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**Challenges Faced by Ethiopian Federal Government Auditors:
the Case of the
Office of the Federal Auditor General**



**A research project paper submitted for the partial fulfillment of
M.Sc. Degree in Accounting and Finance**

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List of Abbreviations

| | | |
|--------|-------|--|
| AICPA | ----- | American Institute of Certified Public Accountants |
| ASOBAC | ----- | A Statement of Basic Auditing Concepts |
| IACC | ----- | International Association of Chartered Accountants |
| ICT | ----- | Information Communication Technology |
| GAAP | ----- | Generally Accepted Accounting Principles |
| GAAS | ----- | Generally Accepted Auditing standards |
| GAO | ----- | Government Accountability Office |
| MoFED | ----- | Ministry of Finance and Economic Development |
| OFAG | ----- | Office of the Federal Auditor General |
| SAS | ----- | Statement on Auditing Standards |
| SPSS | ----- | Statistical Package for Social Sciences |

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Chapter one

Introduction

Currently, governments were highly dedicated in the provision of public services due to the increased demand and expectations of the public. Responsible financial management and accountability are among the factors that can help governments achieve this goal. Hence, government auditors, as agents responsible for auditing government income and expenditures, can have critical role by acting as watchdogs for financial integrity and creditability of reported information. The challenges faced by these auditors in performing their task are the central concern of this project. This chapter introduces on the background of the study; states the problems; and discusses on objectives, significances, scope and limitation of the study

1.1. Background of the study

Auditing is the process by which a competent and independent person accumulates and evaluates evidence about quantifiable information related to a specific economic entity for the purpose of determining and reporting on the degree of correspondence between the quantifiable information and established criteria¹

¹ American Accounting Committee on Basic Auditing Concepts”A Statement Of Basic Auditing Concepts(ASOBAC)”, the accounting review ,vol.47 p.8,1972

The objective of an audit² is to prepare a written opinion or report on the fairness of the financial statements provided and on its compliance with accounting and legal rules and regulations.

To fulfill this objective an auditor³ is expected to plan and design an audit approach, test controls and transactions, perform analytical procedures and tests details of balances and complete the audit and issue an audit report. In addition, professional auditing standards and ethical standards must also be followed.

In Ethiopia, the history of auditing goes back to 1930's and this project paper was conducted at the first audit institute of the country:- Office of the Federal Auditor General⁴ (OFAG). Even if the profession has long life its development is not as expected. Only with a qualified auditors and audit work is the profession's development and the reliability of its output can be thinkable.

There are many challenges facing auditors in exercising their job. A challenge, in this context, can be something, which defend or tackle auditors from achieving their objectives. Auditing as a profession need auditors to be competent enough in skill and experience, be independent from any conflict of interest, be careful in conducting their work and so on. In the absence of such values, it is difficult for them to provide qualified

² Audit: a word derived (in 15th century) from a Latin word *audire* "hearing" from *audire*, the past participle stem of *audire* "to hear", so called because originally the accounts were read aloud.

³ Auditor : somebody who is qualified to audit accounts or to conduct an audit of a department or organization

⁴ Auditor General: an independent auditor reporting on government spending
(Source^{2,3&4} Microsoft Encarta Reference Library 2005)

information. In addition, if the awareness of the public, audited entities and political person's is not positive, the audit work could not be an easy task as they may harm the independence of the auditor.

In this project paper, the researcher has identified the challenges the challenges faced by auditors of the Office of the Federal Auditor General, particularly financial auditors and the ways for solving problems identified. The researcher believes that the study can enhance the profession's development and the quality of the information provided to its users.

1.2. Statement of the problem

According to the generally accepted auditing standard of reporting the auditor's report should be⁵

"... Easy to understand and free from vagueness or ambiguity, include only information which is supported by competent, relevant and reasonable audit evidence, and be independent, objective, fair and constructive."

To have such a report it is not an easy task. Auditors must be able to pass many challenges at all the planning, execution, reporting and follow up stages of the audit process. Some of the problems faced are related to the following major factors:

⁵ American Institute of Certified Public Accountants(AICPA)"Generally Accepted Auditing Standards (GAAS)", statements on auditing standards,AICPA,1947,USA

Lack of knowledge and expertise: To fulfill their responsibility auditors are expected to be skillful, competent and updated with changes in their profession and technology. Other professions, like statistics, are also helpful in facilitating the audit work and increasing the reliability of their information provided. Lack of the necessary knowledge and can distort the over all audit work. And also, most of the activities made by auditors like:- understanding the audited entity, determining materiality, control tests, substantive tests, sample size and risk determination and others need experience to provide reliable information to the its users ⁶.

Inadequate staff capacity and training: Auditors must rely on technical expertise, professional judgment and a good understanding of how an error or fraud is committed in order to detect misstatements. Inadequate staff capacity and training can therefore have a severely debilitating effect on the ability of auditors to address their objectives. In particular, capacity for relatively recent or less widespread audit techniques, such as information technology auditing, is often weak due to a lack of specialized training.

Lack of independence: Auditors should maintain an independent stance and remain impartial not only in facts but also in appearance to provide independent information. Challenges of independence may come from the auditee⁷ or the users of the information. Auditing of governmental entities mostly focus on determining whether the auditee's have discharged their stewarding responsibility and became accountable. So, if the

⁶ Users can be generally categorized as internal (from within the organization) and external(those interested groups outside the organization).

⁷ Auditee: somebody or something being audited (a person or organization that is being audited)
(Source^{2, 3&7} Microsoft Encarta Reference Library 2005)

auditor is not independent from auditee, he/she can face difficulty for him/her to report on auditee's fault. Independence of an auditor can be hindered due to political, economic or social pressures.

Difficulty in collecting the necessary data for audit: Auditors should have competent, relevant and reasonable audit evidence based on which they will judge and make conclusions regarding the organization, program, activity or function under audit. But, intentionally or due to the lack of awareness obtaining all relevant data may sometimes be challenging. Untimely preparation and delivery of financial reports is the other challenge facing auditors in relation to data collection.

Lack of motivation: Auditors should give reasonable care in performing their work. This becomes true if they can be interested with what they are performing and interest is the result of satisfaction. Physical or mental benefits of the work can give the auditor satisfaction. Lack of benefits (salary, trainings, educational opportunities, bonuses etc) may limit the auditor's satisfaction and make him/her to be careless in discharging his/her duties. So, with no motivation, the auditor's out put can not be reliable.

1.3. Objectives of the study

The main objective of this study is to identify challenges faced by Ethiopian federal government public auditors in discharging their responsibilities, and recommending on the actions to be taken in minimizing or eliminating these challenges.

The following are the specific objectives of the study which can help in achieving the above broad objective.

- ❖ Examining the steps used in planning and execution phases of the audit process and identifying related challenges on auditors;
- ❖ Identifying the challenges faced by the Auditors in obtaining the necessary data;
- ❖ Evaluating the analytical procedures and tests made by auditors and identifying the related problems encountered ;
- ❖ Identifying auditors challenges in relation to independence, education, training, experience , job satisfaction and staff capacity;
- ❖ Identifying auditor's challenges faced in reporting the audit result; and
- ❖ Giving suggested solutions for the problems identified above.

1.4. Research methodology

Both the qualitative and quantitative sources of data were used for analyzing, interpreting and recommending on the problems identified above. The main sources of data were primary sources. Interviews were made with three senior auditors, two divisional heads and two department heads. Questionnaires were also filled by selected auditors of OFAG and some officials and employees of auditees. In addition, observation and review of some planning, fieldwork and reporting procedures and working papers were made.

Fifty auditors (35 percent) which were selected using the simple random sampling technique were filled questionnaires. Two questionnaires were distributed for each of the 25 (from the total of 165 federal government organizations) federal government organizations selected using the systematic sampling technique. Supervisors, divisional heads and department heads were also interviewed using unstructured type of interview.

After the necessary data have been collected, edited and coded, the preparation and summary was made using the Statistical Package for Social Sciences (SPSS) 13th version. The data were then presented in the form of tables, charts, graphs and explanatory narrations. In addition to the data collected using the above methods, professional articles, auditing standards, accounting principles, ethnical rules and other related issues were used in analyzing the data in a descriptive type of analysis.

1.5. Significance of the study

This research has a diverse area of contribution to the different bodies which directly or indirectly concerned with an audit. The following are some of the expected benefits of the study:-

- ❖ Increasing understanding of audit firms on the actions to be taken in enhancing the reliability of their information.
- ❖ Creating awareness in the minds of the public and the auditee's on the necessity of an audit.
- ❖ Help auditors understand on the value of improving the profession's competence and quality of work.
- ❖ Remembering auditors on the cares to be taken and professional accountabilities expected from them.
- ❖ Contribution to the profession's development in Ethiopia
- ❖ Can be used as a reference for further studies.

1.4. Scope of the study

The study was conducted at the office of the Federal Auditor General (OFAG). Office of the Federal Auditor general is the supreme audit institute of the country (Ethiopia) having its main office at Addis Ababa and five branches at Addis Ababa, Awassa, Bahirdar, Jimma and Diredawa. Public audits made by this institute, particularly the financial audits are the main concerns of this paper. By investigating the stages of the Audit process,

from planning up to reporting, related challenges on auditors were identified and suggested solutions were recommended⁸.

1.7. Limitations of the study

The objective of this paper is to identify challenges faced by financial auditors (and compliance) of the office of the auditor general and to recommend on possible solutions. According to GAO's standards for audit of governmental organizations, financial and compliance auditors are those who engaged in determining (1) whether the financial statements of an audited entity present fairly the financial position and results of operations in accordance with generally accepted accounting principles (GAAP) and (2) whether the entity has complied with laws and regulations the may have a material effect up on the financial statement⁹. Due to time and resource constraints, the study had limitations to the following aspects:-

Even if some of the common challenges were addressed collectively, the technical aspects of this study can not be inferred to performance and environmental auditors. In addition, regional government auditors, auditors of public enterprises and internal auditors of government organizations are not the concern of this paper.

Additional research may also be necessary to determine the extent to which the challenges faced by government auditors relate to those auditors' reporting relationships, degree of independence, and the structures of their governments. This paper only focuses on identifying challenges and setting possible recommendations.

⁸ The five branches of OFAG were named as coordination office and they are mainly engaged in facilitating the auditors sent to those areas and serving as a place where auditors temporarily stay

⁹ United States Government Accountability Office "Standards for Audit of Governmental Organization's:- Programs, Activities and Functions", U.S government printing office, 1981, Washington

1.8. Organization of the paper

This paper has been structured in five chapters. The first chapter is an introductory section that includes background and statement of the problem, objective of the study, significance of the study, scope and limitations of the study Chapter two deals with literature review about auditing and different issues related to it. Specifically, issues related to governmental audit were highly considered in this chapter.

Chapter three consisted of the research design. This chapter provides all detail techniques used to collect, analyze, and interpret data.

The fourth chapter consisted of the analysis and discussions. In this chapter the different challenges faced by the under consideration were identified and discussed. Based on the findings of the fourth chapter the overall summary, conclusions and recommendations have been made in the fifth chapter.

Chapter two

Review of related literatures

In this chapter reviews of different literatures related to audit and the challenges faced by auditors were made. The sources of the literatures were different books, journals, articles, research papers etc from within the country and abroad. History, evolution, prospects, meaning, types, objectives, values and benefits of an audit were included. In addition, types of auditors, materiality, analytical review procedures, audit risk, sampling in audit, independence, supreme audit institutions, expectation gap, future of public audit and accountability were among the major topics covered in this chapter.

2.1. Auditing: history, evolution, and prospects

As far back as 4000 B.C., historians believe organized businesses and governments in the near east to allay their concerns first instituted formal record-keeping systems about correctly accounting for receipts and disbursements and collecting taxes. Similar developments occurred with respect to the Zhao dynasty in China (1122-256 B.C.) The need for and indications of audits can be traced back to public finance systems in Babylonia, Greece, the Roman Empire, the City States of Italy, etc., all of which developed a detailed system of checks and counterchecks. Specifically, these governments were worried about incompetent officials prone to making bookkeeping errors and inaccuracies as well as corrupt officials who were motivated to perpetrate fraud whenever the opportunity arose. (Mautz & Sharaf, 1961)

Even the Bible (referring to the period between 1800 B.C. and A.D. 95) explains the basic rationale for instituting controls rather straightforwardly: "...if employees have an opportunity to steal they may take advantage of it." The Bible also contains examples of internal controls such as the dangers of dual custody of assets, the need for competent and honest employees, restricted access, and segregation of duties. (O'Reilly et al.,1998)

Historically then, the emergence of double-entry bookkeeping in circa 1494 A.D. can be directly traced to the critical need for exercising stewardship and control. Throughout European history, for instance, fraud cases — such as the South Sea bubble of the 18th century, and the tulip scandal — provided the justification for exercising more control over managers. Within a span of a couple of centuries, the European systems of bookkeeping and auditing were introduced into the United States. As business activities grew in size, scope, and complexity, a critical need for a separate internal assurance function that would verify the (accounting) information used for decision-making by management emerged. Management needed some means of evaluating not only the efficiency of work performed for the business but also the honesty of its employees. (Mautz, 1964)

Government auditing in Ethiopia dates back the early 1931 constitution, which stressed the importance of the proper collection of the state revenue and the necessity of procedures to control expenditures but stopped short of either referring to or requiring any audit as such. This, in fact, had to wait for proclamation 69 of 1944, which established the Commission for Audit which was largely responsible for the

examination and control of the accounts of the Ministry of Finance and was directly accountable to the Prime Minister. Articles 120 and 121 of the revised constitution of 1955 clearly conferred the rights and duties of auditing all ministries, departments, and agencies to the Auditor General, whose office was then established as a separate, independent entity that reported directly to the Emperor and to the Parliament.¹⁰

Subsequently, the functions of the Auditor General were amended by decree No. 32 of 1958, which was later renumbered as proclamation No. 179/1961 (1954 E.C.). This proclamation, in addition to defining powers and duties, also envisioned conditions of appointment and independence of the Auditor General and reporting mechanisms¹¹.

After the 1974 (1966 E.C.) Ethiopian Revolution, proclamation No. 164 of 1979 (1971 E.C.) was enacted to redefine the powers and duties of the Auditor General giving him additional responsibility of auditing mass organizations, development projects as well as conducting performance auditing. No further improvement was enacted to enabling law of the Office of the Auditor General until the power and duties of the Office of the Auditor General were redefined by proclamation 13/1987.¹²

Senait (2003) also mentioned that up to 1994 OFAG was the only government audit institution in Ethiopia. Proclamation No. 68/1997 was enacted to establish the Office of the Federal Auditor General (OFAG) which gave the power and duty to undertake

¹⁰ Senait Melese, 2003, Audit profile: The Office of the Federal Auditor General of Ethiopia, OFAG, Addis Ababa

¹¹ Ibid

¹² Ibid

Financial and Performance audits (or cause to be audited) on accounts of the federal government offices and organizations, accounts involving budgetary subsidies and special grants extended by the Federal Government to Regional States.

2.2. Meaning and objectives of an audit

The general definition of an audit is an evaluation of a person, organization, system, process, project or product. Audits are performed to ascertain the validity and reliability of information; also to provide an assessment of a system's internal control. The goal of an audit is to express an opinion on the person/organization/system (etc) in question, under evaluation based on work done on a test basis. Due to practical constraints, an audit seeks to provide only reasonable assurance that the statements are free from material error. In the case of financial audits, a set of financial statements are said to be true and fair when they are free of material misstatements - a concept influenced by both quantitative and qualitative factors. (Kamal and Ashok, 1999),

In financial accounting, an audit is an independent assessment of the fairness by which a company's financial statements are presented by its management. It is performed by competent, independent and objective person(s) known as auditors or accountants, who then issue an audit report based on the results of the audit. Such systems must adhere to generally accepted standards set by governing bodies regulating businesses; these standards simply provide assurance for third parties or external users that such statements present a company's financial condition and results of operations 'fairly'. (Richiute, 1961)

The concept, content and scope of government audit develop in tune with the political, social and economic development of the country. Government audit aims to ensure accountability of the executive in respect of public revenue and expenditure. The objective of Government auditing is that of systematic, professional and independent examination of financial, administrative and other operations of a public entity made subsequently to their execution for the purpose of evaluating and verifying them, presenting a report containing explanatory comments on audit findings together with conclusions and recommendations for future actions by the responsible officials and in the case of examination of financial statements, expressing the appropriate professional opinion regarding the fairness of the presentation. (Edward et al, 2006),

2.3. Types of audits

SAIs can undertake different types of audits aimed at improving government accountability. These include: (Stapenhurst and Titsworth, 2001)

- Financial audits: assessing the accuracy and fairness of accounting procedures and financial statements;
- Compliance audits: scrutinizing the use of funds for approved purposes through compliance with laws and regulations;
- Performance audits (also known as "value for money" audits): analyzing cost-effectiveness and operational efficiency. Sometimes these can extend to reviewing the general effectiveness of government programs in achieving their objectives and act as impact audits;

- Other audits: in addition, specialized audits may be conducted (as part of one of the main audits listed above or separately in their own right) examining issues such as recruitment and management principles, ethics and integrity of the audited work force and others.

2.4. Types of auditors

There are two types of auditors:

Internal auditors: are employees of a company hired to assess and evaluate its system of internal control. To maintain independence, they present their reports directly to the board of directors or to top management. They provide functional operation to the concern. Internal auditors are employees of the company, so they can easily find out fraud and any mishappenings. (Arens & Loebbecke, 1991)

External auditors: are independent staffs assigned by an auditing firm to assess and evaluate financial statements of their clients or to perform other agreed-upon evaluations. Most external auditors are employed by accounting firms for annual engagements. They are called upon from outside the company. (Millichamp, 1984)

2.5. Materiality level

Statement on Auditing Standards (2006), Audit Risk and Materiality in Conducting and Audit (SAS No.107) includes the following updated guidance with respect to materiality in the context of an audit:

"The auditor's consideration of materiality is a matter of professional judgment and is influenced by the auditor's perception of the needs of users of financial statements. The perceived needs of users are recognized in the discussion of materiality as "the magnitude of an omission or misstatement of accounting information that, in the light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or misstatement."

The standard explains that materiality is not a constant. It varies between two entities of different size and nature. It also can vary for the same entity from year to year. In addition, the discussion recognizes that materiality judgments are made in light of surrounding circumstances and necessarily involve both quantitative and qualitative considerations.

2.6. Analytical review procedures

Analytical procedures are evaluation tools that can greatly enhance the efficiency of financial statement reviews. Analytical procedures are typically used to determine whether a financial statement contains relationships and items that are unusual. These procedures vary depending on the kind of client involved and the amount of financial information under review. These procedures can range from simple basic comparisons of items to complex analytical models of relationships. What is common and essential to all analytical procedures is the need for objectivity in seeking out conclusions regarding the

financial statements being reviewed. Key areas that should be studied during a financial statement review are previous financial information, expected results, industry information and the interrelation of financial and non-financial data. (Blocher & Willingham, 1985)

During the planning stage analytical procedures are used to assist the auditor in planning the nature, timing, and extent of other auditing procedures that will be used to obtain evidential matter for specific account balances or classes of transactions. The analytical procedures used in planning the audit should focus on enhancing the auditor's understanding of the client's business and the transactions and events that have occurred since the last audit date, and in identifying areas that may represent specific risks relevant to the audit.¹³

During the conduct of substantive tests, analytical procedures are used to obtain evidential matter about particular assertions related to account balances or classes of transactions. The expected effectiveness and efficiency of an analytical procedure in identifying potential misstatements depends on, among other things: (1) The nature of the assertion; (2) The plausibility and predictability of the relationship ;(3) The availability and reliability of data used to develop the expectations; and (4) The precision of the expectation.¹⁴

In planning the analytical procedures in substantive testing, consideration should be given to the amount of differences from the expectation that can be accepted without further investigation, after establishing materiality and consistent levels of assurance

¹³ The CPA journal "analytical procedures" pp.2&3,1992, New York

¹⁴ Ibid

desired from the procedures. Significant unexpected differences should be evaluated and corroborated with management's responses to inquiries. If explanations cannot be obtained, then sufficient evidence about the assertion should be obtained by performing other procedures to determine whether the difference is a likely misstatement; recognizing that such unexplained differences may indicate an increased risk or material misstatement.¹⁵

2.7. Audit risk and it's components

According to Srivastava & Shafer (1992) Audit risk is a term that is commonly used in relation to the audit of the financial statements of an entity. The primary objective of such an audit is to provide an opinion as to whether or not the financial statements under audit present fairly the financial position, performance and cash flows of the entity. Audit risk is the risk of the auditor providing an inappropriate opinion on the financial statements, particularly when those financial statements contain a material misstatement. Of less concern is the situation where the auditor states that the financial statements do not meet the standard of fair presentation, when in fact they do.

Srivastava & Shafer (1992) also mentioned the following components of audit risk and their descriptions:

Audit Risk = Inherent Risk x Control Risk x Detection Risk

¹⁵ Ibid

Inherent risk represents the auditor's assessment that there may be a material misstatement relating to an assertion in the financial statements under audit, without taking the effectiveness of the related internal controls into account. If the auditor concludes that there is a high likelihood of such a misstatement, ignoring internal controls, he would assess the inherent risk as being high.

Control risk represents the auditor's assessment of the likelihood that a material misstatement relating to an assertion in the financial statements will not be detected and corrected, on a timely basis, by the client's internal control system.

Detection risk is defined as the likelihood that a material misstatement relating to an assertion will not be detected by the auditor's substantive testing. It is important to note that the detection risk indicates the detection risk that the auditor is willing to "live with", given the acceptable audit risk and his assessment of inherent and control risk. This means that if the detection risk is high, the auditor is willing to accept a high detection risk, and will do less substantive testing as compared to a situation where the detection risk is lower.

2.8. Sampling in audit

Even if 100 percent of the information could be tested, the cost of testing would likely exceed the expected benefits (the assurance that accompanies examining 100 percent of the total) to be derived. What is required is a sampling of the accounts. According to Mckee (1989) the science of sampling design involves: (1) looking at the resources available, the restrictions under which one must work, the mathematical and statistical

tools available, the accumulated knowledge of certain characteristics of the populations to be sampled; and (2) putting these together to arrive at the optimum design for the purpose at hand.

Joseph & Herbert (1986) classified types of samples in audit in to statistical and non statistical, and described both as follows:

2.8.1. Statistical probability sampling

Probability sampling provides an objective method of determining sample size and selecting the items to be examined. Unlike non statistical sampling, it also provides a means of quantitatively assessing precision (how closely the sample represents the population) and reliability (confidence level, the percentage of times the sample will reflect the population). Accounts to be reviewed during an audit are normally selected through one of the following probability sampling methods:

1. Simple Random Sampling: In auditing, this method uses sampling without replacement; that is, once an item has been selected for testing it is removed from the population and is not subject to re-selection. An auditor can implement simple random sampling in one of two ways: computer programs or random number tables.
2. Systematic (Interval) Sampling: This method provides for the selection of sample items in such a way that there is a uniform interval between each sample item. Under this method of sampling, every "nth" item is selected with a random start.

3. Stratified (Cluster) Sampling: This method provides for the selection of sample items by breaking the population down into strata's, or clusters. Each stratum is then treated separately. For this plan to be effective, dispersion within clusters should be greater than dispersion among clusters. If blocks of homogeneous samples are selected, the sample will be biased.

2.8.2. Non statistical sampling

Some selection methods can be used only with non statistical sampling plans. Which include:-

1. Haphazard Selection: In this method, the auditor selects the sample items without intentional bias to include or exclude certain items in the population. Haphazard selection is permitted for non statistical samples when the auditor believes it produces a fairly representative sample.

2. Block Selection: Block selection is performed by applying audit procedures to items, such as accounts, all of which occurred in the same "block" of time or sequence of accounts. If block sampling is used, many blocks should be selected to help minimize sampling risk

3. Judgment Selection: Judgment sample selection is based on the auditor's sound and seasoned judgment. Three basic issues determine which items are selected:

i. Value of items. A sufficient number of extensively worked or older accounts should be included to provide adequate audit coverage.

ii. Relative risk. Items prone to error due to their nature or age should be given special

attention.

iii. Representativeness. Besides value and risk considerations, the auditor should be satisfied that the sample provides breadth and coverage over all types of items in the population.

2.9. Independence in audit

The second general standard of United States General Accounting Office (amendment number 3, revised in 2002) states the following:

In all matters relating to the audit work, the audit organization and the individual auditor, whether government or public, should be free both in fact and appearance from personal, external, and organizational impairments to independence.

According to this standard auditors and audit organizations have a responsibility to maintain independence, so that opinions, conclusions, judgments, and recommendations will be impartial and will be viewed as impartial by knowledgeable third parties. An auditor should avoid situations that could lead reasonable third parties with knowledge of the relevant facts and circumstances to conclude that the auditor is not able to maintain independence and, thus, is not capable of exercising objective and impartial judgment on all issues associated with conducting and reporting on the work.

The standard also sets three general classes of impairments to independence—personal, external, and organizational. If one or more of these impairments affects an auditor's capability to perform the work and report results impartially, that auditor should either

decline to perform the work, or in those situations in which the government auditor because of a legislative requirement or for other reasons cannot decline to perform the work, the impairment(s) should be reported in the scope section of the audit report.

2.10. Supreme audit institutions (SAIs)

2.10.1. Meaning and guidance

According to Stapenhurst and Titsworth (2001) Supreme audit institutions (SAIs) are the national agencies responsible for auditing government revenue and spending. Their primary purpose is to oversee the management of public funds and the quality and credibility of the government's financial reporting. SAIs supply the information needed by the legislature and the public to hold governments accountable for stewardship of public funds and assets.

The international body guiding the work of SAIs is the International Organization of Supreme Audit Institutions (INTOSAI). INTOSAI, based in Vienna, Austria, is the worldwide association of national audit offices. It issues international guidelines for auditing and financial management, develops corresponding methodologies, provides training, and promotes the exchange of information and know-how among its membership of over 170 SAIs.. (Stapenhurst and Titsworth, 2001)

2.10.2. SAIs auditing systems

The legal mandates, reporting arrangements and institutional Napoleonic system structures of SAIs vary depending on a country's legal and administrative system¹⁶. The

most commonly used auditing systems are based on one of the following three models:-

In the, also known as the "court system", SAIs are part of the judiciary, have both judicial and administrative authority and are independent of the legislative and executive branches. This model is used in some European countries (such as France, Italy, Spain, Portugal and others) and most Latin American and francophone African countries.

In the Westminster system, used in many Commonwealth countries, the SAI (referred to as the Auditor General) is an independent body that reports to parliament.

The office serves no judicial function but, where this is warranted, its findings may be passed to legal authorities for further action. The board system, prevalent in Asia, is similar to the Westminster model in that it is independent of the executive and helps parliament perform its oversight function.¹⁷

2.10.3 The role of SAIs in combating corruption

The key objective of SAIs is the provision of effective oversight of government spending and public finance management. Audits are thus a central feature of SAIs' work. Audits can contribute to improving government performance not only by identifying faults

¹⁶ Staphenurst and Tittsworth , Features and Functions of Supreme Audit Institutions, World Bank, Prem Note 59, 2001., Vienna

¹⁷ Ibid

but also by acting as a deterrent to the abuse of power by providing valuable information about government actions to the legislature and the public. (Magnus, 2001):

Experience indicates that no one institution, acting alone, can significantly reduce corruption. Corruption, defined as the abuse of public office for private gain, has been identified as a symptom of something gone wrong with the management of the state. The most successful corrupt practices are those where the corruptor and the corruptee both gain sufficient advantage to be satisfied with the transaction. Other forms of corruption such, as theft of state assets by those who are in charge of the assets is a huge problem. (Kenneth and Rick, 1998)

According to Kenneth and Rick (1998) a recent form of corruption has emerged with of privatization state-owned enterprises for the benefit of officials. Theft of government financial resources such as pocketing revenues, not repaying advances are all forms of corruption that auditors must be more vigilant in identifying. Audit can be a powerful force to combat corruption. It also can be a potent deterrent to waste and abuse of public funds exposing non-transparent decision-making that was not in the public interest.

2.10.4. Factors for SAIs success

Several factors have been identified to SAI success. Of these, the most important are: having a clear Mandate (set of rules and boundaries agreed to by parliament); independence (both from the executive and to investigate issues at its sole discretion); adequate funding (competitive salaries and modern technology) and staff (training,

education and experience); and the sharing of knowledge and experience (International exchange of ideas, knowledge and experience). (*Kenneth and Rick, 1998*)

2.11. Value and benefits of government audit

The activities of SAIs to date have been to strengthen the confidence of their parliaments, governments, citizens and civil society in the independence, objectivity, quality and cost-effectiveness of their audit reporting as a contribution to their country's stability and economic growth, good governance and fight against corruption. According to Josef (2007) the value of SAIs stems from promoting good governance for today and tomorrow, through:

- Enhanced government financial and budgetary reporting and accountability to their parliaments, citizens and the international community, including supporting the adoption of international accounting and reporting standards;
- Greater transparency of government and advocacy of the importance of parliamentary scrutiny, improving public awareness and supporting a culture of scrutiny among legislative bodies and citizens;
- Improvements in public management and public service delivery, increasing its economy, efficiency, effectiveness, equity and ethics; and
- Deterring fraud and corruption in public administration and addressing it in collaboration with anticorruption bodies.
- SAIs working together can bring value in a globalised environment, which is over and above the value from their work in their individual countries;

- Develop targets and measures of their use of resources and their efficiency, using appropriate cost and output recording systems to support their monitoring;
- Report on their delivery of products and other outputs, and achievement of their statutory remit and further parliamentary or other demands for their work;
- Establish rigorous quality assurance procedures and report the results;
- Monitor the timeliness of audit reporting, against statutory or other commitments;
- Systematically follow up audit work to identify and record its impact, for example implementation of audit recommendations, quality of service improvements, actions taken against public officials, the recovery of monies into public funds and financial savings achieved;
- Monitor staff satisfaction;
- Obtain and report feedback on their audit work, for example from parliamentarians, auditees and from other stakeholders;
- Monitor media coverage of their work;
- Continue to exchange knowledge on their work and measurement issues

2.12. Expectation gap

The expectation gap is the gap between the auditors' actual standard of performance and the various public expectations of auditors' performance (as opposed to their required standard of performance). Such public expectations of auditors, which go beyond the actual standard of performance by auditors, have led to the term 'expectation gap'.

The expectation gap may be decomposed initially into two components: the requirements gap and the feasibility gap. (Mary, 2008)

1. Requirements gap: This is the gap between auditors' actual standard of performance and the performance required of them by the current standards of society. The required standard of performance is the standard of performance set out in both professional standards and statutes, the latter being subject to interpretation through courts of law.

The requirements gap may be further divided into:

Performance gap: The requirements gap is the gap between the actual standard of performance and the standard of performance determined by reference to professional standards and statutes.

Standards gap: This is the gap between the standard of performance as determined by reference to professional standards and statutes, on the one hand, and society's required standard of performance on the other. Society's required standard of performance, as stated above, is the standard of performance set out in the statutes and professional standards augmented by the decisions handed down in the courts of law.

2. Feasibility gap: The feasibility gap is the gap between society's required standard of performance and various public expectations (the expected standard of performance).

The examples include expectations that auditors are responsible for the preparation of the financial statements that auditors 'certify' financial statements, and the failure to recognize the limitations of an audit.

2.13. Duties of persons to be audited

According to proclamation number 68/1997 of the Ethiopian constitution persons to be audited are subject to the following responsibilities;

1. Any individual, employees or an official, upon request by the Federal Auditor General, Auditors of the Office of the Federal Auditor (General or Representatives of the Federal Auditor General), shall, forthwith, make available correct and complete books, documents, ledgers, vouchers and all other documentary or oral evidence which the Auditors deemed it useful and necessary for auditing.
2. Any person who has had in his custody or has paid or has expended or is in charge of the accounts of the money and property of the organs auditable by the office of the Federal Auditor General under the provision of this proclamation, shall, upon request, have the obligation to have his accounts audited.
3. Auditee entities are obliged to take corrective measures, within 30 days from the date of delivery on recommendations and comments included in the audit reports sent to them by the Federal Auditor General; if they are unable to take such measures shall inform the same and the reasons there of to the Federal Auditor General within the period specified herein.
4. The head of any audited office whose weaknesses were commented in the report of the Federal Auditor General submitted to the Council of peoples Representatives, Shall have

the duty to take appropriate remedial measures and inform same to the Council of Peoples' Representative and the Federal Auditor General

2.14. Future of public audit and accountability

Future of public audit lies in the role of audit and accountability in the conception of democracy and good governance. The basic need of public audit is constant. In the future the Supreme Audit Institutions, through their audits and related consultancy service, will continue to be strong actors in the assurance of accountability and in the enhancement of good governance. They will continue to be strong actors in the creation trust towards public institutions and, eventually, in creation of trust to public finances.¹⁸

The challenges for accountability in the context of social and economic change call for a better connection between audit and the exercise of legislative and budgetary power. To serve living democracy audit is expected to have more focus on the quality of governance and on the critical and objective appraisal of the effectiveness of various public policy programs.¹⁹

An audit will be closer to the challenges of economic and fiscal policy. Public audit has to ensure that structures, procedures, management and actual behaviors of the governance and managements system uses resources according to the democratic decisions and produces the results and services – the common goods - intended by democratic decision-makers. Public audit will have an increasing role in the assurance of the quality of

¹⁸ Poysti, T. "the future of public auditing and accountability in the European union", a speaking note on the European auditors seminar, pp 2 & 3, 2007, Luxembourg

¹⁹ Ibid

regulatory management. In financial audit more weight needs to be given to a risk based approach combined with audit and certification of the quality of management, control and accounting systems.²⁰

Financial and compliance audit in which the risk prone sectors and stages of management chain are analytically identified will give the best results in terms of cost-effectiveness of audit and usability of audit findings. There is a need for further convergence and international benchmarking of working methods of public audit. Common analyses and understanding of risks of public finances and financial management are an area to start with the mutual learning. A profound understanding of the ICT environment of public administration and efficient use of ICT –based audit tools are conditions for quality and efficiency in the future public audit work.²¹

Today, SAIs around the world face a new set of challenges. Public expectations of government are changing. Citizens are increasingly intolerant of corruption and poor government services. Increasingly, SAIs will need to consider moving beyond routine audits of government finances to alert their countries to emerging challenges-before they become reach crisis proportions. SAIs will need to educate policy makers and the public to the specific long-term challenges facing their nations. (Walker, 2004)

Walker (2007) also noted that, in the future, three elements will be keys to the success or failure of both democracies and audit institutions. These elements are incentives, transparency, and accountability.

²⁰ Ibid

²¹ Ibid pp4

In the years ahead, SAIs can play several roles (Walker, 2004). They can help to combat corruption. They can help to ensure accountability. They can help to enhance economy, efficiency, transparency, and effectiveness in government operations. They can increase insight in to how government programs and policies are working. Finally, they can facilitate foresight about emerging trends and challenges.

The literatures revealed above were not enough by themselves to answer the research question under consideration, they have some limitations .First, most of the literatures were not considered factors unique to our country, Ethiopia and were values of studies conducted in the developed countries. Some of the literatures were conducted on internal auditors of governmental organizations. And even the variables included in those studies were not all inclusive of the variables considered in the current study. In order to fill this gap this study uses the research design presented in the following chapter.

Chapter three

Research design

The main objective of this study was to identify challenges faced by Ethiopian federal government public auditors in discharging their responsibilities and recommending on the actions to be taken in minimizing or eliminating these challenges. Specifically, the study answers the following research questions noted earlier:

- What are the problems auditor's face at the planning and execution phases of the audit process?
- What are the challenges faced by the Auditors in obtaining the necessary data?
- Are the analytical procedures and tests made by auditors reliable?
- What are auditor's challenges in relation to independence, education, training, experience, job satisfaction and staff capacity?
- Do the auditor's report their audit result with no blockage?
- How can the problems identified above be solved?

In order to address the research problems noted above, the researcher used different techniques and philosophies. This chapter discusses on the different procedures, data sources, collection methods, instruments, sampling techniques, data analysis and presentation methods used.

3.1. Research Procedures used

In conducting this study the researcher followed the following procedures step by step. First, examination of different documents; an understanding of working environment; and sharing of ideas with different auditors were made in order to identify potential research problem areas. Then a research proposal was prepared and submitted to the research advisor. After approval of the research proposal, the necessary questionnaires were prepared and distributed to selected sample respondents from the audit institution (OFAG) and auditee's. The questionnaires together with data obtained from informal interviews made with senior officials (auditors) and from different document reviews were prepared in the form of percents, averages and frequencies; and summarized and analyzed using tables, graphs, charts and diagrams other statistical techniques and descriptions. Finally recommendations were given based on the conclusions derived from the analysis made.

3.2. Data sources, collection methods and instruments

Mixed types of data having both qualitative (such as satisfaction of auditors, auditors independence, expectation of the public etc) and quantitative (like average hours trained) characteristics, capturing the advantages of both, were used for analyzing, interpreting and recommending on the problems identified above

The main sources of data were primary data²². Personal (face to face) Interviews were made with supervisors, and department and divisional heads of OFAG. According to Emory (1980) interviews are a two way purposeful conversation initiated by interviewer to obtain information that is relevant to some research purpose. Interviews include oral questions asked and responses collected orally, having advantages of collecting more information with clarity but requiring more time and money specially if the respondents are large in number. Interviews can be structured (with predetermined questions asked orderly) or unstructured (flexible in the order of questions asked). This study used unstructured types of interviews.

The other and the main method used in collecting primary data was a questionnaire. A questionnaire is a series of questions asked to individuals having the advantages of being quite inexpensive; easy to protect privacy of respondents; and easily corroborated with other methods of data collection. In general, there are two types of questions asked using questionnaires, open format and closed format. In open format questions, there are no predetermined set of responses and the respondent is free to answer. Closed ended questions usually take the form of multiple choice questions. Questionnaires with both closed-ended and open-ended questions(see appendices 1A and 1B) were prepared and distributed to the selected senior officials of organizations audited by the office of federal auditor general (auditee's) and auditors who have been directly engaged in the actual field work²³.

²² According to Emory (1980) primary data came from the original source of material and are collected especially for the task at hand.

²³ Allen G.B “ Elementary statistics: a step by step approach”, Mc Graw Hill co.Inc.1998,USA

In addition, observations²⁴ (non behavioral)of some planning, fieldwork and reporting procedures followed by the auditors were made in order to have an insight in to the actual field work and identify problems which may not be easily found using the other methods.

Secondary sources of data were obtained and used from different sources. Audit manuals, internal control questionnaires, memorandums of gathering background information, audit risk assessment forms, substantive review procedures assurance forms, sampling test planning forms, audit planning memorandums, audit planning checklist forms, working papers, audit test review checklists, and reports are some of the documents used.

3.3. Sampling techniques and procedures

As it was mentioned above in the first chapter the office of federal auditor general has one main office and five branches. Currently, the organization has 352 employees of which 204 were auditors and the remaining 148 were supportive staffs. From the total auditors only around 20 were performance auditors and the remaining 184 were financial auditors, and 144 of the financial auditors are currently engaged directly in the actual audit work at field. There are around 165 federal government institutions being audited by the office of federal auditor general.

Questionnaires were distributed to 50 auditors (35 percent of the target population, i.e. 144) which were randomly selected using the simple random sampling technique having

²⁴ Assefa (2002/03) described observation as a technique which includes the full range of monitoring behavioral and non-behavioral activities and conditions

the list of financial auditors provided by the organization under study (appendix 4B). Simple random sampling technique is a sampling technique in which all respondents will have equal and independent chance of being selected as a sample, so that unbiased choice can be made²⁵.

Samples were also drawn from the 165 federal government organizations and 25 (15.15 percent) of them were selected using the systematic sampling technique and two questionnaires were distributed for each organization selected. Systematic sampling technique is a sampling technique in which every *n*th (example, third, fourth etc) respondent will be included in the sample having the starting point randomly selected. Yet again a list of these federal government organizations was provided by the organization under study based on which samples were drawn²⁶.

In selecting individuals for the unstructured interviews and in using different documents the researcher became purposive that those which are related to the audit work and the research objective, and those which are expected to provide the necessary data with the expected precision were selected. Accordingly, three supervisors, two divisional heads and two department heads were interviewed.

²⁵ Having the list of financial auditors provided by OFAG, samples were drawn by writing the name of each person on a piece of paper, putting them in to a hat, mixing them and drawing one by one until the number of samples selected reach fifty.

²⁶ After dividing the total number of federal government organizations (165) by 25 resulting in approximately 6 random number was selected from the numbers 1 to 6 and every 6th organization was selected until the total number of selected organization reach 25.

3.4. Data analysis and discussion method

After the necessary data have been collected and the necessary editing and coding activities were made the preparation of data was facilitated using the Statistical Package for Social Sciences (SPSS) 13th version .According to Emony (1980) SPSS is an integrated set of computer programs that are invaluable for business researchers. Only the simple programs of the software, such as descriptive statistics, frequency distributions and cross-tabulations were used.

The data were then presented in the form of tables, charts, graphs and explanatory narrations. Tables of frequency distributions and cross tabulations were mainly used in helping the descriptive analysis. Frequency distribution tables were used for summarizing (e.g. counts, percentages etc) of data related a single variable or issue under consideration. For analyzing two or more variables or data classified with two or more characteristics cross tabulations were used which show frequency counts, percentages and summary for individual variables as well as for the variables as a whole

In addition to the tables a pie, histogram, and normal and stacked bar charts were also used for having figural presentation of the factors under consideration. Further more the use professional articles, auditing standards, accounting principles, ethnical rules and other related issues were very much significant in analyzing the data.

Chapter four

Data analysis and discussion

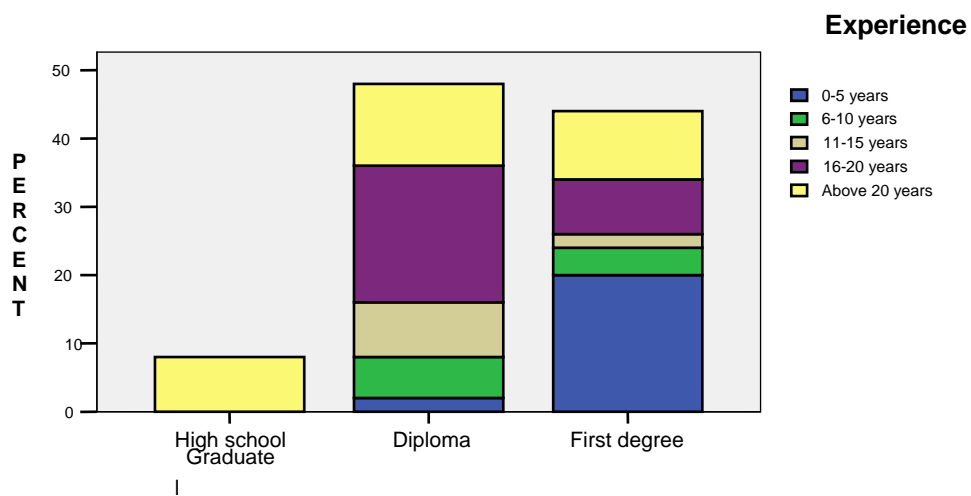
This chapter presents the detailed analysis made to identify the challenges faced by federal government auditors based on the techniques and procedures discussed above in the third chapter. As it was mentioned earlier, data collections were made using questionnaires, interviews, observations and reviews of secondary data. The chapter includes the summaries of data using graphs, tables and charts, different description of values and interpretations.

4.1. Lesser opportunity of pursuing education

The recruitment and retention of qualified accountants and auditors is the most significant in order to provide a competent service and increase the reliance of users on audit outputs. Many of the country's most talented and ambitious young people need better payment and/or better opportunity of pursuing education in order to retain in a given organization. One of the problems (challenges) encountering auditors of OFAG have been the lack of an opportunity to pursue education. According to questionnaire response of the auditors only 32 percent of them believe that the organization provides incentives for improving their educational level. The remaining 68 percent respondents argued that there is no incentive made helping them improve their educational level.

In addition, as it has been shown on the chart below, there is no positive relation ship between the employees' educational level and their experience. For example; from about 44 percent of the total respondents having first degree, 45 percent of them have an experience of less than five years. But only 22 percent of these respondents have first degree even if they have more than 20 years experience and are greater in number from having less than 5 years work experience by 36 percent.

Fig 4.1 the relationship between educational level and work experience



4.2. Inadequate staff capacity and training

Educational specialization in a given field is important, but a blend of skills is necessary to assure that the audit function can perform its duties efficiently and effectively. Auditors must rely on technical expertise, professional judgment and a good

understanding of how an error or fraud is committed in order to detect misstatements. Inadequate staff capacity and training can therefore have a severely debilitating effect on the ability of audit institutions to address their objective(s).

According to an interview made with training, information service, and organization and management head of the organization, the organization's auditing standards require minimum 80 hours of continuing professional training every two years. When continuing professional credits are not earned, it is believed that individuals can face difficulty of meeting requirements of professional standards. But, the average hours the questionnaire respondents trained were only about forty one hours per two years (around only half of the minimum required hours) as it was calculated using the formula below:

$$x = \frac{2 a}{b}$$

Where

x = average hours trained per two years

a = total number of hours trained

b = total years of work experience

This study considered four factors (as shown in table 3.1 below) in order to check whether there is a training system which matches with the current working conditions of government organizations. Integrated budget and expenditure system (IBEX) is a software which almost all federal government organizations were currently using for recording and reporting financial information's, but only eight percent of the respondents took a

training on it. Furthermore, only 34, 26 and 14 percent of the respondents took training on how to collect data; finance rules and regulations²⁷; and premier software²⁸, respectively.

| Response | | Training on how to collect data | Training on finance rules and regulations | Training on premier software | Training on IBEX software |
|----------|-----|---------------------------------|---|------------------------------|---------------------------|
| percent | yes | 34.0 | 26.0 | 14.0 | 8.0 |
| | no | 66.4 | 74.0 | 86.0 | 92.0 |

Table 4.1 Responses on questions related to training

In particular, capacity for relatively recent or less widespread audit techniques, such as information technology auditing, is often weak due to a lack of specialized training. 84 percent of the respondents believe that being updated with technological changes can increase the quality of the audit work, but only 26 percent of them agreed on their being updated with changes in technology in relation to their profession.

²⁷ Finance related rules and regulations are set by ministry of finance and economic development (MoFED). And the auditors in OFAG are expected to check whether the organizations under audit were complying with these rules and regulations.

²⁸ Premier is software planned to be used by the federal governmental organizations which can help them change their basis of accounting from modified cash to accrual. Currently, training is being given for employees' of organizations in how to use the software.

4.3. Challenge in collecting the necessary information

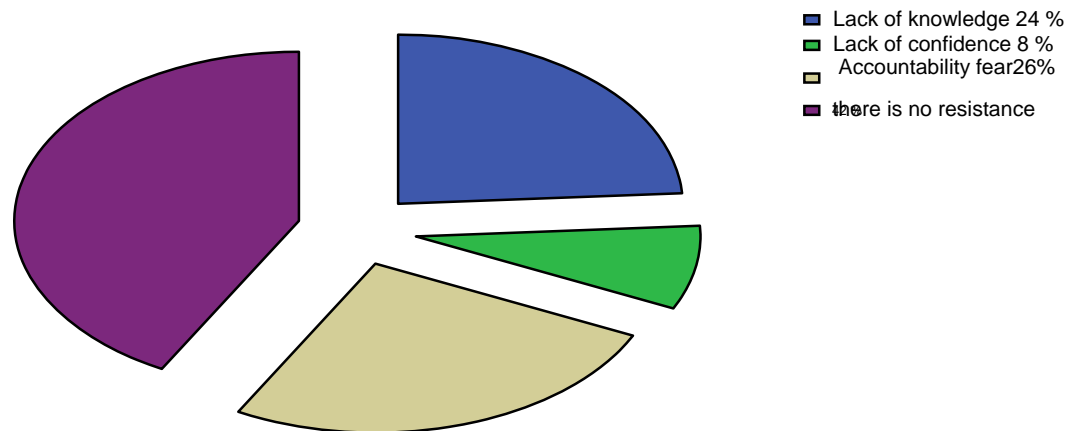
An auditor can not come to a final conclusion if there is a limitation in the scope of an audit due to a restriction on information access. Auditors need to have complete and accurate evidence to conclude their opinions and determine responsibility for failure, incompetence or deceit. Richiute (1982) also noted that sufficient competent evidential mater is the only basis for reaching reasonable and informed audit conclusions. Barriers of complete access to information can have an adverse impact on auditor's performance.

According to the responses collected using interviews and questionnaires there is a limitation for access to information due to auditee's lack of knowledge; fear of accountability; and lack of confidence. About 58 percent of the respondents argued that they face problems in collecting the necessary information due to one or more of the above mentioned reasons.

And about 90 percent of the respondents rated the timely delivery of information by auditee's as very poor, so that the quality of audit work and the reliability of their report have been hindered. Information which is not timely delivered can not be useful for decision making and it may be intentionally changed or cooked by dishonest employees.

(See the figure below)

Fig 4.2 summary of responses on auditee's resistance to provide data



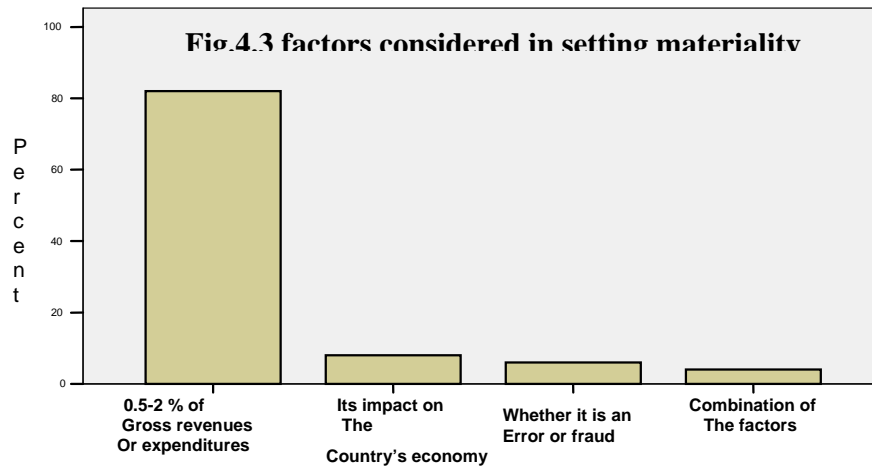
4.4. Inappropriate methods and procedures followed in audit

Generally, there are four steps to be followed in giving an audit service:-planning, execution, reporting and follow up. Planning which is the focus point of this section is the first phase in audit. It includes both preliminary and field work plans. At this stage the auditor is expected to have information's necessary for understanding the organization's background and its internal control. In this sub topic procedures used in setting materiality level, analytical review procedures, and sampling techniques were considered.

4.4.1 Setting materiality level

After having the necessary background and internal control information's, the auditor will proceed its planning phase by setting its materiality level (or maximum tolerable risk). Information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size of the item or error judged in the particular circumstances of its omission or misstatement. The following are factors to be considered on setting materiality according to Richiute (1982): (1) Environmental factors- economic, political and social. (2) Organization related factors- management capabilities, philosophy, plans and expectations; organization characteristics such as size, strength, public image, etc. and (3) Accounting policies.

Users of the audit reports of the office of the federal auditor general were the Ethiopian people represented by the house of people's representatives. So, in setting materiality the auditors should consider the economic condition of the country. But, OFAG's audit standard manual set a guide for materiality to be half- to- two percent of the gross revenues or expenditures (greater of the two) and most of the respondents replied that they use one percent of gross expenditures as their materiality level. The figure below proofs the same thing which shows more than 80 percent of the respondents using 0.5--2 percent of gross revenues or expenditures as their materiality level.



4.4.2. Analytical review procedures

Analytical review procedures help auditor's understand the organization's activities; identify areas of potential risk and also help in planning substantive procedures used. Ricchiute (1982) defined analytical review procedures as substantive tests of financial information made by a study and comparison of relationships among data. He listed five types of analytical review procedures:-

- Comparison of financial information with information for comparable prior periods.
- Comparison of financial information with information with anticipated results.
- Study of the relationships of elements of financial information that would be expected to conform to predictable patterns based on an entity's experience

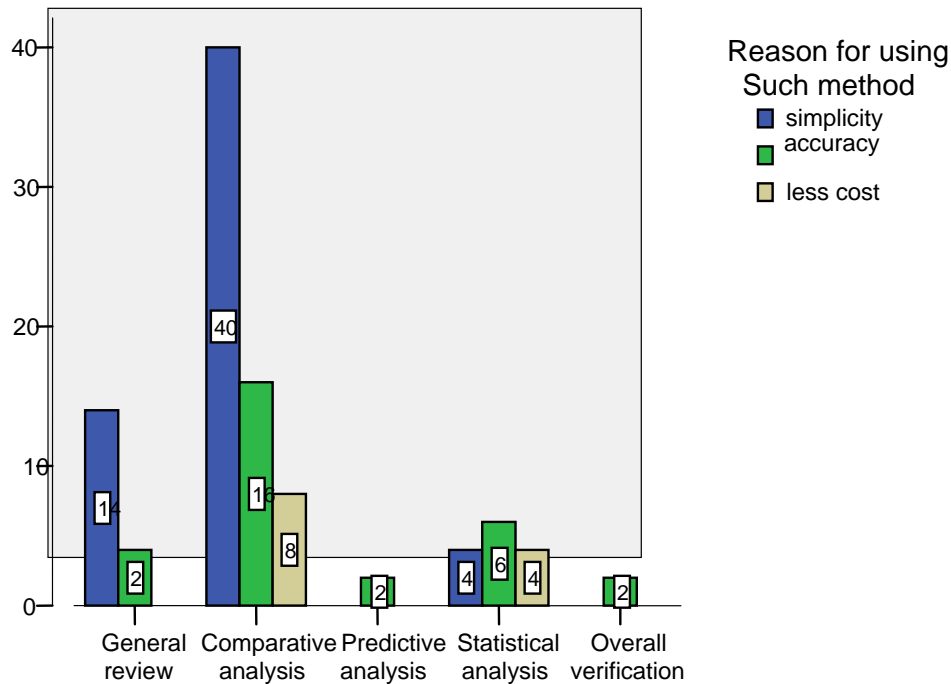
- Comparison of financial information with information with similar information regarding the industry in which an entity operates
- Study of the relationships of elements of financial information with relevant non financial information.

The selection and usage of analytical procedures to be used depends on the availability of the necessary information and resources. But mostly their benefit is inversely related with the cost and simplicity of applying them. For example, the type of analytical procedures which was listed first above is very simple and inexpensive to use but it lacks precision than the other methods especially in very dynamic environment like today's economic conditions. According to Blocher & Willingham (1985), precision in the context of analytical review refers to the degree of confidence the auditor has in the prediction from the analytical review, and it can be influenced by, the nature of the account, nature of the analytical procedure, and the accuracy of the data required. About 64 percent the auditors who filled the questionnaire responded that they use the above mentioned method because of its simplicity and its being cheaper.

Blocher & Willingham (1985), also mentioned that simple quantitative prediction models tend to out perform unaided human decision makers. This suggested that auditors should be cautioned about using strictly intuitive approach than focusing on simple models. OFAG's working manual also shows (appendix 3) that only 30 percent assurance can be obtained from using the comparative analysis technique. In addition, comparing data for only two periods can not be appropriate to have an accurate threshold amount with which

comparison will be made. This prove that the analytical procedure OFAG uses is not appropriate and this can also lead to same problem in other dependant audit procedures, like audit risk and sampling procedures.

Fig 4.4 method used for analytical review procedures



4.4.3. Sampling techniques used

The third factor considered in this sub section is the sampling technique used in audit. As audits are designed to generate reasonable, rather than absolute, assurance most audit conclusions are based on samples, rather than tests of the entire population. Sampling allows an auditor to draw conclusions about transactions or account balances without sustaining the time and cost of examining all available data. For a long period of time OFAG auditors have been using the stratified sampling technique. Under this type of sampling vouchers with birr values of greater or equal to one fourth of the materiality

level will be tested 100 percent and the remaining vouchers will be divided into strata's based on their birr value, i.e. arranged by ascending order as per their birr amount. Then, a sample of ten percent will be drawn from the smallest birr value strata and the sample size will increase by 10 percent for each of higher value strata's then after

But, there are two main problems the researcher identified in using this sampling technique. The first problem is the sampling technique does not take into consideration the audit procedures (elements) like audit risk and analytical procedures and even the materiality level which is used to determine high values (vouchers to be tested 100 percent) is based on only a given percent (0.5-2) of revenues or expenditures. Secondly, the sampling technique needs items in the strata to be homogeneous.

However, the researcher does not believe that birr value can always be a determining factor of homogeneity. Only 2 percent of the respondents from auditors believe that the internal control for small birr values is stronger than large birr values. In addition, as it is shown in table 3.2, 60 percent and 52 percent of the respondents from auditee's replied that more time will be devoted and more employees will participate, respectively, in processing large birr valued transactions than small birr valued transactions. But, only 22 and 18 percent of them responded the reverse. From this it can be concluded that the risk for large birr values being misstated is less than the risk for small values. So, the chance for a voucher to be included in the sample shall not only depend on its birr value.

| | | types of vouchers in which more officials(employees) participate | | | Total |
|--|----------------------|--|------------|----------------------|-------|
| | | large birr | small birr | both take equal time | |
| type of vouchers taking more time for processing | Percent | | | | |
| | large birr | 32 | 10 | 18 | 60 |
| | small birr | 8 | 8 | 6 | 22 |
| | both take equal time | 12 | 0 | 6 | 18 |
| Total | | 52 | 18 | 30 | 100 |

Table 4.2 birr values and related internal controls

Since recently, some auditors of OFAG started to use the monetary unit sampling (MUS) which considered audit risk, materiality and substantive procedures in a better way than stratified sampling. But Monetary unit sampling technique still gives a higher chance or probability of selection to high valued item (vouchers with large birr values) and a comparatively lower chance of selection to small valued items or vouchers, like the stratified sampling technique , and the same method is used for setting materiality.

4.5. Inappropriate design of assessment forms used

Professional judgment is the most important matter in auditing and is the primary reason auditors are engaged by others. Judgment is the intellectual function which differentiates a profession from a skilled occupation. Mostly, different types of formats will be used in order to help the auditor stimulate his judgmental activities. Some of the formats used are internal control questionnaires; risk assessment forms and analytical review procedures

assurance forms. In this section, the researcher has identified the limitations of the inherent risk assessment form and analytical review procedures assurance form even if the problem can be inferred to the other formats.

5.5.1. Inherent risk assessment form

Inherent risk assessment form is used as a guide to assist the auditor in determining an appropriate level of audit risk for the audit. Inherent risk needs to be assessed for each specific financial statement assertion and each related compliance with authority objective for each component, assuming there are no internal controls in place. The form prepared by OFAG calls for the auditor to assess various factors as “high”, “moderate” or “low” risk. The form allows auditors rank the risk for the above factors as 60, 50 and 40 percent, respectively. That is, the highest inherent risk will be 60 % and 40% being the lowest. But only 24 percent of the auditors responded that the inherent risk can not be greater than 60 percent and only 26 percent respondents agreed on lowest inherent risk.

4.5.2. Analytical review procedures form

The analytical review procedures form is used as a guide to assist the auditor in assessing the amount of assurance that the auditor can obtain from applying a particular analytical procedure. The auditor first notes the category of analytical procedure that he/she intends to use – comparative analysis, predictive analysis, etc mentioned above. The auditor then evaluates each factor as to whether, for his/her particular procedure, the factor indicates a higher level of assurance (H) or a lower level of assurance (L). After all the factors are evaluated, the auditor determines, using his/her professional judgment, the amount of

assurance to be obtained for the specific financial statement assertion or related compliance with authority objective being considered. The main problem in using this form is it has only two alternatives; there is no alternative even for a person who is in dilemma between high and low assurance level.

4.6. Lack of the necessary support at field

The actual work of audit will be made at the execution stage which is performed at field. The social, economic and technological progress of recent decades can force auditors to give due professional care in conducting their task. In order to achieve what was planned the audit team sent to a given organization must be given the necessary support and be supervised regularly. Supervision is described in SAS no. 22 as the process of directing the effort of assistants in conjunction with the objectives of the audit and determining whether the objectives are achieved ²⁹.

The researcher used four elements in order to identify whether the auditors were facing challenges at field. According to the questionnaire response, as shown in the table below, 78 percent of respondents argued that there is no orientation given on how to perform a given engagement. 88 and 71 percent, respectively, respondents responded that there is no regular supervision and clear field work division. And still, 76 percent of them mentioned that the organization has no method of measuring whether a specific audit technique used is effective or not. (See table 4.3)

²⁹ Auditing Standards Executive Committee, SAS no. 22 “ Planning and supervision”, 1978, Washington

| | Orientation before each engagement | Regular supervision | Clear work division at field | Method of measuring a specific audit technique used |
|-----------------|---|----------------------------|-------------------------------------|--|
| Response | % | % | % | % |
| yes | 22.0% | 12.0% | 25.0% | 16.0% |
| no | 78.0% | 88.0% | 71.0% | 76.0% |
| I don't know | | | 4.0% | 8.0% |

Table 4.3 summaries of responses on challenges faced at the time of actual investigation

4.7. Inadequate compensation for auditors

Adequate compensation for auditors can be another factor that can help them do their activities with good motivation. According to Kenneth and Rick (1998) inadequate compensation, on the other hand, can have the following consequences:

- ✚ Difficulty to attract new talent
- ✚ Difficulty to retain the most talented
- ✚ Difficulty to motivate performance
- ✚ Promote regular compensation surveys/adjustment
- ✚ Identify alternative compensation strategies
- ✚ Alternative forms of recognition

The response collected from auditors shows that only two percent of them were satisfied with their current salary and the remaining 98 percent were not. Further more, 88 percent of the respondents replied that there is no compensation provided other than salary, as shown in the table below.

| | | compensations other than salary | | Total |
|-------------------------------------|-----|------------------------------------|----|-------|
| | | yes | no | |
| percent | | | | |
| Satisfaction with salary | yes | 0 | 2 | 2 |
| | no | 12 | 86 | 98 |
| Total | | 12 | 88 | 100 |

**Table 4.4 auditor’s satisfaction with salary and other
compensations**

4.8. Lack of independence

The independence of governmental auditor’s and clear agreement about the scope of their auditing role are necessary in audit. To be effective any external auditor must be devoid of accountability to, or susceptible to pressures from, the clients or institutions being audited. In this case, the client is the house of people’s representatives (the legislative organ) and the auditee is the government (the executive organ). If an auditor is going to audit the government, it must have the authority to do so it’s job without threat of retaliation and the power to proceed with its plans. In Ethiopia, the government is the

party holding the majority of the members of people's representatives. So, it can be possible to say that the client and the auditee can have common interest together and the client may not be perfect in taking the necessary measures on the auditee. Besides this, according to an interview made with two senior auditors, OFAG auditors were being governed by same ethical, salary and employment rules and regulations used for government employees. What's more is that there is no clear mandate which shows how an auditee will be penalized for its fault and other actions to be taken.

4.9. Lack of experience sharing activities with other organizations

International, national, regional or local exchange of ideas, knowledge and experience is an effective means of raising the quality of audit, harmonizing standards, sharing best practices and generally helping audit organizations to fulfill their mandate. In addition to experience sharing activities made between them selves, government auditors need to liaise closely with other government organizations or agencies in order to ensure that skills and insights are shared. But, only eight percent of questionnaire respondents (auditors) have got the chance of sharing experience with other similar or different organization(s).

4.10. Expectation gap

According to Mary (2008) expectation gap is the gap between the auditors' actual standard of performance and the various public expectations of auditors' performance.

Members of the public may expect that:

- Auditors should accept primary responsibility for the financial statements,
- Auditors 'certify' financial statements,
- A 'clean' opinion guarantees the accuracy of financial statements,
- Auditors perform a 100% check,
- Auditors are supposed to detect fraud.

According to the auditing profession, the reality is that:

- Management, as preparers of the financial statements, is primarily responsible for their content
- An audit only provides reasonable assurance that financial statements are free of material misstatement.
- Auditors are only required to test selected transactions - it does not make economic sense, in to-days world, to check all transactions; and
- Although auditors plan and conduct an audit engagement with an attitude of professional skepticism recognizing that circumstances such as fraud may exist that will cause the financial statements to be materially misstated, an audit does not guarantee that fraud will be detected.

| | | Auditor takes primary responsibility for financial statements | Audit is a guarantee that fraud will be detected | Auditors expected to check all transactions | An audit can reduce (eliminate) corruption |
|----------------------|-------|---|--|---|--|
| Response in % | yes | 20.0 | 60.0 | 30.0 | 80.0 |
| | no | 80.0 | 40.0 | 70.0 | 20.0 |
| | Total | 100 | 100.0 | 100.0 | 100 |

Table 4.5 expectation gap

As the table above shows about 20 percent of the auditee's still believe that the primary responsibility for the financial statements goes to the auditors and same percent of them responded that an audit can not reduce (eliminate) corruption. More over, about 60 and 30 percent of the respondents, respectively, believe that auditors are supposed to detect fraud and check all transactions. As much as possible these gaps must be narrowed to the minimum level possible, since they can hinder the auditor's work by reducing audit satisfaction of the public.

4.11. Media exposure for audit results

The media can play a significant role in enhancing the role and public stature of an audit organization. Audit institutions can establish a good working relationship with the media to convey essential audit findings and recommendations. Since politicians are highly interested in media, audit findings highlighted in media presentations are likely to take the attention of the parliament.

The media can also play a large role in shaping the public's attitude towards the audit service, increasing the auditor's reputation for competence, independence and fairness. According to interviews made and questionnaire responses obtained from auditors, OFAG's do not work in harmony with public media's, except the cases in which news will be presented to the public when annual reports were made to the parliament.

To summarize, the findings of this study show that the auditors of the office of the federal auditor general face different challenges in conducting their activities. Lesser opportunity of education; lack of training ,supervision ,orientation, clear work division , enough compensation, independence, experience, media coverage; restricted information access; inappropriate methods and formats used ;and expectation gap are among the challenges identified. The fifth chapter presents the summary of the overall project work, the conclusions arrived and the recommended points

Chapter five

Summary, conclusions and recommendations

The social, economic and technological progress of recent decades has radically transformed the framework in which governments operate and deliver their tasks, as well as the way the public at large see the role of the state. Governments are expected to provide service at higher quality, effectiveness and efficiency, and without delay in order to meet the rising needs of the public .In response to this trend, public administrations have started implementing reforms that are designed to enhance their public image and are adopting modern, transparent, goal and service-oriented a well as more efficient approaches to government management. Governmental audit institutions are also expected to be competent enough in order to help government achieve it's objective and improve the reliability of their information by it' users. This chapter presents summary of the over all project work, conclusions made and recommendations given.

5.1. Summary

The national agencies responsible for auditing government revenue and spending are called Supreme audit institutions (SAIs). Their primary purpose of SAIs is to oversee the management of public funds and the quality and credibility of the government's financial reporting. The main objective of this study was to identify challenges faced by Ethiopian federal government public auditors in discharging their responsibilities, and

recommending on the actions to be taken in minimizing or eliminating these challenges. The study focused on financial auditors of the Office of the Federal Auditor General (i.e. the SAI of the country), in particular.

In order to achieve its objective the study used both qualitative and quantitative data collected using interviews, questionnaires, observations and review of secondary data. Samples were drawn and individuals from both the audit institution and auditees were filled questionnaires and interviews were made with supervisors (senior auditors), divisional heads (audit managers) and department heads (audit directors). In addition observations of field works and reviews of different working materials were made.

The collected data were organized and the necessary summaries and preparations were made in the form tables, charts and graphs using Statistical Package for Social Sciences (SPSS). Mainly descriptive types of analysis were made and the challenges facing the auditors under consideration were identified and presented one by one. The following conclusions are (presented below) drawn based on the findings.

5.2. Conclusions

According to the analysis made above in the fourth chapter the researcher has identified large number of challenges which were generally classified in to eleven.

One of the problems (challenges) encountering auditors of OFAG have been the lack of an opportunity to pursue education. About 68 percent respondents argued that there is no incentive made helping them improve their educational level and there is no positive

relationship between the employees' educational level and their experience, showing employees who stayed a long are still found at low educational level than new recruits. Most of the auditors also responded that there is lack of training on technologies and regulations related to their profession.

The study identified that there are problems in collecting the necessary information and timely delivery of information by auditee's is very much poor. The procedures used in setting materiality; the method used for analytical review of procedures; the sampling techniques; risk assessment forms ; and analytical review procedures assurance forms used lack precision and were not appropriate in considering actual and national factors.

It is noted in the findings that auditors at field were lacking orientation on how to perform a given engagement, regular supervision, clear field work division and method of measuring how effective they are. The response collected from auditors shows that 98 percent of them were not satisfied with their current salary and only eight percent of auditors have got the chance of sharing experience with other similar or different organization(s).

The findings also indicated that the government system and lack of effective mandate where lead to problems of independence. And, as a final point, the finding presented that public expectations of auditors' performance were different from the standard of performance, leading to an expectation gap, and the habit of working with public media's to narrow this gap is very near to the ground.

5.3. Recommendations

The following points were recommended in order to help office of the Federal Auditor General minimize (or eliminate if possible) the challenges faced by its auditors and achieve its objectives of serving the public.

1. In order to minimize the challenges related to pursuing education, its better if OFAG tries to work in harmony with educational institutions, like universities and colleges from with in and foreign countries. In addition to providing educational opportunities, these educational institutions can help OFAG by considering their curriculum in relation to audit needs and giving short term trainings.
2. Governmental audit institutions are not expected to be late in using current technologies and new systems. Instead, they can be called upon to assess the strengths and weaknesses of these new systems or technologies adopted and prevent ill-directed developments. They need to adjust their audit work to the new ways in which government operates and align their audit methods and standards accordingly. In this case, it is advised that it is better if new technologies and systems are adopted and used by OFAG earlier than other governmental organizations.
3. The value and benefit of specific and overall audit techniques performance should be assessed objectively and soundly, and become measurable and comparable by international standards.

4. After considering benefits of possible solutions/mitigation techniques and comparing benefits to implementation costs, including possible impacts on budgets, audit plans, staffing levels, and training requirements; it's vital if revisions shall be made on audit techniques used in planning an audit.

In setting materiality, it is advisable if the factors considered in this paper and others(if any) can be included and weighted based on their importance. The precision of analytical procedure used can also be increased with out sacrificing much cost. Using statistical techniques (for example regression analysis) and increasing the number of years considered in the calculation can increase the reliability of the procedures used. It is also advisable if the sampling techniques can be based on identifying and ordering possible risky areas (e.g. projects, departments, etc.) and drawing more samples from more risky ones and less from less risky areas.

5. The formats and other working papers shall be regularly reviewed, corrected and updated in a way which can increase the accuracy of the auditor's judgment. In order to reduce judgmental errors it is advisable if alternate choices can be increased (for example; setting very high , high, moderate, low, and very low instead of high and low only)
6. In today's world no one organization can or should go it alone. Because many government organizations face common challenges, learning from each other will have a great value .By working together, different audit organizations can share in

each other's successes and avoid each other's mistakes. So, it is advisable if OFAG cooperate with various audit institutions found in and out of the country.

7. Auditors shall be adequately paid and trained. To ensure high quality of work, OFAG need to ensure the continuous development of its staff and it needs to employ qualified staff, remunerate them adequately and secure their retention.
8. Regular supervision and orientation, and clear work divisions are necessary as they can increase the effectiveness and efficiency of the auditors and increase the quality of field work. Measures should be taken to insure that the work performed by each member of the audit staff is reviewed by more senior persons to insure that it was adequately performed and enable a proper assessment to be made of the work performed.
9. Working with Medias and increasing the awareness of the public can help in reducing the challenges related to data collection, expectation gaps and independence.
10. Finally the research topic under study is broad and each of the topics mentioned as challenges can be further researched. So it is advisable if future researchers be concerned to each of the items under this study and specially the technical aspects need more attention.

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