Standards (IFRS) while regulatory and non-commercial State and County Corporations are to apply IPSAS Accrual.*
- *Uniformity of Accounting Standards used for financial reporting in the public sector. This has resulted to more efficient audits by the OAG and comparability of performance of entities within the public sector.*