

UNIVERSITY OF LJUBLJANA
SCHOOL OF ECONOMICS AND BUSINESS

UNIVERSITY OF SARAJEVO
SCHOOL OF ECONOMICS AND BUSINESS

MASTER'S THESIS

**THE ROLE OF PERFORMANCE AUDIT IN
MITIGATING THE PRINCIPAL–AGENT PROBLEM IN THE GOVERNMENT:
THE CASE OF YOUTH EMPLOYMENT PROGRAM
IN THE FEDERATION OF BOSNIA AND HERZEGOVINA**

Ljubljana, November 2019

HAZIM ŠABANOVIĆ

AUTHORSHIP STATEMENT

The undersigned Hazim Šabanović, a student at the University of Ljubljana, School of Economics and Business, (hereafter: SEB LU), author of this written final work of studies with the title The Role Of Performance Audit In Mitigating The Principal–Agent Problem In The Government: The Case Of Youth Employment Program In The Federation Of Bosnia And Herzegovina, prepared under supervision of prof. dr. Meliha Bašić

DECLARE

1. this written final work of studies to be based on the results of my own research;
2. the printed form of this written final work of studies to be identical to its electronic form;
3. the text of this written final work of studies to be language-edited and technically in adherence with the FELU's Technical Guidelines for Written Works, which means that I cited and / or quoted works and opinions of other authors in this written final work of studies in accordance with the FELU's Technical Guidelines for Written Works;
4. to be aware of the fact that plagiarism (in written or graphical form) is a criminal offence and can be prosecuted in accordance with the Criminal Code of the Republic of Slovenia;
5. to be aware of the consequences a proven plagiarism charge based on the this written final work could have for my status at the FELU in accordance with the relevant FELU Rules;
6. to have obtained all the necessary permits to use the data and works of other authors which are (in written or graphical form) referred to in this written final work of studies and to have clearly marked them;
7. to have acted in accordance with ethical principles during the preparation of this written final work of studies and to have, where necessary, obtained permission of the Ethics Committee;
8. my consent to use the electronic form of this written final work of studies for the detection of content similarity with other written works, using similarity detection software that is connected with the FELU Study Information System;
9. to transfer to the University of Ljubljana free of charge, non-exclusively, geographically and time-wise unlimited the right of saving this written final work of studies in the electronic form, the right of its reproduction, as well as the right of making this written final work of studies available to the public on the World Wide Web via the Repository of the University of Ljubljana;
10. my consent to publication of my personal data that are included in this written final work of studies and in this declaration, when this written final work of studies is published.

Ljubljana, November 05th, 2019

Author's signature:  _____

TABLE OF CONTENTS

INTRODUCTION.....	1
1 THE PRINCIPAL-AGENT THEORY.....	5
1.1 Introduction of the principal–agent theory	5
1.1.1 Development of the principal–agent theory.....	5
1.1.2 Principal–agent problem and its implications.....	9
1.1.3 Interests alignment mechanisms and associated agency cost	11
1.1.4 Asymmetric information.....	12
1.2 Applying the principal–agent model in the public sector	13
1.3 The impact of the principal–agent problem on the information flow	15
1.4 The role of the audit function.....	19
1.5 Summing up the theoretical review into an analytical framework	23
2 RESEARCH METHODOLOGY	26
2.1 The case study method.....	26
2.2 Qualitative content analysis method	28
2.3 Case study with qualitative content analysis method	29
2.4 Main research questions and analytical matrix	31
3 CASE STUDY: THE YOUTH EMPLOYMENT PROGRAM	32
3.1 The context in which the Program is implemented	32
3.2 Introduction of the Youth Employment Program	33
3.3 Program planning.....	35
3.3.1 Changing the Program goals.....	37
3.3.2 Changing the target group.....	37
3.3.3 Changing of the participation criteria for the Program.....	39
3.4 Program implementation.....	41
3.5 Outcome of the Program.....	43
3.6 Agency reporting about the Program implementation.....	44
3.7 Reporting By The Audit Office	46
3.7.1 Annual audits of the institutions in the principal–agent delegation chain	46
3.7.2 Performance audit	48
3.8 Implementation of the Audit Recommendations	50
3.9 The Main Research Findings	52
3.9.1 The goals and objectives.....	53
3.9.2 Implementation	54
3.9.3 Reporting.....	55
3.9.4 Audit reports	55
3.9.5 Corrective measures.....	56
CONCLUSION	57
REFERENCE LIST.....	60
APPENDIXES	69

LIST OF FIGURES:

Figure 1: Principal - Agent Framework	14
Figure 2: Employment Rate Percentage During the Program Implementation Period.....	43

LIST OF TABLES:

Table 1: Causes and Effects of the Principal–Agent Relationship in the Public Sector.....	25
Table 2: Components of the Case Study Design.....	29
Table 3: Analytical Framework Matrix for Qualitative Analysis of the Case Study.....	31
Table 4: Definitions of the Program Goals Throughout the Delegation Chain	36
Table 5: Target Group in the Annual Plans of the Federation Agency.....	38
Table 6: Overview of the Target Groups and Allocation of Funds	42
Table 7: Financial and Compliance Audit Opinions in the Observed Period.....	46
Table 8: Percentage of the Implementation of Audit Recommendations (%)	51
Table 9: Matrix with Qualitative Analysis Results	53

LIST OF APPENDIXES:

Appendix 1: Povzetek (Summary in Slovene language)

Appendix 2: Research Design Matrix

Appendix 3: Federation Agency annual plans and reports analysis

LIST OF ABBREVIATIONS:

BAM – Bosnian Mark (monetary unit)

BiH – Bosnia and Herzegovina

BSc – Bachelor of Science

FBiH – Federation of Bosnia and Herzegovina (entity within Bosnia and Herzegovina)

INTOSAI – International Organization of the Supreme Audit Institutions

ISSAI – International Standards for Supreme Audit Institutions

MP – Member of the Parliament

MSc – Master of Science

RS – Republic of Srpska (entity within Bosnia and Herzegovina)

SAI – Supreme Audit Institution

PhD – Doctor of Philosophy

UNDP – United Nations Development Program

INTRODUCTION

The principal–agent problem is an inherent problem of conflicting interests between different levels in a vertical management structure. Agents' own interests are not in line with those of their principals, their goals and objectives are different, and their actions and undertakings are not always harmonised. Agents have a better insight into the state of affairs within the area that principals entrusted them with, and they have a better expert knowledge about the area they practically work in. This puts them in an advanced position compared to their principals, and they are better able to pursue their own interests. This is the problem of asymmetric information. The principal–agent theory stems from this intricate relation and it has for many decades been an inevitable part of economic and management studies. Without its contribution, explaining problems in industrial economics would hardly be possible.

Function of internal and external audit is an important tool aimed at mitigating the problems of these relations, by providing the shareholders, as principals, with a proper insight into the state of affairs within the company they own and for which they hired an agent to manage it. This thesis is based on the same logic applied in the public sector.

The general government can be described as a chain of principals and agents, from the parliament on top, with members elected directly by the citizens, who in this structure are the top principals, to the cabinet with its ministries – appointed by the parliament as their agents, further down to the agencies, their managers and finally, to the bureaucrats providing services to the citizens. The principal–agent problem inherent in this structure can cause problems in the management process and impede achieving of the general government goals and objectives. In this context, the role of the supreme audit office (sometimes referred to as national audit office), and the performance audit function within it, is to help provide a full insight into the state of affairs within the government and evaluate its effectiveness, economy and efficiency. This thesis will add some value to understanding how this is done, and more specifically, how can the performance audit help mitigate the problem arising from the principal-agent relations within the government.

Two main objectives of this thesis are to show how the problem of principal–agent relation can contribute to government ineffectiveness and inefficiency, and to show how the performance audit can mitigate this problem by providing principals with a full insight into the state of affairs within the public sector. Lack of such an insight puts principals in an inferior position where they are unable to exercise their full control over the agents' activities. By identifying and reporting about the main causes of the failure to achieve the set goals and objectives, the performance audit provides principals with a full set of information, and offers them an opportunity to request concrete corrective measures from their agents. This way, the performance audit helps mitigate the principal-agent problem.

According to Gustavsson (2015, p. 19), in our contemporary world "almost all countries have a national auditing office, to monitor and evaluate the finances and the performance of the public administration in order to ensure that the public resources are used correctly and in an efficient manner. Nonetheless, if auditing actually leads to a well-performing public administration is a question which has not been answered properly in previous research." This may sound like a surprising observation, considering that modern democracy is unimaginable without a national audit office as an integral part of the general government. Shedding some light onto the mechanism of how does auditing lead to improving the public administration performance, and going deeper with an analysis of how such a positive impact can be achieved, is an important contribution of this thesis in answering this question, especially useful in developing countries.

External evaluation and auditing of the government on behalf of the general public, which is done independently and with results available to any interested reader, was not an established practice of the former Yugoslavia's government. Empowering the taxpayers to expect and request value for their money, asking questions and getting answers from the government about government spending, is a crucial prerequisite for a functioning democracy. Establishing the supreme audit institutions in the Western Balkans countries after the break-up of Yugoslavia, and their strengthening at the beginning of the 21st century, has significantly contributed to this prerequisite. But the newly established supreme audit offices and their performance audits functions are still young in comparison with some long-established traditions in European Union. There is a growing demand for quality performance audit reports, which is a strong incentive for developing the performance audit function in the supreme audit offices in the region.

Developing the performance audit requires new insights and methodological inputs that could contribute to the audit impact. The core question explored by the performance audit is question *why*, which means not just confirming that a problem exists, but going deeper into the audited problem area and finding the root causes of the problem. By applying the principle-agent theory to the public sector, this study aims to shed some light on how performance audit could serve as a mechanism for mitigating the problem between principals and agents in the public sector, by revealing true causes of problems that might otherwise remain invisible. Hopefully, the analytical framework applied in this research could also be a useful methodological input in future performance audits of similar government activities.

The methodology of the thesis is case study research with qualitative contents analysis method, looking at the Youth Employment Program in the Federation of Bosnia and Herzegovina (hereinafter: Program). The analysis looks deep into the responsibility delegation chain and shows how the problem gradually developed between the principals and their agents, how this was revealed by the external audit, and how the audit recommendations helped mitigate the problem.

The analysis covers the Program life cycle in five steps, from strategic planning, through the Program implementation, to reporting, pointing to the asymmetric information that appeared in the communication between institutions within the delegation chain, and showing how the asymmetric information contributed to the Program failure. The analysis then continues by looking at how the external audit, and more specifically the performance audit, reported about these problems and how it filled-in the missing information gaps, which helped the parliament to undertake necessary actions. These five steps are covered through the following five research questions of this thesis:

1. Is there a deviation of tasks, goals and objectives throughout the delegation chain?
2. Is implementation going in line with the principals' expectations?
3. Is there a deviation in reporting from the agents to the principals?
4. Does the audit office fill in the information asymmetry gap?
5. Do the principals use audit reports to demand corrections?

Answers to these five questions are provided based on the qualitative contents analysis of the various government reports and documents related to the Program, including the government strategies, program documents, annual plans and reports of the agencies involved in its implementation, audit reports, and correspondence between the Federation Parliament and cantonal employment agencies during the follow-up stage. The study also uses the official statistics from the statistics agencies with quantitative data from different time periods. The objective of qualitative analysis of the empirical data from these documents is to identify the asymmetric information throughout the Program planning, implementing and reporting cycle along the delegation chain. To facilitate the focus on the main issues, the empirical analysis only contains most important excerpts relevant for the main message; however, for a detailed analysis of empirical data, two tables with detailed numbers and their sources are provided in Appendix 3.

The timeline of this five step cycle is the period of initial Program planning from 2008 until 2013 when the Program ended. The Program was audited by the Audit Office in 2012 and this audit report was analysed and followed up by the Federation Parliament in 2016, which included direct communication with responsible implementing agencies.

This study has a limited capacity to provide a full picture of the entire set of problems troubling the public sector, especially in developing countries like Bosnia and Herzegovina. The problem with the Program and the institutions involved in its implementation serves to illustrate and explain how intricate relations between various government levels can contribute to the failure to achieve expected results. To fully resolve the government ineffectiveness problem would require much more than just the establishment of performance audit function, and there are also a number of other mechanisms and measures aimed at doing so.

A powerful function of monitoring and scrutiny from the NGO sector, a corrective force of the media and public criticism, also have similar effects like that of the performance audit function. In the case of Bosnia and Herzegovina, an ongoing public sector reform process and the EU accession roadmap also represent a very strong driving force improving the overall government effectiveness. One characteristic of this force however is its external motivation, i.e. it involves players from outside of the vertical (principal–agent) government structure, since the EU accession process is externally motivated and often ran and financed by the EU. This is very different from the audit office function, which is essentially a tool in the hands of domestic principals that they use to scrutinize the work of their agents. This tool also provides relevant inputs for all the public sector reform processes and integrations.

There is a strong regional trend in moving towards the program budgeting system, which in the near future is also expected to be implemented in Bosnia and Herzegovina. Characteristic of program budgeting is that it secures a possibility to vertically follow the purposeful spending of the public funds and facilitates measuring of the intended goals and objectives. However, even if the budget lines are allocated vertically per specific goals and objectives, the problem of principal-agent relation can still impact the clarity of their definition and measurability, and ultimately, a possibility to follow them up.

The structure of the thesis consists of the following chapters:

The first chapter provides an overview of the principal–agent theory and theory behind the role of the external audit function in the public sector. The theory is then summed-up into an analytical framework used for empirical analysis.

The second chapter provides a description of the research method applied in this thesis, concretely, the case study research method with qualitative contents analysis method, elaborated into the research questions and matrix.

The third chapter consist of empirical analysis of the Program, where the government goals are followed from their origin in the Strategy adopted by the Federation Parliament, through the planning process, to their implementation and finally their outcome, showing how the asymmetric information developed along the delegation chain. Next, the results of the audit are presented, showing how the audit revealed deviations along the delegation chain and provided recommendations to remedy the problem. Based on this, the Parliament of Federation BiH requested actions from the agencies responsible for the Program.

In conclusions, the meaning of the research results and their contribution to the main goal of the thesis are presented and discussed, with some recommendations on possible improvements of the audit impact, as well as recommendations for further research.

1 THE PRINCIPAL-AGENT THEORY

1.1 Introduction of the principal–agent theory

Tracing the exact origins of the principal–agent theory is a rather difficult task if one wants to do justice to all the authors who contributed to its development. The theory and its model are coined under several names – such as agency theory, agency problem, agency dilemma, principal problem, etc., which all address the same problem from different angles and with different consequences. Determining the exact time of its emerging and its original author(s) actually depends on how widely defined is the threshold of what the principal-agent theory is and what it is not. Focusing on the problems in economics and management, it is safe to say that the origins of the principal–agent theory in its current form and terminology framework are several decades old and arise from the scientific need to explain the complex structure of interests that govern industrial economics. This would, however, not do justice to the previous researches. If the focus would include the society as a whole and the problems of democracy and politics, and if the terminology framework were extended to include issues of delegation, social contract, constitution, etc., the origins could be traced all the way to Aristotle's works on politics.

Application of the principal–agent theory and model is multidisciplinary in contemporary scientific discourse, and it is perhaps most frequently used in industrial economics to addresses issues such as information asymmetry and moral dilemma, in political science it is used to address issues such as political delegation, in law it is used to address issues such as optimal contract, etc. The terms principal and agent, often also associated with the term delegation, are frequently used in the scientific literature to explain relations between the actors. A different discipline and the area of their use can have different implications on their meaning, depending on the situation between the actors. Applied in the principal-agent theory, the two terms determine the main framework in which two actors function together based on their personal preferences and internal and external conditions which influence their decisions. The model relies on much more than just purely rational economic reasoning and involves the issues of psychology and behaviourism to explain how the do the actors function with each other.

1.1.1 Development of the principal–agent theory

The main building blocks of the principal–agent theory applied in industrial economics today have originated from the theory of the firm and organizational theory authors from the last century. These mainly psychological aspects provided important inputs for the later development of the principal–agent model and relations within it, not only in economics but also in political science. These works marked a gradual departure from neoclassical economic models based on purely rational choice only aimed at profit maximization and introduced the concepts based on individualism, human nature and intricate organizational problems that actually govern industrial economics.

One of the traditional works on the subject was written by Berle and Means (1932), where they discussed the separation of ownership and control, the problems of risk sharing and the control mechanisms based on delegation. Their work was also focused on the inclusion of the board of directors as an intermediate layer between owners and managers, and associated problems of decision-making in this structure, including the problem of managerial shirking and its impact on the corporation market position. Their discussion about the issue of specialisation later created grounds for discussion about information asymmetry. These issues are considered some of the building blocks of the principal–agent theory.

Through his works on the nature of the firm, Coase (1937, 1972) demonstrated that the organizational theory can be constructed around individualistic interests that govern numerous transactions of labour, capital, specialized knowledge, etc. rather than relying only on market forces as the only determination factor that governs decisions on such transactions. According to Coase, a rational economic agent who wants to start the production of a good will select internalized sources of production factors inside the firm, which is characterised by relations of hierarchical authority, rather than obtaining them from the market, whose relations are purely characterised by the market forces outside his or her control. In this case, the issues of authority and interest are specifically important and will later represent an important source in coining the principal–agent model.

A similar and equally important work from the same time period which addressed this issue and often quoted by later authors is the work of Barnard (1938) in which he addressed the issue of relation between employer and employee, or supervisor and worker. He has identified that this relation is strongly determined by a zone of discretion and indifference, in which the worker has a possibility of making key choices and decisions regardless of the supervisor.

Simon (1947, 1955) discussed individual choice as the main building block of the organizational theory. His work is focused on the ways of people's own thinking and its limitation by input information and knowledge, further determined by the human capacity to calculate, and finally shaped by the forces of authority. By limiting information and knowledge, managers are able to create boundaries within which the organizational hierarchy functions. Simon's concept introduced authority as a two-way relation because a subordinate first has to willingly accept someone's authority and then they jointly agree on the zone of exercising that authority.

One of the first mentioning of relation between the principals and the agents, among others, comes from Cooper (1948, 1951) who used the roles of the principal and the agent to explain external and internal behaviours of the firm that could otherwise not be explained by purely rational principles of the profit maximization objectives. Cooper drew attention to the issues that were simply ruled out as awkward or irrational by purely neoclassical economic thinking of that time, and suggested that the theory of the firm

should be revised and extended to include an analysis of the agents' self-interests. According to Cooper, taking into account the agent's self-interests was one way to explain problematic decisions that were otherwise considered simply irrational.

It is also important to mention the work of Alchian (1950), where he, similar like in Darwin's theory of evolution, introduced the concept of natural choice into the firm's life cycle and the concept of external forces that shape decision-making process within firms, thus widening the perspective from solely individualistic interests to a requirement to adjust oneself to external working conditions. Later on, Alchian (1965) also conducted an overview analysis of the theory of the firm and pointed towards the issues of guiding the manager's actions by the owners and the resulting costs.

Other works worth mentioning as influential are those of behavioural scientists, notably the work of Cyert and March (1963), where they completely rejected all the neoclassical and rational models of optimization and profit maximization and introduced the behavioural theory as the solely determining factor that actually governs organizations and the firm's life cycle. Similar work addressing the issue of individual choice, by Kahneman and Tversky (1973), additionally developed psychological aspects that impact the decision-making process, going further beyond just purely rational choice.

The relation between the principal and the agent was used to explain different variants of compensations and profit-sharing between shareholders and the managers they employed to run their company, notably by Williamson (1964). He also referred to Barnard (1938) and developed a managerial discretion model, explaining the possibility of managers to make such allocation decisions that benefitted themselves while leaving shareholders with less than maximum returns.

Later, Berhold (1971) in his study of profit-sharing incentives and Stiglitz (1974) in his work on the agricultural economy also used the concept of analysing the distribution of risk and incentives between principals and agents, offering a model for determining the optimum equilibrium. Although Stiglitz did not specifically discuss the principal's and agent's position, he addressed the relations between landowners and farmers in ways that were a large step forward from the neoclassical model.

These newly introduced theoretical models and concepts have created the building elements of what was to become the principal-agent theory in industrial economics during the seventies. One could say that the principal-agent theory partly emerged from this gradual abandoning of the neoclassical model and the paradigm change. Such a change was needed to explain issues that were not fully explainable by the purely rational choice concept. It required inclusion of issues of individualism, delegation and behaviourism, which altogether contributed to the foundations of the principal-agent theory and how is it developed today.

The most important works that developed the principal–agent theory and applied it in economics and institutional theory are those of Mitnick (1973) and Ross (1973). Both authors in their works refer to similar authors from organizational theory and the theory of the firm, following parallel and overlapping lines of thoughts. Based on the views of the scientists above, both Mitnick and Ross built their models and presented their views of the problems that had already been long present in the scientific arena but introduced a new view of looking at them, the view that is now referred to as the principal–agent theory. There is some disagreement as to which of the two authors is actually the "father" of the principal–agent theory, but the two scholars arrived at the theory independently and concurrently, addressing the same problem, although from somewhat different angles. Essentially, both authors analysed the problem of agency which in this case referred to acting for someone else's interest, and identified the agency problem as a misalignment between the principal's and agent's interests.

Ross devoted his work to the ways and tools of aligning these interests by economic means, while Mitnick took the path of utilising institutional means for the same goal. This difference between the two approaches is a center pole around which the two directions of the theory were formed and continued to develop over the following years – economic and institutional. Mitnick (2007, rev. May 2019, p. 3) argues that "In short, Ross introduced the study of agency in terms of problems of compensation contracting; agency was seen, in essence, as an incentives problem. Mitnick introduced the now common insight that institutions form around the agency, and evolve to deal with agency, in response to the essential imperfection of agency relationships: Behaviour never occurs as it is preferred by the principal because it does not pay to make it perfect. But society creates institutions that attend these imperfections, managing or buffering them, adapting to them, or becoming chronically distorted by them. Thus, to fully understand agency, we need both streams – to see the incentives as well as the institutional structures." (Mitnick, 2019, p. 3).

The works of both these authors continued to evolve over time and became one of the most important concepts applied in both economics and political science. Mitnick continued publishing his works, not always nominally on his theory itself, but often applying it in various topics, such as analysing the incentives systems and a different context of regulation, interest group behaviourism and law. Moe (1984) analysed these works and created grounds for application of the principal–agent theory in political science. Driving the links and explaining how the relationship between the principal and the agent can also be applied on democracy, he identified several main mechanisms how the principal–agent theory concept can be fully applied in public sector and defined the entire democratic system as a chain of principals and agents. The principal–agent theory and the problems it addresses are presented in the following sections.

1.1.2 Principal–agent problem and its implications

The principal–agent model essentially applies to any relationship in which one or more persons on the one side delegate authority and tasks to one or more persons on the other side, to represent their interest or to conduct some work on their behalf, for certain compensation. Such situations can exist in various social arrangements, from employment to business economics, from politics to law. Analysis of the principal's and the agent's positions and roles and the process of delegation between them can help explain a range of different causes and consequences arising from their relationship. The main root of the problem within this relationship is in specific vested interests of each position, which are more often in conflict than aligned. Principals delegate authority to agents to manage their assets or represent their interests, but in exercising this authority, agents are not always led by the best interests of their principals and instead often prioritise their own interests. This affects their decision making process and finally the outcome. Such scenarios are illustrated through the following three cases – manager, lawyer and politician.

In the case of management, the principal's position refers to the capital owners in the firm (shareholders) but can also refer to other stakeholders who may have a special interest (for instance, citizens, if the firm is providing public services such as waste management, electricity production, etc.). The principals employ a manager as their agent and delegate him or her the authority and means to run the business on their behalf. The two main areas where the interests between shareholders and the manager collide are profit and risks. As capital owners, the principals will prefer safer transactions against those with a potential risk of losses, be it an immediate financial loss, a loss of potential future profit or a goodwill loss in case of such business endeavours that can be regarded as socially or ethically unacceptable. The manager, on the other hand, is interested in a quick gain and immediate success usually associated with higher risk transactions, and since the consequences for the manager are inherently smaller, the manager will easier take risks on behalf of the company he or she represents. A practical example could be bank management. While the bank shareholders would rather refrain from giving loans to high-risk clients, the bank manager will easier go into such arrangements as they provide short-term gains and profits, even if these loans may be lost in the long run.

The principal–agent relation becomes additionally complicated when there is more than one principal involved. A group of company shareholders may have different portfolios and depending on that, a different vision of their company's future. As a result, the shareholders group will not act as one and their voices will be scattered, sometimes even in opposite directions. This opens a manoeuvring space for the company manager who can take advantage of this situation to work more in line with own interests and much easier get away with it by manipulating internal relations and information exchange or simply align his or her actions with those shareholders that suit them best.

A defence lawyer is given a mandate from a client to defend them and represent their interests before the court. To be able to do that, the lawyer first has to pass the bar exam and be licensed from the state, which is the state's way to secure that the lawyer will represent the interest of law and justice. However, the interests of law and justice are not always aligned with those of the defendant – on the contrary. If the lawyer has to choose between such opposing directions, he or she will be easily inclined to profit from the given situation even if it means jeopardizing the license, and will readily manipulate any information needed to secure their profit while preserving the license. This means that the lawyer will be guided by own interest and make decisions not in the interest of law and justice but instead on the basis of their short-term profit gain.

This means that a lawyer may align own interest with the client's, not because the lawyer wants to represent the client's interest but because it suits the lawyer. Being guided strictly by the financial gain, the lawyers' own interests are not always aligned with the interests of those that they represent. For example, if paid per hour or court session, a lawyer may be interested in long court proceedings rather than closing the case efficiently, simply because this increases their profit. They will justify such long proceedings by hiding behind slow bureaucracy and its requirement to closely follow the procedures of "law and order", although the true motivation is actually different. In a gap between different interests of their principals, the lawyers or any agents will rather choose an option where they are better off.

In a democracy, the citizens are the principals who elect politicians in general elections and delegate them the power and authority to run the country. The citizens are interested in long-term stability and progress, quality government services such as healthcare and education, employment, security, justice, and so on. As taxpayers, the citizens are interested to receive value for the money they pay. On the other hand, politicians are interested in having a possibility to manage the tax money, i.e. the position of power and authority. This position brings them personal profit and gain and they want to keep it for as long as possible. These two interest sides are inherently misaligned. Also, this is where the issue of a gap between the short- and long-term interests becomes especially problematic.

Elections are usually every four or five years, and politicians' actions are aligned with these cycles, they are only interested in getting yet another term and will work more efficiently in the election year. As soon as the elections are over, they return to their old practices. In the case of the public sector, the problem of many principals is even more complicated. An appointed politician is in a position to have to represent numerous interests from different groups with often very different agendas and interests. Even if the politician wanted to, he or she cannot possibly look after and satisfy all these groups; instead, such a position opens and widens their manoeuvring space.

1.1.3 Interests alignment mechanisms and associated agency cost

In the process of engaging their agents, principals can employ many different mechanisms to control the agents' behaviour and secure that the agent as closely as possible follows and represents their principal's interest. Such mechanisms can be institutional, as presented by the institutional theory and discussed in the work of Mitnick (1975), or economic, as discussed in the business economics and also in the work of Ross (1973). Alignment mechanisms can also be a combination thereof, and however they are designed, they both cause an agency cost which increases with the increase of the mechanism effectiveness. A well cited and widely influential work by Jensen and Meckling (1976) applied the basic elements from the principal-agent theory into the theory of the firm, also integrating aspects of the property rights and theory of finance, and based on these, extensively defined the concept of agency cost.

An example of the institutional mechanism is the bar exam and license for lawyers. By imposing this obligatory exam, the state, as the principal, secures that lawyers represent interests of law and justice. A challenge with this mechanism is in its implementation, as once the bar exam is passed and the license obtained, it becomes difficult for the state to actually monitor lawyers' actions and assess whether eventual misconduct could cause revoking the license. A downside of all institutional mechanisms is that they function on the basis of the projected consequences of misconduct, while the agents' and principals' interests still remain misaligned. Economic mechanisms function in a different way, focusing on aligning the interests of the principals and their agents. Drafting a contract between the shareholders and the manager in such a way that the manager will receive a part of the profit will automatically align the managers' own interest with the shareholders'. Additionally, risk sharing and short- and long-term interests can be aligned by allocating a percentage of ownership shares to the manager. This puts the manager's interests in equal position with those of the owners, as the manager will now be interested in a long-term prosperity and avoiding any risks that might jeopardize their assets.

Increasing the effectiveness of both economic and institutional mechanisms increases the agency cost. In the case of economic mechanisms, the agency cost gradually grows from the manager's financial compensation and a profit share, to allocating a percentage of the company ownership, raising the manager on the same level with principals. At this stage, the cost reaches the maximal reasonable level, but it is still not guaranteed that all the interests are fully aligned and that the manager will not use the advanced position as an agent to pursue own interests. It is similar with the agency cost of institutional mechanisms. In the case of the bar exam, there is a cost of the exam itself and the cost of issuing and maintaining the license. One way of addressing this issue is to transfer these costs to the lawyers by imposing a fee to access the exam procedure. Such a solution for transferring the agency cost to agents is, however, not always possible and can even be counterproductive.

1.1.4 Asymmetric information

Agents get the decision making authority from their principals, but the extent of this authority is still limited by the principals, as they want to keep their final say in important issues that can impact them. The line between the principal's and the agent's decision making authority depends on the agency arrangement, however, the outcome of any decision depends on information that the decision-makers have at their disposal. This is where asymmetric information as the main problem of the principal-agent relation comes into equation. As mentioned earlier, the neoclassical model based on purely rational decision-making and purely economic reasoning was gradually updated by including psychological and behavioural aspects, which are well framed in the principal-agent theory. In practice, this means that the principal's or the agent's decisions depend on personal preferences related to different paths, and calculation capacity to foresee the outcome. In the decision-making process, the decision maker can only process relevant inputs – the data and information about the conditions and possible outcomes and consequences of different paths taken. Thus, the availability of data and information is of key importance.

Some of the most important works in this area include that of Akerlof (1978) where he describes how market conditions are determined by the presence of asymmetric information. He uses the analogy of a second-hand car market to describe how a buyer and a seller do not have equal knowledge and information about the real condition of the car, which puts them in different positions regarding the transaction regardless of their personal preferences. In practice, asymmetric information can have numerous examples. A lawyer knows the law, administrative and court procedures and has experience in applying them. A client does not, which puts the lawyer in a much-advanced position over the client. Even if the client makes all the ultimate decisions about what to do and how to be defended, all these decisions only depend on the lawyer's inputs.

The firm manager is responsible to run all operations and report the firm's business operations and financial status to the steering board. The steering board can never have all the specialised knowledge about business operations, production, employee recruitment and all work aspects of the firm. and this is why the board hires a manager. However, their main source of information about the firm's status comes from or through the manager. Even if the board limits the manager's decision-making powers and requires him or her to ask for board's approval for some decisions, the approval still depends on the information received from or through the manager. This can be mitigated by obtaining additional sources of information, such as an internal auditor or an independent consultant. However, this does not change much the manager's unique advanced position, where he or she can hide some information or part of it, tweak it and finally manipulate it to guide the superiors' decision in a way that suits his or her own interest.

The situation and the problem of asymmetric information are even more complex in the public sector. The first major problem starts already at the top principal side and a lack of the citizens' capacity to understand the consequences of decisions they make at the elections. The citizens' interests are scattered between many issues and priorities, so politicians can take this to their advantage. Also, the entire principal–agent delegation chain is much more complex and includes many layers of governance. This opens much more space for manoeuvring for every actor. The reporting process in such a complex system is even more susceptible to deviation of information being exchanged, with hindered possibilities to pinpoint the exact sources, causes and consequences of these deviations. The agent in each layer is at the same time a principal for the lower layer of the government, which opens even more room for manoeuvring within their position, make decisions that suit their interests, and even guide others into making such decisions.

1.2 Applying the principal–agent model in the public sector

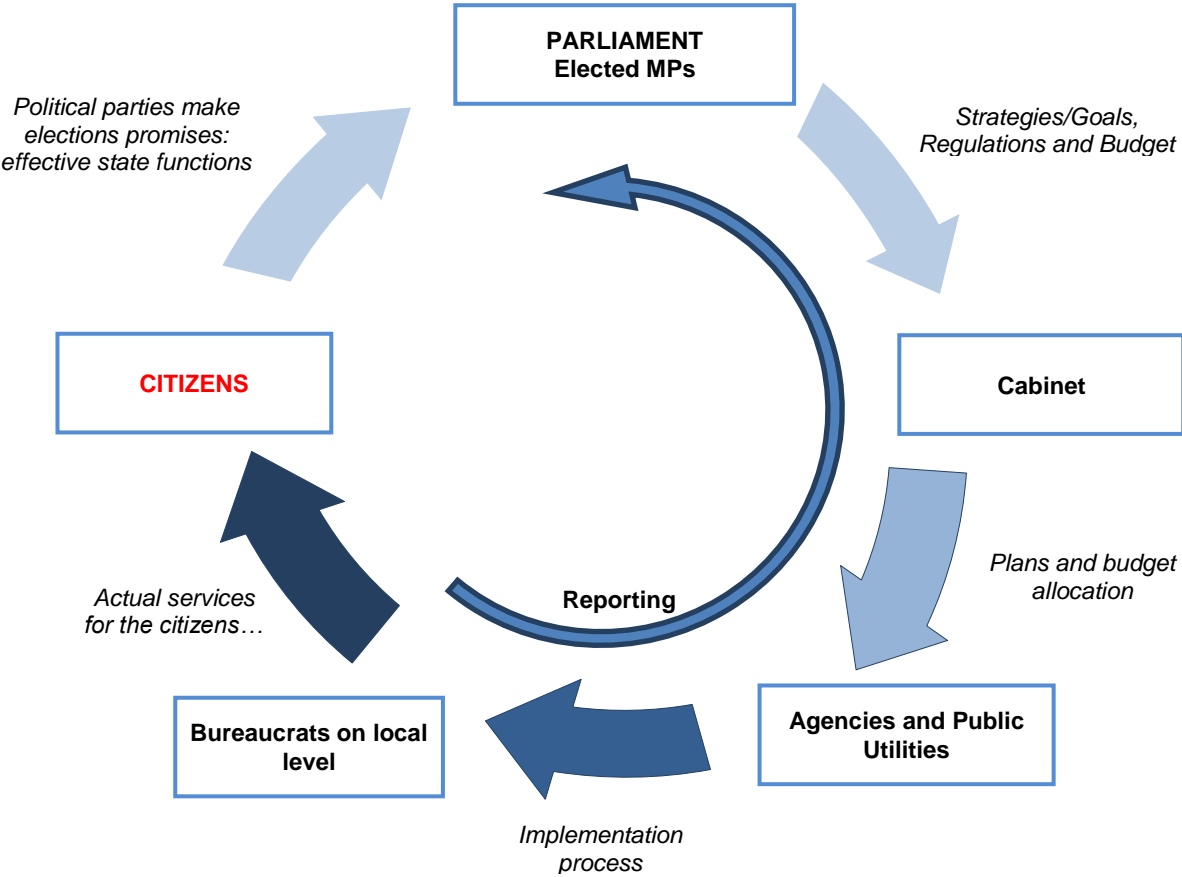
The public sector governance consists of a complex mechanism with numerous functions spread in different vertical and horizontal layers, but it can be generally structured in the principal–agent model. The asymmetric information problem is in the center of the principal–agent relation and can be considered as a common issue with adverse effects on all functions of the state. The constitution of every modern democratic state defines the general government with three main branches – legislative, executive and judicial – which in themselves contain functions that provide for the citizens' security, justice, economic development, education, health-care system and other functions of the state. The legislative branch – the parliament – is elected by the citizens in general elections. The representative government is one where voters select their representatives in the legislative branch of the government, and they become agents of the citizens. Lupia and McCubbins (1998, p. 79) emphasize that "Democracy requires delegation. The people, through elections, delegate their authority to its representatives. Elected representatives, in turn, delegate some of their authority to the leadership of their assembly and to the bureaucracy. /.../ Each of these delegations involves a principal, the person or persons delegating, and an agent, the person or persons to whom authority has been delegated." (Lupia and McCubbins, 1998, p. 79)

According to Moe (1984), "Democratic politics is easily viewed in principal-agent terms. Citizens are the principal, politicians are their agents; politicians are principals, bureaucrats are their agents. Bureaucratic superiors are principals, bureaucratic subordinates are their agents. The whole of politics is therefore structured by a chain of principal–agent relationships, from citizen to politician to bureaucratic superior to bureaucratic subordinate and on the down of the hierarchy of government to the lowest-level bureaucrats who actually deliver services directly to the citizens." (Moe, 1984, p. 766). This arrangement is loaded by numerous problems and issues caused by differing interests between the different sides. Analysing this, Higgs (2018, p. 479) concludes that "a perfect agent is, for various reasons, pretty much impossible, and in many cases a great gap exists between

what the agent does and what the principal wanted him to do but could neither compel nor induce him to do with any feasible agency contract." The author further explains that due to the complex and widely differing political preferences, the political task to represent all these interests is impossible. There is a lack of effective mechanisms to secure that elected agents follow interests of the electorate; the only opportunity to implement such a mechanism is at the following elections, however, once they enter office, political representatives have many possibilities of manipulating the electoral body and "the principals (the voters in this case) cannot discipline or dismiss them. For the most part, political agents are not truly accountable to the principals, but only to the major contributors to their re-election campaigns. Accountability is in general more myth than substance." (Higgs, 2018, p. 479).

The principal–agent relation model applied in the public sector is presented in Figure 1, with five general levels: the citizens, the parliament, the cabinet, agencies and bureaucrats. There can be organizational variations in different countries or on different levels (national or local level of the state), but the logic is the same. This diagram also serves as a framework model to show the information flow and describes how does the problem of asymmetric information develop and how does the audit function deal with it.

Figure 1: Principal - Agent Framework



Source: own work.

The public sector management process starts in the top left corner of the Figure 1. With every elections, the politicians give promises to the citizens, which are related to the basic functions of the state – such as employment, economic stability and growth, security, various public sector services (healthcare, education, etc). These promises are then turned into the government goals and strategies adopted by the parliament, together with required regulations and budget for their implementation. This is where the parliament completes its role as an agent of the citizens and begins its role as the principal of the executive branch. The process description follows with the next arrow bottom right: every year, the government prepares its annual plans and budget aimed at fulfilling the general established goals adopted by the parliament. These plans break the goals into more measurable and operational objectives. The line ministries provide practical instructions and define expected outcomes and results for their sectors. These are accompanied with the state budget appropriations and any laws and regulations required for the implementation process, and moved on towards the agencies and local offices in charge of providing services to the citizens. In this stage, the government completes its role as the agent of the parliament and begins its role as the principal to the agencies and local offices.

Heads of the agencies and the local offices manage the practical work conducted by the bureaucrats who provide actual services to the citizens. They, as the managers, create annual operational plans with practical tasks, the division of work and responsibilities, concrete expected results, etc. In this stage, they take their role as the agents of the ministries and at the same time act as principals to the bureaucrats that directly provide services to the citizens. This is where the execution process is complete.

After that, the process of reporting on the outcome and results begins. While the delegation of tasks moves in the direction from principals to their agents, the process of reporting goes backward, from agents towards principals, as indicated by the thin dark blue arrow in the diagram. Bureaucrats report their managers on their daily work, the managers submit annual reports on behalf of their agencies to the line ministries, based on which the government produces its annual report and submits it to the parliament. This is where the entire cycle of planning, executing and reporting throughout the delegation chain is closed.

1.3 The impact of the principal–agent problem on the information flow

Lupia and McCubbins (1998, p. 79) argue: "The central dilemmas of delegation are that agents often do not have common interests with their principals and that agents may have information about the delegation that their principals lack. In studying democracy, we are interested in when these dilemmas do and do not cause delegation to fail". As shown in the above model, the original functions of the state are delegated to the parliament members, turned into goals and objectives and then implemented throughout the delegation chain, which then reports about the execution.

These two processes – the process of delegating the tasks in the form of goals and plans, and the process of reporting on their outcome – are closely connected with each other. Reports from the previous period are an inevitable input to plan the next period as the goals and objectives set for the future are always based on the previous experience and state of affairs. Any alterations in the reports ultimately cause alterations in the plans. As a result, in the process of reporting, the agents can influence the plans that they will later receive as their own tasks. In this structure, the actors in every phase of the process introduce their own interests and add own values.

A specific problem with this arrangement is that almost all the agents' and principals' roles are mixed. Except for the citizens who are the ultimate principal and bureaucrats providing services to the citizens who are only an agent, every other link in the vertical chain at the same time has a role as an agent for their superiors, and as the principal for the levels below. This creates additional complexity in the mixing of vested interests and opens more room for asymmetric information, as each agent at the same time receives tasks, implements them, and then reports about them. All the information flows in two ways, throughout the entire chain passing through each of the links.

The central problem here is again in the selective or incomplete sharing of information. As in the example from the car market from Akerlof (1978), agents will as much as possible avoid sharing any information that does not suit their personal interests. In the case of the public sector, the agents will gladly share with their principals such information that, for example, implies a need for higher budget allocation for the organization they manage, but also hide such information if it would adversely affect the budget. The same applies to the aspects of their responsibility implications – the agents will try as much as possible to extend their manoeuvring space and open it to suit their own interests rather than the principals'. Such differences on every level of the delegation chain cause a deviation in communicated information, and as the process goes, the deviations multiply. For example, by the time the originally envisaged goals from the parliament reach their final stage of implementation by the bureaucrats, they are only a grey picture of the original intentions. This deviation is illustrated by the changing colour of arrows in Figure 1. After every stage, the definition of goals and objectives set by principals for their agents changes and becomes increasingly vague.

The same happens during the reporting phase. Reporting back on executed tasks includes further deviations because agents will seldom – if ever – admit their own failure. Instead, they will tweak information about their working conditions and try to improve their personal situation by influencing the future plans and the budget received from principals. The actors in every link of the chain are very likely to change the information in line with their own interests, which gradually turns into major deviations from reality. In the end, there is a generally large gap between the reality, and the description of the state of affairs in the plans and the reports. This gap is present in every link of the delegation chain. By

the time the information reaches general public, the information asymmetry grows very strong. The general public is not interested in learning the information they disagree with and mostly does not understand complexities of the contents of government activities, as concluded by Bos, Kruikemeier and Vreese (2016). When this is amplified by the information asymmetry, the role of the citizens as an ultimate principal is dispersed and becomes ineffective.

This is, however, only one dimension of asymmetric information. According to Arrow (1975) and earlier works by Marschak (1955), by definition, the agent has been selected for his specialized knowledge in an area, and the principal can never hope to completely check the agent's performance. The root of deviation comes from the agent's position in relation to the principal's position. The most accurate information about the actual state of affairs is in hands of agents – because they have the expertise, a direct connection with work implementation and a possibility to choose how much to share with principals.

On the other side, principals are not directly connected with the actual work, they do not have the expertise in the field and this is why they delegate tasks to the agent in the first place. "However, by the mere fact of this delegation, the agent may get access to information which is not available to the principal. The exact opportunity cost of this task, the precise technology used, or how good is the matching between the agent's intrinsic ability and this technology are all examples of pieces of information which may remain private knowledge of the agent." (Lafont and Martimort, 2001, p. 37).

McCubbins, Noll and Weingast (1987, p. 244) define that possible mechanisms aimed at overcoming this problem can be placed by strict procedural requirements that allow political leaders to secure their interests without specifying or even knowing the substantive outcome. This means that "procedures can be used to mitigate informational disadvantages faced by politicians in dealing with agencies. Second, procedures can be used to enfranchise important constituents in agency decision-making processes, thereby assuring that agencies are responsive to their interests." (McCubbins et al., 1987, p. 244).

In their study, McCubbins, Noll and Weingast (1987) further define that the other solution would be based on monitoring of the agent, combined with a system of rewards and punishments, including hearings, investigations, budget reviews and legislative sanctions. "Inevitably, elected officials delegate considerable policymaking authority to unelected bureaucrats. Because elected officials have limited resources for monitoring agency performance, the possibility arises that bureaucrats will not comply with their policy preferences. This gives rise to the question how – indeed, whether – elected political officials can reasonably effectively assure that their policy intentions will be carried out. In this complex administrative structure inhibited by the self-interests and asymmetric information problem, the issue of accountability also comes into focus." (McCubbins et al., 1987, p. 243).

Due to the principals' and agents' conflicting interests and their different positions in relation to the actual work done, the whole structure is loaded with ambiguity reflected in the definition of tasks and expected outcomes. In the study of arrangements that may tackle this problem, Kellner (2017) concludes that the ambiguity raises the risk of failure, and ambiguity aversion by both principal and agent is crucial for lowering this risk. In purely profit-oriented businesses, risk aversion may also lead to lower profits, however, financial profit goals do not apply to the public sector, and this could explain why the public sector is more inclined towards an institutional approach in the alignment of the principals' and agents' interests.

The problem of the vertical delegation also includes the problem of time shift that elections introduce between committing wrongful acts by public officials (or simply not fulfilling their promised goals and objectives), and citizens' opportunity to hold them accountable for such acts by not voting for them in the next elections. This poses a risk that the citizens may lose trust in the government system, especially in young democracies. Addressing such a risk requires enhanced control mechanisms, including government institutions able to supervise the public sector between the elections.

This supervision can be exercised through the process of information asymmetry balancing by introducing the institutions that safeguard transparency, like external and internal audit function, as well as control mechanisms like oversight steering boards and commissions. According to O'Donnell (1998), while elections are important, "in the absence of duly authorized state agencies of investigation and oversight capable of parcelling out responsibility and sanctions,/.../ sometimes they risk merely creating a climate of public disaffection with the government or even the regime itself." (O'Donnell, 1998, p. 113).

Scott (2000) explains that accountability has vertical and horizontal lines of "who is accountable to whom" and separates these directions of accountability from their substance or "what" one is accountable for. Agents are accountable to their principals to represent their interests, but reality shows that this is often not the case, and author divides the substance of accountability into three groups of values – economic values, social/procedural values and continuity/security values, which all require accountability mechanism to secure them. "Changes in accountability structures since the Second World War have resulted in a recognition of some extended forms of accountability, as courts have been supplemented by a growing number of tribunals (for example in the immigration and social security domains) and new or revamped administrative agencies such as grievance-handlers and public audit institutions have played a greater role in calling public bodies to account. Simultaneously parliament has enhanced its capacity for holding ministers and officials to account through the development of select committee structures, in some cases linked to new oversight bodies such as the Parliamentary ombudsman and the National Audit Office." (Scott, 2000, p. 3).

1.4 The role of the audit function

The structure of the public sector governance system, with the horizontal and vertical control mechanisms – such as treasury function, government inspectorates, internal controls, etc., enables control and supports the achievement of the state functions and the government goals and objectives. Among these, the audit office is an institutional mechanism with an indispensable role in securing accountability. As Oyesola and Agbeja (2007, p. 45) say: "The audit function and the form in which audit results are reported tend to reinforce the traditional line of public sector accountability to elected representatives rather than establish new forms of accountability." Adding the audit function is not a final solution to all public sector problems, but it can address the problems of asymmetric information, and in doing so, enhance the principals' capacity to exercise their control over the delegated tasks implemented by agents and improve overall accountability. (Oyesola and Agbeja, 2007, p. 45).

From the theoretical perspective of the principal–agent theory, the external audit function could be categorised as an institutional mechanism aimed at securing the alignment of interests between principals and agents. By balancing the information asymmetry that inevitably exists between various levels of the government and the citizens, the external audit function helps mitigate the problem rather than impose the institutional obligation to align interests between principals and agents. To achieve this, the external audit function must be uninhibited by the vested interests, it must be independent from both the principal and the agent, have capacity and mandate to look into any aspect of the actual state of affairs, and evaluate the outcome of government functions. Finally, the audit office needs to make its reports available to all the links in the chain, including the ultimate principal – the general public and the parliament.

The external audit function can check any level in the principal–agent accountability chain and provide independent and relevant information, free from vested interests. For example, the ministry of finance as the principal in charge of budget spending may demand from the line ministries certain expected results and outcome of their budget spending, but the line ministries may unfairly take advantage of their superior knowledge of the subject matter and simply manipulate the results of their activities. "If external conditions are favourable, the line ministry could exert little effort and produce a low output, while claiming that this low output is due to unfavourable external conditions. The ministry of finance is not in a position to disentangle the two factors unless it uses some form of audit or supervision." (Leruth and Paul, 2006, p. 8).

Similar scenarios happen at any level of the principal–agent delegation chain – producing and sharing misleading information which creates conditions that suit the agents' personal interests. As a consequence, the real state of affairs remains unknown, causes and effects are difficult to track, and finally, the problems are impossible to detect and only multiply with time. Asymmetric information thus becomes a key element and the center of the

principal–agent problem in the public sector administration, so introducing institutions that could balance such information gaps is crucial. However, while securing a proper exchange of complete and true information within the government is crucial for its success, the involvement of the general public – the citizens and taxpayers – in the whole picture is just as important, as placing citizens into the position of having access to full and objective information creates pressure on the politicians.

In the study of democratic origins of auditing, including a historical review of external audit function from ancient Greece until modern days, Gustavsson (2013, p. 2) states that "good auditing of the public sector is distinguished by recognizing the people as the principal, independence to the auditee and professionalism in the exercise of the audit practice", arguing that "from a democratic perspective there is need for auditors to recognize the citizens as the principle, which implies fulfilling the people's expectations of their role as well as aiming at limiting mismanagement of the public sector. This requires a higher ambition than merely report to the administrative management and elected politicians." The audit success in fulfilling its role in improving government efficiency depends on the three main principles in which the audit office must be embedded – independence, professionalism, and recognising the people as the principal. Almost all modern countries around the world have a national audit office that monitors the performance of the entire public sector in the country. "Political representatives and ordinary citizens may have a difficult time in constituting a sufficient democratic control, merely through access and insight in the public sector organizations. This has given rise to the need for specific government agencies controlling other parts of the public sector, such as auditing or inspection agencies." (Gustavsson, 2015, p. 5).

In their study of the effects of agency costs and information asymmetry on audit quality, Ghanbari, Rashidi and Abbasi (2018) explain how reporting along the delegation chain can suffer from misleading information, so it strongly depends on auditing financial reports and the quality of audits. Asymmetric information and a need to match the interests of principals and agents add to the agency costs. Ghanbari et al. (2018, p. 141) conclude that "the effects of audit services quality on agency costs and information asymmetry /.../ show that there is a negative and significant relationship between agency cost and audit quality." It has to be clarified that the role of external audit function is not a mere "control" of financial statements. Filling in the gaps of the asymmetric information requires providing a complete and true picture of reality to principals, and this goes far beyond checking whether the financial statements are true and fair like in the auditing of private sector companies. Mitigating the information gap between principals, including the general public as the ultimate principal, is crucial for system functioning. It has been reported that "the legally sensitive nature of audit in the private sector has tended to deflate shareholders' expectations of the audit. In practice, the audit is more wide ranging than official definitions suggest." (Jones and Pendlebury, 2000, p. 231).

The private sector is driven by profit and competition, which creates inherent driving forces that secure economic behaviour, production efficiency, and effectiveness of investments. However, the public sector lacks such driving forces, thus it requires specific audit functions directly aimed at achieving economical, efficient and effective operations. The 20th century has seen the rapid development of performance audit function, sometimes also referred to as value for money audit and effectiveness audit. According to Fawcett (2010), advances in public sector auditing have extended beyond what the commercial audit has to offer, and there are lessons from the public sector to be learned by the private sector. In the concluding remarks, Fawcett (2010, p. 10) argues: "The fact that the public sector audit extends beyond the financial statements to making assessments about the performance of an organization has to some extent allowed public sector audit to be more innovative and challenging in its approach. For example, this has probably allowed the Audit Commission to develop the most sophisticated audit in the world (CAA), one focused on outcomes."

There is also an aspect of laws and regulations. Mere looking at financial statements will not likely uncover all areas of potential violations of regulation or misconduct of public officials, hence the audit of compliance is also required, i.e. how the officials adhere to the laws and regulations in their activities. According to Fisman and Werker (2011), one of the methods to enforce frequently ignored rules is to have an auditor. "Sometimes countries are endowed with a set of laws that, in theory, promote economic activity. However, in practice those laws may be consistently violated by businessmen exploiting weak enforcement and by politicians or bureaucrats taking advantage of opportunities for personal enrichment." (Fisman and Werker, 2011, p. 83).

Besides the aspect of performance and compliance audits, there are other strong differences between the private sector and the public sector auditing that are rooted in the nature of taxpayers' money and information sensitivity. According to Wardman and Fawcett (2008), reporting in the public interest may include a matter that maybe requires public attention. The level of tolerance for misstatements in financial reports in the private sector is determined by the effect such an error may have on the decision-making process. In the public sector, however, the scrutiny by the general public makes such tolerances much smaller, not only regarding the misstatements but also potential misconduct by the public officials.

The public sector audit and its specific requirements rooted in the sector's very nature and its differences from the private sector are further developed in the International Standards for Supreme Audit Institutions (hereinafter: ISSAIs). The ISSAIs are regularly updated and adopted by INTOSAI (International Organization of Supreme Audit Institutions), a UN agency gathering all national audit offices of the UN member states. As stated in the ISSAIs (INTOSAI, 2013): "In general, public-sector audits can be categorized into one or more of three main types: audits of financial statements, audits of compliance with

authorities, and performance audits." Each of the three types of public sector audits has their own criteria and goals:

- *Financial audit* is checking whether the auditees' financial statements are in line with the financial reporting framework (accounting standards, budget, etc);
- *Compliance audit* is checking whether the auditees' activities are in line with applicable regulation (the laws and by-laws regulating operations and processes);
- *Performance audit* is checking whether the auditees' activities are in line with the principles of economy, efficiency, and effectiveness (i.e. economic behaviour, efficient processes, achieving the expected goals and objectives).

The financial audit focuses on the question whether the financial statements prepared by agents represent a true and fair picture of their business operations during the year, while the compliance audit checks whether the auditees adhered to the relevant laws and regulations in their work.

Both of these forms of the audit are an input that provides a level of comfort to principals, helping them exercise control over the agents' behaviour, however, there are some limitations. Laws and regulations may often impair effectiveness, especially in transitional countries, by creating cumbersome and bureaucratic administrative processes. Besides, agents can do everything in line with the laws and regulation and all their activities can be fully and correctly reflected in their financial statements; however, this still does not guarantee the achievement of the goals and objectives they have been delegated by the principals.

Instead of focusing on financial reporting framework and relevant regulation, the performance audit focuses on government goals and objectives, and asks whether the set goals and objectives have been achieved, and if not, why? In exercising this approach, the performance audit does not benefit from the laws and regulations and does not take the pre-defined goals and objectives in the government programs for granted, as these can often be unrealistic or may not provide value for money for the taxpayers. Even if common expectation is such that performance audit could easily measure agents' performance against their own pre-defined goals, in its most advanced form, the performance audit re-evaluates feasibility of these goals and their value for the citizens.

An important aspect and added value of audit, especially its performance audit function, is advising principals on how to improve things. Principals inherently do not have necessary expertise nor capacity to understand problems on a practical implementation level, and audit fills this gap by first evaluating the full, true and fair picture of the state of affairs in the public sector and through its expertise proposes corrective measures aimed at addressing the observed problems.

This role of audit function is extended throughout the entire principal-agent delegation chain, including the citizens as the ultimate principal. By looking at the entire delegation chain, the Supreme Audit Institutions (hereinafter SAIs) act as an agent for the citizens. International auditing standards closely describe the role of the SAIs in the public sector, and put the SAIs in a centrally important position for achieving the government goals and objectives and "making a difference to the lives of the citizens." (INTOSAI, 2013, p. 12).

1.5 Summing up the theoretical review into an analytical framework

As presented in the theoretical review, the principal-agent theory has for many decades been an established framework applied in industrial economics and its principles are fully applicable in the public sector governance. In the public sector, the problems of principal-agent relationship have a very strong impact. The links in the delegation chain between principals and agents include double roles, since the principals are at the same time agents of a higher-order principal, and vice versa. This is presented in Figure 1, which provides an overview of the government system from the perspective of principal-agent vertical relation.

If one typical government goal is observed, such as increasing the employment rate of young population through the Youth Employment Program in the Federation of Bosnia and Herzegovina (hereinafter: Program), the Program life cycle can be followed through the delegation chain to understand how the principal-agent relation affects it. The initial task starts from the top government principal, in this case, the Parliament of Federation of Bosnia and Herzegovina (hereinafter: Federation Parliament), which on behalf of the citizens delegates the task to its agents, in this case, to the Government of the Federation of Bosnia and Herzegovina (hereinafter: Federation Government), and further down to the Federation Employment Agency (hereinafter: Federation Agency) and cantonal employment agencies. They implement the Program and report about the process. The reports and the implementation process are audited by the Audit Office for Institutions of Federation BiH (hereinafter: Audit Office), and audit reports are offered to principals as an input for their further decisions.

The whole process consists of five main steps implemented along the delegation chain presented in Figure 1:

1. *Initial delegation of tasks from principals to their agents*, in this case the Federation Government and Federation Parliament designed and adopted the Program, set its strategic goals and objectives and delegated the task of implementation to the Federation Agency and cantonal employment agencies.
2. *Program implementation* is conducted on the practical level by the Federation Agency and cantonal employment agencies.
3. *Reporting about the Program implementation* is done by the employment agencies towards the Federation Government and the Federation Parliament.

4. *Auditing* is conducted by the Audit Office, which verifies whether the agents' reports are true and fair, whether the set goals and objectives are achieved, and if not, find out why and provide recommendations for improvements.
5. *Follow-up of audit recommendations* is the final step of the management cycle, where the principals, by using the reports from the Audit Office, overcome the information asymmetry problem and can exercise their control function.

The five steps described above are subject to deviations and problems characteristic of the principal–agent relation described in the theory. The root cause of these problems is in the vested interest of the agents who like to use all opportunities to tweak the information they exchange with the principals in ways that suit their own interests. For example, the agents are interested in receiving budget funds to achieve the goals and objectives they have been delegated – in this case a higher employment rate among the young population. They will often increase their budget requests and justify those increased requests by the demand to achieve the goals they have been delegated. However, they will not disclose full and precise information about the state of affairs within the Program activities, and will avoid describing cause-and-effect relation of how does the budget they utilise actually contribute to achieving the increased employment rate.

Information related to the unemployment problems, their causes and mechanisms to tackle them, is on a professional and expert level. The principals have very little capacity, knowledge, and skills to understand this. To get deeply involved, principals heavily depend on inputs from their agents. This creates asymmetric information. The agents on the other hand deal directly with these issues, which puts them in an advanced position over their principals and gives them a possibility to manipulate the situation to suit their own interests.

In order to tackle this situation, the constitutions of modern democratic states introduce mechanisms of control and supervision, including the audit office operating directly under the parliament. Audit office has the mandate to look at and analyse any aspect of the government work through financial, compliance and performance audits, each addressing the asymmetric information from their own angle, and report about it to the parliament and the general public. These reports fill in the gaps of asymmetric information and offer a possibility to principals to act on equal terms with their agents and demand corrective measures.

Table 1 shows the main highlights from the theoretical review of the principal–agent problem in the form of the causes and effects applied in the five-step cycle described above. The causes described in the first three rows on left emerge from agents' vested interests described in the principal–agent relationship theory. The causes from two bottom rows emerge from the role of the audit office.

These causes will serve as propositions for qualitative analysis in the case study (further explained in Chapter 2). The hypothetical effects of these propositions are described on the right side of the table and will be formulated as main research questions referred to each level in the principal–agent chain.

Table 1: Causes and Effects of the Principal–Agent Relationship in the Public Sector

Causes	Effects
In trying to avoid or diminish their responsibility to work in the interest of principals, agents tweak and obscure the definition of results they are expected to deliver, and extend their manoeuvring zone.	Government tasks, goals and objectives of public services gradually deviate along the delegation chain, lose their clarity and tangibility, and it becomes difficult to define responsibility for their achievement.
Agents use their position of advanced knowledge compared to that of their principals. They work in line with their own interest, increase budget and operate to achieve their own goals, failing to disclose the full information about state of affairs.	Asymmetric information between principals and agents develops. The deviation started in the delegation stage continues during program implementation. Expenses grow while the results are not getting achieved.
Agents tweak information about reality and hide problems and reasons for failure. Principals do not have capacity, expertise, or desire to see this.	Reporting about the outcome is incomplete and information sharing is selective and limited only to the aspects that suit agents' interests. The asymmetric information deepens.
The audit office reports a problem that would otherwise remain obscured and offers principals an opportunity to demand concrete corrective actions from agents.	Audit office, with a mandate to scrutinise the agents' work and report to principals, balances the asymmetric information between principals and agents.
The asymmetric information has been balanced by audit reports. Principals know the real situation. Audit recommendations provide basis for corrective measures.	Principals demand corrective measures from their agents and have means to follow up on their actions.

Source: own work.

2 RESEARCH METHODOLOGY

2.1 The case study method

The case study as a scientific research method has its earliest origins in law where it served as an effective method of showing a deeper picture and explaining complex legal cases. Similarly, in medicine, the case study method provided scientists with a profound understanding of complex medical problems, which would not be feasible through wider scope methods. During the beginning of 20th century, the case study research method also became dominantly associated with sociology, where it provided added value of deeper understanding of social problems, enabling scientists to take onboard a deeper qualitative aspect of issues under research and a better understanding of the views of actors under research.

According to Tellis (1997), the case study techniques are extensively used in government evaluations of the government programs' effectiveness, mostly because merely quantitative techniques tend to obscure important information that the researcher needs to uncover to determine whether the government's goals and objectives are being met. Adding qualitative data obtained through the case study method to the quantitative data from statistics allows researchers to deeply understand and explain a phenomenon through the process of observation, analysis and reconstruction of elements.

In her overview of case study methodologies, Yazan (2015, p. 134) distinguishes three prominent methodologists, namely Robert K. Yin, Sharan Merriam, and Robert E. Stake. She describes them as three "foundational methodologists in the area of case study research whose methodological suggestions largely impact educational researchers' decisions concerning case study design." In her analysis of their works, she shed some light on often opposing views of using the case study as a research method. A similar analysis of the case study method as the main scientific tool was also conducted by Zainal (2007), with the same conclusion. According to Zainal (2007), despite the criticisms of the case study research as a purely exploratory tool "researchers continue to deploy the case method particularly in studies of real-life situations governing social issues and problems." (Zainal, 2007, p. 5).

Yin (1984, p. 23; 2017, p. 15) defines the case study research method as "an empirical inquiry that investigates a contemporary phenomenon within its real-life context; when the boundaries between phenomenon and context are not clearly evident; and in which multiple sources of evidence are used." Such an inquiry provides the researcher with a longitudinal and systematic examination of events over a longer period of time, a possibility for analysing and understanding deeper contextual circumstances and the relationship between a limited number of events and conditions. According to Yin, there are three categories of case studies:

- *exploratory* case study, usually conducted as a preliminary door opener for designing a further study (such as pilot studies) or as preliminary fieldwork and data collection aimed at defining research hypothesis or questions;
- *descriptive* case study, which may be a narrative, beginning with a descriptive theory that should support the description of the phenomenon or story being told, both in its scope and its depth, and formulate a hypothesis of cause and effect relationships. However, if this theoretical support fails, it means the description lacks rigour;
- *explanatory* case study, which closely examines data at the surface and on a deeper level of the phenomena to explain why and how the phenomena occur in complex and multivariate conditions, which according to Yin and Moore (1987) can be explained by three competing theories – the knowledge-driven theory, the problem-solving theory and the social interaction theory.

According to Yin (1984, p. 15), these three categories are not clearly separated and cannot be placed in any hierarchical order with each other. Case studies can specifically not be considered as purely exploratory as they are often aided by experiments, descriptions and explanations. He advocates that the case study method is a legitimate research method like any other, but in order to make it so, the researcher must very precisely apply a systematic research design and structure and rigorously adhere to it throughout the research process.

Contrary to this rigorous view, Stake (1995) argues that the researcher should be able to make changes and adjustments to their research design in any stage, apart from the initial problem definition and initial questions regarding the observed phenomena that lead to research questions. This viewpoint assumes that the exact course of the study flow cannot be precisely mapped in advance and that every stage of the researcher's work brings new perspectives and clarifications of the observed problems. However, he abandons this rather flexible approach for data validation and insists on data triangulation not only from the sources, but also from analysis of methodology and theory, and researcher's own triangulation of their own interpretations. Stake's definition of case study is similar to Yin's, but he strongly advocates qualitative research and opposes the use of quantitative data. This approach requires sensitivity and scepticism of the researcher, significant understanding and capacity to recognise good sources of data and interpret them robustly.

Among other case study methodologists, it is important to mention the work of Merriam (1998), who along the same lines as Stake is also a strong advocate of the qualitative analysis approach. Her definition of case study is wider than those of Stake and Yin, and she defines it as "an intensive, holistic description and analysis of a bounded phenomenon such as a program, an institution, a person, a process, or a social unit" (Merriam, 1998, p. xiii), and advocates it as a fully legitimate research method on par with other quantitative and qualitative methods. Her work compliments the works of both Yin and Stake, providing detailed guidelines for theoretical construction and qualitative research design.

2.2 Qualitative content analysis method

Qualitative content analysis is an important part of the case study. It is a systematic methodology for analyzing data obtained from archival records, documents and mass media. The messages contained in such written communications can serve as a basis for analysis and testing the hypothesis. "Instead of observing people's behaviour directly or asking them questions about that behaviour, the researcher obtains copies of the communication produced (when available) and asks questions about these records. The content of the communication serves as the basis for making inferences." Frankfort-Nachimas and Nachimas (2000, p. 295).

According to Bengtsson (2016), qualitative research methods help the researcher understand and explain human behaviour in different contextual conditions, and to achieve this, the researcher ought to follow the same research design rules as in any other study. This is also in line with well-established case study research concept rules set by Yin, Stake and Merriam. The process of qualitative contents analysis consists of breaking the text into its comprising elements, then rebuilding them into a new message relevant from the perspective of the research aim, as described through four main process stages:

- *decontextualization* is breaking the text down into smaller *meaning units* that contain some of the insights needed in the research. This is followed by coding these units according to their meaning *context*, or in other words, determining the value they add or effect on issues they refer to. For example, a *meaning unit* can be one word or statement, and a *context* can be a sentence in which these are used;
- *recontextualization* is checking, from the perspective of the research aim, whether all aspects of the content of analysed text have been covered, marking parts of the texts that contain the *meaning units* and keeping it for further analysis. The remaining parts of the text are excluded from the scope to help keep the focus only on messages necessary to support the aim of the analysis;
- *categorization* is defining themes and categories based on the *meaning units* and their *contexts*. Dividing themes and categories can be done on the basis of research questions or theoretical assumptions;
- *compilation* is the process of analysis of the *meaning units* and their *contexts*, synthesizing them into messages from the perspective of the research aim, and writing up researcher's observations based on this. This requires the researcher's effort to maintain neutrality and objectivity.

This method is sometimes also applied in interviews analysis by first writing them down and then subjecting them to the same process. In wide scope social studies, such as the effects of marketing campaigns or wide social phenomena, this method can also be aided by quantitative dimension, for instance by counting the frequency of a certain term (as a meaning unit) in news articles (as context).

2.3 Case study with qualitative content analysis method

This thesis is based on the case study research method in combination with qualitative content analysis method. The main reason for using the case study method is that it provides a possibility to go deep into the cause and consequence analysis. The nature of the principal-agent problem is that it spreads along the vertical management structure, and having a full picture of this problem requires a good insight deep into the relations between different levels of this vertical structure. The results of this case study are possible to generalise and are fully applicable on any other government program or activity observed from the same vertical perspective. Lessons learned from this research can also be applied in performance audit, which adds value to this research.

According to Yin (1994, p. 20; 2017, p. 27), the case study design consists of five main components presented in the table below. These components are widely accepted by other authors as well and are generally considered as one of the main conditions securing that the case study method, if repeated by other researchers, allows arrival at the same conclusions. The five components are listed in the first column of the below table, followed by their explanation in the middle column and by a description of how they are applied in the analytical framework of this thesis.

Table 2: Components of the Case Study Design

Case study design components	Explanation	Application in this thesis
<i>Unit of analysis</i>	Primary unit of analysis – an organization or a group that is the subject of study.	Youth Employment Program and implementing institutions <i>(Described in sections 3.1, 3.2).</i>
<i>Propositions</i>	A statement, an idea or criteria, arising from theory, for judging the phenomena or characteristics.	Behaviours that are characteristic of principal–agent relation <i>(Laid out in section 1.5).</i>
<i>Questions</i>	Study questions focusing attention to some phenomena within, or characteristics of the primary unit.	Five research questions derived from principal–agent relation <i>(Laid out in section 1.6).</i>
<i>Interpretation criteria</i>	Criteria for interpretation of the findings in order to answer the questions.	Qualitative analysis of the government documents related to the Program <i>(Appendix 2).</i>
<i>Linking logic</i>	Connecting facts from empirical evidence with propositions or criteria.	Explanation and discussion of the empirical evidence meaning <i>(Laid out in Chapter 6).</i>

Source: Adapted from Yin (2017, p. 27).

The subject of the qualitative content analysis applied in this research are the government documents related to the process of planning, implementation and reporting about the Program, audit reports, as well as correspondence between the Federation Parliament and responsible agencies. These documents are the main channel of communication between principals and agents. Since the research aims to show the asymmetric information between principals and agents, it is the qualitative contents of these documents that is the main focus of the research. Also, the Program selected for analysis by the case study method is well documented by the government in its publicly available documents, which facilitated completeness and comprehensiveness of the research.

The four-step analysis described in the subchapter 2.2 meant reading and analysis of a total of 72 various government documents, selected based on their place and time of institutional origin. Computer-aided tools, including search functions in MS Word and Adobe Reader, were also used to exclude documents without the necessary information. The average size of these documents is around 50 pages and sometimes more than 200. All the documents have a clear and standardized structure, which facilitated easier focusing on the content necessary to answer the research questions.

All the documents are publicly available, however, since they originate from different institutions and different time periods, they are scattered in various online locations and physical archives of the government. To facilitate the repetition of this research, an electronic copy of all the source documents is secured in an online shared folder and organized into subfolders according to their subject and origin (access to this folder is available upon request). This process was also an essential part of the four analytical steps below. The four qualitative analytical steps have been implemented:

1. *Decontextualization* stage included the identification of relevant government documents and then within them, finding *meaning units* – the stated definitions of program goals and objectives, description of delegated tasks, conditions, norms, and all other terms, statements and definitions relevant for each of the research questions. This also included the careful finding of *contexts* in which these meaning units are laid out, practically, providing a possibility to understand their meaning and effect they have in the entire system;
2. *Recontextualization* stage included the selection of text parts relevant for the research questions (*meaning units* and *context* as defined above), highlighting them and marking as relevant, thus identifying their location within the mass of the text. This was important in order to clear out thousands of pages of text unimportant for the research questions. An important part of this process was also making sure that a *meaning unit* or *context* is taken into account each time it is mentioned in order to secure relevance;
3. *Categorization* stage was the process of copying relevant *meaning units* and their *contexts* from all the documents into the empirical analysis chapter and sorting them out according to research questions;

4. *Compilation* meant the analysis of the *meaning units* and their *context* from the perspective of theoretically based propositions from Section 1.5, connecting cause and consequence links, and based on this, providing grounds for later answering to the research questions.

Empirical evidence presented in Chapter 3 consists of meaning units and contexts collected during decontextualization and recontextualization, which are categorized into sub-chapters. Each sub-chapter ends with a couple of paragraphs of compilation. These four steps of the qualitative analysis process, together with questions, propositions, criteria, connecting logic, sources, etc. are presented in the main research design matrix in Appendix 2.

2.4 Main research questions and analytical matrix

The five questions of this thesis follow the five steps management cycle: planning, implementing, reporting, auditing and follow-up. The questions are referred to each level of the delegation chain and follow the communication process between them, as described in Figure 1. This is presented in research design matrix in Table 2. A more detailed research design matrix with research questions, propositions, criteria and sources of qualitative analysis is provided in Appendix 3. To facilitate an easy overview of the research outcome, the answers are provided in the same matrix in Chapter 4.

Table 3: Analytical Framework Matrix for Qualitative Analysis of the Case Study

Delegation chain level	Goals delegation and planning	Implementing	Reporting	Auditing	Follow-up
<i>Federation Parliament</i>	Is there a deviation of tasks, goals and objectives throughout the delegation chain?	Is implementation going in line with the principals' expectations?	Is there a deviation in reporting from agents to principals?	Does the audit office fill in the information asymmetry gap?	Do the principals use audit reports to demand corrections?
<i>Federation Ministry of Labour</i>					
<i>Federation Employment Agency</i>					
<i>Cantonal employment agencies</i>					
<i>Employers and employees</i>					

Source: own work.

3 CASE STUDY: THE YOUTH EMPLOYMENT PROGRAM

3.1 The context in which the Program is implemented

Bosnia and Herzegovina gained its independence from the break-up of Yugoslavia in March 1992 and was immediately turned into war until the end of 1995 when the Dayton Peace Agreement was signed. Due to compromises of the peace accord, the government is organised in a very cumbersome structure and split between two entities, Federation of Bosnia and Herzegovina (hereinafter: FBiH), and Republic of Srpska (hereinafter: RS), which does not facilitate a progressive economic recovery. The war, followed by a difficult transitional process, has left deep economic and social consequences, including a very high unemployment rate. According to official data from the Labour and Employment Agency of Bosnia and Herzegovina, at the end of 2010 – which is 15 years after the war – more than 43% of the working-age population was officially unemployed. Due to a high share of the black economy, this official data is not fully accurate, however, it still indicates a government failure to achieve one of its main overall objectives, i.e. to maximise employment. There are many reasons for such a situation, the government structure is only one of them. The government system of Bosnia and Herzegovina consists of five different levels, each with their own legislative, executive and judicial government branch:

1. State level (Institutions of Bosnia and Herzegovina);
2. Entity level (FBiH and RS);
3. Cantonal level in FBiH (10 cantons);
4. Municipal level (79 municipalities in FBiH and 63 in RS, total 142);
5. Brcko District (an administrative district under the jurisdiction of the state).

Different roles and functions of the government are divided between different levels. For example, the macroeconomic monetary policy – whose one of the main goals is general employment – is managed at the state level, while almost all fiscal policy instruments are managed at the entity level. Such an arrangement does not facilitate the synergistic implementation of different government tools and instruments, especially since the functions of coordination between different levels and stakeholders are often inefficient due to political instability. Almost all responsibilities directly and indirectly affecting employment are on the lower levels, and in the case of Federation BiH, they are split between the Federation Parliament, the Federation Government, the Federation Ministry of Labour and Social Policy, the Federation Employment Agency, and ten cantonal employment agencies. These responsibilities include the regulation and development of the labour market, supporting and facilitating connections between employers and job seekers, providing direct financial support to the unemployed population and other related activities and programs.

3.2 Introduction of the Youth Employment Program

Since the beginning of 2001, the institutions in the FBiH have been conducting many regular and ad hoc activities addressing unemployment, including various activities focused on support to the younger population. Through different implementation phases, these activities have undergone many adjustments and changes. Since April 2010, they were structured under the umbrella of the "Youth Employment Program in the Federation of Bosnia and Herzegovina" (hereinafter: Program), designed by the Federation Employment Agency (hereinafter: Federation Agency).

The Program was based on the "Employment Strategy of the Federation of BiH 2009–2013" (hereinafter: Strategy), drafted by the Federation Ministry of Labour and Social Policy (hereinafter: Federation Ministry of Labour). The Federation Ministry of Labour conducted a comprehensive and in-depth analysis of social and economic circumstances in Bosnia and Herzegovina, which identified various causes of unemployment problems and drew lines between these causes and their effect on different social groups.

This analysis served as a basis to define strategic goals and objectives, each of them focused on a specific social target group, with explained nature of their unemployment problem. The goals were then broken down into sub-goals with defined operational programs and measures designed to address the causes, which altogether comprised the Strategy vision to "achieve maximum employment and use of existing human resources." (Strategy, p. 9, 2008).

Young population aged 15 to 24 is one of the target groups specifically recognised in the Strategy. According to statistics from 2007 and 2008 based on which the Strategy was drafted, there were 67,000 unemployed young people in the Federation of BiH in this age, with completed education, and as job seekers. However, due to an imbalance between the education system and what it supplies, and labour market demand and employers' workforce needs, these young people had difficulties in finding jobs. The Strategy further elaborated specifics of the problem and defined concrete measures to address the causes and roots of these problems (which will be further explained in later sections). The expected result defined by the Strategy was that the employment rate of this target population group should increase from 11.6% in 2007 up to 25% by the end of 2013. (Ministry of Labour and Social Policy of the Federation of BiH, p. 57–58, 2008).

One foreseen measure to achieve this objective was to facilitate the transition from school to work through financial subsidies for potential employers for recruiting young people and cover the cost of their salaries for a certain period of time. After that, these young people would become more experienced and more desirable for employers. This was elaborated under the Strategy sub-goal "securing active participation in the labour market of young people aged 15 to 24 by increasing their capacity for integration into the labour market." (Ministry of Labour and Social Policy of the Federation of BiH, p. 10, 2008).

The Strategy served as a basis for designing the Program in the Federation of BiH. The Federation Government approved funds for this purpose, and through the Program, awarded them to employers to cover the salaries costs. The Program was implemented by the Federation Agency together with 10 cantonal employment agencies. The Program was conducted through the following phases:

1. *Planning phase* – the Federation Agency allocates financial quotas for employment agencies in each of ten cantons. The number of beneficiaries for each canton is based on their size and social and economic circumstances. The quotas and financial plans are laid out in the annual plan approved by the Federation Government.
2. *Implementation phase* – the Federation Agency publishes a media invitation for potential employers to apply for funds for financing youth employment, together with the criteria and conditions for selection and awarding. Interested employers apply to cantonal agencies who process applications and select successful applicants, sign contracts and implement the Program. Cantonal agencies have a responsibility to closely cooperate with employers during the jobs co-financing period, to monitor results and safeguard the proper implementation of the Program.
3. *Reporting* – the cantonal agencies draft reports about the process of the Program implementation, the number of beneficiaries of co-financing for the salaries and the outcome. These reports are submitted to the Federation Agency, which drafts annual reports and submits them to the Federation Government.

These three phases follow the first three (of five) steps of the analytical framework of this research. There were some minor differences in this Program structure during the observed period, with minor overlaps in the responsibilities and the implementation process but not in a way to make the Program not applicable as a case study in this research. Nevertheless, these differences are worth mentioning and explaining for the sake of clarity:

- When the Program implementation in its current form started in 2010, the Federation Agency was already implementing activities designed in the same way as those in the Program, except that these were implemented by the Federation Agency directly, without cantonal agencies participation. These activities started in 2009 and were continued during 2010. Their share in total Federation Agency activities are much smaller, however, these overlaps contribute to difficulties in measuring the direct effects of the Program, as will be described later.
- In 2013, besides the financing from the Federation Agency budget, a part of financing was covered by UNDP under the program initiative titled "400+". In some instances, financing from the cantonal level sources and those from the Federation level was also combined. However, the exact financing source is not in a specific focus of this research and does not affect the perspective of the principal-agent problem, the majority of funds still came from the Federation level, and vertical division of responsibilities was not affected.

- There have also been other programs implemented in the observed period, such as those focused on the return and reintegration of refugees, self-employment, the employment of minorities, etc. which have been implemented by the Federation Agency as well as by the cantonal agencies. These programs sometimes overlapped with the Program, however, such instances did not affect the Program as a whole, only some implementation details. For example, between two Program applicants with the same score, the one fulfilling the criteria of some other program would simply be given an advantage.

The delegation chain regarding the phases of planning, implementing and reporting is unchanged by these structural differences. A detailed description of the Program laid out in the next sections follows the three Program phases described above.

3.3 Program planning

The main planning document related to the Program is the "Program for Co-financing the Employment of Young Persons Without Work Experience" (hereinafter: Program Document) prepared by the Federation Agency in April 2010. The Program Document lays out the overall program objective, structure, finances, processes, and criteria for selection of program beneficiaries. This is further elaborated in the annual plans of the Federation Agency, which include the budget and the number of expected beneficiaries for every year.

On the cantonal level, each employment agency adopts their own annual plans, which are aligned with the plans from the Federation level. As their main basis, all these planning documents refer to the Strategy and the Law on Mediation in Employment and Social Security of Unemployed Persons in the Federation of BiH.

The overall Program goals and objectives are originally defined on the top level by the Strategy and in the background notes of adopted laws which regulate the area. All the detailed program plans and annual plans refer to these goals definitions as their main purpose. This means that the planning process is going along the delegation chain, starting from the principals on the top level of the Federation of BiH (the Parliament and the Government), via the Federation Agency (the agent), all the way down towards the cantonal-level employment agencies as actual implementers on a more practical executive level. In this case, the largest one, Sarajevo Canton, will be used as an illustration.

Table 4 shows the definitions of the Program goals (exactly translated into English), as they are laid out in relevant government documents – the Strategy, the main Program Document and the Program implementation plan on the level of Sarajevo Canton. On the left side are the levels of delegation chain from top to bottom, followed by the relevant document they adopt. On the right side is the Program goal cited from the relevant document.

Table 4: Definitions of the Program Goals Throughout the Delegation Chain

Delegation chain level	Related Program document	Definition of the Program goal
Federation Parliament (Ministry of Labour and Social Policy of the Federation of BiH)	Strategy of Employment of the Federation BiH 2009–2013 (2008, October, p. 9)	"Securing active participation in the labour market of youth aged 15 to 24 by increasing their capacity for integration into the labour market."
Federation Employment Agency	Program of Co-financing the Employment of Young Persons Without Work Experience (2010, April, p. 2)	"Enabling the employment of people younger than 30, without work experience, who are recorded in the evidence of unemployed people in Federation BiH, who are getting a job for the first time."
Canton Sarajevo Government	Program for employment incentives and increasing the employment rate in Canton Sarajevo (2011, February, p. 1)	"Co-financing of employment, in their professional area, of young people without work experience younger than 30, who are registered in unemployment records before the publication of the public invitation."

Source: Ministry of Labour and Social Policy of the Federation of BiH (2008); Federation Employment Agency (2010d); Canton Sarajevo Government (2011).

By careful reading of the Program goals and comparing the goal definition in the Strategy adopted by the top principals, against the goals definitions in the Program work plans of the agents, a gradual deviation is noticeable in three main dimensions:

1. Changing of the *expected effects* of the Program, by changing the key terms used in the definition of the goals: **securing, enabling and co-financing**;
2. Changing the age of the Program *target group* and extending the upper age limit from originally envisaged **24 years** up to **30 years** of age;
3. Changing the *criteria* so that only the **first-time** job seekers can be the Program beneficiaries.

The changes which appeared in the planning stage have an intricate impact on the Program implementation and later on the final effect of the Program. Loose definitions of the Program goals are easier to achieve for the implementer and expectations of the environment regarding the effectiveness are less binding. Changing the implementation framework by extending the target group age and changing the beneficiary selection criteria leaves more room for manoeuvring during the implementation process, as described in following subsections.

3.3.1 Changing the Program goals

The key term used in the Strategy adopted by the top principals is "securing", while the employment agency uses the term "enabling". These two terms do not contradict, but their meanings have a different strength and imply a major difference in understanding the Program effect and the tangibility of the Program outcome. The Strategy clearly defines "securing active participation...", which implies that through the Program, active participation of young people in the labour market is secured, or in other words, they do get jobs. On the other hand, the Federation Agency defines the Program goal as "enabling the employment of young people...", which means the expected outcome is that young people are "able" to participate in the labour market, but this participation does not necessarily mean that they do get jobs. Moving further down the delegation chain, the difference in the Program goal definition becomes even greater. Sarajevo Canton defines that the Program goal is "co-financing...", however, co-financing (or financing) of any activity cannot be a purpose in itself, it can only be a tool or an instrument for achieving a certain goal, not the goal in itself.

The employment agencies' responsibility for the Program implementation means they should strongly engage and closely cooperate with the employers to secure that job financing brings results in long-term employment. But this way of completely leaving out the expected Program effect from the goal definition implies that the implementer's responsibility ends with the completion of the financing cycle for a work post, without caring about the purpose or the expected effect – whether the participants will keep these jobs after the Program completion or not. Such a release of responsibility for the final effect of the Program means smaller expectations and lower pressure on the employment agencies, which leaves more room for manoeuvring and following their short-term interests as the agents.

3.3.2 Changing the target group

One of the specific target groups defined in the Strategy is the young population aged 15 to 24, especially those with a lower level of education. The typical age of completing primary school is 15 and between 18 and 20 for secondary school. After obtaining a school diploma, young people are ready to take low-paid jobs requiring basic knowledge and skills – if they can find an employer demanding their services. With less education and skills, they have more difficulties in finding a job than people with a university degree, and they need more support. Those who decide to resume education complete their higher education cycle typically by the age of 24, or up to the age of 30 for the post-graduate studies. A higher-level education, and more time to obtain some work experience, makes people in this age group more desirable and they find jobs much easier. This is verified by the official statistics. According to the Statistical Bulletin published by the Agency for Statistics of the Federation of BiH for 2007 and 2008, the number of people in the age from 25 to 29 who have jobs is double higher than those in the age under 24.

The analysis from the Strategy shows that one of the main causes of unemployment of the youngest population in the age up to 24 is an imbalance between the school-acquired skills and those that the labour market demands. Many school programs focus on such professional areas that the labour market does not demand, producing a surplus of unneeded professions. Besides, even for in-demand professions, school programs are highly theoretical and do not provide the practical skills required by the companies, especially in labour-intensive areas such as industrial production and manufacturing. The system is focused on teachers rather than students. When they finish school, young people are not prepared to do the jobs which they have formally been educated for, so the companies are not interested in recruiting them as they would need to invest much more to make these people useful for work. This is the reason why the Strategy states that the highest priority for support measures should be given to the young population of up to 24 years of age.

However, during the Program design by the Federation Agency, the upper age limit of the Program target group was increased from 24 up to 30 years of age and specifically included young people with a university degree as one of the target groups. In the Program, the Federation Agency allocates funds for co-financing their first job experience using the official levelling scheme defined in the formal qualifications framework in Bosnia and Herzegovina, which splits labour force into eight levels depending on the completed level of education. The period of time for co-financing and the amount of money per month is different for every group, as allocated in the annual plans of the Federation Agency. This scheme is presented in the following table.

Table 5: Target Group in the Annual Plans of the Federation Agency

Level	Category	Explanation	Typical age	Period (months)	Amount per month	Total cost per person (BAM)
I, II	Unskilled	Primary school	> 16	6	300	1,800
III	Low-skilled	Secondary school (3 years)	> 19	6	300	1,800
IV	Skilled	Secondary school (4 years)	> 20	6	350	2,100
V	High-skilled	High school up to 2 years	> 22	12	400	4,800
VI	BSc	University diploma (3–4 years)	24 <	12	450	5,400
VII,VIII	MSc, PhD	Postgraduate (+2 or more)	26 <	12	450	5,400

Source: Council of Ministers of Bosnia and Herzegovina (2011).

Co-financing the jobs of higher educated people costs significantly more – because their expected monthly payments are higher and the co-financing period is much longer, so the total cost per person is two or three times higher. Practically, for the cost of co-financing such a job, three persons with a lower level of education can start getting their first work experience. Extending the age limit of the target group originally defined in the Strategy and this way of distributing the financial resources for the Program has severe consequences:

- The total number of young people who are eligible to apply and participate in the Program is much wider, which has an impact on the Program implementation process and the total financial cost;
- Due to the widening of the age limit, the population group with the highest priority for receiving assistance is not in focus throughout the Program implementation. This undermines the very idea and purpose of the Program.

The Program Document in its definition of the target group, says that "in the case there are not enough applications from one education level group, the Program funds will be reallocated to the education level group which has a higher number of applications" (Federation Employment Agency, 2010d, p. 2). This indicates that already in the initial stage, the Federation Agency was planning to simply go with the flow instead of pushing for proper implementation of the Strategy goals. Addressing the right target group means additional efforts and activities to assist the most endangered group of population, but instead, the Federation Agency chose to allow and this way indirectly support the employers' behaviour in which their short-term interests prevail. As will be seen later, this trend continued throughout the implementation process.

In practice, employers' participation in the Program practically means getting a free workforce for a certain period of time. Inclusion of a higher education group in such an arrangement means a longer period for financing these free work posts and higher payments from the government per person. This means that for them it will be easier to fill in the operational gaps for free. For the employment agencies, fewer individual beneficiaries for the same amount of funds means less administration and less follow-up.

3.3.3 Changing of the participation criteria for the Program

As shown in Table 4, the Program goal of the Federation Agency as well as the Employment Agency of Sarajevo Canton both define that the target group for Program participation is limited to individuals seeking jobs for the first time. It is also worth noting that the Federation Agency's definition of the Program goal says the Program is focused on young people "without work experience", then again in the same sentence later "...who are getting job for the first time", which is basically a repetition of the same principle strongly underlining who can and who cannot participate in the Program, but it does not contribute to the clarity of the goal definition.

This limitation practically means that a person is prohibited from participating in the Program in case they have any work experience. However, such a limitation does not exist in the Strategy, it is rather a result of agencies' own design of the Program rules and criteria, similar to the case of determining the Program target group described above.

The agencies' motivation for this alteration could be explained by their desire to narrow down any possibilities for the Program abuse. Without this formal limitation, some individuals and their employers could repeatedly apply for new financing cycles and participate in the Program indefinitely. The limitation also makes sense from the perspective of opening opportunities for a new round of individuals to participate and benefit from the Program in every new financing cycle, since the Program purpose is to offer an opportunity for the first job experience to as many individuals as possible.

There are, however, different implications of this limitation when it is introduced in such a flat and exclusive way. First of all, there is a problem of discrimination against certain groups – there are many individuals who could just have a temporary job or a job unrelated to their education and skills, but such an experience would immediately exclude them from a possibility to participate in the Program. Practically, having some job experience makes them less desirable than those without any experience at all. Secondly, many individuals had participated in the Program but were let go after the financing period was over and could not participate in the Program anymore. The main problem with both scenarios is in the fact that keeping the job does not only depend on those young individuals – however much they may try, the final decision on their permanent or long-term employment depends whether the employers want to keep them.

This is where the main problem with this Program lays – in the employers' motivation to give young people an opportunity for long-term or permanent employment. The idea of the Program is that the Federation Government, by covering the initial salaries cost, should facilitate a smooth transition from school to work, so that the employers do not have to bear the cost of employees' skills that would normally have been provided by the school system. This way the Program would fill in the gaps from the education system and fresh graduates would obtain additional skills needed to become useful for the employers. The employers could keep them because, in the long run, this would mean extending the business operations and increasing their profit. Even if they would not stay at the same work posts with the same employers, obtaining proper skills and experiences would facilitate finding a long-term job very quickly.

An outcome in which the employees acquire necessary skills and experiences would require on-the-job training, career development opportunities and first-hand practical experience in exactly the area of work they have been educated for. If on top of that they would be gradually integrated into the company organization, they can simply just continue working and contributing to the business after the government financing cycle is finished.

Making this work requires a business development plan from the employers and a clear vision of long-term expansion with a new workforce. From the perspective of the employment agencies, this would mean that they need close work with the employers and follow-up the personal development of the employees whose salaries are paid for, in order to secure that employers do not use the employees as a free workforce, and instead offer them jobs with an opportunity for their professional growth, and finally, that they keep them when the financing period is over. A business and market-oriented company standing on healthy feet and interested in its own long-term growth could normally be expected to have this way of thinking. However, the reality has proved to be different. As will be shown in section 3.4., the employers did not keep the employees in most cases, which indicates that they rather opted for their short-term interests and filling in their operational gaps with a free workforce.

In order to prevent such a behaviour, the Federation Agency defined in its Program Document a set of rules and provisions that, in order to be eligible to receive funds from the Program, the employers are obliged to keep the employees for at least half a year after the completion of the job co-financing period (or one full year for employees with a university degree). The applicants must also submit paperwork proving they have all their taxes paid, that they have returned any state loans or fulfilled their obligations arising from any other arrangements with the government based on other economic development programs. Sure enough, these provisions indicate that the employment agencies have introduced tools and mechanisms in their Program selection criteria to prevent misconduct and abuse; however, in doing so, the agencies have opted for a rather superficial bureaucratic solution.

In practice, these provisions do not require much effort from a bureaucrat to simply demand additional paperwork from the applicants; however, close cooperation with the employers, continuous contacts with both employers and employees during the financing cycle, follow-up of their personal developments, demanding deeper involvement of employees in organization, etc. require much more work.

3.4 Program implementation

The changes in the Program goals and objectives observed in the planning stages continued throughout its implementation. Deviations from the Strategy that appeared during the planning became even more drastic during the implementation. This can be seen by analysing the annual plans and reports of the Federation Agency for the period defined in the Strategy, from 2009 until the end of 2013 (detailed analysis provided in the Appendix 3). Comparing the planned number of beneficiaries with actual Program participants at the end of the observed period, it can be concluded that there are strong inconsistencies between the Federation Agency plans and reports related to the Program. It is not possible to clearly track the Program implementation over the observed period, there are no result indicators, and the jobs co-financing activities are scattered around various programs.

Contrary to the strategic priorities to focus on young people with lower education, the outcome at the end of 2013 shows that almost half of all the Program beneficiaries were from the category of higher education. Since their job co-financing costs more, when financial indicators are taken into account, this discrepancy becomes even stronger: more than two thirds of all financial funds were allocated for the category with higher education. Overview of this data is laid out in Table 6, with a more precise analysis in Appendix 3.

Table 6: Overview of the Target Groups and Allocation of Funds

Year	Low education		High education	
	Beneficiaries	Amount (BAM)	Beneficiaries	Amount (BAM)
2009	300	570,000	90	462,000
2010	401	1,128,000	123	871,000
2011	325	736,800	544	3,762,900
2012	245	590,940	78	526,968
2013	413	1,139,880	537	2,964,240
TOTAL	1,684	4,165,620	1,372	8,587,908

Source: Federation Employment Agency (2008), Federation Employment Agency (2010d), Federation Employment Agency (2012a), Federation Employment Agency (2013), Federation Employment Agency (2014).

Annual plans and reports of the Federation Agency do not provide any explanation or motivation for this deviation from the Strategy. By looking at these documents, it is only possible to see the numbers and the elaboration about the general purpose of allocated funds, including references to the Strategy and the Law, however, these references do not include any other documents or communications that elaborate reasoning behind these significant changes.

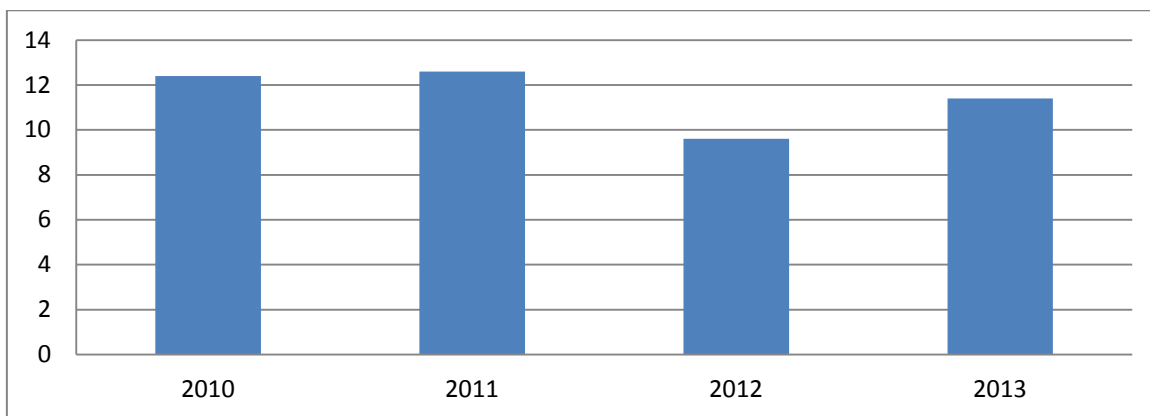
According to the Program rules and procedures, the only applicants for the Program funds could be companies. Unemployed persons could not apply for the Program directly. The only thing they could do was to first find an employer who would be willing to take them and then apply to the Federation Agency for the Program funds to finance their temporary employment. This would, however, still not guarantee that they would be the ones who get the job. Practically, the employment agencies have completely focused their Program on the support of unemployed persons to the employers rather than supporting the employees who were supposed to be the final Program beneficiaries. This way of managing the Program contradicts its very nature defined in the Strategy.

The practice during the implementation was the same as in the case of the main Program Document described in section 3.3, it indicates the continued presence of short-term interests of employers who practically receive a free workforce through the Program. They are naturally interested in more funds per person and in longer periods in benefiting from their free work and service. The Federation Agency responsible for the funds distribution appeared to follow this same interest, which could be explained by simple pressure from the employers. They were naturally less interested to participate in the Program with low-educated people when they could just as easily get higher educated people to participate, and thus be better off from the perspective of their short-term interests. Finally, as explained at the end of section 3.2.2., the Federation Agency already said it clearly in their Program Document during the planning stage that they would allow this trend.

3.5 Outcome of the Program

As we have seen, the differences in the definitions of the Program goals and design framework were reflected in the Program plans and throughout the process of implementation. As for the projected Program effect, the Strategy defines that the employment rate of the target group of the young population aged 15 to 24 should grow from 11.6% in 2007 to 25% in 2013. Figure 2 shows the changes in the employment rate percentage of this target group in Federation BiH during the Program implementation period.

Figure 2: Employment Rate Percentage During the Program Implementation Period



Source: Agency for Statistics of Bosnia and Herzegovina (2010), Agency for Statistics of Bosnia and Herzegovina (2011), Agency for Statistics of Bosnia and Herzegovina (2012), Agency for Statistics of Bosnia and Herzegovina (2013).

As can be seen from the Figure 2, the result foreseen by the Strategy has clearly not been achieved. The employment rate has hardly changed, it is even slightly lower than at the start of the Program. Explanations for the failure can be found in many different internal and external factors. The observed period was marked by the world economic crisis which also affected the economy of Bosnia and Herzegovina. Besides, the success of the Strategy required a strong synergy of different tools and instruments, coordination between all

relevant stakeholders in different matters and activities related to the Program. In such a wide variety of different factors of success, it is rather difficult to point towards a lame definition of the Program goals or Program design and implementation as one of the causes for failure. Question is also raised as how realistic were the set expectations of 25%, or the premises and analysis that preceded them.

However, one can surely not point towards the responsibility of the employment agencies for not achieving the expected result – because in their Program goals and plans, they never stated they would achieve such a result. The agencies did refer to the Strategic goals in their activity plans and when requesting funds for the Program implementation, however, their activities and the funds invested in the Program were practically not connected with the expected outcome.

Such a release of responsibility for expected results is even more visible if we look closer into the direct outcome during the Program implementation – the Program did not manage to achieve long-term employment even for its participants. According to the Performance Audit Report on Management of the Youth Employment Program (2012, pp. 24–25), more than half of the participants did not get a permanent job after the Program completion. In the survey conducted as part of the audit, a majority of those employers who did keep the employees after the Program completion said that they were going to employ these people anyway, even without temporary co-financing their salaries. This practically means that the Program did not directly result in young people getting jobs, and in the cases it did, it was due to other reasons that were not contributed by the Program itself.

3.6 Agency reporting about the Program implementation

The reporting process was going along the same delegation chain in the backward direction – from the agents on the bottom towards the principals on the top. Every year, the cantonal agencies submit their information about implementation to the Federation Agency, which they collect from the companies they work with, including the data about the end-users of the Program funds and achieved results. The Federation Agency compiles all the information into its own annual report and submits it to the Federation Government. The Program was designed on the basis of the Strategy which included some very detailed analysis of causes and effects contributing to the unemployment problem, with proposed activities and explanations of how these measures improve the situation. One could expect that reporting about the Program implementation should include information about these essential issues, with references about the root causes and how certain Program activities addressed them. Such reporting would normally cover the total Program outcome with many people who got a long-term or permanent job as a direct result of the Program activities. It could be expected that some in-depth analysis and explanations of the processes, first-hand observations of the situation in the field, etc. would follow. Additionally, explanations for deviations, if any, from the expected results could be expected as well.

However, the reports did not include any of these insights. Instead, they only cover information about the finances and some superficial issues related to the processes. For example, the Federation Agency states in all its annual reports the number of Program beneficiaries, e.g. how many young people went through the Program and what was their level of education, but without mentioning if they kept their jobs after the completion of the financing cycle. Besides, there are some other problematic issues with the contents of these annual reports:

- In the 2011 report, the Federation Agency mixes the Programs implemented via cantonal agencies and those implemented directly, which makes it difficult to clearly follow the effects of individual activities. It is especially difficult to identify any problems in the implementation or how they might have been caused. (Federation Employment Agency, 2012);
- In the 2012 report, the Federation Agency reports about the Program activities implemented together with UNDP, including the finances donated by the UNDP, however, just like in other Program activities, it remains unclear whether this had any positive impact on the youth employment rate. (Federation Employment Agency, 2013);
- Reports for 2012 and 2013 do not distinct between the four categories of the beneficiaries' levels of education, instead, they are grouped in two categories. (Federation Employment Agency, 2013, 2014);

Reading the Federation Agency's reports does not offer a possibility to get familiar with the state of affairs in the Program. Even at the very first sight, by simply looking at the number of users and distribution per age group, it is obvious that throughout its implementation, the Program highly deviated from the strategic goals and directions. However, the Federation Agency reports do not offer any explanation or reasoning for these deviations. The continuous changing of the target group and failure to support the most vulnerable population are left without any explanation. From the Federation Agency reports, the principals cannot get a real picture about fulfilling the tasks delegated to the agencies at the entity and cantonal levels.

It is interesting to note that all these annual reports were every year adopted by the Federation Ministry of Labour and Social Policy which is responsible for the employment area, similar to annual plans that go through the budgeting process. All these documents are also publicly available on their web sites. The fact that adoption of both the plans and reports continued uncritically over the years, indicates the problem of information asymmetry. This also shows the lack of capacity of the Federation Ministry of Labour and Social Policy, who in this structure is a principal responsible for the area, to understand and critically evaluate the issues and the subject matter.

3.7 Reporting By The Audit Office

This section describes how the Audit Office of Institutions of the FBiH (hereinafter: Audit Office) reported about the Program implementation. Every year, the Audit Office audits the Federation Budget (which basically covers the overall work of the entire Federation Government for one year), and the Federation Ministry of Labour and Social Policy. Besides, the Audit Office also audits the Federation and cantonal level agencies, but not every financial year due to its limited resources. Instead, it is done ad hoc and depending on the indications for risk analysis.

3.7.1 Annual audits of the institutions in the principal–agent delegation chain

Financial audit answers the question of whether the financial statements prepared by the auditees reflect a true and fair picture of its accounts, while the compliance audit is done only to an extent of an impact that eventual non-compliance may have on the financial statements of the auditee. These audits thus do not focus on specific activities or programs, but on general auditees' operations observed separately during a financial year. Audit reports are submitted to the management of the audited institutions, to the respective parliaments and the general public. Table 7 shows an overview of audit opinions from the audit reports covering all the institutions in the delegation chain in the period from 2010–2013, which could also impact the Program implementation.

Table 7: Financial and Compliance Audit Opinions in the Observed Period

Year	Federation Budget	Federation Ministry of Labour and Social Policy	Federation Employment Agency	Sarajevo Cantonal Employment Agency
2010	Negative	Negative	Positive	
2011	Negative	Negative		
2012	Negative	Negative	Reserved	Reserved
2013	Negative	Reserved	Reserved	

Source: Audit Office for Institutions of the Federation of BiH (2011a), Audit Office for Institutions of the Federation of BiH (2011b), Audit Office for Institutions of the Federation of BiH (2011c), Audit Office for Institutions of the Federation of BiH (2012b), Audit Office for Institutions of the Federation of BiH (2012c), Audit Office for Institutions of the Federation of BiH (2013a), Audit Office of Institutions for the Federation of BiH (2013b), Audit Office for Institutions of the Federation of BiH (2013c), Audit Office for Institutions of the Federation of BiH (2013d), Audit Office of Institutions for the Federation of BiH (2014a), Audit Office of Institutions for the Federation of BiH (2014b) Audit Office of Institutions for the Federation of BiH (2014c).

As can be seen from Table 7, the financial and compliance audits during the observed period have almost all resulted in negative or reserved audit opinions. This means that the end-users of these reports cannot rely on the financial statements of the audited institutions involved in the Program implementation. The reasons for the criticism are mostly related to the problems in budget execution, financial reporting, accounting, public procurements, transparency, activity reporting and internal controls. These problems are general problems of operations and management of these institutions, and refer to the scope of work much wider than the Program itself. These indications do not necessarily relate to the Program alone, but to the context in which the Program operated. Nevertheless, these issues can be directly related to the Program or can have an impact on it, as can be seen from the following summarised list of the main audit findings:

- Audit reports of the Federation Budget execution 2010–2013, which all resulted in negative audit opinion, emphasize a lack of proper supervision in the vertical responsibility chain from the Federation Parliament towards the Federation Government and further down towards the ministries and agencies. (Audit Office for Institutions of the Federation of BiH, 2011c, 2012c, 2013d, 2014c);
- Audit reports of the Federation Budget execution 2010–2013 also emphasize the problem of insufficient reporting from the lower levels, especially for transfers, because there is no information from the end-users about the use of funds (including the transfers for social programs). (Audit Office for Institutions of the Federation of BiH, 2011c, 2012c, 2013d, 2014c);
- Annual audit reports of the Federation Budget execution 2010–2013 strongly criticise the Federation Ministry of Finance and the Federation Government for the lack of transparency in their work. (Audit Office for Institutions of the Federation of BiH, 2011c, 2012c, 2013d, 2014c);
- Annual audit reports of the Federation Ministry of Labour and Social Policy 2010–2013 emphasize the problem of lacking a department (or a function) in charge of efficient monitoring and follow-up of the activities related to the social programs, the category of which also covers the employment programs. (Audit Office for Institutions of the Federation of BiH, 2011a, 2012b, 2013a, 2014a);
- In the 2012 and 2013 annual audit reports of the Federation Employment Agency, the Audit Office specifically emphasizes that, due to delay in the start of social programs the implementation, they overlapped with the following year, and since the financial plan is annual-based, it is very difficult to monitor the Program effects. (Audit Office for Institutions of the Federation of BiH, 2011b, 2013b, 2014b);
- In the 2012 and 2013 annual audit reports of the Federation Employment Agency, the Audit Office also emphasizes the problems of a lack of reporting from the cantonal level to the Agency, which indicates deeper problems of a lack of monitoring system. (Audit Office for Institutions of the Federation of BiH, 2011b, 2013b, 2014b);

These findings are a result of the annual audits of all the institutions in the accountability chain related to the Program and show the nature and the environment in which the Program was implemented. The audits clearly indicate deficiencies in the delegation chain and the problems with implementation and reporting about the effects. Recommendations offered in these reports focus on correcting deviations from established financial reporting procedures and regulations that determine the framework of operations of audited institutions.

The main contribution of the annual audits is in a clear fact that the principals cannot rely on the annual financial statements and associated activity reports from their agents. In other words, reporting has failed. These audit reports are focused on the financial and compliance aspects, so they do not point towards the exact issues impeding the implementation and effectiveness of the Program or any other expected goals and objectives delegated to agents, but they clarify the general picture – even if it is a negative one. Performance audit adds one additional analytical dimension to the whole picture and provides some inputs related to the causes of the observed deficiencies.

3.7.2 Performance audit

Besides financial and compliance audits in the Program implementation period, the Audit Office conducted a comprehensive performance audit of the Program in 2012 and published the "Performance Audit Report on Management of the Youth Employment Program (2012)". Unlike annual audits covering operations of institutions during one year, the performance audit covered several years of activities, all functions specifically related to the Program, and all institutions involved in the Program planning, implementing and reporting.

The audit focused on the Program efficiency and the identification of weak links in the processes which could lead to failure. The audit looked at the activities directly related to the Program, interaction between different institutions involved and focused on all issues that have an impact on it. As a result, auditors have identified several weaknesses which can be summarised in the following main findings (Audit Office for Institutions of the Federation of BiH, 2012a):

- Definitions of the Program goals and objectives were poor and wider than those in the Strategy.
- There were no measurable indicators and there was no defined expected outcome of the Program.
- Responsible institutions failed to use relevant inputs during the planning process, such as indicators about the labour market and analysis of experiences from the previous years.

- Distribution of the Program funds was not balanced between the cantons and was inconsistent with the labour market situation.
- There were unclear selection criteria for the Program beneficiaries, and the Program did not address the target group in the greatest need for assistance.
- Abuse of the Program was not prevented and responsible institutions failed to closely supervise the implementation. A single employer could repeatedly participate and collect funds from different sources.
- The employers who did not even apply for the Program during the public invitation, could still participate at later stage.
- There were no equal opportunities for employers to participate in the Program.
- Due to a lack of appropriate information and promotion activities, the Program target group did not have timely and comprehensive information about their possibility to apply and benefit from the Program.
- The responsible institutions failed to monitor and follow-up the Program implementation with the end-users, so the outcome of the Program and the destiny of the beneficiaries remained unknown.
- In addition to these overall findings, the Audit Office points to the missing system of overall supervision and evaluation, and due to this, a lack of possibility to timely undertake corrective measures.

The audit report presents these findings supported with data and information collected from the responsible agencies and ministries, drawing cause-and-effect logical lines of how these findings contribute to the overall audit conclusion that the Program has deviated, in its design and management, from the goals and objectives defined in the Strategy, and failed to support the most vulnerable groups of young people.

Based on these conclusions, the Audit Office gave recommendations to the institutions responsible for the Program. As stated in the International Standards for Supreme Audit Institutions (INTOSAI, ISSAI 300, p. 16, 2013), performance audit recommendations should be aimed at the causes of the failure and should not just be inverted audit conclusions. In line with this, the Audit Office has presented its recommendations broken into parts and addressed to two levels of the principal-agent delegation chain.

These recommendations are summarised in the following lines (Audit Office for Institutions of the Federation of BiH, 2012a):

- It is recommended to the Federation Agency, prior to designing a program, to have a detailed planning process based on an analysis of the labour market and previous experiences, including procedures for close cooperation with partners.

- Criteria and objectives ought to be clear, measurable and precisely aimed at the target group.
- Employers ought to be closely followed-up in their work and activities with the financed employees, in order to stop possible abuse.
- The general public, and especially the target group, ought to be regularly informed about the program.
- The Federation Agency ought to follow-up, coordinate and synchronise the work of cantonal employment agencies.
- All institutions participating in the Program implementation need to have a common vision and uniform working procedures.
- Cantonal employment agencies ought to conduct an analysis and evaluation of the Program on the local level to obtain relevant planning inputs, and based on this, to focus their activities to narrow groups of unemployed population.

In 2019, the Audit Office conducted a new performance audit, covering all active measures implemented by the Federation Agency. The "Performance Audit Report on Management of the Employment Co-financing Programs" (Audit Office, 2019) covers the period long after completing the Program and a much wider range of activities. Since the nature and the context are the same, it is important to mention that this new audit report concludes that there are still the same problems with defining goals and objectives, implementation inefficiency and a lack of supervision and follow-up. Practically, this means very little or no change from the situation seven years ago.

3.8 Implementation of the Audit Recommendations

As explained in the theoretical introduction, typically there is no direct communication between two ends of the delegation chain, the communication happens through several links of delegation. In the case of the Program, recommendations were given to the Federation Agency and the cantonal employment agencies. By following up on these recommendations, the Federation Parliament got a unique opportunity to look directly all the way to the very end of delegation chain, and the Federation Parliament Commission in charge of audit used this opportunity to request concrete information from the Federation Agency and cantonal agencies about their implementation of audit recommendations.

From the Federation Parliament's notes, it is visible that the Federation Agency did not reply to this request, and seven out of ten cantons sent their responses, with percentage presentation of "the level of audit implementation", accompanied with elaboration in few sentences. This is presented in the Table 8, followed by a brief explanation and a summary of the textual responses.

Table 8: Percentage of the Implementation of Audit Recommendations (%)

Canton:	Recommendation: Having a uniform vision and working procedures	Conduct analysis and evaluation of the Program on local level	Focus the measures and activities on unemployed persons
Una-Sana Canton	80	90	100
Tuzla Canton	100	60	80
Central Bosnia Canton	100	0	80
Zenica-Doboj Canton	0	100	100
Herzeg-Bosnia Canton	100	60	60
Western Herzegovina Canton	0	0	0
Herzegovina-Neretva Canton	90	30	60

Source: Parliament of the Federation of BiH (2016).

The percentages presented in the Table 8 are a reflection of the cantonal agencies own assessments, there was no uniform formula or measurement with target indicators that could provide a clear picture of what they actually mean. It may be easy to conclude when absolute values like 100% and 0% are used, but in instances with values like 30% or 60%, it seems hardly possible to get any meaning.

When the provided percentages are accompanied by textual elaboration, they provide some indication about the implementation status. As it appears from the Table 8, cantonal agencies refer to the Audit Office's recommendations as mostly implemented. However, the accompanying textual elaborations show that the real picture is more complex and that there are more missing gaps in the overall implementation level.

Western Herzegovina Canton has all answers marked at the zero level of implementation. In their explanation, they simply state that the first and second recommendations do not apply to them because the vision, the working procedures and the Program design are the responsibility of the Federation Agency, not theirs. Regarding the third recommendation, they state that "unemployed persons are interested in participating in the Program, even if it means only temporary employment, but we have to be aware that there are no jobs since employers who can offer long-term employment are very rare." (Parliament of the Federation of BiH, p. 14, 2016). From their answer, it can be concluded that they also seem to believe the main problem is not the Program focus, but external conditions.

Their answers may look unrelated to the actual audit recommendation and indicate a lack of mutual understanding between the Audit Office and Western Herzegovina Canton. Either the recommendation was not clearly communicated and explained by the Audit Office, or the Western Herzegovina Canton did not understand it. Such a gap in understanding indicates there is a need for deeper elaboration and analysis of the subject matter, and wider and clearer communication.

Elaborations from other cantons state that deviations identified by the Audit Office are mostly caused by complex and inadequate coordination between different levels of the government in Bosnia and Herzegovina, and just like Western Herzegovina Canton, they mostly refer to the Federation Agency as the one responsible to make a difference. This practically means that cantonal agencies do not take responsibility for the recommendations they were asked to implement.

The follow-up process in the case of the Program was a part of a larger package of several sessions that included 10 different performance audit reports analysed by the Federation Parliamentary Commission in charge of the audit. As can be seen from timing of the above correspondence, the follow-up process was done after four years of delay, because the performance audit report was published in 2012, and it was in 2016 that the Federation Parliament sent their questions to the responsible agencies – years after the Program in its original form was completed.

Nevertheless, the fact that many responsible agencies did not find it worthwhile to inform the Parliament on the implementation status of the audit recommendations indicates a lack of accountability and inefficiency of communication along the delegation chain. It also shows that the structure of relations between the principals and agents, which originally created the problem, continued after the introduction of the audit function.

3.9 The Main Research Findings

The empirical part of this research is based on the analytical framework matrix presented in section 1.6, with a five-step process distributed along the delegation chain between principals and agents. Chapter 3 so far presented a detailed analysis of the empirical evidence, and provided grounds for answering the five questions laid out in the following matrix in Table 9.

The far left column shows the links of the delegation chain placed in their vertical order. The top row shows the analytical questions describing the subject matter. Short answers to these questions in the form of "yes", "no" and "partly", indicate overall results of the empirical evidence analysis.

Table 9: Matrix with Qualitative Analysis Results

Question: Delegation chain:	Is there a deviation of tasks, goals and objectives throughout the delegation chain?	Is the implementation going in line with the expectations of the principals?	Is there a deviation in reporting from agents to principals?	Does the audit office fill-in the information asymmetry gap?	Do the principals use audit reports to demand corrections?
<i>Federation Parliament</i>	No	-	-	-	Yes
<i>Federation Ministry of Labour and Social Policy</i>	No	No	Yes	-	No
<i>Federation Agency</i>	Yes	No	Yes	Yes	No
<i>Cantonal employment agencies</i>	Yes	No	Yes	Yes	Partly
<i>Employers and employees</i>	-	No	-	-	-

Source: own work.

A short summary of findings and answers to the research questions presented in the above matrix lead to a rather obvious conclusion that the delegation chain has failed to secure the consistent implementation and achievement of the government goals and objectives. Even though the audit provided inputs filling in the information asymmetry gap, this has not resulted in immediate corrections.

These answers to the research questions are elaborated in the following sections, with a reminder of causes and effects from theoretical section 1.5. During the qualitative analysis, these causes have served as propositions. Their effects are written in the form of a newly observed situation arising from the evidence.

3.9.1 The goals and objectives

Cause: In trying to avoid or diminish their responsibility to work in the interest of principals, agents tweak and obscure the definition of results they are expected to deliver, and extend their manoeuvring zone.

Effect: Government tasks, goals and objectives of public services gradually deviate along the delegation chain, lose their clarity and tangibility, and it becomes difficult to define responsibility for their achievement.

The goals and objectives have deviated along the delegation chain. The origin of the task came from the strategic goals of the top principals. The Federation Parliament adopted the "Employment Strategy of the Federation of BiH 2009–2013", with its clearly defined vision to maximise the employment rate among the working-age population. The Strategy was drafted by the Federation Ministry of Labour and Social Policy in charge of this area, with clearly defined program tasks, goals and measures, all based on a comprehensive analysis of the reasons of the problem of unemployment.

When the Strategy was delegated to the Federation Agency, the original design was distorted – definition of goals, target group and selection criteria were significantly altered. The same trend continued in the next delegation stage, on the cantonal level. The agents tweaked the situation to suit their short-term interests – to minimise their responsibility, but still get the budget for the Program implementation, thus widening their manoeuvring zone. Changes of the Program criteria and the target group created conditions that served the interests of the employers, not the employees.

3.9.2 Implementation

Cause: Agents use their position of advanced knowledge compared to that of their principals. They work in line with their own interest, increase budget spending and operate to achieve their own goals, failing to disclose the full information about state of affairs.

Effect: Asymmetric information between principals and agents develops. The deviation started in the delegation stage continues during program implementation. Expenses grow while the results are not getting achieved.

Asymmetric information between principals and agents has developed. The same trend of deviation of goals and objectives along the delegation chain during the planning stage, continued during the implementation. This has created operating conditions for the agents that were easy to handle, in line with the agents' short-term interests and tendencies of managerial shirking. The Program costs were increasing towards categories of beneficiaries that suited interests of the agents.

Focusing the Program towards the employers rather than the employees opened a wide comfort zone that allowed the businesses to opt for short-term goals of using a free work force, rather than using this opportunity to establish a long-term business development and long term employment. Together with moving the target group further away from those in need of support, this contributed to the Program failure to support the youngest population in getting jobs.

The goals and objectives, after having been clearly established by the principals, were later tweaked in the agent's planning documents, which resulted in lower expectations of the Program outcome that such definitions imply. Such a release of responsibility, however, did not prevent the agents to refer to higher goals when it suited their interests – obtaining resources for Program running. Still, when the Program failed to achieve any of its originally projected results, connection with the expectations was vague and ambiguous. This diminished the responsibility for failure.

3.9.3 Reporting

Cause: Agents tweak information about reality and hide problems and reasons for failure. Principals do not have capacity, expertise, or desire to see this.

Effect: Reporting about the outcome is incomplete and information sharing is selective and limited only to the aspects that suit agents' interests. The asymmetric information deepens.

Reporting back along the delegation chain did not contain information that could provide the principals with relevant inputs about the reality and true state of affairs in the Program. Superficial data in annual reports only included numbers of users of funds and related financial information, but without any explanation about the changes from the originally projected direction and framework determined by the Strategy.

The reporting was void of any information about the actual Program effects. The Audit Office gave negative or reserved audit opinions about almost all the annual reports from all the institutions along the delegation chain in the observed period. This means that users of these reports, the principals, could not rely on information they got from their agents.

The very fact that deviation in the plans and reports was visible, and the fact that all of these documents must be – and have been – adopted by the principals every year, shows that the principals have not used their supremacy position to force corrective measures. One reason for that could be their lack of capacity to understand subject matter, managerial shirking, or simply that each level of the chain is not only a principal but at the same time an agent of the principal above them. Such mix of positions creates an opportunity to create more room for manoeuvring and leave less space for clarity and correctness of information that would fully and correctly represent the reality.

3.9.4 Audit reports

Cause: The audit office reports a problem that would otherwise remain obscured and offers principals an opportunity to demand corrective actions from agents.

Effect: Audit office with a mandate to scrutinise the agents' work and report to principals balances the asymmetric information between principals and agents.

The Program failure was visible based on official statistics. The Audit Office reports, especially the performance audit report, provided important additional insights into the causes of this failure, pointing to the problem of ambiguous goals, criteria and changes of the target group. The performance audit report also criticised implementation process, revealing that certain employers used the Program funds repeatedly and without formal application. This indicates the failure of control and supervision mechanisms. Such serious implementation problems indicated a connection between the businesses and cantonal agencies responsible for implementation, as well as the Federation Agency responsible for overall supervision.

Revealing the true problem causes enabled the principals to understand situation with the Program. Based on these causes, the audit also provided practical recommendations of activities that need to be undertaken by the agents with an aim to improve things. These inputs from the Audit Office have balanced the asymmetric information between the principals and their agents. Principals came to equal terms in relation to their agents and they became empowered to exercise their superior position.

3.9.5 Corrective measures

Cause: The asymmetric information has been balanced by audit reports. Principals know the real situation. Audit recommendations provide basis for corrective measures.

Effect: Principals demand concrete corrective measures from their agents and have means to follow up on their actions. This creates improvements in the audited area.

The Federation Parliament used the performance audit reports as a basis for getting an insight into situation with the Program implementation. The Parliament used the opportunity to get an insight into the areas where improvements of the agents' work are possible and to follow-up the implementation of the audit recommendations. As an effect, the cantons reported that most of the audit recommendations are implemented. This created improvements in the Program.

One weakness in this last stage was similar to the original problem of the principal-agent relation and lack of accountability. The request from the Federation Parliament was ignored by the Federation Agency. Federation Parliament did not undertake any corrective measures towards the implementing agencies. In some instances, cantonal agencies did not fully accept responsibility for all the recommendations they were asked to implement. This shows that there is clearly a gap, either from the side of the Audit Office and their problem analysis and presentation, or from the side of the agencies and their understanding of their roles.

The repeated performance audit report in 2019 showed that the same problems were still present in the system as in 2012. This also indicates the lack of vertical pressure from general public, as an ultimate principal of the whole structure.

CONCLUSION

Vertical governance structures based on delegation of tasks and objectives from top to bottom, followed by reporting about their implementation in the opposite direction from bottom to top, inherently suffer from problems that can cause failure to achieve the projected goals and objectives. The science recognizes this as the principal–agent problem, and as a consequence of it, the problem of asymmetric information. This theoretical concept was developed during the 1970ies, primarily to explain relations in industrial economics. In the 1980ies, it also found its application in the public sector. The theory explains that the relationship between principals and agents is strongly inhibited by their own interests, which are misaligned with each other. This inhibits effective implementation of projected goals and objectives, consequences of which are multiplied throughout the multi-layer delegation chain in the public sector.

There were two main goals of this thesis – to show how the problem of principal–agent relation can contribute to government ineffectiveness and inefficiency, and to show how the performance audit can mitigate this problem. Through the case study of the Program of Youth Employment in Federation BiH, this study has shown how the asymmetric information gradually developed along the principal–agent delegation chain, how it contributed to the failure of the Program, and how the external audit function helped mitigate this problem by revealing its causes. The case study research included five research questions covering five steps of the Program’s life cycle (planning, implementation, reporting, auditing and follow-up). Answers to these questions have shown following:

- In the planning stage, the goals delegated from top to bottom gradually lost their clarity with every link of the delegation chain. The goals became vague and not measurable. The responsibility for their achievement was not clearly defined and it was not possible to determine what links of the delegation ought to do what.
- The process of implementation was inhibited by vested interests of agents, which gradually caused failure to achieve originally projected goals.
- Reporting was inhibited by the same interests and the information about implementation became incomplete and misleading. This reporting failure was verified by the financial audit reports. Asymmetric information deepened, and as a consequence, the principals were not able to exercise their full control over the actions of their agents.
- The performance audit reports provided the principals with a full picture and deeper insight into the problem causes that would otherwise remain invisible.
- Using these insights, and recommendations from the performance audit report, the principals got an opportunity to demand concrete corrective measures from their agents.

The case study analysis in this thesis has shown how the principal-agent problem impedes the successful implementation of government programs. The root causes of failure remain invisible due to numerous misinterpretations and asymmetric information between different levels. The principals do not have knowledge and understanding about the practical implementation of the programs, or capacity to get directly involved. In making decisions and exercising control over the programs, they are dependent on inputs and reports of their agents. However, the agents' reports do not provide principals with reliable and sufficient inputs for decision-making process. As a result, they fail to exercise their superior control position and secure the successful achievement of their goals and objectives.

The financial and compliance audit reports clearly noted the seriousness of the problem in the analyzed case study and confirmed that principals could not rely on their agents' reports. The function of performance audit shed some light on the problem causes, and revealed certain aspects that would otherwise remain unseen. The performance audit report provided recommendations directly addressing the issues arising from the intricate principal-agent relation along the delegation chain. Through these recommendations, the principals received concrete inputs on what corrective measures they can demand from their agents. This has partly balanced the asymmetric information problem between the principals and their agents.

As a result, the principals, in this case, the Parliament, communicated directly with the lowest-level agents and enquired about concrete actions and measures that could remedy the problem. In the outcome, the cantonal agencies have, at least partly, implemented audit recommendations. Even if the performance audit report did not make a revolutionary change, it has revealed the problem that might otherwise remain invisible, and initiated gradual steps towards improvements. This way, the performance audit has mitigated the principal-agent problem in the government.

The Federation Employment Agency ignored the Parliament request to report about the implementation of audit recommendations. The Parliament simply noted the absence of their reply – without following it up and demanding any additional actions. This shows how the principal-agent chain suffers from a lack of vertical pressure force, which is a typical problem with many different principals – in this case the Parliament members, whose individual interests are not the same and not fully aligned. A lack of their focus opened more room for agents to play by their own rules.

One more problem inherent in this structure is the mixing of the roles of principals and agents. While they are top principals in the government chain, Parliament members are still only agents of the citizens. The executive government below the Parliament is their agent, but at the same time, a principal to lower level agencies. In all the levels of the delegation chain, the roles of the principals and agents mix, and this impedes alignment of their own interests with the general interests of the citizens.

These structural weaknesses have been clearly presented in this research, and root causes have been explained by the principal-agent theory. Based on this, some recommendations for improvements are possible, primarily focused on the principal-agent delegation chain and the audit office:

- As seen from the case study, the performance audit can provide relevant inputs and offer a full and true picture of the state of affairs in a matter. However, any corrective measures and activities still remain in the agents' domain, under pressure from the principals. A recommendation for such a situation could be the involvement of a higher-level principal – in this case, the citizens.
- Even if the time between elections may be long, it is highly unlikely that politicians and government officials would remain inert under the pressure from the general public. This is where the audit office again comes into play: as an ultimate agent of the citizens, the audit office can increase its public relations activities and use the media to trigger public attention to the issues of concern.

To conclude, the most important dimension of the performance audit is one that concerns its core question: the question of *why* do the problems in the government develop in the first place. Locating problems and showing their consequences is one thing, but adding value requires going deeper and pinpointing the root causes of the problems. The main success factor in doing this is the exact opposite of the asymmetric information problem: providing complete information, offering a full and clear picture, avoiding any ambiguity and keeping the focus. Finally, in order to make a change, the performance audit reports must be promoted in a way to mobilise the public attention, focus it on the root causes of the audited problems, and create vertical pressure in the principal-agent chain.

Additional research can help further elaborate and strengthen these conclusions. The principal-agent theory looks at the vertical management structure and explains problems by looking at the vested interests of the key players in the vertical plane. However, there can be other organisational, institutional, social and political factors with a strong impact on the outcome of government programs or any economic activity. Further research in this area would include aspects covered by the organisational theory in order to address problems of teams and groups sharing the responsibility for achieving the goals, institutional theory addressing the social traditions and their impact on economy, and game theory addressing the issues of logical decision making and social contract cost.

REFERENCE LIST

1. AFROSAI-E. (2014). *Performance Audit Template Manual*. Pretoria: African Organization of Supreme Audit Institutions of English-speaking African countries (AFROSAI-E).
2. Agency for Statistics of Bosnia-Herzegovina. (2007). *Labour Force Survey 2007*. Sarajevo: Agency for Statistics of Bosnia-Herzegovina.
3. Agency for Statistics of Bosnia-Herzegovina. (2008). *Labour Force Survey 2008*. Sarajevo: Agency for Statistics of Bosnia-Herzegovina.
4. Agency for Statistics of Bosnia-Herzegovina. (2009). *Labour Force Survey 2009*. Sarajevo: Agency for Statistics of Bosnia-Herzegovina.
5. Agency for Statistics of Bosnia-Herzegovina. (2010). *Labour Force Survey 2010*. Sarajevo: Agency for Statistics of Bosnia-Herzegovina.
6. Agency for Statistics of Bosnia-Herzegovina. (2011). *Labour Force Survey 2011*. Sarajevo: Agency for Statistics of Bosnia-Herzegovina.
7. Agency for Statistics of Bosnia-Herzegovina. (2012). *Labour Force Survey 2012*. Sarajevo: Agency for Statistics of Bosnia-Herzegovina.
8. Agency for Statistics of Bosnia-Herzegovina. (2013). *Labour Force Survey 2013*. Sarajevo: Agency for Statistics of Bosnia-Herzegovina.
9. Agency for Statistics of Bosnia-Herzegovina. (2014). *Labour Force Survey 2014*. Sarajevo: Agency for Statistics of Bosnia-Herzegovina.
10. Aghion, P. & Tirole, J. (1997). Formal and Real Authority in Organizations. *Journal of Political Economy*, 105(1), 1-29.
11. Akerlof, G. A. (1978). The market for “lemons”: Quality uncertainty and the market mechanism. In P. Diamond & M. Rothschild (Eds.), *Uncertainty in economics* (pp. 235–251). New York: Academic Press.
12. Alchian, A. (1959, June). Uncertainty, Evolution and Economic Theory. *Journal of Political Economy*, 58, 211-21.
13. Arrow, K. (1975). Vertical Integration and Communication. *Bell Journal of Economics*, 6, 173-183.
14. Audit Office for the Institutions of the Federation of BiH. (2011a). *Izveštaj o reviziji finansijskih izvješća Federalnog Ministarstva rada i socijalne skrbi na dan*

- 31.12.2010. godine [Report on audit of the financial statements of the Federation Ministry of Labour and Social Policy on the date 31.12.2010]. Sarajevo: Audit Office for the Institutions of FBiH.
15. Audit Office for the Institutions of the Federation of BiH. (2011b). *Izveštaj o reviziji finansijskih izvještaja Federalnog zavoda za zapošljavanje za 2010. godinu* [Report on audit of the financial statements of the Federal Employment Agency for 2010]. Sarajevo: Audit Office for the Institutions of FBiH.
 16. Audit Office for the Institutions of the Federation of BiH. (2011c). *Revizorski izvještaj o izvršenju budžeta Federacije BiH za 2010. godinu* [Audit Report on Federation BiH Budget Execution for 2010]. Sarajevo: Audit Office for the Institutions of FBiH.
 17. Audit Office for the Institutions of the Federation of BiH. (2012a). *Izveštaj revizije učinka: Upravljanje Programom zapošljavanja mladih* [Performance Audit Report: Management of the Youth Employment Program]. Sarajevo: Audit Office for the Institutions of FBiH.
 18. Audit Office for the Institutions of the Federation of BiH. (2012b). *Izveštaj o reviziji finansijskih izvješća Federalnog Ministarstva rada i socijalne skrbi na dan 31.12.2011. godine* [Report on audit of the financial statements of the Federation Ministry of Labour and Social Policy on the date 31.12.2011]. Sarajevo: Audit Office for the Institutions of FBiH.
 19. Audit Office for the Institutions of the Federation of BiH. (2012c). *Revizorski izvještaj o izvršenju budžeta Federacije BiH za 2011. godinu* [Audit Report on Federation BiH Budget Execution for 2011]. Sarajevo: Audit Office for the Institutions of FBiH.
 20. Audit Office for the Institutions of the Federation of BiH. (2013a). *Izveštaj o reviziji finansijskih izvješća Federalnog ministarstva rada i socijalne skrbi na dan 31.12.2012. godine* [Report on audit of the financial statements of the Federation Ministry of Labour and Social Policy on the date 31.12.2012]. Sarajevo: Audit Office for the Institutions of FBiH.
 21. Audit Office for the Institutions of the Federation of BiH. (2013b). *Izveštaj o reviziji finansijskih izvještaja Federalnog zavoda za zapošljavanje za 2012 godinu* [Report on audit of the financial statements of the Federal Employment Agency for 2012]. Sarajevo: Audit Office for the Institutions of FBiH.
 22. Audit Office for the Institutions of the Federation of BiH. (2013c). *Izveštaj o reviziji finansijskih izvještaja Agencije za zapošljavanje Kantona Sarajevo za 2012 godinu* [Report on audit of the financial statements of the Sarajevo Cantonal

Agency for Employment for 2012]. Sarajevo: Audit Office for the Institutions of FBiH.

23. Audit Office for the Institutions of the Federation of BiH. (2013d). *Revizorski izvještaj o izvršenju budžeta Federacije BiH za 2012. godinu* [Audit Report on Federation BiH Budget Execution for 2012]. Sarajevo: Audit Office for the Institutions of FBiH.
24. Audit Office for the Institutions of the Federation of BiH. (2014a). *Izvještaj o reviziji finansijskih izvješća Federalnog ministarstva rada i socijalne skrbi na dan 31.12.2013. godine* [Report on audit of the financial statements of the Federation Ministry of Labour and Social Policy as of 31.12.2013]. Sarajevo: Audit Office for the Institutions of FBiH.
25. Audit Office for the Institutions of the Federation of BiH. (2014b). *Izvještaj o reviziji finansijskih izvještaja Federalnog zavoda za zapošljavanje za 2013. godinu* [Report on audit of the financial statements of the Federation Employment Agency for 2013]. Sarajevo: Audit Office for the Institutions of FBiH.
26. Audit Office for the Institutions of the Federation of BiH. (2014c). *Revizorski izvještaj o izvršenju budžeta Federacije BiH za 2013. godinu* [Audit Report on Federation BiH Budget Execution for 2013]. Sarajevo: Audit Office for the Institutions of FBiH.
27. Audit Office for the Institutions of the Federation of BiH. (2019). *Izvještaj revizije učinka: Upravljanje programima sufinansiranja zapošljavanja* [Performance Audit Report: Management of the employment co-financing programs]. Sarajevo: Audit Office for the Institutions of FBiH.
28. Bengtsson, M. (2016). How to plan and perform a qualitative study using content analysis. *NursingPlus Open Journal*, 2, 8-14.
29. Barnard, C. I. (1938). *The Functions of the Executive*. Cambridge, MA: Harvard University Press.
30. Berhold, M. (1971, August). A Theory of Linear Profit-Sharing Incentives. *The Quarterly Journal of Economics*, 85(3), 460-482.
31. Berle, A., and Means, G. (1932). *Private property and the modern corporation*. New York: Macmillan.
32. Bos, L., Kruikemeier, S. & de Vreese C. (2016). Nation Binding: How Public Service Broadcasting Mitigates Political Selective Exposure. *PLoS ONE*, 11(5),

[e0155112]. Retrieved from <https://journals.plos.org/plosone/article?id=10.1371/journal.pone.0155112>

33. Canton Sarajevo Government. (2011). *Zaključak o Programu mjera za podsticaj zapošljavanja i održavanja više stope zaposlenosti u Kantonu Sarajevo* [Conclusion on the Program for employment incentives and increasing the employment rate in Sarajevo Canton]. Sarajevo: Sarajevo Canton Government.
34. Council of Ministers of Bosnia-Herzegovina. (2011). Osnove kvalifikacijskog okvira u Bosni i Hercegovini [Basis of Qualifications Framework in Bosnia and Herzegovina]. *Službeni glasnik Bosne i Hercegovine* [Official Gazette of Bosnia-Herzegovina] no. 31/2011.
35. Coase, R. (1937). The nature of the firm. *Economica*, 4, 386-405.
36. Coase, R. (1972). Industrial organization: A proposal for research. In V.R. Fuchs (Ed.), *Policy issues and research opportunities in industrial organization* (pp. 59–73). New York: National Bureau of Economic Research.
37. Cooper, W. (1949). Theory of the Firm: Some Suggestions for Revision. *The American Economic Review*, 39(6), 1204-1222.
38. Cooper, W. (1951). A proposal for Extending the Theory of the Firm. *A quarterly Journal of Economics*, 65(1), 87-109.
39. Commission for Coordination of Youth Affairs in Bosnia and Herzegovina. (2008). *Analiza položaja mladih i omladinskog sektora u Bosni i Hercegovini* [Analysis of the position of youth and youth sector in Bosnia and Herzegovina]. Sarajevo: Commission for Coordination of Youth Affairs in Bosnia and Herzegovina.
40. Cyert, R. M. & March, J. G. (1963). *A Behavioural Theory of the Firm*. Englewood Cliffs, N.J.: Prentice-Hall.
41. Fawcett, G. (2010). *Enhancing External Audit: Learning from the Public Sector*. Glasgow: The Association of Chartered Certified Accountants (ACCA).
42. Federation Employment Agency. (2008). *Program rada za 2009. godinu* [Work Program for 2009]. Sarajevo: Federation Employment Agency.
43. Federation Employment Agency. (2009). *Program rada za 2010. godinu* [Work Program for 2010]. Sarajevo: Federation Employment Agency.
44. Federation Employment Agency. (2010a). *Izveštaj o radu Federalnog zavoda za zapošljavanje za 2009. godinu* [Work Report of the Federation Employment Agency for 2009]. Sarajevo: Federation Employment Agency.

45. Federation Employment Agency. (2010b). *Program rada za 2011. godinu* [Work Program for 2011]. Sarajevo: Federation Employment Agency.
46. Federation Employment Agency. (2010c). *Javni poziv za učešće u Programu sufinansiranja mladih osoba bez radnog iskustva* [Public invitation for participation in the Program of co-financing young persons without work experience]. Sarajevo: Federation Employment Agency.
47. Federation Employment Agency. (2010d). *Program sufinansiranja zapošljavanja mladih osoba bez radnog iskustva* [Program of co-financing employment of young persons without work experience]. Sarajevo: Federation Employment Agency.
48. Federation Employment Agency. (2011a). *Izveštaj o radu Federalnog zavoda za zapošljavanje za 2010. godinu* [Work Report of the Federation Employment Agency for 2010]. Sarajevo: Federation Employment Agency.
49. Federation Employment Agency. (2011b). *Program rada za 2012. godinu* [Work Program for 2012]. Sarajevo: Federation Employment Agency.
50. Federation Employment Agency. (2012a). *Izveštaj o radu Federalnog zavoda za zapošljavanje za 2011. godinu* [Work Report of the Federation Employment Agency for 2009]. Sarajevo: Federation Employment Agency.
51. Federation Employment Agency. (2012b). *Program rada za 2013. godinu* [Work Program for 2013]. Sarajevo: Federation Employment Agency.
52. Federation Employment Agency. (2013). *Izveštaj o radu Federalnog zavoda za zapošljavanje za 2012. godinu* [Work Report of the Federation Employment Agency for 2012]. Sarajevo: Federation Employment Agency.
53. Federation Employment Agency. (2014). *Izveštaj o radu Federalnog zavoda za zapošljavanje za 2013. godinu* [Work Report of the Federation Employment Agency for 2013]. Sarajevo: Federation Employment Agency.
54. Federation Office of Statistics. (2008). *Statistical Yearbook 2008*. Sarajevo: Federation Office of Statistics.
55. Federation Office of Statistics. (2009). *Statistical Yearbook 2009*. Sarajevo: Federation Office of Statistics.
56. Federation Office of Statistics. (2010). *Statistical Yearbook 2010*. Sarajevo: Federation Office of Statistics.
57. Federation Office of Statistics. (2011). *Statistical Yearbook 2011*. Sarajevo: Federation Office of Statistics.

58. Federation Office of Statistics. (2012). *Statistical Yearbook 2012*. Sarajevo: Federation Office of Statistics.
59. Federation Office of Statistics. (2013). *Statistical Yearbook 2013*. Sarajevo: Federation Office of Statistics.
60. Federation Office of Statistics. (2014). *Statistical Yearbook 2014*. Sarajevo: Federation Office of Statistics.
61. Fisman, R., & Werker, E. (2011). Innovations in Governance. *Chicago Journals, Innovation Policy and the Economy*, 11(1), 79-102.
62. Frankfort-Nachimas, C., & Nachimas, D. (2000). *Research Methods in the Social Sciences* (6th ed.). New York: Worth Publishers and St. Martin's Press.
63. Ghanbari, M., Rashidi A. & Abbasi, N. (2018). A study of the effects of agency costs and information asymmetry on audit quality. *Journal of Advance Pharmacy Education & Research*, 8(2), 137-142.
64. Gustavsson M. (2013). Democratic Origins of Auditing. *The Quality Of Government Institute Working Paper Series*, 13:2013. Retrieved August 16, 2019, from https://qog.pol.gu.se/digitalAssets/1463/1463210_2013_13_gustavsson.pdf
65. Gustavsson M. (2015). Does Good Auditing Generate Quality of Government? *The Quality Of Government Institute Working Paper Series*, 15:2015. Retrieved August 16, 2019, from https://qog.pol.gu.se/digitalAssets/1538/1538160_2015_15_gustavson.pdf
66. Higgs, R. (2018). Principal–agent theory and Representative Government. *The Independent Review*, 22(3), 479–480.
67. IDI. (2014). *ISSAI Implementation Handbook – performance audit*. Oslo: INTOSAI Development Initiative (IDI).
68. INTOSAI. (2010). *ISSAI 20: Principles of Transparency and Accountability*. Vienna: International Organization of Supreme Audit Institutions (INTOSAI).
69. INTOSAI. (2013). *ISSAI 12: The Value and benefits of Supreme Audit Institutions – making a difference to the lives of the citizens*. Vienna: International Organization of Supreme Audit Institutions (INTOSAI).
70. INTOSAI. (2013). *ISSAI 100: Fundamental Principles of Public-Sector Auditing*. Vienna: International Organization of Supreme Audit Institutions (INTOSAI).

71. INTOSAI. (2013). *ISSAI 300: Fundamental Principles of Performance Auditing*. Vienna: International Organization of Supreme Audit Institutions (INTOSAI).
72. Janssen, M.C. & Meckling, W.H. (1976). Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure. *Journal of Financial Economics*, 3: 305-360.
73. Jones, R. & Pendlebury, M. (2000). *Public Sector Accounting* (5th ed.). Edinburgh Gate: Cardiff University, FT Prentice Hall, England.
74. Kahneman, D. & Tversky, A (1973). On the Psychology of Prediction. *Psychological Review*, 80, 237-51.
75. Kellner, C. (2017). *The principal-agent problem with smooth ambiguity*. Review of Economic Design 21:83-119. Southampton: University of Southampton.
76. Labour and Employment Agency of Bosnia and Herzegovina. (March). *Statistical Information Sheet no. 18 – IV/2010*. Sarajevo: Labour and Employment Agency of Bosnia and Herzegovina.
77. Lafont, J. & Martimort, D. (2001). *The Theory Of Incentives I: The Principal-Agent Model*. Princeton: Princeton University Press.
78. Leruth, L. & Paul, E. (2006), A Principal-agent Theory Approach to Public Expenditure Management Systems in Developing Countries. *IMF Working Paper No. WP/06/204*. Retrieved February 28, 2017, from <https://www.imf.org/external/pubs/ft/wp/2006/wp06204.pdf>
79. Lupia, A. & McCubbins, M. (1998). *The Democratic Dilemma*. Cambridge: Cambridge University Press.
80. Merriam, S. B. (1998). *Qualitative research and case study applications in education*. San Francisco, CA: Jossey-Bass.
81. Marschak, J. (1955). Elements for a Theory of Teams. *Management Science*, 1, 127-137.
82. McCubbins, M.D., Noll, R.G. and Weingast, B.R. (1987). Administrative Procedures as Instruments of Control. *Journal of Law, Economics and Organization*, 3(2): 243-277.
83. Ministry of Labour and Social Policy of the Federation of BiH. (2008). *Strategija zapošljavanja Federacije Bosne i Hercegovine 2009-2013* [Strategy of Employment in the Federation of Bosnia-Herzegovina 2009-2013]. Sarajevo: Ministry of Labour and Social Policy of the Federation of BiH.

84. Mitnick, B. M. (1975). The theory of agency: The policing "paradox" and regulatory behaviour. *Public Choice*, 24, 27-42.
85. Mitnick, B. M. (2019). Origin of the Theory of Agency: An Account by One of the Theory Originators. *SSRN Electronic Journal*. Retrieved from <https://ssrn.com/abstract=1020378>
86. Moe, T. (1984). The New Economics of Organization. *American Journal of Political Science*, 28(4), 739-777.
87. O'Donnell, G. A. (1998). Horizontal Accountability in New Democracies. *Journal of Democracy*, 9(3), 112-126.
88. Oyesola, S. & Agbeja, O. (2007). Auditing and Accountability Mechanism in the Public Sector. *The International Journal of Applied Economics and Finance*, 1(1), 45-54.
89. Parliament of the Federation of BiH. (2016). *Informacija o provedbi preporuka iz izvještaja revizije učinka, interni akt br. 01/1-02-753/16* [Information about implementation of recommendations from performance audit reports, internal act no. 01/1-02-753/16]. Sarajevo: Parliament of the Federation of BiH.
90. Ross, S. (1973). The Economic Theory of Agency: The Principal's Problem. *The American Economic Review*, 63(2), 134-139.
91. Scott, C. (2000). Accountability in the Regulatory State. *Journal of Law and Society*, 27, 38-60.
92. Simon, H. (1947). *Administrative Behaviour*. New York: Macmillan.
93. Simon, H. (1955). A behavioural model of rational choice. *Quarterly Journal of Economics*, 69, 99-118.
94. Stake, R. E. (2005). Qualitative Case Studies. In N. K. Denzin & Y. S. Lincoln (Eds.), *The Sage handbook of qualitative research* (pp. 443–466). Thousand Oaks, CA: Sage Publications Ltd.
95. Stake, R. E. (1995). *The art of case study research*. Thousand Oaks, CA: Sage Publications.
96. Stiglitz, J. (1974). Incentives and Risk Sharing in Sharecropping. *The Review of Economic Studies*, 41(2), 219-255.
97. Tellis, W. M. (1997). Introduction to Case Study. *The Qualitative Report*, 3(2), 1-14. Retrieved September 21, 2019 from <https://nsuworks.nova.edu/tqr/vol3/iss2/4/>

98. Wardman, M. & Fawcett, G. (2008). Ethical Governance in Local Government in England: A Regulator's View. In Huberts, L.W., Maesschalck, J. & Jurkiewicz C.L (Eds.), *Ethics and Integrity of Governance* (pp. 123–138). Northampton, MA: Edward Elgar Publishing.
99. Williamson, O. E. (1964). *The Economics of Discretionary Behaviour: Managerial Objectives in a Theory of the Firm*. Englewood Cliffs, NJ: Prentice-Hall.
100. Yazan, B. (2015). Three Approaches to Case Study Methods in Education: Yin, Merriam, and Stake. *The Qualitative Report*, 20(2), 134-152. Retrieved September 21, 2019, from <https://nsuworks.nova.edu/tqr/vol20/iss2/12>
101. Yin, R.K., (1984). *Case Study Research: Design and Methods*. Beverly Hills, CA: Sage Publications.
102. Yin, R.K., (2017). *Case Study Research: Design and Methods* (5th ed.). Beverly Hills, CA: Sage Publications.
103. Yin, R.K., & Moore, G.B. (1987). The Use of Advanced Technologies in Special Education: Prospects from Robotics, Artificial Intelligence, and Computer Simulation. *Journal of Learning Disabilities*, 20(1), 60–63.

APPENDIXES

Appendix 1: Povzetek (Summary in Slovene language)

Vertikalne strukture upravljanja, ki temeljijo na prenosu nalog in ciljev z vrha do dna, nato pa poročanje o njihovem izvajanju nasprotno, od spodaj navzgor, inherentno trpijo zaradi težav s komunikacijo, ki lahko povzročijo neuspeh pri doseganju načrtovanih ciljev. Znanost to prepozna kot problem principal-agent in kot del tega, problem asimetričnih informacij. Ta študija primera Programa zaposlovanja mladih v Federaciji BiH kaže kako se asimetrične informacije postopoma razvijajo po verigi principal-agent, kako prispevajo k neuspehu in kako lahko funkcija zunanje revizije pomaga ublažiti to težavo z razkritjem vzrokov.

Raziskava je osredotočena na načrtane cilje in cilje programa, analizirajoč njihovo odstopanje skozi življenjski cikel programa, po verigi delegiranja iz Parlamenta Federacije BiH kot principala, na agencije za zaposlovanje kot agente, odgovorne za izvajanje programa. Z opazovanjem odstopanja skozi prizmo teoretičnega ozadja, raziskovanje pojasnjuje kako informacije, ki se izmenjujejo med principali in agenti, postanejo asimetrične in kako zastopani interesi agentov povzročajo odstopanje. Raziskava tudi pokaže, kako je razkrit prepad v informacijah s pomočjo funkcije revizije učinkovitosti, ki je principalom omogočala, da ukrepajo.

Ena od glavnih posledic asimetričnih informacij v kakršnem koli razmerju med principalom in agentom je nejasnost temeljnih razlogov za neuspeh. Ponavadi ostajajo glavni razlogi za neuspeh skriti, nejasni in zajeti z zapleteno mrežo različnih vrst odgovornosti in določenih interesov. To otežuje opozarjanje na dejanske težave in iskanje načinov za izboljšanje učinkovitosti. Poročilo o reviziji učinkovitosti je to, v primeru Programa za zaposlovanje mladih, razsvetlilo in nosilec odločanja ponudilo priložnost, da vidijo vprašanja, ki sicer ne bi bila vidna.

Raziskava ugotavlja, da zajemajoč celoten programski cikel in gledajoč ga skozi prizmo problemov med principalom in agentom, funkcija revizije učinkovitosti, z dojetjem strukture kot celote, lahko uravnoteži problem asimetričnih informacij, ki se razvijajo v verigi prenosa pooblastil. Odpravljanje posledic zapletenih odnos znotraj strukture med principalom in agentom zahteva več kot celoten prikaz problemov; kljub temu pa lahko težavo omilimo z odkrivanjem celotne slike njegovih vzrokov.

Appendix 2: Research design matrix

Table 1: Matrix with research questions and methodology

Question:	Is there a deviation in the delegation of tasks, goals and objectives?	Did the implementation go in line with the expected goals and objectives?	Is there a deviation in reporting from the agents to the principals?	Has the performance audit reported a problem or deviation?	Have the principals and the agents undertaken measures on the basis of performance audit report?
Proposition	In trying to avoid or diminish their responsibility to work for the principals' interest, agents will tweak and obscure definition of results they are expected to deliver and extend their manoeuvring zone.	Agents use their advanced position related to principals to work in line with their own interest, increase budget and operate to achieve their own goals, failing to disclose full information about the actual state of affairs.	Agents tweak information about reality, hide problems and reasons for failure. Principals do not have capacity, expertise, or desire to see this.	The audit office reports a problem that would otherwise remain obscured, and offers principals an opportunity to demand corrective actions from agents.	Asymmetric information has been balanced by audit reports. Principals know the real situation. Audit recommendations provide basis for corrective measures.
Effect	Government tasks, goals and objectives of public services gradually deviate along the delegation chain, lose their clarity and tangibility, and it becomes difficult to define responsibility for their achievement.	Asymmetric information between principals and agents develops. Deviation started in delegation stage continues during program implementation. Expenses grow while the results are not getting achieved.	Reporting about the outcome is incomplete and information sharing is selective and limited only to aspects that suit interests of the agents. Asymmetric information deepens.	The audit office with a mandate to scrutinise the agents' work and report to principals balances the asymmetric information between principals and agents.	Principals demand corrective measures from their agents and have means to follow-up on their actions.
Meaning units	Definition of goals, objectives, tasks, norms, criteria, beneficiaries, expected results and responsibility for their achievement	Budgets, concrete activities, number of users and beneficiaries, their description (age and similar)	Expenditures, reported beneficiaries and users (age and similar) and undertaken activities	Expenditures, audit findings, audit opinions and audit recommendations	Description of undertaken activities aimed at implementation
Context	Clarity, tangibility	Numeric values	Numeric values	Quality judgement by the auditors	Level of implementation
Source	Strategic and planning documents	Annual plans and reports, announcements, special reports	Annual activity and budget reports	Audit reports	Correspondence between parliaments and agencies
Criteria	<p>Yes – means maintaining identical and consistent meaning units in all contexts;</p> <p>No – means any changes of meaning units in any of the contexts that can impact the outcome;</p> <p>Partly – means slight changes of the meaning units, but without significant impact.</p>				

Source: own work.

Appendix 3: Federation Agency annual plans and reports analysis

The purpose of this analysis is to show inconsistent data in the annual plans and annual reports of the Federation Agency for the period from 2009 to 2013. It is not possible to compare plans and reports for every year and follow up on the continuity of the activities. Also, the reports sometimes contain information about plans, and plans sometimes contain reports of activities, however, it is not possible to cross-check the same information in the related annual plans and reports. These inconsistencies are mentioned in the annual audit findings of the Audit Office and are the reason why the Federation Agency received "reserved audit opinion" for 2012 and 2013.

Table 2 provides an overview of annual plans and reports related to the Program implementation in the observed period, including the page numbers. The table is divided into two main parts – activities implemented directly by the Federation Agency and activities implemented together with the cantonal agencies, since these two are separated in the agencies' reports and plans. The two modes of implementation are then aggregated on the right side of the table. The top of the table indicates four categories of beneficiaries, based on their level of skills and education. The categories are created based on Table 2: *Target Group in the Annual Plans of F BiH Agency* from subchapter 3.3.2.

The plans and reports of the Federation Agency do not always contain the specification of allocated funds per category of beneficiaries, and such instances are noted. In 2012 and 2013, the Federation Agency aggregated the four categories into two, one with a generally low level of education (up to the completion of secondary school), and one with higher education (university level). For easier viewing, the same logic is followed in total aggregation at the bottom of the table.

The main inconsistency related to the Program implementation is in the mixing of different lines of the Federation Agency programs and activities, so they cannot be compared against the criteria and target groups indicated in the Strategy. However, the table includes all beneficiaries of the Federation Agency's activities, which covered the target group of the young population of age up to 30, in the period 2009–2013 covered by the Strategy. Concretely, these are 323 beneficiaries from 2012 which were included in the program titled "400+", implemented together with United Nations Development Program (UNDP), 950 beneficiaries from the program titled "First Work Experience 2012", and 568 beneficiaries from the program titled "Opportunity for all". It is worth noting that these three programs were not mentioned in the agencies' annual plans and data about them is taken from the annual reports only.

Table 2: Overview of the Program budgets and beneficiaries per year

Program:		Program implemented directly by the Federation Agency						Program implemented together with cantonal agencies						All program activities combined		
Year	Reference document:	Beneficiaries:	Not skilled, low skilled	Skilled	High skilled	Bachelor degree or higher	Total	Funds BAM	Not skilled, low skilled	Skilled	High skilled	Bachelor degree or higher	Total	Funds BAM	TOTAL BAM	TOTAL Beneficiaries
2009	Work plan for 2009 (Federation Employment Agency, 2008, p. 9)		200	100	40	50	390	1,002,000							1,002,000	390
	Annual Report for 2009 (Federation Employment Agency, 2010a, p. 16)		<i>Unspecified.</i>					122,300							122,300	-
2010	Annual Plan for 2010 (Federation Employment Agency, 2009, p. 9)		<i>Plan from 2009 updated to total 1.170.000 BAM.</i>					168,000							2,167,800	524
	Program Document (Federation Employment Agency, 2010d, p. 2)								250	151	23	100	524	1,999,800		
2011	Annual Report for 2010 (Federation Employment Agency, 2011a, p. 16)		67	55	9	160	291	968,751							968,751	291
	Annual Plan for 2011 (Federation Employment Agency, 2010b, p. 6)		<i>Funds for completion of cycle started in 2010.</i>					50,000	350	450	50	500	1,350	6,000,000	6,050,000	1,350
2012	Annual Report for 2011 (Federation Employment Agency, 2012a, p. 13)		128	200	33	514	875	3,897,250	144	181	57	487	869	3,850,000	7,747,250	1,744
	Annual Plan for 2012 (Federation Employment Agency, 2011b, p. 7)		<i>Continued from 2010-2011.</i>												-	-
2013	Annual Report for 2012 (Federation Employment Agency, 2013, p. 13)		<i>Activities from 2010-2011, finalized in 2012.</i>					871,250		245		78	323	1,070,020	1,941,270	323
	Annual Plan for 2013 (Federation Employment Agency, 2012b)		<i>No planned activity.</i>												-	-
2013	Annual Report for 2013 (Federation Employment Agency, 2014, p. 20)		<i>No reported activity.</i>							413		537	950	3,260,060	3,260,060	950
	Annual Report for 2013 (Federation Employment Agency, 2014, p. 18)					-						<i>Unspecified.</i>	568	<i>Unspecified.</i>	-	568
	TOTAL Plan		300		90	390	1,220,000		1,201		673	1,874	7,999,800	9,219,800	2,264	
	TOTAL Report		450		716	1,166	5,859,551		983		1,159	2,710	8,180,080	14,039,631	3,876	

Source: Federation Employment Agency (2008), Federation Employment Agency (2009), Federation Employment Agency (2010a), Federation Employment Agency (2010b), Federation Employment Agency (2010d), Federation Employment Agency (2011a), Federation Employment Agency (2011b), Federation Employment Agency (2012a), Federation Employment Agency (2012b), Federation Employment Agency (2013), Federation Employment Agency (2014).

Overall inconsistency is immediately visible by simple comparison of numbers in the plan report lines. Based on this, few important conclusions that can be drawn from the Table 2:

1. There is no connection between annual plans and annual reports. Some activities during the year normally do not go as planned, however, any deviations from the plans would then be reported in annual reports. They would include explanation of such instances and an elaboration of reasons for the deviations, explanation of the consequences they had on the overall expected outcome, what measures the implementing bodies plan to take to prevent such deviations, etc. The next years' plans would include corrective activities and measures taken aimed at tackling possible consequences. None of such elaborations can be found in the annual plans and reports related to the Program.
2. From a purely financial perspective, inconsistencies between annual plans and annual reports also indicate that the budget planning and execution were not going in line with the Budget Law. Normally, every budget line of a public institution should have a clear connection with an activity conducted during the year, however, this is not the case with the budget of the Federation Agency in the observed period.
3. Co-financing activities related to the Program implementation are scattered around in different forms throughout the years, and it is not possible to follow them up consistently and uniformly to create grounds for conclusions on the actual outcome of the Program or a follow-up on its effectiveness.

Since there are no expected result indicators and no definition of expected outcome per year or the period covered by the Strategy, it is not possible to track the Program implementation. The fact that the Federation Agency presented information about the Program in such a confusing way indicates that the Program was implemented on an ad hoc basis, without following the Strategy. One very important observation visible from Table 2 is a gradual increase in the number of beneficiaries with higher education, followed by a gradual increase in the allocation of funds for co-financing their jobs.

In order to present this trend in a more detail, the Table 3 shows how the allocation of funds and the number of beneficiaries in different categories was changing over the years. For easier following, beneficiaries from UNDP and other programs are excluded from the Table 3, nevertheless, the message remains the same. On the left side is the year of implementation, followed by the data source document. The four categories are the same as in the table above, including the number of beneficiaries, the amount in BAM for co-financing their job and the number of months for co-financing (BAM x months), and the category total for every year. As in the Table 2, the four categories are grouped into two by the Federation Agency in 2012 and 2013; hence the following table contains the same aggregation on the right hand side.

Table 3: Overview of the target groups and allocation of funds

Year	Reference document	Not skilled, low skilled	Skilled	High skilled	Bachelor degree or higher	Low education beneficiaries	High education beneficiaries	
2009	Annual Plan for 2009 (Federation Employment Agency, 2008, p. 9)	Beneficiaries:	200	100	40	50	300	90
		BAM x months:	300 x 6	350 x 6	400 x 12	450 x 12		
		TOTAL BAM:	360,000	210,000	192,000	270,000	570,000	462,000
2010	Program Document (Federation Employment Agency, 2010d, p. 2)	Beneficiaries:	250	151	23	100	401	123
		BAM x months:	450 x 6	500 x 6	550 x 12	600 x 12		
		TOTAL BAM:	675,000	453,000	151,800	720,000	1,128,000	871,800
2011	Annual Report for 2011 (Federation Employment Agency, (2012a, p. 13)	Beneficiaries:	144	181	57	487	325	544
		BAM x months:	350 x 6	400 x 6	500 x 9	600 x 12		
		TOTAL BAM:	302,400	434,400	256,500	3,506,400	736,800	3,762,900
2012	Annual Report for 2012 (Federation Employment Agency, 2013, p. 13)	Beneficiaries:	<i>Unspecified.</i>		<i>Unspecified.</i>		245	78
		BAM x months:	<i>Unspecified.</i>		<i>Unspecified.</i>		402 x 6	563 x 12
		TOTAL BAM:	<i>Unspecified.</i>		<i>Unspecified.</i>		590,940	526,968
2013	Annual Report for 2013 (Federation Employment Agency, 2014, p. 18)	Beneficiaries:	<i>Unspecified.</i>		<i>Unspecified.</i>		413	537
		BAM x months:	<i>Unspecified.</i>		<i>Unspecified.</i>		460 x 6	460 x 12
		TOTAL BAM:	<i>Unspecified.</i>		<i>Unspecified.</i>		1,139,880	2,964,240
TOTAL Beneficiaries:						1,684	1,372	
TOTAL BAM:						4,165,620	8,587,908	

Source: Federation Employment Agency (2008), Federation Employment Agency (2010d), Federation Employment Agency (2012a), Federation Employment Agency (2013), Federation Employment Agency (2014).

Two main dimensions can be seen from Table 3. One is the number of beneficiaries per category of education level, which was changing over the years. At the end of 2013, more than 55% of all the beneficiaries were from the group with lower education, and less than 45% from the group with higher education. This is clearly not in line with the priorities defined in the Strategy. However, taking financial indicators into account, this discrepancy with Strategic priorities becomes even more drastic.

The Table 3 also shows changes in the allocation of funds for co-financing the jobs during the years. In 2010, with the official Program start, there was a rather significant increase of BAM 150 monthly allocation per beneficiary, flat for all categories. Since the co-financing period for the beneficiaries with higher education was twice longer, this increase is not flat – it is non-linear and results in doubling of the amounts allocated for the higher education category.

This non-linearity of funds allocation became even more apparent in 2011 when the co-financing amounts for both categories with lower education were decreased for BAM 100 flat, while the amounts for the high-skilled category was decreased only BAM 50, and the highest category remained unchanged. As a direct result of such funds allocation, the financial outcome shows that category with lower education actually used less than one-third of all the funds allocated for the Program, while the group with higher education used more than two-thirds.