



Conference of Public Sector Internal Auditors of the Republic of Slovenia

Conducting Performance Audits in the Public Sector

Approach, Methodology and Experience of the IAS

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Agenda

1. What is the role of the European Commission and its Internal Audit Service?
2. Reasons for, and the contribution of, performance audit to the core responsibilities of the IAS
3. The IAS definition of performance auditing and general approach
4. Outline of EC's performance audit methodology
 - The 4 pillars
5. Indicative findings of completed performance audits: Examples of common elements
6. Your Questions !



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What is the Role of the European Commission and its Internal Audit Service (IAS)?



What is the Role of the European Commission?

“Executive” of the EU

- Manages the **EU Annual Budget**, together with the Member States
 - 2019: 166 billion Euro
 - Part of a multi-annual financial programming framework (MFF 2014-2020)
- Implements **non-spending policies**
 - Internal Market
 - Competition, State Aids
 - Trade policy



EU budget – Pyramid of Key Actors



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Article 319 Treaty on the Functioning of the EU (TFEU)

1. The European Parliament, acting on a recommendation from the Council which shall act by a qualified majority, shall give a discharge to the Commission in respect of the implementation of the budget /.../

**EUROPEAN
PARLIAMENT /
COUNCIL**

**EUROPEAN COURT OF
AUDITORS (ECA)**

Article 287 TFEU

1. The Court of Auditors shall examine the accounts of all revenue and expenditure of the European Union. /.../
The Court of Auditors shall provide the European Parliament and the Council with a statement of assurance as to the reliability of the accounts and the legality and regularity of the underlying transactions /.../
This statement may be supplemented by specific assessments for each major area of Union activity.

Article 317 (TFEU)

The Commission shall implement the budget /.../ on its own responsibility and within the limits of the appropriations, having regard to the principles of sound financial management.

COMMISSION

**Directorates-General
(DGs)**

**MEMBER STATES /
THIRD COUNTRIES / AGENCIES**

**Regions / Programmes /
Projects**

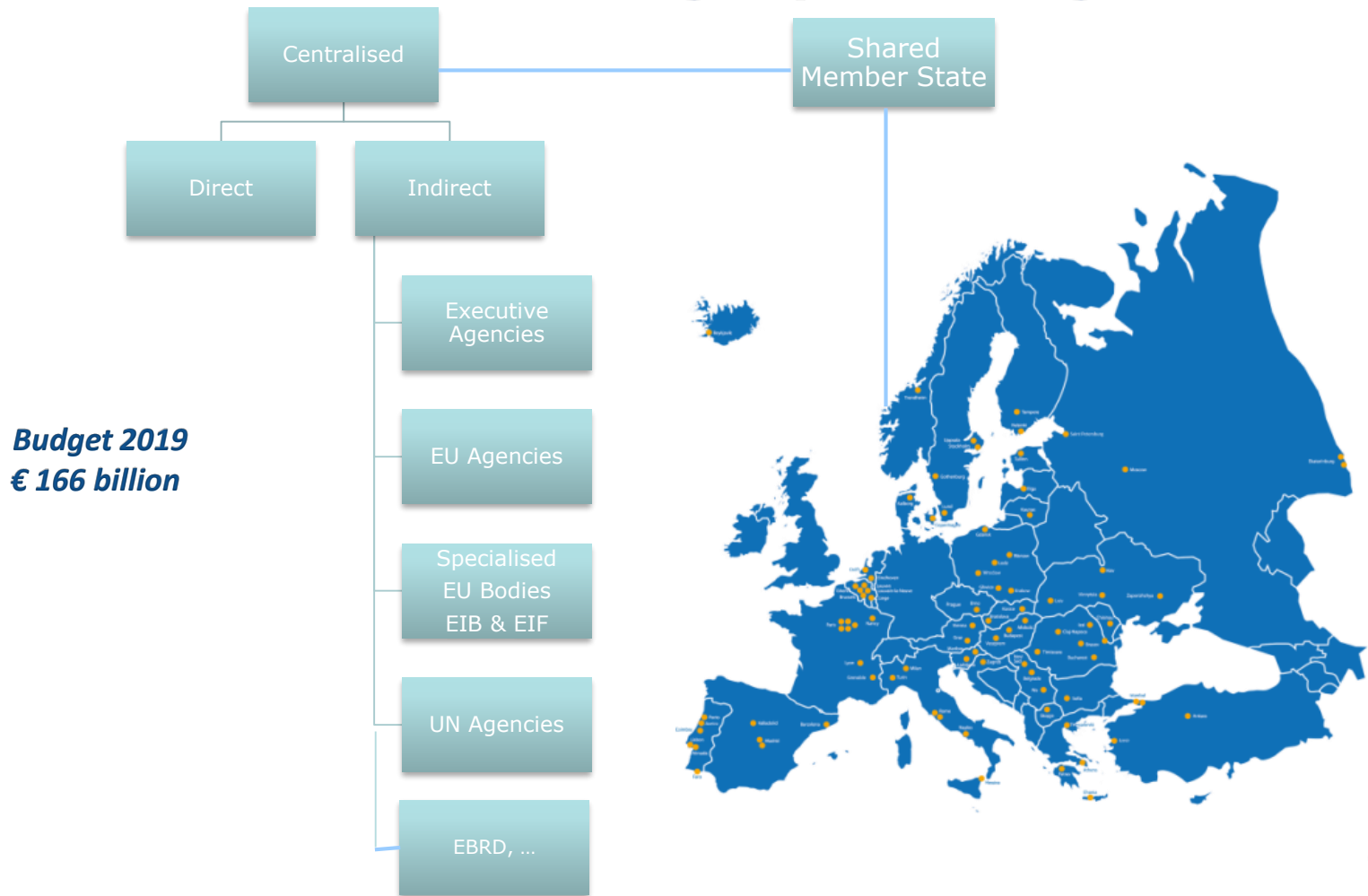
Article 317 TFEU

Member States shall cooperate with the Commission to ensure that the appropriations are used in accordance with the principles of sound financial management.



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European Commission Supervision of the Implementation of the EU Budget per Management Mode



What is the Role of the European Commission's Internal Audit Service (1)?

- The European Commission's internal audit function
- 160 staff, 73% of these are certified internal auditors!
- 90 different auditees (European Commission's Directorates-General and EU agencies)
- Three year strategic audit plan
- About 90 financial, compliance, performance and other audits per year plus consulting engagements
- Recommendations for improving risk management, control, and governance



What is the Role of the European Commission's Internal Audit Service (IAS)(2)?

- As per the EU Financial Regulation, IAS audits the internal management and control systems in the:
 - European Commission
 - Executive Agencies (6)
 - European External Action Service
 - Decentralised EU Agencies (30)
 - Other autonomous bodies (11)
- Through its audits, IAS provides independent and objective assurance to the College of Commissioners and audited entities aiming at
 - Adding value
 - Improving the operations
- Upon request from the College of Commissioners or Director Generals (DGs), IAS provides consultancy services





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Reasons for performance audit in the EC



Reasons for performance audit in the EC

- Increased focus of the Commission on performance management and performance measurement
=> Achieve its objectives with evermore scarce resources
- Increased focus of External Audit body (ECA) and European Parliament on the performance of the EC's DGs and Services
=> Spending must achieve its policy objective, not just comply with the rules
- Stakeholders' expectations
=> Not only compliance but also performance-oriented assurance

IAS Increased Focus on Performance and Comprehensive Audits

The IAS Strategic Audit Plan 2019-21 covers the following two main strands*

- 1. Audits addressing Compliance/Financial Risks*
- 2. Audits addressing Performance risks*

Audits covering both elements and are known as Comprehensive Audits

- Performance and Comprehensive Audits comprise c.90% of planned engagements 2019-21*
- Some 48% of planned audits focus on Strengthening the performance focus Commission wide*

** Others; IT Audits, limited reviews, follow up audits, consulting*

Addressing Stakeholder Expectations

Assurance and accountability chains determine:

- Key stakeholders

- Management
- Audit Committee
- Parliament
- External Auditor
- Staff



- Key expectations of Internal Audit

- Assurance and/or advice
- Subject matters to be covered
 - ✓ Financial issues
 - ✓ Compliance issues
 - ✓ **Performance issues**
 - ✓ Governance issues
- Type of reporting





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EC's definition of performance auditing and general approach



IAS' definition of performance auditing*

Performance auditing is an independent and objective assessment of an entity's activities, processes, internal controls systems, governance and risk management, with regard to one or more of the three aspects of economy, efficiency and effectiveness, aiming to lead to improvements.

** This definition is based on that of the European Court of Auditors, adapted to the needs of the internal audit profession and the EC environment*

Performance audit (PA) results:

Performance audit reports must include an overall assessment on how satisfactory is the performance of the audited entity/process/activity with regard to one or more of the **3 E's** (sound financial management):

- **Efficiency** – relationship between resources employed and results achieved (inputs vs output)
- **Effectiveness** – are the intended results achieved or specific objectives attained?
- **Economy** – resources available on time, in appropriate quantity and quality and at the best prices

Performance audit is NOT:

- Performance management/measurement
- Business Process Reengineering (BPR)
- Evaluation
- Impact assessment

**Management
responsibility**

What Performance audit in the EC covers and does not cover

Performance audit covers:

- Auditee's activities, processes and internal control systems (how the auditee organises the achievement of its objectives in line with mission of IAS as stipulated in the Financial Regulation applicable to the EU budget)
- European Commission's DGs/Services

Performance audit does not cover:

- Direct assessment of the *impact of policies and programmes* on society at large (= evaluation)
- Implementing bodies (Member States authorities, third countries authorities) and beneficiaries (outside scope of IAS mandate)

Performance audit approaches

- **DIRECT APPROACH**

Examine directly the (internal) performance of the EC's services in terms of input, output, results.

The IAS assesses whether the EC's DGs/Services/other Bodies soundly manage their resources.

- **INDIRECT APPROACH**

Examine the external performance (achievement of programme objectives) through the assessment of the adequacy of policies and procedures to monitor and evaluate performances.

The IAS assesses how the DGs/Services measures the achievement of the programme objectives for which they are responsible.

The indirect approach is used most often due to the lack of performance measurement systems and clearly identified benchmarks.



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Outline of EC's Performance audit methodology – 4 pillars

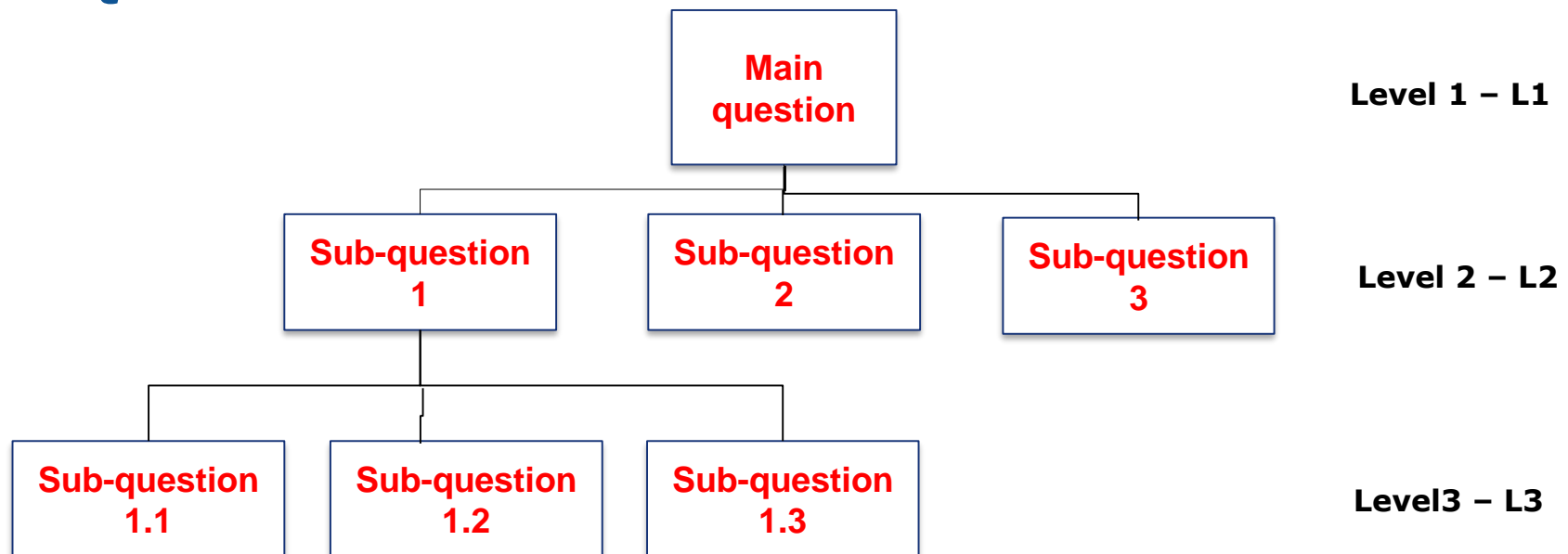


The Tools/Pillars of the IAS PA methodology

Audit process phase	Tool	Objective
Preliminary survey and fieldwork	Question tree approach	Definition of the objective and scope of the audit as the Main Question the audit should answer, breaking it down into detailed sub-questions
	Audit criteria	To guide the fieldwork and the identification of findings using standards against which the performance is compared/assessed
Reporting	Drafting plan (optional)	To summarise the results of the fieldwork and consolidate the replies to the audit sub-questions to reply to the main question (basis of the audit conclusion)
	Audit conclusion	Overall assessment of the conditions found during the audit drafted in a narrative and balanced way (no standard statement)

1st pillar: The question tree

The objectives of the audit are defined under the form of "questions" the audit should answer. The overall objective is set out in the form of a **main question the audit has to answer** (L1) and further detailed in sub-questions (L2, L3, Lx), so to form a **"Question tree"**



Example of question tree:

L1

Does DG XX have adequate performance measurement systems in place for monitoring, reporting and evaluating the performance of activities both in terms of its day to day, operational and administrative activities (internal) and in terms of measuring the delivery of policy objectives (external)?

1. Internal dimension

1.1. Have SMART objectives and RACER KPI been set ?

1.2. Does the DG adequately monitor and measure the performance of its activities (including the use of HR)?

1.3. Does the DG adequately report on the performance of its activities?

2. External dimension

2.1. Have SMART objectives and RACER KPI been set ?

2.2. Does the DG adequately monitor the delivery of the policy/programme

2.3. Does the DG perform adequate evaluation activities ?

2.4. Does the DG adequately report on the delivery of the policy/ programme?

L2

2nd Pillar: the audit criteria

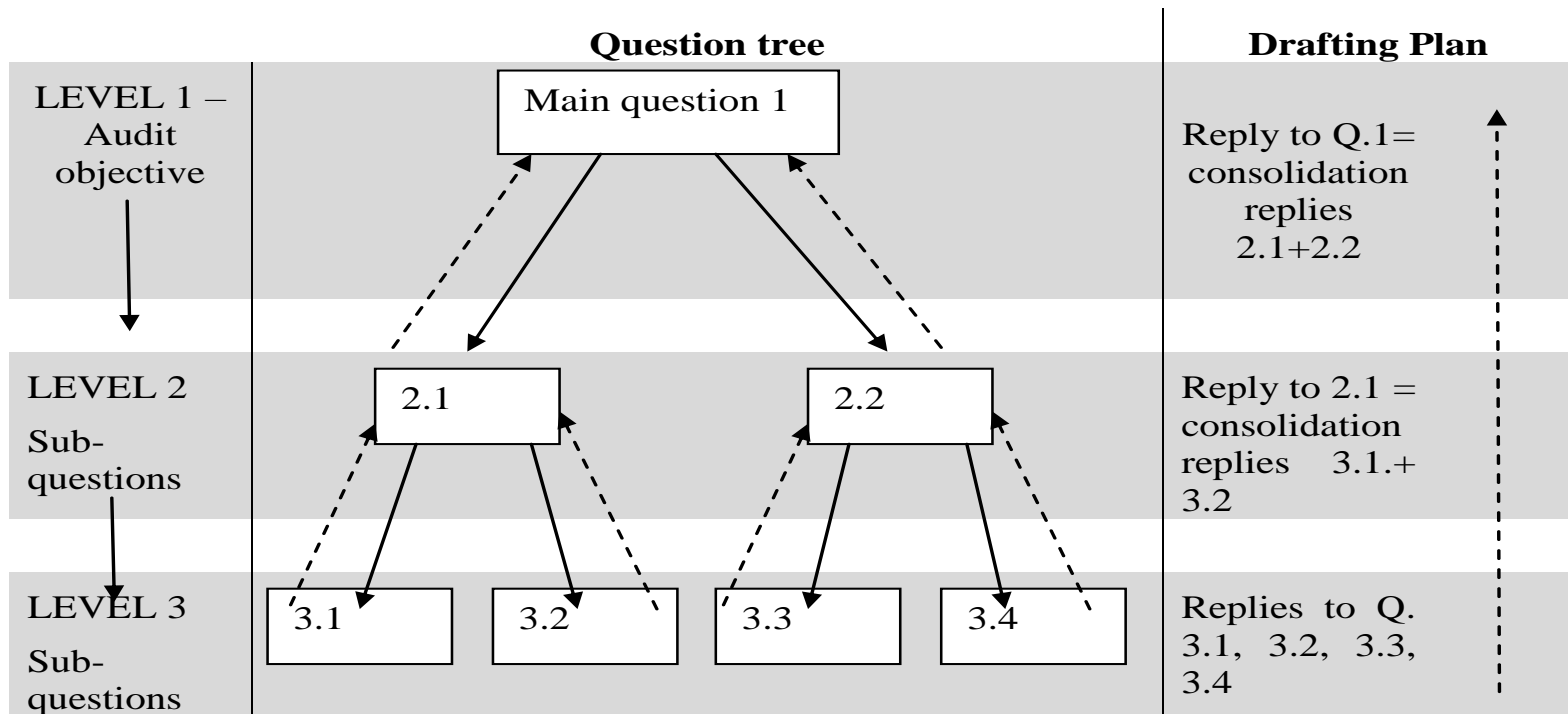
Audit criteria are "*standards against which the actual performance is compared or evaluated*".

They set the "expected level" in terms of:

- *what should be* according to laws, regulations, internal policies, objectives or target defined by the organisation;
- *what is expected* according to sound principles, scientific knowledge and best practice
- *what could be* (given better conditions)

By comparing the actual situation with the identified target (*what is*), they allow assessing whether or not an activity is properly performed.

3rd pillar: Question tree to audit conclusion: Bottom-up approach for the audit conclusion



4th pillar: the audit conclusion

- Used in the context of *performance audits* or integrated audits
- No standardised statement but the ***answer to the main audit question*** (the “audit objective”)
- Narrative description of the result of the audit, including both the positive elements and the areas for improvement (***balanced conclusion***, not exception-based)
- Describe circumstances and context to arrive at a specific conclusion
- No audit jargon

Applicable Audit Standards

IIA Standard - 2410 Criteria for Communicating

Communications should include the engagement's objectives and scope as well as applicable conclusions, recommendations, and action plans.

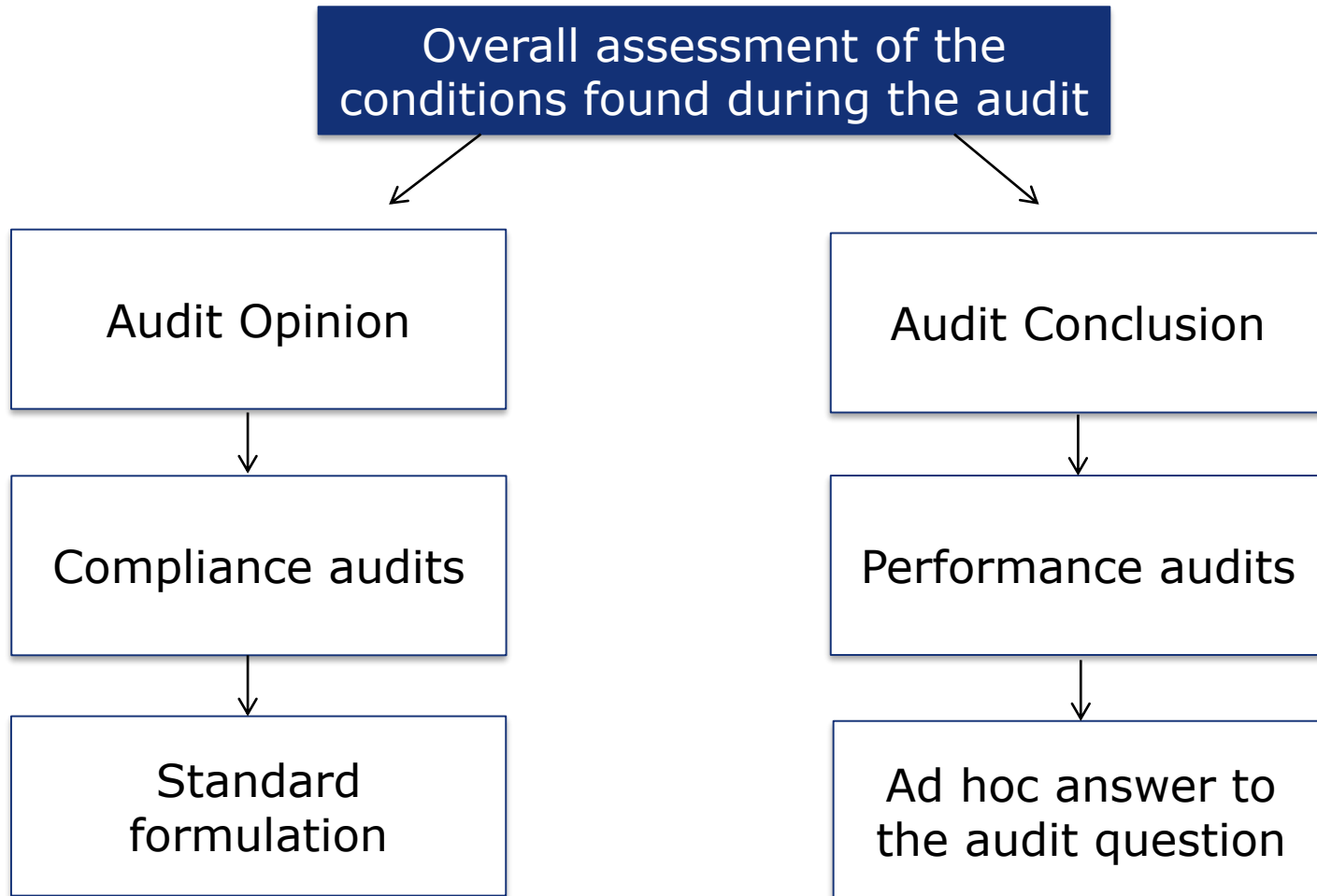
ISSAI 3100 - Performance Audit Guidelines – Key principles

The auditor is not normally expected to provide an overall opinion on the achievement of economy, efficiency and effectiveness by an audited entity in the same way as the opinion on financial statement. Where the nature of the audit allows this to be done in relation to specific areas of an entity's activities, the auditor is expected to provide a report which describes the circumstances and context to arrive at a specific conclusion rather than a standardised statement"

A recent example: Audit Conclusion

While acknowledging the steps already taken, the IAS concludes that the performance measurement system put in place by DG X to monitor, report and evaluate the performance of XXX needs to be significantly enhanced to strengthen its effectiveness, notably with regard to the lack of indicators on the economic and efficient use of the operating grant. In this context, the IAS has identified the following three Very Important issues:
[...]

Audit opinion versus audit conclusion





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Indicative findings of completed performance audits: examples of common elements



Management planning and annual reporting cycle

Setting of objectives and indicators:

- Links not well explained between objectives set at the general policy area level and at the specific operational level, insufficiently clear linking of specific objectives with EU strategic objectives and no clear objectives for the services' own day-to-day activities which contribute to the achievement of specific objectives.
- Performance indicators do not meet the widely accepted RACER criteria and in some cases can be more numerous than needed and/or insufficiently targeted according to need.

Internal performance measurement systems:

- Insufficient real central guidance to the services on how to develop an internal performance measurement framework.
- Reporting on performance by services to their senior management does not always cover all relevant activities and the associated indicators are not always appropriate or adequately prioritised.

Human resource management

- Lack of a common and comparable base to take account of workload assessments and/or skills surveys in order to prepare for future changes in HR.
- Lack of strategy (Incl. performance indicators) on HR management , weaknesses in regular monitoring of HR issues and HR needs (in both qualitative and quantative terms).
- Allocation of HR being aligned with business priorities is not always supported by the necessary tools and methods to gather the related information (workload assessment, jobs/skills mapping, HR plan).

Questions, Conclusions, and Closing Remarks



Thank you for your attention and participation!

