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PUBLIC GOVERNANCE AND TERRITORIAL DEVELOPMENT DIRECTORATE
PUBLIC GOVERNANCE COMMITTEE

PARTNERS FOR GOOD GOVERNANCE: MAPPING THE ROLE OF SUPREME AUDIT INSTITUTIONS

ANALYTICAL FRAMEWORK (PRELIMINARY VERSION)

Meeting of the Public Sector Integrity Network

16-17 June 2014 at OECD Headquarters in Paris, France

This is the preliminary version of the Analytical Framework for the OECD study on the role of Supreme Audit Institutions (SAIs) on enhancing good public governance. The Framework identifies challenges and presents opportunities for how SAIs can have a greater impact on governance relating to resource allocation, law making and policy coherence. In particular, the Framework suggests ideas for consideration within specific country contexts on budgeting, regulatory policy, the Centre of Government and internal control.

The policy questions to be discussed during the audit session in the morning of 17 June 2014 relate to the ideas presented in the Analytical Framework, as summarized in GOV/PGC/ETH(2014)9.

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FOREWORD

As governments are grappling with fiscal consolidation, they are also facing a decline in public confidence in their ability to tackle complex policy challenges that were borne out of, or were exacerbated by, the financial crisis. They are revisiting policy tools and processes in order to provide value-for-money in the face of continuing fiscal constraints. The complexity of interwoven policy issues requires solutions that are sufficiently innovative, cross-cutting and coherent. Achieving good public governance cannot be an insular endeavour but instead requires a whole-of-government approach. To the extent that the financial crisis highlighted weaknesses in existing analytical tools, frameworks and governance arrangements, new ones should be considered.

Restoring trust in public institutions is vital to enabling governments to take a more proactive approach to addressing the long-term needs of citizens and society. In order to be trusted, governments must demonstrate evidence-based policy-making and sound management of public resources to make the trade-offs and policy decisions that improve economic and social well-being. The OECD's New Approaches to Economic Challenges seeks to enable governments to find better ways to cope with policy trade-offs, while identifying, prioritising and combining reforms to support sustainable and inclusive growth. Citizens need to be confident that both the policy process and markets are not structured in a way that favours growth at the expense of their well-being. At the heart of this is ensuring that policy formulation, implementation, and monitoring and evaluation are effective, efficient and economical and, critically, designed with citizens in mind. In essence, this means more strategic and open public governance.

A key player in holding governments to account for their stewardship of public resources is a country's Supreme Audit Institution (SAI). As an independent actor, SAIs provide objective and credible information on the effectiveness, efficiency and economy of government policies and programmes. From their bird's eye perspective, SAIs are uniquely placed to provide the cross-cutting evidence and insight that governments need to inform difficult policy choices, and to develop the foresight required to support long-term visions.

SAIs are often an understated yet important partner in ensuring a whole-of-government approach to enhancing good governance – a prerequisite to restoring public trust. With this in mind, this OECD study explores how SAIs can better support and enhance public governance across government functions that are key to the policy-making process: appropriate resource allocation, law making and policy coherence. It assesses the challenges and opportunities in government budgeting, regulatory policy, the Centre of Government and internal control to identify how SAIs' independent audit work can contribute towards better functioning governments and more effective policies.

This study provides practical guidance to inspire and inform new dialogues between SAIs and their respective Executive branch. It draws upon years of good governance thinking within the OECD as well as the crucial collaboration of its sponsor, the SAI of Brazil, and the input of twelve peer SAIs from both OECD members and key partners. Through a frank awareness of the gaps in good public governance, a more collective and effective approach can be employed to serve the public interest and help governments in reaching the common goal of better policies, for better lives.

ACKNOWLEDGEMENTS

The development of this analytical framework was led by the Public Sector Integrity Division of the OECD's Public Governance and Territorial Development Directorate (GOV). The work was spearheaded by Ishat Reza, Portfolio Manager, and Alison McMeekin, under the supervision of Janos Bertok, Division Head. The analytical framework also benefited from early guidance and planning by Paloma Baena Olabe, Deputy Head, proofreading by Douglas Herrick, and formatting and finalisation assistance by Sophie O'Gorman.

This framework is indebted to a strong team of public policy experts at the OECD. The sections on budgeting and regulatory policy were written by Ronnie Downes of the Budgeting and Public Expenditures Division, and James Sheppard of the Regulatory Policy Division, respectively. The section on Centres of Government was substantially written by Andrew Davies of the GOV Director's Office.

The framework benefited further from the expert reviews and commentary from the OECD Internal Audit and Evaluation Directorate, Edwin Lau and Christoph Demmke of the Reform of the Public Sector Division, and Adam Ostry and Andrea Grifoni of the Governance Reviews and Partnerships Division.

Valuable external viewpoints were provided by the Institute of Internal Auditors, which provided expertise and commentary on the internal control section, and by auditor Michel Carles in the form of advice, research and review of the section on Supreme Audit Institutions.

The framework, and this project more broadly, is reliant upon the generous and continued support of its 12 peer Supreme Audit Institutions, and their dedicated representatives, who are key to the developing network surrounding this project and who provided substantial input and peer review of this analytical framework. Additionally, many actively consulted representatives from their Executive body as part of the review. For this, we thank our colleagues at the Supreme Audit Institutions of Canada, Chile, the European Union, France, India, Korea, Mexico, the Netherlands, Poland, Portugal, South Africa and the United States. This framework was possible due to the valuable contributions of the study's sponsor, the SAI of Brazil - the Tribunal de Contas da União (TCU). In particular, we extend our gratitude for their valuable guidance and input to Marcelo Barros Gomes, Paulo Roberto Simao Bijos, and Virginia de Angelis Oliveira de Paula of the TCU.

We are grateful for the support of all contributors, and look forward to further developing this network in Phases II and III of this study.

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EXECUTIVE SUMMARY

A whole-of-government approach is needed to encourage trust and to foster good governance, and SAIs are uniquely placed to support this process

The financial crisis highlighted weaknesses in public governance, institutions, policy tools and processes. With subsequent fiscal consolidation timelines extending beyond what governments had anticipated, they are facing the challenge of revisiting and reforming their activities with limited resources. This coincides with a wider public management trend of demonstrating value-for-money, and using evidence about government performance to drive strategic change that will sufficiently address complex policy challenges emanating from or exacerbated by the crisis. The interconnectedness of the machinery of government, highlighted by the systemic ripple effects of the financial crisis, suggests that improvements to governance need to be driven from a whole-of-government perspective. This approach to good governance can be embodied in what the OECD calls a strategic and open state (Box 0.1).

Box 0.1. **Good Governance in a Strategic and Open State**

Public governance, simply put, is how governments use public resources to develop policies, implement programmes and deliver services for the benefit of citizens and society. In this study, *good* governance is the optimisation of the public policy process. It is the assurance that the policy process – policy formulation, implementation, and monitoring and evaluation – is operating optimally with effectiveness, efficiency and economy, and that it is underpinned by broader governance principles such as rule of law, transparency, integrity and accountability.

Good governance is operationalised through a strategic and open state that is proactive and delivers responsive and effective public policies while managing tight fiscal pressures. A strategic and open state has the following characteristics (OECD, 2012, 2013a):

- **Strategic agility**: This refers to the state's capacity to identify and address internal and external challenges and risks, strengthen efficiencies in policy design and service delivery to meet these challenges, and mobilise actors and leverage resources to achieve integrated and coherent policy outcomes that address these challenges effectively as it pursues its strategic long-term vision for the country.

- **Institutional robustness**: This refers to the institutional structures and networks that enable the state to achieve coherence in strategy, policy and purpose, without inefficiencies, fragmentation, redundancies or overlaps.

- **Openness:** This refers to the ability and willingness of the state to show how its actions and decisions are consistent with clearly defined and agreed objectives, and to work outward with non-state actors through discussion, partnership and other means in order to advance a shared societal vision.

- **Effective processes:** This refers to the systems and processes, or the machinery of government, that the state can leverage to ensure efficiency and effectiveness in its delivery of public outputs and ultimately to achieve its strategic objectives and government-wide vision.

A major policy challenge that governments face is to restore the public trust that was shaken as a result of the financial crisis. A lack of trust is difficult to overcome when governments, and particularly the Executive, continue to take a short-term, reactive approach to governing. Thus it is critical that governments regain the trust needed to shift from a reactive to a proactive approach, which is a prerequisite to addressing other lingering policy challenges.

The OECD's experience and data show that trust in public institutions is driven, in large part, by (i) the way policies are designed and implemented and (ii) the way policy-makers comply with standards that ensure their behaviour is in the interest of citizens. Restoring trust in the system will require governments to provide evidence of good governance – to show that policies are developed and programmes are delivered with the public interest in mind. For this, the Executive should rely on public institutions that can provide credible evidence or reasonable assurance of a government's trustworthiness. Through its role as an independent institution, a Supreme Audit Institution (SAI), responsible for external public auditing, is uniquely placed to provide this credible and objective evidence.

An SAI's contribution to good governance can be considered in two ways. On the one hand, SAIs are part of the system of accountability in a state by reinforcing the effectiveness of bodies responsible for government oversight and for public financial management. When SAIs are professional and independent they strengthen the accountability chain, which is required to ensure that public interest prevails over personal interest in policy-making. On the other hand, SAIs are evolving from limiting their audit work to traditional assessment of compliance and are increasingly conducting useful assessments of the performance of policies and programmes. Thus, through their work, SAIs (i) provide reasonable assurance and assessment of the way policies are designed and implemented and compliance of policy-makers, and (ii) provide evidence of the performance of the machinery of government and programmes.

This independent, objective and reliable information is needed by governments to demonstrate to citizens their trustworthiness, as well as to make informed, evidence-based decisions about policy trade-offs, keeping in mind value-for-money and broader principles of good governance.

Independent and professional SAIs are a source of credible and objective information about public institutions and cross-cutting processes

An SAI is responsible for overseeing and holding government to account for its use of public resources, together with the Legislature and other oversight bodies. In a democratic system, SAIs usually report to the Legislature and to citizens, and in some cases to the Executive or the head of state. Where there is more than one body fulfilling the public sector external audit role, the SAI is usually distinguished as possessing the strongest constitutional guarantees of independence (OECD, 2011).

The type of assessment an SAI undertakes varies depending upon the reason for its execution, the type of audit, the conclusions that are drawn, the "users" or audience of the audit findings and the way in which findings are reported, explained in more detail in Section 4. SAIs have been evolving, repackaging their audit work in non-traditional ways. SAIs are moving away from limiting their work to simply financial and compliance audits of the management of public funds, and are undertaking audits of new scope often under the banner of performance audits or combined audits. In some cases, SAIs may even investigate complaints, at the request of citizens, where damages have been caused by the public service or a public official. Some SAIs can also audit implementation of previously agreed upon audit recommendations from past audits.

The expanding knowledge base that is accumulated through audit work enables SAIs to provide different levels of analysis. SAIs are not only providing oversight, but increasingly insight and foresight to audited entities with respect to their functioning and to the Executive and Legislature with respect to whole-of-government issues.

Well-functioning SAIs provide **oversight** to ensure that government resources are spent appropriately, that policy is implemented as intended, that strategies are met, and that the overall performance of the government meets stated policy objectives in conformance with laws and regulations. Some SAIs provide **insight** to assist audited entities and other decision-makers by assessing which programmes and policies are working and which are not, providing feedback to adjust policies and by sharing best practices information. One way in which some SAIs are providing this insight is through programme evaluations, which are extensions of performance audits that aim to provide explanations for successes and failures of policies based on objectives and implementation. Some SAIs are providing **foresight** to help entities in looking forward by identifying trends and bringing attention to emerging challenges before they manifest into significant risks.

In addition to providing audit reports aimed at the audited entities, some SAIs are drawing on their oversight and insight to issue good practice guidance as well as to provide counselling and advice, usually upon request of the government or Legislature.

There are a variety of ways that SAI work could support good governance by providing assessment of and reasonable assurance on the performance of key government functions

As good governance is the optimisation of the policy process, governments need to ensure that the key functions that guide the policy process are working with effectiveness, efficiency and economy. Law-making, policy coherence and appropriate resource allocation are the cogs of the policy process that both feed off of and feed into principles that underpin the policy process, such as adherence to the rule of law, transparency, integrity and accountability.

Law-making, policy coherence and appropriate resource allocation and use rely on activities, tools and processes, for their well-functioning. This study focusses on four areas that are key to the policy-making process: **budgeting, regulatory policy, the Centre of Government and internal control**. Resource allocation and law-making rely on effective budgeting and sound regulatory governance. Government-wide policy coherence and strategy is underpinned by strong Centres of Government, and good use of public resources relies on effective internal control systems.

This study looks at what is considered good governance in each of these areas, and what challenges exist in achieving it. Analysis is framed by international best practice guidance and the idea of a strategic and open state. Through this analysis, the analytical framework offers different options for SAIs to consider in using their assurance and assessment work to strengthen the four areas of government activity in focus. They can be categorised in three ways:

- Assessing processes, systems and frameworks;
- Assessing actors or institutions; and
- Assessing government policies and programmes.

The ability for an SAI to engage in these areas will depend on its specific context including its mandate and capacity. As such, options for evolving SAI work will need to be considered in light of the roles of relevant actors, and particularly the Executive, to pinpoint the most useful and relevant value-added work to tackle the policy challenges of that country.

Ensuring appropriate resource allocation through effective budgeting

Effective budgeting is a necessary component of sound financial management, which ensures that resources are allocated to the areas for which they were authorised, and that resources are deployed appropriately in that context. The OECD's work on budgetary governance shows that many OECD countries had extended the depth and duration of their previous budget consolidation plans in view of fiscal difficulties that continued for longer than anticipated. In view of continued fiscal consolidation and budgetary trade-offs, there has been an intensified focus on the budgetary tools, mechanisms and processes that can be utilised to support governments and public administrations in this complex endeavour. More generally, the broader role of Public Financial Management (PFM) and budgeting is being re-assessed to underscore the necessary linkages and inter-connections with other areas of public governance - including whole-of-government medium-term planning, performance-related budgeting, full transparency and accessibility of budgetary information, identification and management of fiscal risks, and enhanced quality assurance throughout the different phases and functions of the budget cycle.

SAIs have traditionally interacted with the basic functions of PFM and budgeting through their work in ensuring that resources are allocated to the areas for which they are authorised and that they are deployed accordingly. SAIs have been producing reports on PFM and end of year accounts through audits, as well as issuing opinions or observations on the government's financial reporting.

As the understanding of the role of PFM and budgeting widens, it is appropriate that the role of SAIs should be reassessed too. What may be particularly useful is to couple the contribution of SAIs between their traditional scrutiny of PFM concepts in action, with more nuanced evaluations of the performance of closely related activities including medium-term planning and identification and management of risks. Table 0.1 provides a summary of the ways in which SAI work may support governments aspiring to integrate best practices in PFM and effective budgeting into their policy-making process.

Table 0.1. **Potential ways in which SAIs can support sound Public Financial Management and effective budgeting**

Effective Budgeting	Assessing processes, systems, and frameworks	Assessing actors or institutions	Assessing government policies* and programmes
Accuracy of fiscal forecast	SAIs could assess whether adequate institutional procedures and safeguards are in place to ensure reliability and quality of tools that underlie the budget		
Top-down budgetary management and planning; alignment with strategic priorities	SAIs could assess whether the processes and procedures in place facilitate an alignment between budgeting and strategic objectives		
Medium-term aspects of budgeting	SAIs could assess whether there is an effective framework in place for guiding the annual process of resource allocation		
Capital budgeting	SAIs could assess the effectiveness of the national framework capital investment projects SAIs could assess whether there are sufficiently robust procedures and technical capacity in place to effectively evaluate procuring capital investment projects		
Comprehensiveness of budgetary information and accounting	SAIs could assess whether the existing public accounting framework is fit for informing citizens, Parliament and key stakeholders of the true position of the public finances SAIs could assess whether the budget document provides a true, full and fair account of the position of the public finances SAIs could audit whether the budgetary information conforms with stated accounting standards, communicating the resource-management and policy implications		
Ensuring quality of budgetary implementation and delivery	SAIs could assess the effectiveness of the procedures in place for managing, monitoring and overseeing financial allocations SAIs could assess whether there are adequate mechanisms in place to generate and capture quality performance information during the phase of budget execution		
Identification and management of longer-term sustainability and other fiscal risks	SAIs could assess the integrity and quality of the systems in place for assessing long-term fiscal sustainability SAIs could assess the overall risk-management system within system of public and budgetary		

Effective Budgeting	Assessing processes, systems, and frameworks	Assessing actors or institutions	Assessing government policies* and programmes
Promoting integrity and quality in budgetary management	SAIs could assess the soundness and quality of the overall national framework of budgetary governance in promoting optimal resource allocation, implementation, evaluation and review	SAIs could audit the annual public accounts of public bodies and of the government as a whole, as to their accuracy and probity, and as to the effectiveness of the public financial management systems in place SAIs could maintain a public log of the key audit findings and recommendations in respect of each public body and of the government as a whole, and updating the log by reference to the actions taken to address the issues arising	
Performance, evaluation and value-for-money	SAIs could assess the quality of performance information used in performance-related budgeting processes, as to its quality, availability and auditability; and advising on how this information could be improved SAIs could assess the soundness of the programme logic models in place in performance-related budgeting processes, as to their evidential basis, and as to the quality of processes in place for developing such models		SAIs could audit the performance of particular programmes as to their effectiveness, efficiency and economy

**Note: Apolitical assessment of a policy's rollout that is distinct from, and does not include, the agenda setting or decision-making processes related to the prioritisation or justification of the policy.*

Ensuring sound law making through effective regulatory policy

Effective regulatory policy ensures that regulations are delivered to meet underlying public policy objectives and to positively impact the economy and society. Regulations are indispensable to the proper functioning of the economy and societies and to the implementation of policies so that objectives can be achieved. They underpin markets, protect the rights of citizens and facilitate the delivery of public goods and services. Many OECD countries are increasingly recognising the importance of effective regulatory governance and are beginning to articulate their own regulatory policies. Yet it appears that often a country's regulatory governance policy consists of not one but a series of often disjointed regulatory policies.

Regulations are not costless and have continuing, if not expanding, economic significance, justifying a permanent need to assess regulatory policy and tools. In addition, governments are also facing the challenges of closing the regulatory policy gap to facilitate implementation and enforcement; finding an appropriate institutional arrangement for regulatory reform; generating evidence about regulatory policy trade-offs, costs and benefits of reforms; and addressing better regulation beyond the border.

While SAIs are not typically considered to have a role related to regulatory policy, it appears that some are indeed making efforts to support better functioning on regulations in their country. SAIs' work in this area mainly falls under the banner of performance audit, and covers aspects of regulatory policy formulation, implementation and monitoring and evaluation through:

- Performance audits of regulatory policy and governance (e.g. use of impact assessment, administrative burdens reduction programme);
- Performance audits of regulators (e.g. performance of regulatory in achieving their operational objectives, having regard to public sector resources consumed); and
- Performance audits of regulations (e.g. considering also, or instead, achievement of the benefits sought through the adoption of the regulations, and taking into account the consumption of non-public sector resources, such as compliance costs – the cost to regulated entities and others of complying with the regulations).

A continuation or expansion of external audit work in the area of regulatory policy may be beneficial in view of the challenges that governments are facing in establishing coherent regulatory policy systems, and in view of the continuing economic significance of regulatory policy. Table 0.2 provides a summary of the ways in which SAI work may support governments wanting to strengthen their regulatory policy regimes.

Table 0.2. **Potential ways in which SAI work can support sound regulatory policy**

Effective Regulatory policy	Assessing processes, systems, and frameworks	Assessing actors or institutions	Assessing government policies* and programmes
Effective performance of regulatory policy and governance	Assessing the use of integrated, regulatory impact assessment, administrative burdens reduction programme Reviewing regulatory stock, for examples, providing *ex-post* regulatory evaluation Assessing regulatory coherence across levels of government		
Effective performance of regulators		Assessing performance of regulatory in achieving their operational objectives, having regard to public sector resources consumed Assessing frameworks for communication, consultation and engagement Assessing the organisation of regulatory agencies Assessing the regulatory management capacity at sub-national level	
Effective performance of regulatory programmes and tools	Assessing the existence of an explicit policy on regulatory quality		Assessing also, or instead, achievement of the benefits sought through the adoption of the regulations

**Note: Apolitical assessment of a policy's rollout that is distinct from, and does not include, the agenda setting or decision-making processes related to the prioritisation or justification of the policy.*

Ensuring policy coherence through strong Centres of Government

The Centre of Government is defined as the administrative structure of core institutions that serve the Executive. Strong Centres of Government are critical for facilitating coherence of policies and programmes across government, and the productive co-ordination among stakeholders involved in the policy process. Ensuring horizontal and vertical co-ordination helps policies to be formulated without redundancies or inefficiencies.

Centres of Government are expected to lead ever more complex policy agendas and co-ordinated responses that offer a whole-of-government perspective. They are increasingly active in budget and policy development, and in steering of implementation across government. The expansion of mandates has highlighted the limited resources of Centres of Government and has raised questions in OECD and non-member countries about the viability or reform of structures, resources and linkages to other key areas of governance in order to accomplish its widening range of complex tasks.

A strong Centre relies on quality and evidence-based decision making, strategic planning and foresight, and policy co-ordination for effective implementation and monitoring of programmes across its departments and agencies to avoid redundancies across ministry functions or conflicts between sectoral interests. It involves a careful balancing of trade-offs between ideal policies and programmes and political and practical limitations, including the need to do more with less.

SAIs do not appear to have a systematic approach for supporting or assessing the Centre. Involvement to date is seemingly limited to an ad hoc basis. Nevertheless some SAIs have provided valuable whole-of-government assessments, which could inform further development in this area. SAIs can offer the Centre of Government insight and foresight on the performance of other key functions of government that Centres are trying to link into a coherent rollout of the Executive's strategy. Particularly where Centres of Government are limited in resources, they should rely on the evidence base that SAIs can provide as valuable input. Table 0.3 offers potential ways that SAI audit work may support strong Centres of Government in completing their tasks to ensure that strategic policy objectives are translated into policies that benefit citizens in reality.

Table 0.3. **Potential ways in which SAI work can support strong Centres of Government**

Strong Centres of Government	Assessing processes, systems, and frameworks	Assessing actors or institutions	Assessing government policies* and programmes
Quality and evidence-based decision making; awareness of challenges and risks			Conducting horizon scanning activities or synthesising cross-cutting findings on risks and implementation challenges, as input into the budgeting process
Strategic planning and foresight	Assessing the clarity of responsibilities and division of tasks in Centre of Government institutions. Assessing the codification of processes that govern Centre of Government institutions (in legislation, for example).		Assessing the existence of a government-wide strategic plan for personnel management.
Effective policy co-ordination	SAIs could provide valuable information at a whole-of-government level for the Centre's oversight and co-ordination functions, to enable quality policy formulation, policy coordination and monitoring. Assessing the existence of a reasoned evaluation programme in each ministry, to gather cross-cutting information on the effectiveness of Centre of Government performance.	Assessing the functions fulfilled by the Centre in relation to other bodies to understand synergies and overlaps.	Assessing the outcomes of major initiatives led by the Centre, particularly "mission-oriented" policies or programmes.

**Note: Apolitical assessment of a policy's rollout that is distinct from, and does not include, the agenda setting or decision-making processes related to the prioritisation or justification of the policy.*

Ensuring good use of public resources through strong internal control mechanisms

Internal control systems form the set of checks and balances of government operations that are necessary for the effectiveness and efficiency of operations, the reliability of financial reporting, and compliance with applicable laws, regulations and policies. Internal control exists at two levels through the government-wide internal control systems, and the internal control processes of individual public institutions. Strong internal control mechanisms – both systems and processes – facilitate implementation of programmes and allow for transparent and fluid monitoring and evaluation.

Internal control systems require a clear delineation of roles and responsibilities for risk management to avoid duplication or redundancies. To be effective, risk management frameworks must be applied organisation-wide and not conducted in silos or limited to discrete parts of an organisation.

Establishing effective internal control processes is not a costless endeavour, and requires a cost-benefit analysis to determine the optimal level of control processes that will facilitate the achievement of objectives. This is an important balance to strike because excessively burdensome controls – similar to poorly designed internal control systems – can lead to a greater risk of circumvention of control processes, inefficiencies or unnecessary delays in delivering public services. Internal control processes should be designed to mitigate risks to an acceptable level and should permeate an entire ministry's operations.

SAIs have the responsibility of conducting the external audit of the ministries, or public entities, in which internal control processes are embedded, and over which internal control systems preside. Given that SAIs interact with internal control at these two levels, SAIs can contribute to more efficient and effective internal control processes at the ministry level, and to more efficient and effective internal control systems at the whole-of-government level. Some ways in which SAIs could do this are presented in Table 0.4.

Table 0.4. **Potential ways in which SAI work can support effective internal control mechanisms**

Strong Internal Control Mechanisms	Assessing processes, systems, and frameworks	Assessing actors or institutions	Assessing government policies* and programmes
Strong internal control processes at the ministry level	Assessing the objectivity and independence of internal audit Assessing the quality and accuracy of information provided from internal audit to external audit Assessing processes for establishing risk tolerance, prioritisation and criteria Assessing whether roles and responsibilities of management oversight and responsibilities are clear Co-ordinating with internal audit to avoid overlaps and maximise synergies	Assessing internal audit units, particularly with respect to their efficacy in ensuring internal control and using a risk-based approach	
Strong government-wide internal control systems	Assessing the rollout of internal control processes across government by synthesising information gathered at the ministry level Assessing the design and quality of anti-corruption and anti-fraud frameworks	Assessing the level of independence of audit committees Assessing the audit committee's mandate for the adequate coverage of risk monitoring, including of fraud and corruption	

**Note: Apolitical assessment of a policy's rollout that is distinct from, and does not include, the agenda setting or decision-making processes related to the prioritisation or justification of the policy.*

Oversight of internal control systems is key, and internal auditors are important contributors in this regard. Thus, in addition to auditing or overseeing internal control units, SAIs can maintain a professional relationship with internal audit units and audit committees, to make both audit and internal control processes more efficient and effective by learning from each other and removing redundancies.

Catalysts for impact

To enhance the impact of all types of audit assignments, new and old, SAIs may also consider broader external engagement through the audit process, and presenting the findings in a way that provides further reach and clarity for a broader audience base. Some SAIs have been successful in increasing the use of their work by engaging with its "users" – namely citizens, Legislature and the Executive – to understand how to package and present work in a way that is more useful. The importance of this is evidenced by a growing and valuable discourse in the international community, particularly on SAIs and citizen engagement.

Engaging audited entities during all stages of an audit can help them to grasp the origins of and reasoning behind any recommendations. Furthermore, information derived from engagement with internal and external stakeholders can be used as valuable input to audits and also to the policy-making process. This can be done by engaging citizens to gather external perspectives and evidence on the efficacy of programmes, and communicating key results to policy-makers during policy formulation stages.

A professional working relationship with Parliament or key committees provides greater opportunity for two-way communication that not only enhances the audit findings, but potentially also the follow-up of findings and recommendations. These dialogues provide a forum to elevate key findings, trends and risks that bolster traditional reporting methods by reiterating key points. This contributes to the efforts of legislative committees responsible for following up on audit recommendations, where they exist.

Many SAIs have been using their wealth of knowledge to provide counselling to the Executive and Legislatures and to issue guidance to its audited entities. Guidance has included, for example, the provision of guidelines on administering regulations, and on developing criteria for designing, implementing and operating an internal control system. Good practice guidelines encourage coherence and consistency in government processes, like streamlining auditees' reporting methods, which facilitate a smoother and more efficient audit process.

Engagement enables SAIs to acquire a better understanding of what its "users" deem as useful and relevant, and to repackage their findings with this in mind. Many SAIs are providing results of key audit findings and of other technical assessments in a format and in language that is accessible to citizens, including through simple publications and through on-line media. These approaches not only broaden the reach and impact of audit work, but help to strengthen the accountability chain by ensuring stakeholders are better informed on the effectiveness, efficiency and economy of policy making and programmes. Capitalising on transparency and openness to empower citizens with credible information is not only important to raising the profile and recognition of SAI work, but is also a critical step toward restoring or maintaining trust in government.

Productive discussions between necessary actors can help to determine what SAI work is particularly relevant and useful for good governance in each country context, and how this work is best facilitated

The relevance and usefulness of the audit engagements suggested in this analytical framework will depend on the country context. The impact that an SAI will have in conducting this work will also depend on their capabilities. Considering the ways in which SAIs can support good governance in budgeting, regulatory policy, the Centre of Government and internal control, should be based on (i) a discussion between relevant actors in a country's constitutional arrangements for the execution and oversight of public financial management, and (ii) an introspective view on the part of the SAI to understand how its capabilities align with existing and new work.

This wealth of information that SAIs generate on public institutions and cross-cutting processes is already considered as valuable input for strengthening governance. Yet, in many cases, audit work can be better leveraged for the purposes of supporting the agility, processes, robustness and openness of a state.

As governments explore how to revisit or reform activities in the name of value-for-money, they will require evidence on how well public institutions and the machinery of government are functioning in order to make quality, evidence-based decisions. Independent and professional SAIs may be well placed to provide this information through their increasing wealth of knowledge and expanding whole-of-government perspective. SAIs can help governments to inject principles of effectiveness, efficiency and economy into its policy-making process.

To understand how exactly SAIs can enhance the impact of their work on good governance, a discussion should be held between the actors responsible for public sector oversight, and with the Executive, as to which areas of audit work are most useful and relevant in the country context. These discussions may include the following considerations: the SAI's mandate, as provided in the constitution or supporting legislation; the relationship between SAI, Legislatures and legislative committees; the reporting lines of the SAI; and the existence of other committees where complementarity or overlaps may arise.

Ensuring capacity for relevant and useful work

How the ideas presented in this framework can be integrated into an SAIs' audit programme will be context specific. The elements of an SAI's audit work - the reason for its execution, the type of audit, the conclusions that are drawn, the ways in which they are reported and the audience or "users" of that information - can be varied or repackaged in a way that is most useful and relevant for tackling policy challenges in the SAI's country.

For SAIs to update existing work or to undertake new work, they will need to (i) hold themselves to the same standards expected of the entities they audit; (ii) to embody the independence needed to provide credible and objective findings; and (iii) have the institutional capability to do so. This puts the onus on the SAI to take an introspective view of its own ability to re-evaluate its work in the context of the ideas presented in this analytical framework. Yet it also places a responsibility on the appropriate constitutional actor to ensure that the SAI has independence and autonomy, and is adequately resourced to carry out any expansion or modification to the SAI's audit programming that would be required to support good governance.

An SAI's ability to assess public systems, actors and institutions, and programmes may depend on the maturity of audit subjects, notwithstanding the availability and presentation of sufficient data to conduct the actual assessment. It may also depend on the extent to which an SAI's work is predisposed to assessing materiality and risk based on government spending.

In considering the potential areas for SAI audit engagement, this study puts forth distinct, but interrelated guiding principles to frame the discussions between necessary actors. They are that:

- Changes to a SAI's work should be in areas in which the SAI is likely to have, or should be in a position to develop, relevant expertise, consistent with its mandate

- Duplication of functions should be avoided; the SAI should not be expected to exercise functions that are already being serviced by, or should be serviced by, another expert body or institution

- An SAI's role should support, but should not displace*,* the proper role of other bodies – democratic or bureaucratic in supporting government activity

- An SAI, like other public institutions, has limited resources and must operate in a manner that is efficient and effective; therefore it can only reasonably be called upon to exercise new functions in line with its financial and human resources

SAIs as partners for good governance moving forward

Key functions of government – law-making, policy coherence and appropriate resource allocation and use – are converging, relying on the same cross-cutting activities for their well-functioning. Thus establishing the effectiveness, efficiency and economy of budgeting, regulatory policy, Centres of Government, and internal control is a whole-of-government endeavour. It requires evidence on performance from those bodies that are in a position to offer input on trends, sustainability and risks to establishing good governance.

SAIs are well placed to provide the insight to support a whole-of-government approach to good governance. Yet, they need to be both empowered to develop their cross-cutting knowledge about the performance of key functions of government, and have the capabilities and independence to do so effectively. With this in mind, a professional partnership between SAIs and the Executive could facilitate the credible, objective and independent information that is useful and relevant for supporting good governance needed to restore trust and tackle complex 21st century challenges.

PART I

1. INTRODUCTION

Major global trends – including globalisation and shifting wealth, population growth and ageing, and environmental challenges – have been placing pressure on governments to come up with innovative and cost-effective ways of addressing the unprecedented policy challenges these trends present. In some countries these pressures have been compounded by the financial crisis, which exposed weaknesses in the government's ability to both protect the economy and society, and to recover from its negative impacts. In some cases, this has resulted in citizens' loss of confidence in their government's ability to also handle other pervasive and complex policy issues that pre-dated the crisis.

Governments must now demonstrate, and restore trust in, their ability to deliver programmes and services that meet societal expectations and address complex challenges. The OECD's experience and data show that trust in public institutions is driven, in large part, by (i) the way policies are designed and implemented, and (ii) the way policy makers comply with standards that ensure their behaviour is in the interest of citizens (OECD, 2013). In a sluggish post-crisis recovery, governments are expected to foster better public management with fewer public resources.

Public governance is the process through which governments orchestrate institutional and process-oriented arrangements to develop policies and deliver programmes and services that benefit citizens and society. This study sees good governance as the optimisation of this process – delivering programmes and services efficiently, effectively and economically. Good governance signifies that this process is underpinned by broader principles such as rule of law, transparency, integrity and accountability that work to ensure policy makers have the public interest in mind.

The post-crisis environment has been characterised by ongoing fiscal consolidation and evidence that government functions are inexplicably linked. Accordingly, governments are revisiting their activities with value-for-money in mind. This complex endeavour requires credible evidence about the performance of public institutions and the machinery of government in order to make quality, evidence-based decisions about policy trade-offs. This requires a whole-of-government approach that respects the autonomy and roles of all actors involved in public governance, but that also maximises their positive impact.

When Supreme Audit Institutions (SAIs), champions of external public sector audit, are well-functioning and independent, they play a key role in ensuring the effective use of public resources, sound fiscal management and proper execution of administrative activities (INTOSAI, 1977). This is accomplished through their audit work, which detects deviations from standards of legality, effectiveness, efficiency and economy of financial management. However, SAIs are no longer limiting their audit and counselling work to assessing compliance with financial standards. Increasingly, they are looking at the way in which policies are designed and implemented, assessing their effectiveness, efficiency and economy as well as their performance against policy objectives – thus, providing important information for maintaining trust in public institutions and holding governments to account for their stewardship over public resources.

There is an opportunity for SAIs' work of providing assurance and assessment to be further leveraged to help governments manage public resources optimally and tackle complex policy issues. From their external and independent vantage point, SAIs can provide the type of credible and objective information that governments need to make well informed decisions. This requires a productive and professional partnership between SAIs and other actors responsible for implementation and oversight of public financial management. It requires SAIs to undertake work that is useful and relevant for addressing governance challenges, and it requires increased awareness and openness by audited entities and the broader public of the potential usefulness of audit work.

2. METHODOLOGY

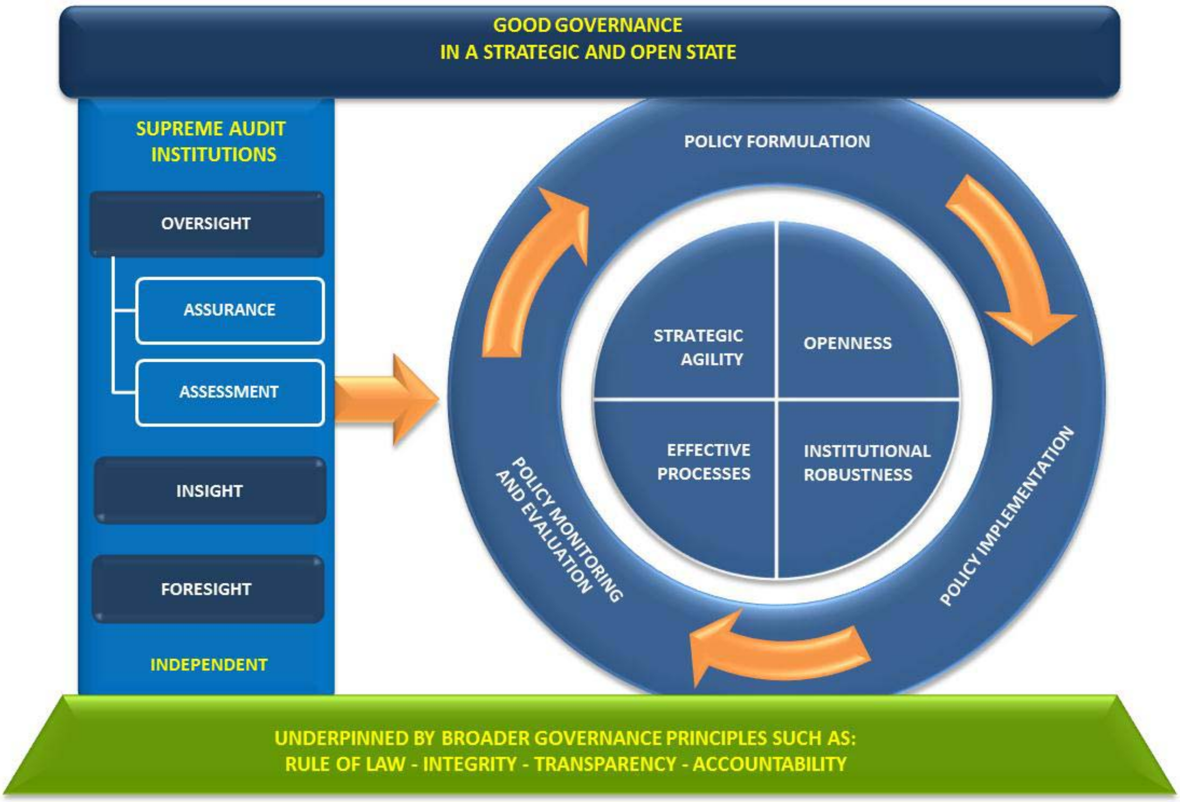
The purpose and scope of the study

The purpose of this study is to help SAIs enhance their impact on good public governance. The study examines key areas of government activity to identify and present opportunities for further SAI engagement in supporting and enhancing good governance at the national government level.

The study recognises that there are multiple actors in, and approaches to, good governance, and thus it does not attempt to create a one-size-fits-all approach. Instead it offers good governance ideas for consideration by SAIs and governments to be assessed within their country-specific contexts. The opportunities identified in the study may or may not fall within some SAIs' current legal mandates or resource bases. Where they do not, it is up to governments to decide whether they wish to broaden the scope of SAIs' work within their constitutional frameworks to support better governance. Equally important in considering any evolution in SAIs' work is to safeguard their independence – a paramount attribute for maintaining their credibility.

The focus of the study, as illustrated in Figure 2.1, is to consider how effective, independent SAIs can contribute to good governance.

Figure 2.1. **The study's purpose and scope**



Effective SAIs

Effective SAIs produce work that is relevant, useful and credible for its audiences. This study defines "SAI work" as the variety of tasks that an SAI may undertake. Audit tasks may differ depending on the reason for their execution, the type of audit, the conclusions that are drawn and the entity to which those conclusions are reported. SAIs also undertake non-audit tasks including counselling and other advisory roles.

The impact of an SAI's work, and thus its ability to support and enhance good governance, relies upon its independence, its mandate, its ability to navigate the external environment and its internal capabilities including leadership, human resources management and the flexibility of its budgeting. Of course there exist other variables affecting the performance, quality and overall impact of an SAI's function that are outside the present scope of analysis. These concepts of SAI work and determinants of its impact are explained in more detail in the "Supreme Audit Institutions" section (Section 4).

Good public governance at the national government level

This study looks at good governance at the national government level. Good public governance, or the optimisation of the policy process, is required during all stages of the public policy cycle. This study focusses on three key stages of the policy cycle:

1. Policy formulation

2. Policy and programme implementation

3. Monitoring and evaluation

The study looks at how government functions that are key to the policy-making process can be more effective, efficient and economical. This analysis is framed by international standards and guidelines, the need for a strategic and open state that demonstrates a proactive responsiveness to emerging issues, and the ability to develop effective policies in the face of fiscal limitations. The application of the concepts of good governance, a strategic and open state, and the three policy stages are discussed in further detail in the "Good Governance in a Strategic and Open State" section (Section 3).

The objective and approach of the study

The objective of this study is to facilitate ongoing dialogues within SAIs, and to encourage new dialogues between SAIs and actors responsible for oversight and implementation of public financial management, particularly the Executive, in order to identify how SAIs can contribute to the government's delivery of more effective, efficient and economical programmes and services. This dialogue is meant to be a two-way learning process. It is intended to provide the Executive and Legislature with a better understanding of the importance, relevance and usefulness of an SAI's function and its existing audit and counselling work. Similarly, it aims to provide SAIs with a better understanding of the challenges that the Executive branch faces, and what type of audit and counselling work is considered relevant and useful in addressing those challenges.

Traditionally, much of the discussions about and between SAIs have centred on the type or model of audit institution, of which there are generally considered to be three, as elaborated in Section 4. This study uses a common language familiar to the SAI community, and presents comparative data on SAIs and their surrounding contexts to provide evidence on similarities and differences that exist between SAIs, going beyond the traditional discussions about an SAI's model. The study aims to give rise to new discussions that are based around the types of tasks that SAIs perform with respect to the maturity of the public sector area in which they undertake those tasks.

Discussions with SAIs, moving forward, should be based more on similarities and differences of the external environment in which SAIs conduct their audit work. The maturity frameworks of the public sector will, to a certain extent, determine how SAIs conduct audits within that framework. By way of example, it is neither feasible nor effective for an SAI to expend resources pursuing an audit of performance budgeting if the government is not close to adopting the practice. Rather than knowledge-sharing on the basis of similar models, or even types of work alone, it may prove more useful for SAIs to share experiences based on the maturity of their audit subjects.

In order to present helpful ideas for SAI engagement in supporting and enhancing good governance, this study uses a collaborative approach, relying on expertise and input from Brazil's SAI, the Tribunal de Contas da União (TCU), which is the sponsor of the study, and twelve peer institutions, the SAIs of Canada, Chile, the European Union, France, India, Korea, Mexico, the Netherlands[1], Poland, Portugal, South Africa and the United States.[2] These peer institutions are members of various committees and groups of the SAI community, representing both OECD and non-OECD member countries in five continents. Their expertise is contributed through the provision of guidance, benchmark data and peer reviews. The study also importantly relies on the expertise of representatives from the peer SAIs' respective Executive branch for feedback on various aspects of the project and for comparative data. This collaborative approach allows the study to take a critically neutral approach to understanding how SAIs can best support and enhance good governance, while respecting the roles and responsibilities of the various actors.

The study is structured in three phases:

- **Phase I: January 2014 – June 2014**: In developing the analytical framework that is presented below, four key areas of government activity were examined. The analytical framework presents opportunities for consideration on how SAIs can support and enhance good public governance in three stages of the policy cycle.

- **Phase II: June 2014 – June 2015**: Surveys will be conducted and an in-depth description of comparative best practices and case studies primarily relating to the four areas of government activity examined in the analytical framework will be gathered with the participation of the peer SAIs and their respective Executive representatives.

- **Phase III: June 2015 – August 2016**: An assessment of Brazil's SAI will be undertaken. It will include an analysis of the ways in which it can strengthen its role in supporting and enhancing good public governance in Brazil at the national level.

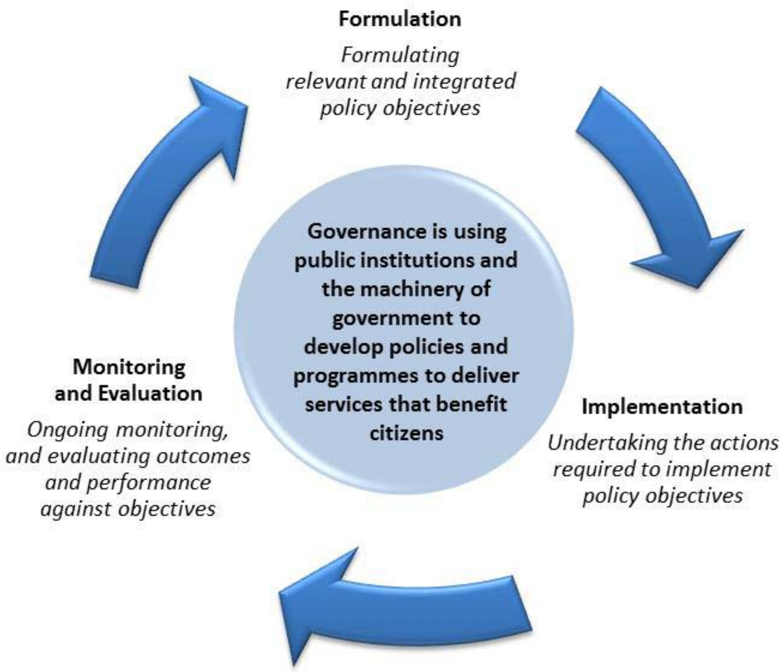
3. GOOD GOVERNANCE IN A STRATEGIC AND OPEN STATE

Before proceeding with the analytical framework for how SAIs can support and enhance good governance, it is important to define what is meant by good governance in this study, beginning with what public governance is, in general.

Public governance

Public governance, simply put, is how governments use public resources to develop policies, implement programmes and deliver services for the benefit of citizens and society. Public institutions use processes and systems, or the "machinery of government," to fulfil their mandates. This requires governments to formulate relevant and integrated policy objectives, to undertake actions (through programmes) to implement these objectives, and to monitor on an ongoing basis and evaluate the outcomes and performance of their delivery against those objectives (Figure 3.1).

Figure 3.1. **Public Governance**



The recent global financial crisis highlighted weaknesses in public governance. It highlighted governments' inability to solve large-scale issues that were created or exacerbated by the crisis, such as unemployment, growing inequality and poverty, and the hollowing out of the middle class. The weaknesses that were exposed in government institutions and systems have reduced citizens' confidence in their ability to tackle these and other increasingly complex policy issues. Even countries that have been less impacted by the crisis are still facing complex policy challenges, many of which pre-date the crisis, such as ageing societies and climate change.

Good governance

The term *good* governance requires precision. In this study, good governance refers to the optimisation of the public policy process. It is the assurance that the policy process – policy formulation, implementation, and monitoring and evaluation – is operating optimally with effectiveness, efficiency, and economy, and is underpinned by broader principles such as rule of law, transparency, accountability and integrity.

A well-operating governance system can restore citizens' trust in their government's ability to develop and implement policies that lead to sustainable and inclusive growth. It can also position governments to address weaknesses that were exacerbated by the crisis. In the post-crisis context, this means demonstrating value-for-money with limited public resources to deliver the best possible outcomes. This need for effectiveness, efficiency and economy is present throughout the policy cycle. For the purposes of exploring the opportunities for SAI engagement, the following three stages that are featured in this study with the recognition that, in reality, it is difficult to extract the stages from one another.

Policy formulation

Policy formulation in the public sector is the process through which a set of actions are laid out in pursuit of goals and priorities that are established to overcome a policy issue that has already been placed on the government agenda. Formulation may include articulating and drafting the actions, as well as assigning policy tools to facilitate said actions. It comes after the distinct process of government-wide agenda setting, during which decision-makers prioritise and decide upon policies to be pursued. Deciding which policies are on the government agenda is inherently political in nature, and thus, is not an appropriate area for SAI engagement.

Policy formulation is often undertaken by ministries that are responsible for the policy's implementation based on their sectoral mandate within the public administration. Formulation inherently requires budgets to be allocated to meet policy goals. In order to develop effective, efficient and economical policies, the formulation stage requires effective coordination across government. It is also important to incorporate insights from those responsible for the implementation of policies and programmes "on the ground", as that is when citizens judge governments' ability to address their needs.

Effective engagement of key stakeholders, environmental scanning and foresight are critical to developing policies that are relevant to the context and of benefit to society in the long-term. The plan of action for each policy needs to take these elements into consideration so that policy objectives can be met in the most effective, efficient and economical way possible. There may be ways in which SAIs could assess the integrity and quality of processes for policy setting, including strengthening the linkages between the three stages of the policy cycle, without encroaching on decision-making with respect to which policies are set. Criteria SAIs could consider using to do so are discussed further in Section 5.

Policy implementation

Policy implementation in the public sector is the process through which policies are operationalised through programmes and services. The detailed design of programmes falls under the implementation phase, though a notional programme plan is usually developed at the policy formulation stage.

Policy implementation can be difficult since, as mentioned above, there can be a disconnect between those who formulate the policy and those designated to carry it out, even if they are from within the same ministry. Policy implementation requires communication between these parties, as well as coordination with other government actors to avoid duplication of effort or redundancies. Efficient and economical budget management is key as programmes are rolled out to ensure policy effectiveness.

Policy monitoring and evaluation

Monitoring and evaluation are important to holding governments to account for their use of public resources, to improve public policies and to help inform the improvement future policy development and implementation. Policy monitoring in the public sector is the process through which a government actively monitors programme implementation to track progress against policy objectives. Ideally, active monitoring allows governments to correct course when problems arise instead of waiting until the end of a programme when public resources have been fully expended. Systematic evaluation is important at key milestones, and particularly at the end of a programme with a view to checking performance and quality of delivery against policy objectives. Proper monitoring and evaluation mechanisms should be set up during the policy formulation stage.

A challenge in monitoring and evaluation is ensuring that there are clear criteria against which to evaluate the policy or programme, and obtaining the appropriate information to do so. A second challenge is in ensuring that relevant information is taken from monitoring and evaluations to improve performance and quality, and using lessons learned as inputs into future policy formulation and implementation.

A strategic and open state

To ensure that a government's policy process is functioning in an optimal way, this study posits that good governance is operationalised through a strategic and open state. A strategic and open state refers to a government that exhibits the strategic agility and openness required to be proactive and improve responsiveness and effectiveness of public policies while managing tight fiscal pressures. A strategic and open state has the following characteristics (OECD, 2012; 2013).

- **Strategic agility**: This refers to the state's capacity to identify and address internal and external challenges and risks correctly and in a timely manner through enhanced evidence-based decision-making, to strengthen efficiencies in policy design and service delivery to meet these challenges, and to mobilise actors and leverage resources across governments and society to achieve integrated and coherent policy outcomes that address these challenges effectively as it pursues its strategic vision for the country in the long-term. Strategic agility refers to the ability to shift from a reactive to a proactive approach, having foresight to anticipate future issues based on current data and trends, and informing policy decisions with future costs and anticipated changes, including demographic, environmental and economic factors.

- **Institutional robustness:** This refers to the institutional structures and networks that enable the state to achieve coherence in strategy, policy and purpose, without inefficiencies, fragmentation, redundancies or overlaps. It requires adequate systems of co-ordination and checks and balances. This includes a strong Centre of Government, a functioning Parliament and independent external and internal control that collectively, over time, articulate and implement a long term, big-picture strategic vision for the country aimed at sustaining prosperity and well-being for its citizens, the economy and society.

- **Openness:** This refers to the ability and willingness of the state to show how its actions and decisions are consistent with clearly defined and agreed objectives, and to work outward with non-state actors through discussion, partnership and other means in order to advance a shared societal vision. This in turn requires the government to produce reliable and robust information on the objectives, costs and benefits of policies before, during and after implementation. It requires a policy-making process that is embedded with integrity to protect public interest and prevent capture. These efforts can be channelled through a commitment to transparency and accountability.

- **Effective processes:** This refers to the systems and processes, or a machinery of government that the state can leverage to ensure effectiveness, efficiency and economy in its delivery of public outputs and to ultimately achieve its strategic objectives and government-wide vision. These processes rely on evidence-based decision-making, appropriate consultation and feedback mechanisms, effective management of human and financial resources, coherent internal control mechanisms and helpful integrity tools.

Good public governance and trust

Policies that are designed for the benefit of society should be underpinned by fundamental good governance principles in order to ensure they meet their objectives and lead to a well-functioning society. There are a myriad of principles relating to good governance, all of which contribute to good public management. This study considers the principles of rule of law, transparency, integrity effectiveness and efficiency, and accountability as being key to achieving good governance in a strategic and open state:[3]

- **Adherence to the rule of law** means having fair and clear legal frameworks that are enforced impartially.

- **Transparency** means that decisions are taken and enforced in a manner that respects the rule of law and is clear to those who will be affected by such decisions and their enforcement. It also means that relevant public information is accessible at no cost through tools that foster transparency, including effective and efficient on-going communications and robust citizen engagement. These tools can be used to harness feedback, which in turn influences government decision-making meaningfully and on an on-going basis.

- **Integrity** means the adherence to sound ethical values, ensuring the proper use of public resources in line with the public interest.

- **Effectiveness** and **efficiency** mean that institutions use their processes to achieve objectives that meet the needs of society while making the best use of resources at their disposal.

- **Accountability** is the process through which governments are made answerable for their actions by those who are affected by them.

These principles are important to gain and maintain the trust of citizens and other actors who are affected by government action. Trust is borne out of the policy formulation stage and realised in the implementation stage, when citizens judge whether policies were designed with them in mind. When there is distrust, policy horizons are shortened between the system of governance and its citizens, as the policy process focusses on mitigating dissent or crises rather than benefitting from the support that is required to plan for the longer-term. Good governance leads to trust, which legitimises government action in creating a better society. Trust in governments can help with implementing structural reforms that have long-term benefits, and allows and motivates governments to build sustainable solutions to complex economic and social problems.

Open governance

A related and similarly important governance principle is that of openness. Openness is the willingness of governments to demonstrate how their activities align with policy objectives. The public wants evidence that policy objectives are being developed, and programmes delivered, in their best interest. Yet openness is broader than the transparency that citizens are demanding globally, as it also includes the willingness to open the policy-making process to those that have a stake in the process or outcome, or are well-placed to strengthen it.

Openness is most often conceived from the public or stakeholder point of view, referring to the right to information acts and mandatory disclosures, for example. From the public sector point of view, good public openness means that civil society has the ability to (i) request and receive relevant and clear information; (ii) the ability to access services and understandable information; and (iii) the opportunity to participate in decision-making and policy-making processes (OECD, 2005). The way that governments facilitate the latter will depend on the institutional context and the administrative process that accompanies it. Yet there is pressure mounting on governments to limit openness only when necessary, which makes sharing information and the opportunity to contribute a default procedure.

From all perspectives, openness is also a cross-cutting principle that facilitates more inclusive and sustainable policy-making. It is inherently linked to other good governance principles including accountability and transparency, and requires effectiveness and efficiency itself. It also links to the adherence of the rule of law in those countries that are codifying openness principles. Through these inextricable linkages to good governance principles and as an element of a strategic and open state, embodying openness is a way to restore public trust. As discussed, tackling new and complex challenges cannot be the sole endeavour of the Executive, but requires the willingness to undertake a whole-of-government approach.

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1 The full involvement of the SAI of the Netherlands will begin in Phase II of the study.

2 Data on these peer institutions will appear in the following phases of the project. Most data presented in this framework is taken from a previous source and covers only some, but not all, of the peer institutions involved this project.

3 Adapted from various sources including: The World Justice Project's "The Rule of Law Index"; IFAD's "Good governance; an overview"; UNDP's "Governance for Sustainable Human Development" Policy Paper; UNESCAP.

4. SUPREME AUDIT INSTITUTIONS

Before elaborating on the role of SAIs in promoting good governance, a general explanation of SAIs is warranted to ensure a common understanding of their purpose, their standards and fundamental principles and their work. This section provides information on how an SAI operates internally and in relation to its external environment, and provides a scan of the factors that affect the capability of an SAI to fulfil its mandate, to revisit its existing portfolio or to undertake new work.

Introduction to SAIs

A Supreme Audit Institution (SAI), or national audit institution, fulfils the independent and technical public sector *external* audit function that is typically established within a country's constitution or by the supreme law-making body. An SAI is responsible for overseeing and holding government to account for its use of public resources, together with the Legislature and other oversight bodies. In a democratic system, SAIs usually report to the Legislature and in some cases, to the Executive or the head of state (Table 4.1). Where there is more than one body fulfilling the public sector external audit role, the SAI is usually distinguished as possessing the strongest constitutional guarantees of independence (OECD, 2011).

Table 4.1. **Location of supreme audit institutions within government in selected countries**[4]

Legislature	Neither	Executive	Other
Brazil, Costa Rica, Denmark, Mexico, Spain	Chile, Israel, the European Union, Italy, Portugal, South Africa	Korea	Australia

Source: Adapted from "Chile's supreme Audit Institution: Enhancing strategic agility and public trust", OECD, 2014.

SAIs are trusted to provide expertise and credible findings on the use and management of public resources. In order to do this, SAIs require the ability to access all relevant documents, to work on-site and to follow-up with audited entities on their findings (INTOSAI, 1977). In line with their status as independent external bodies, SAIs require full discretion and sufficiently broad mandates (INTOSAI, 2013a), although this differs depending on the SAI country context. An OECD survey of twelve SAIs showed that while all twelve are able to audit their central governments, only eight are able to audit the Legislature and nine are able to audit the judiciary (Table 4.2).

SAIs' guiding principles

In order for an SAI to effectively hold governments accountable for their stewardship of public resources, SAIs must operate on the fundamental principles of independence, transparency and accountability, ethics and quality control (INTOSAI, 2013a; 2013b). An independent and professional SAI should hold itself to the principles that it expects of the public sector entities that it audits, so as to lead by example.

Independence is the cornerstone of a well-functioning SAI, and this should ideally be carved out in the country's constitution with further specifications made in legislation (INTOSAI, 2013b). Functional, operational and financial independence are required to protect SAIs from undue influence in carrying out their work. Equally important is the independence of SAI officials and particularly the heads or collegial members of the institution (INTOSAI, 1977). They should have security of tenure and legal immunity in the normal discharge of their duties (INTOSAI, 2010b).

4 Australia: The Auditor‑General is an independent officer of the Parliament and all audit reports are tabled in the Parliament. The Australian National Audit Office is an agency established by law to assist the Auditor-General to perform his/her functions. Israel: The State Comptroller is accountable only to the Israeli Parliament, the Knesset, and shall not be dependent upon the government; this provision has been interpreted to say that principally the State Comptroller and Ombudsman are not part of any of the above branches, including the Legislature. Korea: The Constitution of the Republic of Korea establishes the Board of Audit and Inspection under the direct jurisdiction of the President (Art. 97); the Board of Audit and Inspection Act states that the Board of Audit and Inspection is established under the President but shall retain an independent status (Art. 2). Portugal: The Court of Accounts is an independent, sovereign court, subject only to the law (1976 Constitution, Arts. 202, 203 and 214; Law 98/97, Art. 24). It is the supreme audit institution in Portugal, with the statute of Supreme Court, with the power to audit all the public resources and also the jurisdictional power to judge financial responsibility.

Table 4.2. - **Audit scope of selected supreme audit institutions**

Country	Legislature	Judiciary	Central government ministries, agencies	Recipients of public funds (e.g. contractors)	Financial public corporations	Non-financial public corporations	Social security	State government budgetary resources	Local government budgetary resources	Armed forces	Loans	Other
Australia	o	o	●	●	●	●	●	o	o	●	●	o
Brazil	●	●	●	●	●	●	●	o	o	●	●	o
Chile	o	o	●	●	●	o	o	x	●	●	●	o
Costa Rica	●	●	●	●	●	●	●	●	●	o	●	●
Denmark	o	o	●	o	●	●	●	●	o	●	●	o
European Court of Auditors	●	●	●	●	●	●	x	x	x	x	●	●
Israel	●	●	●	●	●	●	●	x	●	●	●	●
Italy	o	●	●	●	●	●	●	●	●	●	●	o
Korea	●	●	●	●	●	●	●	x	●	●	●	o
Portugal	●	●	●	●	●	●	●	x	●	●	●	●
Spain	●	●	●	●	●	●	●	●	●	●	●	●
South Africa	●	●	●	o	●	●	●	●	●	●	●	●

Notes: ● = Yes; o = No; x = Not applicable (unitary government); .. = Not available.

European Court of Auditors (ECA): Central government ministries and agencies refer to the European Commission and European Union agencies. The mandate of the ECA is set out in Article 287 of the Treaty on the Functioning of the EU which stipulates that the ECA is responsible for examining the accounts of all revenue and expenditure of the European Union. Israel: Audit of the Legislature and judiciary is only administrative aspects. The State Comptroller Law [Consolidated Version], 1958, which provides a detailed framework for the State Comptroller's Office governance and activity, adds the following audited bodies: *i)* every person or body holding, otherwise than under contract, any state property or managing or controlling any state property on behalf of the state; *ii)* every enterprise, institution, fund or other body in the management of which the government has a share; *iii)* every person, enterprise, institution, fund or other body made subject to audit by law, by decision of the Knesset or by agreement between it and the government; *iv)* every general employees' organisation, and every enterprise, institution, fund or other body in the management of which such employees' organisation has a share, provided that the audit shall not be carried out on their activities as a trade union. No audit of such a body shall be conducted except and insofar as the Comptroller so decides and subject to international conventions to which the state of Israel is party. Note that the application of this section is extremely rare.

Source: Adapted from "Chile's Supreme Audit Institution: Enhancing strategic agility and public trust", OECD, 2014.

It is also vital that SAIs adhere to the highest standards of integrity within the institution – the same standards that it requires of its audited entities. By demonstrating independence, transparency and accountability, ethics and quality control, SAIs strengthen the state through their participation as an accountable actor within it. SAIs can be an example by both requiring the adherence to these principles and by also exposing itself to the same good practice of independent performance and financial auditing and peer review. This establishes the legitimacy that an SAI needs to deliver the credible findings that can be used to hold government to account, and to recommend better practices to public policies and programmes. Public perception of an SAI's conduct with respect to these principles is also important to maintaining or regaining trust and confidence in public financial management.

The OECD's "Recommendation of the Council on Improving Ethical Conduct in the Public Service Including Principles for Managing Ethics in the Public Service" provides twelve guiding principles that fall under the categories of establishing appropriate guidance, management and control (OECD, 1998). These are necessary prerequisites for cultivating an environment that encourages high standards of behaviour. Guidance and management are required to establish guidelines or codes of conduct set from the top that cultivates a professional and fair environment. The independence, powers and responsibilities of an SAI and its officials are also often specified in a code of ethics in addition to specifications being made in the constitution and supporting legislation. Many SAIs usually refer to supranational guidance such as that provided by the International Organisation of Supreme Audit Institutions (INTOSAI) *Code of Ethics* or to International Federation of Accountants (IFAC) *Handbook of the Code of Ethics for Professional Accountants*. Auditors are generally expected to conduct their work with integrity, to be independent, objective and impartial, to exercise professional secrecy and to demonstrate competence to perform their tasks (INTOSAI, 1998). Guidance and management of ethics includes providing appropriate training and education to integrate the values into daily work.

Control of ethics is assured through a legal framework that enforces standards as needed, as well as proper accountability mechanisms (OECD, 1998). While applicable for the entire public sector, compliance with a code of ethics in daily conduct is critical for work that necessitates such high moral integrity and impartiality. For SAIs to be models for the main principles they champion, they are encouraged to make public the outcomes of peer reviews or audits of their institution, including an assessment of their level of compliance with their own codes. The international SAI community, spearheaded by EUROSAI's Task Force for Audit and Ethics, is promoting the relevance of ethical conduct and integrity in SAIs and other public sector entities. To integrate these principles into daily work, SAIs can lead by example. They could also use their audit work to assess the integration of ethics into other entities' organisational culture. To this end, the EUROSAI Task Force has suggested criteria for assessing compliance with codes of conduct.[5]

The SAI community

SAIs are supported by a strong network of SAIs and related organisations. The largest of these is the International Organization of Supreme Audit Institutions (INTOSAI), which is an umbrella organisation for external public sector auditors with a current membership of 192 SAIs and 5 observers, founded in 1953. INTOSAI endorses a series of International Standards of SAIs (ISSAI), which form a collection of professional standards and good practice guidelines for public sector auditors, including on general, field and reporting auditing standards. In addition, INTOSAI issues guidance for good governance on internal control and accounting.[6]

INTOSAI also has a seat on the International Auditing Assurance Standards Board (IAASB) covering both public and private sectors. The ISSAIs are based on the IAASB's International Standards of Audit. INTOSAI collaborates with the United Nations through a co-ordinated annual Symposium, covering widely relevant topics including SAIs and good governance.

Another institution that provides guidance related to financial audits is the International Federation of Accountants (IFAC). It is a global organization representing the accountancy profession covering public sector reporting and transparency, and the adoption of international reporting and professional standards, through its public sector accounting branch (IPSAS). In partnership with the Chartered Institute of Public Finance and Accountancy (CIPFA), IFAC also helps to foster good governance in the public sector through the establishment of governance principles and benchmarks.

The efforts of the SAI community are reflected in international fora, with the United Nations' General Assembly Resolution Act (66/209), encouraging its members and institutions "to continue and to intensify their cooperation, including in capacity-building, with the International Organization of Supreme Audit Institutions in order to promote good governance by ensuring efficiency, accountability, effectiveness and transparency through strengthened supreme audit institutions" (UN, 2011).

The international community for SAIs is strong, with large membership to INTOSAI and its regional bodies and committees. The content on which INTOSAI focuses is also indicative of the collegial efforts that SAIs are making to strengthen their capacities and ability to support good governance. Notably, the "Beijing Declaration on Promotion of Good Governance by Supreme Audit Institutions" outlines many principles that are aligned with the spirit of this paper. While it is beyond the scope of this study, the Beijing Declaration importantly covers the need for SAIs to support good governance at the supranational level, recognising that no country can improve its own governance in isolation in this interconnected world (INTOSAI, 2013c).

The types of SAIs

An SAI's structure typically falls into one of following three models (DFID, 2004):

- The **Westminster model**, otherwise known as the Anglo-Saxon or Parliamentary model, is one in which an SAI audits the implementation of expenditure authorised by the Legislature. The SAI reports audit findings and submits annual financial reports back to the Legislature, although it is not a part of the Legislature. The SAI cannot impose recommendations directly on the Executive, but works through a dedicated legislative committee, often called the Public Accounts Committee. This model is directed by a single head, usually called the Auditor General.

- The **Collegiate or Board model** in which the SAI resides within the Parliamentary system, is led by multiple members who form a college or board to make consensus-based decisions. It operates with independence and reports to a Parliamentary committee that is charged with acting upon its findings. The board is headed by a chairperson, similar to the Auditor General of the Westminster model.

- The **Court or Jurisdictional** model is one in which the SAI is usually associated with the judicial system and has the jurisdictional power to convict public accountants for improper acts when performing their duties, to suggest or impose recommendations upon audited entities and sometimes to penalise public officials. The SAI is led by a president and is staffed by judges. It can present the end of year state account to the Legislature and citizens, or an annual report of its findings. Depending on its findings, Executive officials can be held personally liable for incorrect expenditures.

While the distinctions of each model can be useful for academic and didactic purposes, these differences are not necessarily meaningful in discussing the role SAIs can play in relation to fostering good governance, for two main reasons. First, there are differences between SAIs that share the same model in theory (Champomier and Lins Dutra, 2013). Not all Court of Accounts/Audits are part of the judicial system. The Brazilian Federal Court of Accounts (TCU), for instance, follows a Court of Accounts model and has juridical powers to judge and punish those it finds guilty of misconduct (Table 4.3). However, it is established as an independent and auxiliary body to the National Congress, not the judiciary, under Brazil's Constitution.

Table 4.3. **Existence of judicial powers of selected supreme audit institutions**

Yes	No
Brazil, Chile, Costa Rica, Italy, Portugal, Spain	Australia, Denmark, European Court of Auditors, Israel, Korea, Mexico, Peru, South Africa

Source: Adapted from "Chile's supreme Audit Institution: Enhancing strategic agility and public trust", OECD, 2014.

Second, there are similarities that exist within SAIs across models. A mapping conducted by INTOSAI Professional Standards Committee of 37 SAIs across all regions sought to understand whether a common language could be established for SAIs across mandates, respective national contexts and SAI models (INTOSAI, 2010a). The mapping found that there exist more similarities than differences among SAI characteristics and thus that a common language could be used to describe an SAI's functions. INTOSAI regional representatives involved in the mapping found it more useful to have recommendations or standards classified by audit assignments, rather than audit institution models. Regional representatives further found that the variety of tasks for an SAI can be described through a limited set of concepts. The mapping found that making a few key distinctions regarding objectives and scopes of audits was sufficient to cover the variety of audit assignments around the world.

In view of the difficulty in categorising SAIs under one of the three models and the usefulness of differentiating between audit work, rather than audit institution models, this study focuses on how SAI work, irrespective of an SAI's model, can better support good governance.

The work of SAIs

Types of tasks, audits and other engagements

Generally, SAIs are empowered to conduct work in accordance with a self-determined programme within their mandates. They often have prioritisation processes to ensure the relevance of their audit work, which can take risk and materiality assessments into account. However, some SAI work can be requested or required from external sources. The impetus for SAI work can be categorised as follows (INTOSAI, 2010a):

- Fixed tasks are audits that are required for a prescribed entity at specified time intervals
- Discretionary tasks are audits that the SAI initiates at its own discretion
- Requested tasks are audits that SAIs are obliged to conduct upon request
- Negotiated tasks are audits that SAIs are engaged to conduct upon contract

SAIs can be mandated to undertake a variety of audit assignments that are related to the responsibilities and management of public resources. These include audits related to (INTOSAI, 2010a):

- Compliance with norms and performance of the use of public monies, resources, or assets, by a recipient or beneficiary;
- Oversight of the proper collection of revenues owed to the government or public entities;
- Legality and regularity of government or public entities accounts;
- Quality of financial management and reporting; and
- Effectiveness, efficiency, and economy of government or public entities' operations.

INTOSAI's Lima Declaration makes a distinction between pre-audit and post-audit, also known as *ex-ante* audit and *ex-post* audit respectively. Simply put, pre-audit is a review that occurs before administrative or financial activities take place, in order to approve their execution. Post-audit is a retrospective review of activities, and is an indispensable requirement for an SAI to be able to fulfil its tasks, as listed above.

Pre-audits are not always carried out by SAIs, but rather by other bodies depending on the legal context. When pre-audits are done effectively, they can be a helpful part of good public financial management in that they can detect damage in advance. However, they can create an excessive amount of work and confuse responsibilities under law (INTOSAI, 1977). Over the last 20 years, SAIs have been moving away from conducting pre-audit assignments (Ruffner and Sevilla, 2004), a trend that is also reflected in internal auditing. It is interesting to note that SAIs are still engaging in the pre-audit *stage* of a policy or programme through the provision of advice or counselling, but this is different from being responsible for the approval of its execution.

For any given audit assignment, SAIs gather evidence to evaluate a targeted subject against a set of criteria and to then express a conclusion about the outcome. Auditors apply different criteria depending on the type of audit work being undertaken. There are three main types of audit work, which INTOSAI (2013a) explains:[7]

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

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

3. **Compliance audits** focus on whether a particular subject matter is in compliance with authorities identified as criteria. Compliance auditing is performed by assessing whether activities, financial transactions and information are, in all material respects, in compliance with the authorities which govern the audited entity. These authorities may include rules, laws and regulations, budgetary resolutions, policy, established codes, agreed terms or the general

principles governing sound public-sector financial management and the conduct of public officials.

SAIs are increasingly undertaking tasks that further enhance the effectiveness, efficiency and economy of public sector programmes and policies. They are gathering new pieces of information by refocussing the audit criteria, packaging those findings in new and useful ways. They may conduct **combined audits** incorporating aspects of financial, performance and/or compliance audits. Some SAIs are also undertaking **programme evaluations**. While classified as a performance audit by certain institutions, INTOSAI's working group on Program Evaluation reasons that it is in fact a related, but separate, extension of a performance audit.[8] Regardless of the classification, programme evaluations seek to provide explanations for successes and failures of policies or programmes based on objectives and implementation (INTOSAI, 2010c).

SAIs are synthesising an expanding base of information in new ways, allowing them to provide non-traditional value-add audit work. They are providing not only oversight, but also insight and foresight services. SAIs provide **oversight** to ensure that policy is implemented as intended, strategies are met, and the overall performance of the government meets expectations and needs within policy laws and regulations.

SAIs provide **insight** to assist audited entities and other decision-makers by assessing which programmes and policies are working and which are not, providing feedback to adjust policies and by sharing best practices information.

Some SAIs are providing **foresight** through assessments that are oriented towards identifying risks and opportunities in the long term. Specifically, risk-based auditing focusses on the government's overall risk management framework and provides useful and relevant information about the audited entities, policies or programmes, to help governments manage risks to meet their objectives. An important element foresight is that SAIs also help government look forward by identifying trends and bringing attention to emerging challenges before risks materialise. Foresight is inherently linked to both insight and oversight, but few SAIs are known to offer this type of analysis at present.

SAIs may provide **counselling** or **advice** to the Executive or legislative bodies, often at their request. It is important to note that SAIs can audit policy implementation by government and public entities, but they do not audit the soundness of a policy decision unless specifically instructed to do so by the Legislature (INTOSAI, 2010b). At present, SAIs do not assess *why* a policy is established, but rather may assess *how*, as does the French SAI in its policy evaluation work.

Issuing **good practice guidance** to the Executive is also a proactive measure to enable smoother external audits and encourage coherence in practices across government ministries. The Australian SAI publishes numerous better practice guides on topics ranging from preparing financial statements to implementation of programme and policy objectives. The SAIs of Korea and Italy similarly issue good practice guides to the Executive. And in Costa Rica, its SAI is legally tasked with issuing guidelines and directives regarding audit and control.

Some SAIs can also undertake judicial reviews or **investigations** into the use of public resources when the public interest is at stake (INTOSAI, 2013b). Some are conducting assessments of irregularities to target financial impropriety, fraud and corruption that hinder a government's ability to provide policies for the benefit of citizens. Further tasks include conducting elections audits, public procurement audits and forensic audits in relation to corruption and fraud investigations.

In addition to requested tasks from the Legislature or the Executive, SAIs may receive and **investigate complaints** from citizens or civil society organisations. Some are requested to investigate a claim where damages have been caused by the public service or a public official, to public patrimony or private interests in order to evaluate the amount of finances to be repatriated.

Reporting on findings

SAIs usually report their findings, and related conclusions and recommendations, to Legislatures in a published format, sometimes accompanied by an oral presentation. SAIs also aim to inform citizens by making findings and information about their institution available to the public.

INTOSAI states that audited entities should comment on their audit findings within a period of time that is established by law, indicating what measures will be taken as a result of the findings. The follow-up procedures for all SAI findings, however, are dependent on its model and structure with respect to other actors, and the capabilities of those actors. Thus, tracking implementation of measures indicated in response to audit conclusions or recommendations can be fragmented and difficult.

Conclusions drawn from financial audits express assurance to indicate the degree of confidence in the findings, and are expressed in a statement of a standardised format with a qualified or unqualified opinion (INTOSAI, 2010a). Assurance of financial audits can be expressed with explicit reference to a level of "reasonable assurance" or "limited assurance", but not absolute assurance. Alternately, SAIs can provide assurance without explicitly stating but instead objectively explaining how the findings, criteria and conclusions were developed (INTOSAI, 2013a). Recommendations that are issued at the end of compliance and performance audits are not imposed on the audited entity. Giving teeth to recommendations can be politically challenging, particularly when an SAI reports to the Executive (Ramkumar et. al, 2009).

Officials or judges of the Court or Jurisdictional model can impose penalties or sanctions when irregularities are detected about audited officials, including public accountants. Usually, under this model, a year-end report is presented to the Legislature that then relies on this report to grant a "discharge" of responsibility to the government for the year if it is satisfied with the way the government managed its funds. SAIs also report specifically on important events during the year, covering all audit activities in its annual report. Reports are factual and present an objective and clear assessment of the SAI's activities.

In other cases, the Legislature or legislative committees, such as Public Accounts Committees, are typically responsible for reviewing and issuing a report to which the Executive must respond. While committees are endowed with the rights to follow up on audits, their effectiveness in doing so depends on their own capacity (Ramkumar et. al, 2009).

In light of pressures from citizens for governments to demonstrate more accountability and integrity, SAI recommendations that stem from the findings of audit tasks are gaining weight. In response to these pressures, some SAIs are becoming more involved in the follow-up of their recommendations. The Australian SAI has recently produced a performance audit on the arrangements for implementing and monitoring the implementation of its past recommendations at the ministry level. The recommendations stemming from this follow-up audit were provided with a response from the relevant ministry, and the audit report was made available online.[9]

Ensuring that audit work has meaning includes raising the awareness of the role of SAIs, and the importance, objectives and scope of their audit work. SAIs are taking proactive steps to engage citizens by promoting and sharing this information through social media outlets. Additionally, the media can play an important role in raising awareness about the role and work of an SAI, effectively promoting SAIs. Where citizens understand the salience of audit work, sharing information, particularly on the effectiveness, efficiency and economy of policies and programmes that directly affect citizens, could go a long way in piquing their interest. Communication strategies help to ensure that the wealth of knowledge SAIs produce is presented in a clear and useful manner, and that it does not go unnoticed.

In line with principles of transparency and openness, and their mission to serve citizens, SAIs empower citizens with the information that they need to hold their government to account, thereby strengthening the accountability chain and giving more teeth to audit findings. While covering this aspect of SAI work in detail is outside of the scope of this project, there is growing literature on the importance of and options for SAI engagement with civil society that can and should be appealed to.[10]

Capability and catalysts for impact

The degree to which an SAI can support good governance depends on its mandate, and its ability to reassess the variety of its tasks and undertake new tasks. An SAI's ability to make changes in line with institutional goals or external needs depends on (i) its skill in navigating its external environment to ensure impact and (ii) its institutional capacity. These skills and capacities can also help to increase the awareness of the importance and usefulness of audit work, and to strengthen follow up of recommendations.

Navigating the external environment

SAIs do not operate in isolation, but rather are part of a complex web of a state's accountability framework. For this reason in looking at options to reassess its portfolio of work, an SAI not only needs to consider its mandate, but also needs to be cognizant of its role in relation to other actors, such as anti-corruption authorities, investigative agencies and oversight bodies.

An SAI's effectiveness is enhanced when it co-ordinates with the actors with whom it shares the responsibility of overseeing government accountability, while respecting constitutionally established roles. The importance of maintaining its independence while navigating the external environment cannot be overstated. SAIs require a strong legal framework and the institutional capacity (professional and organisational) in order to protect its independence, regardless of the SAI model to ensure objectivity and credibility of its findings, which is necessary for reporting to the Legislature.

However, whether SAIs are accountable to the Executive or to Parliament, protecting independence can be politically challenging (Ramkumar et. al, 2009). In the same vein, following up on recommendations can be politically challenging. In particular, where SAIs are accountable to the Executive, and not to Parliament, independence of SAIs and of their findings can come into question, diminishing the validity and credibility of their work. In these situations the Executive has power to influence directly what gets audited and reported, and to indirectly control the scope of the SAI's work (Ramkumar et. al, 2009).

Understanding an SAI's relationship with the Legislature, a key component of public scrutiny, is important to providing coherent oversight. For example, the International Budget Partnership's 2012 Open Budget Survey found that countries with weaker SAIs also showed greater weaknesses in budget transparency and legislative oversight of budgets (IBP, 2012).

The existence of other actors, either within or outside of the Legislature, may determine the mandate of an SAI or the scope of work that an SAI undertakes. At the national government level, an SAI may interact with ad hoc Parliamentary committees including Parliamentary accounts committees, finance commissions, audit commissions and investigative commissions. Until 2003, the SAI of Sweden was under the Executive branch, with a small audit organisation under the Parliament (TI, 2012). Recent reforms have further established the Parliamentary Council to enhance co-operation between the Swedish SAI and

Parliament. In Finland, the creation of the Parliamentary Public Accounts Committee was seen as a major step forward in terms of creating a platform to discuss the issues that SAIs' work identified and to develop possible responses (OECD, 2010).

In addition to Parliament and public entities, INTOSAI's *Building Capacity in Supreme Audit Institutions: A Guide* (2007) takes it a step further to suggest that SAIs should, within mandates and while maintaining independence, forge ties with a wide range of entities including press and civil society organisations.

In considering how to maximise the impact of their work, SAIs should take into account various stakeholders' work that may complement, or duplicate, the work of the SAI. Where well-functioning bodies exist, SAIs may be able to co-ordinate so that efforts are complementary. This could include co-ordinating to find an effective means of strengthening audit recommendations, and ensuring follow-up to the responses of audited entities to audit findings. Other bodies to co-ordinate with could include: internal control and internal audit units; institutions that issue opinions and data on economic and social trends including statistics agencies; institutions including ministries of finance or public treasuries that deal with the management of public funds; holders of public accounts and appointing public accountants; and private external auditors.

Institutional Capacity

Efforts to modernise, address current policy challenges and support good governance rely on institutional capacity. An SAI needs to consider enablers that can facilitate transitions: leadership, human resource management (including professionalisation) and effective budgeting (INTOSAI, 2007).

Leadership

An SAI's strategic direction and willingness to embrace institutional-wide change is set from the top. Strong leadership is key to effect internal change as well as for external audiences accepting an SAI's evolution. Thus an SAI's auditor general, chairperson/board or president is required to provide strategic direction and ensure that a clear rationale is presented internally and externally for any changes to an SAI's remit, including addressing issues of the SAI's mandate. This includes providing a value-added rationale and explaining how the changes contribute to filling gaps and enhancing good governance.

Given the influential role held by the head of an SAI both internally and increasingly externally, leadership should be independent and free from conflicts of interest. The independence of leadership can be enforced through organisational mechanisms that ensure leadership is appointed based on sound selection criteria. In a survey of twelve SAIs, the OECD found that all but two establish incompatibilities of a leader's appointment to office. Incompatibilities of office include membership in a political party union, or employment in the public sector (Table 4.4).

Leadership can exercise more effective scrutiny when they are safeguarded against undue influence or removal from office. In the same OECD survey of twelve SAIs, legislation was established in eleven countries to provide clear criteria for a leader's removal from office. However, it is interesting to note that there are only two cases reported in which the leader of an SAI was actually removed from office (Table 4.5).

Table 4.4. **Organisational independence of supreme audit institutions' leadership in selected countries**

		Selection criteria							Incompatibilities of office					
Country	**Position**	**Legislation defines qualifications**	**Education qualification**	**Professional qualifications**	**Character qualifications**	**Experience**	**Age**	**Other**	**Legislation defines incompatibilities**	**Membership in a political party**	**Membership in a union**	**Employment in the public sector**	**Professional activities**	**Other**
Australia	Auditor-General	No	o	o	o	o	o	o	Yes	o	o	o	o	●
Brazil	9 ministers, one of whom is elected internally as president	Yes	o	o	●	●	●	o	Yes	●	o	●	●	●
Chile	Comptroller General	Yes	o	●	o	●	●	o	No	o	o	o	o	o
Costa Rica	Comptroller General	Yes	o	o	●	o	●	●	Yes	●	o	●	●	●
Denmark	Auditor-General	No	o	o	o	o	o	o	Yes	o	o	●	o	o
European Court of Auditors	28 members, one of whom is elected internally as president	Yes	o	●	●	●	o	o	Yes	o	●	●	●	●
Israel	State Comptroller	Yes	o	o	o	o	o	●	Yes	●	●	●	●	o
Italy	President	Yes	o	●	o	●	o	o	No	o	o	o	o	o
Korea	Commissioners, including chair	Yes	o	●	o	●	●	o	Yes	●	o	●	●	o
Peru	Comptroller General	Yes	●	●	o	●	●	o	..	..	..	..	..	..
Portugal	President	No	o	o	o	o	o	●	Yes	●	●	●	o	o
	Members of Court	Yes	●	●	●	●	●	o	Yes	●	●	●	o	o
South Africa	Auditor-General	Yes	o	o	●	●	o	●	Yes	●	o	●	●	●
Spain	12 members, one of whom is elected internally as president	Yes	●	●	o	●	o	o	Yes	o	o	●	●	●

Notes: ● = Yes; o = No; x = Not applicable; .. = Missing data.

Source: Adapted from "Chile's Supreme Audit Institution: Enhancing strategic agility and public trust", OECD, 2014.

Table 4.5. **Safeguards for the removal of supreme audit leadership in selected countries**

Country	Head of organisation	Legislation provides criteria for removal from office	By which authority?				Reasons for removal?						Has the leadership ever been removed?
			Legislature	Executive	Judiciary	Other	Loss of confidence	Incapacitation – health	Misconduct	Absence	Bankruptcy	Other	
Australia	Auditor-General	Yes	o	o	o	●	o	●	●	o	●	●	No
Brazil	9 ministers, one of whom is elected internally as president	Yes	●	o	o	o	o	o	●	o	o	o	No
Chile	Comptroller General	Yes	●	o	●	o	o	●	o	o	o	●	Yes (1945)
Costa Rica	Comptroller General	Yes	●	o	o	o	o	o	●	o	o	o	Yes (2004)
Denmark	Auditor-General	No	o	o	o	o	o	o	o	o	o	o	No
European Court of Auditors	28 members, one of whom is elected internally as president	Yes	o	o	●	o	o	o	o	o	o	●	No
Israel	State Comptroller	Yes	●	o	o	o	o	●	●	o	o	o	No
Italy	President	No	o	o	o	o	o	o	o	o	o	o	No
Korea	Commissioners, including chair	Yes	●	●	●	o	●	●	●	o	o	o	No
Mexico	Superior-Auditor	..	..	..	..	..	..	..	..	..	..	..	..
Peru	Comptroller General	..	..	..	..	..	..	..	..	..	..	..	...
Portugal	Members of Court, including President	Yes	o	o	o	o	o o	o ●	●●	●●	o o	o o	No
South Africa	Auditor-General	Yes	●	o	o	o	o	●	●	o	o	o	No
Spain	12 members, one of whom is elected internally as president	Yes	●	..	●	●	o	●	●	●	o	o	No

Notes: ● = Yes; o = No; x = Not applicable; .. = Missing data.

Source: Adapted from "Chile's Supreme Audit Institution: Enhancing strategic agility and public trust", OECD, 2014Human Resource Management

Human resource management is key for an SAI given that technical skill, knowledge and sound professional judgement are required to carry out its work. This applies particularly when implementing change within the organisation.

Multi-year workforce planning can help an SAI to ensure that it has adequate human capital to support the implementation of its mission, vision and strategic goals, as well as to respond to internal changes and those within the public administration. Successful management of human resources includes strategic workforce planning, attention to workforce competencies and the use of traditional tools such as recruitment, compensation and career development (OECD, 2014). Multi-year workforce planning has already been introduced as a formal and regular instrument in the SAIs of some countries including Australia and Brazil and as an *ad hoc* instrument in South Africa (Table 4.6). By using planning to identify the knowledge, skills and competencies needed, SAIs can begin to determine the gaps in recruitment and training that need to be addressed for change.

Table 4.6. **Multi-year workforce planning in supreme audit institutions**

Country	Is forward-looking planning in place to ensure that the supreme audit institution has an adequate workforce to deliver its mission and achieve its vision?			How many years are covered by the supreme audit institution's workforce planning?	What are the key aspects explicitly considered by the supreme audit institution when conducting workforce planning?
	Formal and regular	*Ad hoc*	None		
Australia	●			2-3 years	People-related investment choices and associated strategies
Brazil	●			4-5 years	Change in audit standards, efficiency savings
Chile			●	x	x
Costa Rica	●			..	Changes in institutional mandate, changes in audit standards, possible efficiency savings
Denmark	●			2-3 years	Efficiency savings, reorganisation
European Court of Auditors	●			2-3 years	Possibilities for outsourcing, efficiency savings, staffing needs and turnover
Israel		●		2-3 years	Possibilities for outsourcing in the case of information and communication technology services only
Italy			●	x	x
Korea		●		4-5 years	Change of auditees, that is, the operation, personnel, mission, work of the auditees; change of society, public administration and people's expectations
Portugal	●			2-3 years	Possibilities for outsourcing, efficiency savings (e.g. e-government)
South Africa		●		4-5 years	Changes in institutional mandate; changes in audit standards; possibilities for outsourcing; availability of skills
Spain	●			3-5 years	Staff turnover, changes in public administration (and impact on audit work)

Notes: x = Not applicable; .. = Missing data.
Source: Adapted from "Chile's Supreme Audit Institution: Enhancing strategic agility and public trust", OECD, 2014.

Multi-year workforce planning includes attracting and retaining capable employees who exhibit the competencies necessary to respond to current and emerging demands, which in turn supports an SAI's ability to competently do its work of supporting good governance over the long term. This move towards professionalization of an SAI's workforce has taken place or continues in some SAIs, and is required in others. The SAI of the United States, for example, has greatly restructured the scope of its audit function over the last sixty years, which necessitated a restructuring of its workforce. As it focussed its work more and more on auditing the performance and efficiency of programmes, it systematically reduced the number of non-experts and accountants in favour of hiring more subject-matter experts.

Effective budgeting

Additionally, an SAI can more readily address resource changes when it has the ability to reallocate its financial resources in line with its institutional needs or directions. This ability varies within country contexts but is key to enabling organisational change. The SAI of Chile, for example, has much budget flexibility and receives lump sum appropriations for personnel expenditure and materials, consumables and goods expenditures. However, there is relatively less flexibility for investment expenditure such as in information and communications technology, similar to the SAI of Denmark (Table 4.7).

Table 4.7. **Budget flexibility of selected supreme audit institutions**

Country	A. How is the budget for the supreme audit institution prepared?			C. "Lump sum" appropriations	D. Flexibility to vire (i.e. reallocate) funds between expenditure categories
	Same policies, procedures as other public entities	Included in draft state budget without change	Sent directly to Legislature for approval		
Australia	●			For personnel, materials and capital	Yes, without any limit and without Executive/legislative approval
Brazil		●		For personnel, materials and capital	Not possible without *ex-ante* legislative approval
Chile	●			For personnel, materials and capital	Yes, without any limit and without Executive/legislative approval
Costa Rica	●			No	Flexibility to make internal modifications without Executive/legislative approval
Denmark			●	For personnel and materials only	Flexibility to allocate between operating, capital expenditure without Executive/legislative approval
European Court of Auditors	●			No	Yes, up to certain threshold with *ex-ante* legislative approval
Israel			●	For personnel, materials and capital	Yes without any limit, and without Executive/legislative approval
Italy				For personnel, materials and capital	Yes
Korea				No	Yes up to certain threshold
Mexico		●		..	..
Peru	●			For capital	Yes, up to a certain threshold
Portugal	●			For personnel, materials and capital	Yes without any limit, and without Executive/ legislative approval
South Africa	x	x	x	..	Yes without any limit, and without Executive/legislative approval
Spain	●			For personnel, materials and capital	Yes up to certain threshold

Notes: ● = Yes; o = No; x = Not applicable; .. = Missing data. Block/lump sum appropriations involve allocating a lump sum to line ministries or agencies, which are then free to determine the best mix of economic inputs to produce their services.

Source: OECD (n.d.), *International Budget Practices and Procedures Database* (v2), www.oecd.org/gov/budget/database, responses to Q. 30: "In practice, which option most accurately describes the way in which the budget is prepared for the supreme audit institution?" and adapted from unpublished OECD Survey of Benchmark Supreme Audit Institutions 2013, responses to Q. 20.

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5 As reported by the EUROSAI Task Force of Audit and Ethics (TFA&E), assessment criteria for compliance are found in the appendix to ISSAI 5600 on peer review guidelines, and in the drafts of Performance Measurement Framework and of the ISSAI Compliance Assessment Tools (iCATS). See also EUROSAI's "Auditing Ethics in the Public Sector", available on their website http://www.eurosai-tfae.tcontas.pt/DOCUMENTS1/default.aspx.

6 INTOSAI (http://www.intosai.org) and ISSAI (http://www.issai.org/)

7 INTOSAI covers the three branches of auditing in "Fundamental Principles of Public Sector Auditing" (ISSAI 100), which are individually elaborated upon in "Fundamental Principles of Financial Auditing" (ISSAI 200), "Fundamental Principles of Performance Auditing" (ISSAI 300), and "Fundamental Principles of Compliance Auditing" (ISSAI 400).

8 More information about the INTOSAI Working Group on Program Evaluation is available at: http://www.intosai.org/committeesworking-groupstask-forces/goal-3-knowledge-sharing/working-group-on-programme-evaluation.html and at the Website of its Chair, the French Cour des Comptes, http://program-evaluation.ccomptes.fr/index.php.

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PART II

PHASE I: THE ANALYTICAL FRAMEWORK

5. THE ROLE OF AN SAI IN GOOD GOVERNANCE

Trust is an enabler of good public management as it gives governments space to establish longer-term policy goals and to develop and deliver programmes and services that meet those goals. Trust by citizens in their government is determined by their perception and the reality of how well policies, programmes and services meet their needs. Thus it is driven by the way policy-makers comply with standards that ensure their behaviour is in the interest of citizens (OECD, 2013). Citizens must trust that governments will develop the right policies to deliver effective programmes in order to address long-term and complex policy issues. Yet, in many countries, confidence in government has declined. This increases enforcement costs and reduces the policy horizon. Regaining trust requires a whole-of-government approach, as the financial crisis demonstrated that the Executive cannot tackle pervasive 21st century challenges alone.

There are many public institutions that have or should play an important role in regaining trust and, thus, in being part of the collective action towards good governance. SAIs have a strong role to play. Through their most basic function of auditing the expenditure of public funds, SAIs help to ensure transparency and reliability of government financial management. Increasingly, SAI audit work is assessing the transparency and reliability of information related to policy and programme performance too.

In a study of 27 European countries, SAIs ranked higher with respect to integrity in law and in practice compared to other watchdog institutions including Ombudsman Offices and Electoral Management Bodies (TI, 2012). This study was conducted by an international watchdog organisation and provides evidence that the role of SAIs and the principles of good governance have been elevated beyond national borders. Discussion of SAIs and their role in good governance have been the focus of the international SAI community. INTOSAI's most recent ISSAI (12) focusses on the value and benefits of external audit for citizens. Also, the Report on the 19th UN/INTOSAI Symposium on Government Audit (2007) stated that the value of SAIs stems from promoting good governance now and in the future.

A whole-of-government approach is needed to restore trust in government, and to address complex policy challenges through better policy formulation, implementation and evaluation. Given that, within the whole-of-government, SAIs are widely perceived as credible and independent verifiers of information, governments should be considering how SAIs audit and counselling work can be better used as inputs to a more effective, efficient and economical policy process. This analytical framework aims to provide suggestions on how this could be done.

Supporting good governance broadly

SAIs are by definition contributing to good public governance by holding public bodies to account for their management of public resources. When SAI work is underpinned by fundamental principles, particularly independence, it contributes to good governance directly by providing the intended users with independent, objective and reliable information based on sufficient and appropriate evidence. While the focus of the study is to better understand how this work can be targeted to support good governance more effectively, there are many avenues through which SAIs support good governance, as outlined in INTOSAI's 2013 Beijing Declaration (INTOSAI, 2013c):

- enhancing accountability and transparency, encouraging continuous improvement and sustained confidence in the appropriate use of public funds and assets and the performance of public administration;

- reinforcing the effectiveness and efficiency of those bodies within the constitutional arrangement that exercise general monitoring and corrective functions over government, and those responsible for the management of publicly funded activities;

- creating incentives for change by providing knowledge, comprehensive analysis and well-founded recommendations for improvement;

- promoting democracy, the rule of law and maintenance of order, and promoting the improvement of people's livelihoods by ensuring that public funds achieve their desired impact; and

- playing a role in detecting and deterring fraud, combating corruption and safeguarding national interests through identifying risks to the economy and society.

SAIs can foster good governance by enhancing transparency, ensuring accountability, and promoting performance through their financial, compliance and performance audit work. Against this backdrop, a great emphasis has been placed on performance auditing, which is often broad in scope and has empowered SAIs to review the effectiveness, efficiency and economy of government or public entities' operations. Closely related is programme evaluation, which is often conceived as an extension of performance audit. In a few instances, SAIs have gone further to check the equitability, ethics or impact of programmes or policies on the environment. This performance-related audit work of SAIs is a critical link in the chain of public sector accountability and good governance insofar as it can provide reliable and robust reports that those able to directly influence government decisions have sufficient information upon which to base their actions (OECD, 2007).

SAIs can also foster good governance through their contribution to the openness of a state by continuing the practice of making clear and useful information available on the institutions and processes that form the state, including on its own institution. SAIs could also assess the openness of the state – namely the ability for citizens to receive relevant information, to obtain services and undertake transactions, and to participate in decision-making and policy-making processes (OECD, 2005). Internationally established principles on the good governance of key activities can provide evidence of the cross-cutting nature of openness. The *draft OECD Principles of Budgetary Governance* (2014) suggest that budget documents should be open, transparent and accessible, and that the budget process should be inclusive, participatory and realistic. The *2012 Recommendation of the OECD Council on Regulatory Policy and Governance* includes a recommendation on adhering to principles of open government, transparency and participation in the regulatory process with an eye to ensuring regulations serve the public interest and are based on legitimate needs. International guidelines can be explored by SAIs interested in establishing criteria for assessing how well a state is performing on the important principles of openness.

Independent and professional SAIs are often considered an important player in the fight against fraud and corruption, in light of their critical role in ensuring transparency and compliance of public resource expenditure. In addition to contributing to public sector integrity through fulfilment of their basic function, some SAIs have a role in national anti-corruption strategies, developing and maintaining officials' private interest disclosures and in auditing political financing (Tables 5.1, 5.2, 5.3).

Table 5.1 **- Selected SAIs playing a formal role in national anti-corruption strategies**

Yes	No
Brazil, Chile, Costa Rica, European Court of Auditors, Italy, South Africa	Australia, Denmark, Israel, Korea, Portugal, Spain

Source: "Chile's Supreme Audit Institution: Enhancing strategic agility and public trust", OECD 2014.

Table 5.2 **- Role of SAIs in the development and maintenance of public officials' private interest (income and asset) disclosures in selected countries**

Yes	No
Chile, Costa Rica, Israel	Australia, Brazil, Denmark, European Court of Auditors, Italy, Korea, Portugal, South Africa, Spain

Source: "Chile's Supreme Audit Institution: Enhancing strategic agility and public trust", OECD 2014.

Table 5.3 **- Role of SAIs in auditing political financing in selected countries**

Yes	No
Denmark, Israel, Italy, South Africa, Spain	Australia, Brazil, Chile, Costa Rica, European Court of Auditors, Peru, Portugal

Source: "Chile's Supreme Audit Institution: Enhancing strategic agility and public trust", OECD 2014.

Supporting good governance at the 3 policy stages

SAIs are increasingly undertaking tasks that further enhance the effectiveness, efficiency and economy of public sector programmes and policies through performance audits, a combination of financial, performance or compliance audits and/or increasingly through programme evaluations.

Some SAIs are providing oversight, insight and foresight services as inputs to the policy process. Oversight ensures that policy is implemented as intended, strategies are met, and the overall performance of the government meets expectations and needs within policy, laws and regulations. Insight is provided to assist audited entities and other decision-makers by assessing which programmes and policies are working. This involves providing feedback to adjust policies and sharing good practices information. SAIs also provide audited entities with assistance in foresight, by identifying trends and bringing attention to emerging challenges before they become risks. Given that policy formulation relies on foresight to ensure policy development adequately addresses public needs and policy goals, these oversight, insight and foresight services are important to bolstering the policy process (NAO Mauritius, 2008).

From this perspective, there are some examples of audits by different SAIs that can inform the policy-making process, particularly during programme design, implementation and evaluation. The UK's SAI, for instance, has conducted several audits on impact assessment procedures and efforts to reduce administrative burden. The European Union's SAI has done an audit on the impact assessment procedure as well. And the Netherlands' SAI has been active in audits on administrative burden reduction programmes. Several SAIs have conducted audits on the implementation of EU directives.[11]

Another interesting example may be found in the field of sustainable development. According to INTOSAI: "while it may be difficult to audit the government's strategy against any firm audit criteria, it may well be possible to examine the success with which government bodies are integrating a sustainable development approach to their day-to-day decision making. Working alongside government bodies, and looking at comparisons on the international stage and other large organizations, the SAI may help strategic decision-makers within government to identify and disseminate examples of best practice" (INTOSAI, 2004).

Accordingly, although most SAIs focus their audits on policy implementation, SAIs may look at "how" strategies and policies are set without encroaching on "why". In the case of the French SAI, this falls under its "policy evaluation" area of work, rather than performance audit. Regardless of how an SAI may subsume this work into its audit programme, SAIs could consider the following questions as criteria for exploring the link between strategies and policies (INTOSAI, 2004):

- *Does the government have a strategy or plan that clearly describes its objectives?*
- *Does it clearly identify the policy instruments to be used to achieve the aims?*
- *Is the strategy and choice of policy instruments based on good data about what needs to be done?*
- *Is the strategy truly integrated, reflecting the interactions between policies, and the balance to be struck between economy, society and the environment?*
- *Where budget proposals are scrutinized by the SAI, what is the total budget for sustainable development, and what proportion of this is allocated to green issues?*
- *Has the government evolved any system to monitor and co-ordinate the activities of Non-Governmental Organisations (NGOs) working on environmental issues?*

Good governance of budgeting, regulatory policy, Centre of Government and internal control

The analytical framework presents opportunities for SAI engagement in supporting and enhancing good governance by examining four key areas of government activity: budgeting, regulatory policy, the Centre of Government and internal control. These areas of public administration must be operating well through the policy cycle in order for government to achieve its policy objectives:

- **Effective budgeting** is at the heart of enabling programme and service delivery, along with good public financial management, which ensures that resources are allocated to the areas for which they were authorised, and that the resources are deployed appropriately in that context. Effective budgeting is critical in policy **formulation**, so that programmes are adequately resourced and incorporate value-for-money principles. Effective budgeting is an **effective process** of a strategic and open state.
- Effective **regulatory policy** delivers regulations that meet underlying public policy objectives and positively impacts the economy and society. Regulations are indispensable to the proper function of economies and societies. Good regulatory policy helps to establish regulations that ensure policies are **implemented** in a way that achieves policy objectives. Good regulatory governance is an **effective process** of a strategic and open state.
- Strong **Centres of Government** are critical for ensuring coherence across government with respect to policies and programmes, and co-ordination among stakeholders in the execution of the policy process. Horizontal and vertical co-ordination led by strong Centres of Government is

critical to policy **formulation**. Strong Centres of Government are part of the **strategic capacity** and, more specifically, the institutional robustness of a strategic and open state.

- Strong **internal control** systems assure the effectiveness and efficiency of government operations, the reliability of financial reporting and compliance with applicable laws, regulations and policies. These systems, along with internal audits, complement SAI work in ensuring integrity, efficiency and economy in the use of public resources. Strong internal control mechanisms provide the ability to effectively **implement**, **monitor and evaluate** policies and their delivery, and can highlight trends and risks that feed into future policy formulation. Strong internal control systems contribute to the **openness** of a strategic and open state.

Building on this understanding, the analytical framework identifies good governance with respect to each area, and the challenges faced in their implementation within the Executive branch. In so doing, the framework offers an approach for a practical assessment of the ways in which SAI audit and counselling work can provide useful support in these key areas of public management to enhance good governance.

Suggested areas for exploration should be considered with regard to the country context, including respecting the SAI's independence, as well as the autonomies and established roles of all actors contributing to good governance, based on legal and constitutional frameworks. To this end, some distinct but closely inter-related guiding principles in assessing the feasibility of the opportunities identified under the four areas covered in this analytical framework for SAIs to contribute, in practice or potentially, to good governance are:

- Changes to an SAI's work should be in areas in which the SAI is likely to have, or should be in a position to develop, relevant expertise, consistent with its mandate

- Duplication of functions should be avoided: the SAI should not be expected to exercise functions that are already being serviced by, or should be serviced by, another expert body or institution

- An SAI's role should support, but should not displace, the proper role of other bodies – democratic or bureaucratic in supporting government activity

- An SAI, like other public institutions, has limited resources and must operate in a manner that is efficient and effective; therefore it can only reasonably be called upon to exercise new functions in line with its resources

Any normative suggestions that the study makes about the current or potential role of SAIs are to be considered with these guiding principles in mind. These principles should underline any discussions between SAIs and respective Executive bodies about strengthening the whole-of-government approach to good governance.

Notes

[11] This information is based on discussions held between the SAI of Brazil and the SAI of Finland.

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6. BUDGETING

This section considers the potential role of SAIs in promoting good governance in relation to budgeting and public financial management (PFM). The audit function is most traditionally associated with the basic functions of PFM – ensuring that resources are allocated to the areas for which they are authorised, and that the resources are deployed appropriately in that context. SAIs already produce reports on governments' financial management through audits, end of year reports or opinions or observations on governments' financial reporting.

However, against the backdrop of the difficult economic and fiscal experiences internationally over recent years, the role of PFM and budgeting is being re-assessed to underscore the necessary linkages and inter-connections with other areas of public governance – including whole-of-government medium-term planning, performance-related budgeting, full transparency and accessibility of budgetary information, identification and management of fiscal risks, and enhanced quality assurance throughout the different phases and functions of the budget cycle. The major international organisations have, over recent years, been updating their guidance on fiscal management frameworks, and the OECD in particular is developing draft *OECD Principles of Budgetary Governance* (PBG) that reflect the experience and insights of the long-standing OECD Senior Budget Officials (SBO) Working Party.

As the understanding of the role of budgeting widens, it is appropriate that the role of SAIs should be re-assessed in particular to consider the extent to which the traditional strengths of the SAI – independent, objective and rigorous scrutiny of PFM concepts in application – could and should be extended to the new reaches of budgeting.

Budgetary governance: a broader understanding

Traditionally, public budgeting was concerned primarily with the allocation, authorisation and management of financial resources. Within this traditional framework, SAIs have played a central role in ensuring accuracy in the rendering of accounts, probity in the management of public moneys and, to some extent, examining issues of cost-effectiveness. More recently, it has come to be appreciated that PFM, as a discipline, must encompass a wider range of government-wide objectives.

The ***OECD Best Practices on Budget Transparency*** of 2002 take as their starting point the relationship between open budgetary governance and better economic and social outcomes:

> *Transparency – openness about policy intentions, formulation and implementation – is a key element of good governance. The budget is the single most important policy document of governments, where policy objectives are reconciled and implemented in concrete terms.*

In outlining how the budget policy document can be framed in an open and transparent manner, the Best Practices deal with budgetary governance under three dimensions:

1. The provision of budgetary documentation at various stages of the policy-making cycle: in advance of the budget (i.e. policy formulation stage), during the course of budget execution, and after the conclusion of the budget year;

2. The various elements and specific disclosures that should feature in the budget documentation, including contingent liabilities and tax expenditures (i.e. the costs of preferential tax measures for particular activities); and

3. The role of integrity, control and accountability is highlighted, including the specific role in this context of both internal and external audit processes and institutions, and the need for public information and engagement on budgetary matters.

Since the Best Practices were adopted in 2002, there have been very significant developments in the economic and budgetary landscape, and a deepening understanding of how the various aspects of budgeting and fiscal policy should be elaborated and inter-connected.

With the onset of the global financial crisis in 2008 and its economic and fiscal implications for many OECD countries, the focus of budgetary policy shifted markedly to correction and consolidation of the public finances so that excessive public deficits are narrowed, and debt levels are reduced, in the interests of restoring the sustainability of the public finances. This can involve expenditure cutbacks, tax increases or structural economic reform measures to enhance economic growth. This trend towards fiscal correction and consolidation was tracked and reported in the OECD's *Restoring Public Finances* of 2011 and its 2012 Update. It showed that fiscal consolidation has been a major preoccupation of most OECD countries in the period 2010-2012 and, despite progress achieved in correcting fiscal imbalances, continued budgetary correction is planned into the medium term against a backdrop of elevated – and still rising – debt levels. Indeed, the 2012 Update showed that many OECD countries had extended the depth and duration of their earlier budgetary consolidation plans in the face of longer-than-expected fiscal difficulty. The analysis also showed that fiscal consolidation was weighted towards the expenditure side of the budget rather than the revenue side. Within public expenditure, savings have been sought most commonly from the areas of health care, social security, pensions and infrastructure investment – areas where savings must be calibrated and evaluated carefully as to their political, social and broader economic impacts.

Within this overall context of fiscal consolidation and difficult budgetary trade-offs, there has been an intensified focus on the budgetary tools, mechanisms and processes that can be brought to bear to support governments and public administrations in this complex endeavour. A feature of the fiscal consolidation agenda in many countries – such as Ireland and Spain – has been the re-design and reform of traditional budgetary frameworks, as part of a more comprehensive reform of the public sector and of public governance more broadly, and as part of an economic restructuring agenda aimed at making their respective economies more competitive and responsive.

Against the background of budgetary turbulence among its members over recent years, the EU has sought to promote the credibility and effectiveness of national fiscal frameworks by adopting a range of new economic governance rules (see Box 6.1. below). These rules emphasise the need for a coherent, government-wide response to the challenges of budgetary consolidation and co-ordination.

Based on OECD surveys of budget practices and procedures across OECD countries and other global regions, including Central and Eastern Europe, Latin America and the Caribbean, together with analysis and peer discussion at the SBO, the following broad developments in budgetary practice have been identified.

Box 6.1. **Overview of EU Economic Governance Rules**

The key elements of the EU economic governance framework applicable to most EU countries, following the reforms of 2011-2013, can be summarised as follows:

Countries must manage their public finances within fixed limits

- The debt level and the deficit level must not exceed ceilings of 60% of GDP and 3% of GDP, respectively; both expressed in general government terms.
- The public finances should be maintained close to a balanced position (i.e. a deficit of no more than 0.5% of GDP) in cyclically-adjusted terms, net of one-off factors.
- The growth in public expenditure must not exceed the underlying medium-term level of economic growth, unless it is financed by additional revenues.

If these limits are not respected, budgetary correction must proceed at a minimum pace

- Any unduly high, non-structural budget deficit (i.e. not close-to-balance) must be corrected by 0.5% of GDP each year, in structural terms; while any excess above the debt limit of 60% of GDP must be reduced by 1/20th each year.

Exceptions to these rules are very limited

- Countries may delay compliance with these fiscal limits in the event of a sudden severe economic shock, provided that they are making satisfactory fiscal effort in structural terms.

Numerical fiscal rules to achieve these targets must be enshrined in national constitutions or laws

There are financial penalties for non-compliance

- Sustained failure to comply with the fiscal commitments leads to an escalating process of 'recommendations' and sanctions, culminating in financial penalties.
- Under new voting rules, it is harder for member states to block decisions on these matters.

Coordination of national budgetary calendars

- As well as preparing medium-term Stability or Convergence Programmes in April of each year, countries should submit a draft annual budget in October of each year for consideration at the EU level prior to being adopted at the national level by year-end.

A medium-term budgetary framework must be put in place

- Countries must develop an institutional framework so that the annual budget is framed within the context of clear multi-year fiscal objectives, projections and policy orientations.

A role for independent fiscal institutions

- Within each country, an independent fiscal body should monitor compliance with the fiscal rules, and should be responsible for preparing, or endorsing, national economic forecasts.

Long-term fiscal sustainability

Public fiscal sustainability is the ability of public governments to maintain public finances at a credible and serviceable position over the long run, in light of the prevailing mix of spending and revenue policies. Public fiscal sustainability also takes into account debt servicing costs and future socio-economic and environmental factors that challenge the public budgets. Prudent macroeconomic assumptions, sensitivity and risk analysis and appropriate fiscal rules are factors that can help to orient spending and revenue policies within sustainable levels in the short and medium term. For more forward-looking perspective, long-term fiscal projections that incorporate demographic and socio-economic trends are a useful analytical tool.

In most OECD countries, the Central Budget Authority is responsible for long-term fiscal projections. In some countries this responsibility is located in other departments of the Ministry of Finance other than the CBA or in other core ministries.

Long-term fiscal uncertainty is a challenge for most OECD countries. The INTOSAI community recognises that the long-term sustainability of financial policies is necessary to further the social and economic development of nations (INTOSAI, 2013). A growing elderly population, higher longevity, increased demand for health services and, in some cases, simultaneous reductions in the government's tax base are some factors that create long-term challenges. Long-term fiscal projections can play a useful role in identifying the expected future costs and associated debt of current policies in light of forecasted demographic and economic developments.

Long-term projections of the public sector's role in the economy could also contribute to the informed political and public discussion of a broader reform agenda, to ensure that the costs of the public sector are assessed against benefits delivered to society and issues of affordability. The size and structure of the public sector in several OECD countries pose challenges in terms of long-term sustainability. Some governments also present long-term fiscal challenges in a cross-generational perspective, in order to distribute benefits and cost in a reasonable way over generations.

Sensitivity and fiscal risk analysis

Two-thirds of OECD countries include fiscal sensitivity analysis in their publicly available budget. Sensitivity analysis is a hypothetical type of analysis used in quantitative modelling to test the sensitivity of outcomes to changes in parameters or underlying assumptions. If a small change in a parameter results in relatively large changes in the outcomes, the outcomes are said to be sensitive to that parameter (IMF, 2007). Sensitivity analysis is one way to account for uncertainties associated with forecasting macroeconomic variables that are important to the budget as a whole or to individual expenditure items. It is used to test the importance of different assumptions to the projected performance of a government intervention. For example, sensitivity analysis could be used to test the extent to which projected revenue growth is affected by changes in the price of key export commodities on the world market.

Another method of taking uncertainty into consideration in fiscal projections and macroeconomic assumptions is to identify and assess specific risk elements that would negatively influence the assumptions and projections should they materialise. Actions should be taken in accordance with the risk elements' probability and consequence.

Fiscal rules that limit the budget

A fiscal rule is a permanent constraint on fiscal policy expressed in terms of a summary indicator of fiscal performance (Kopits and Symansky, 1998). A fiscal rule has two fundamental characteristics. First, it presents a constraint that binds political decisions made by the Legislature and by the Executive. Second, it serves as a concrete indicator of the Executive's fiscal management. Budgeting in democratic countries is inherently biased towards expansionary outcomes (Schick, 2003). If observed, fiscal rules constrain politically-motivated spending to improve macroeconomic stability in the short-term, while contributing to long-term fiscal sustainability. Fiscal rules also signal a government's creditworthiness and provide justification for making tough fiscal decisions. Finally, fiscal rules can control the negative spill-overs and externalities that arise within a federation or union (Inman, 1996).

There is no one-size-fits-all fiscal rule. Four broad yet distinctive categories of rules exist, namely: expenditure rules, fiscal balance rules, debt rules, and revenue rules.

- *Expenditure rules* limit the amount of government spending and can be expressed in nominal or real terms as limits on spending levels or expenditure growth, or as an expenditure-to-GDP ratio.

- *Fiscal balance (i.e. deficit or surplus) rules:* directly target the fiscal balance (i.e. the gap between government spending and revenues), e.g. a requirement to run a balanced position, not to exceed a defined deficit limit, or a requirement to attain a defined surplus at minimum. Such rules can be expressed in nominal or cyclically adjusted terms, usually by reference to a percentage of GDP.

- *Debt rules* limit the amount of government debt that can be accumulated and can be expressed in nominal terms as a debt-to-GDP ratio or as an explicit reduction of the debt-to-GDP ratio.

- *Revenue rules* impose constraints on the tax-to-GDP ratio and place restrictions on government revenues raised in excess of projected amounts.

Where they are used, fiscal rules and targets should be clearly stated and explained, with specific attention paid to their design. Rules should be based on appropriate summary indicators and be simple and transparent so as to facilitate management and monitoring activities. Furthermore, they should be responsive to cyclical fluctuations and should include provisional mechanisms to deal with revenue windfalls. Fiscal rules should involve all levels of government where possible.

While evidence suggests that fiscal rules can assist governments to achieve fiscal consolidation, practices vary and there is no academic consensus on what design features are most effective. It is notable, however, that countries that fail to enforce or renew fiscal rules are unlikely to achieve fiscal discipline. The effectiveness of fiscal rules is also linked to other budget practices and procedures. According to Schick (2003), these include: medium-term budget frameworks; top-down budgeting; long-term fiscal projections; policy change impact assessments; monitoring and follow-up procedures; and enforcement mechanisms. Recent literature also highlights the supportive role of independent enforcement bodies (Schaechter et. al., 2012).

Top-down budgeting

A natural complement to a fiscal-rules-based environment or to an environment in which clear fiscal objectives are laid down by government, 'top-down budgeting' refers to the budgeting practice whereby the fiscal targets are determined from the outset, with annual and multi-annual budgetary policies subsequently determined in conformity with these overall levels. Typically in top-down budgeting, the Executive first determines aggregate public finance targets (spending and revenue levels) given medium-term fiscal objectives and prevailing economic conditions. Within this aggregate, sectoral ceilings are set (and approved by cabinet) reflecting existing commitments, political priorities in general and new key policy initiatives. The detailed allocation decisions are typically delegated to individual line ministries. To be implemented effectively, top-down budgeting requires rigorous and prudent economic forecasts and must be combined with complementary fiscal management practices such as medium-term expenditure frameworks.

Many OECD countries began to adopt top-down budgeting practices in the 1990s in an effort to control deficits and constrain expenditure growth (Kim and Park, 2006). Top-down budgeting marks a shift not only in the sequence of budget decisions but also in budgetary roles, responsibilities and relationships. While the Central Budget Authority works to control aggregate spending by establishing and enforcing spending ceilings, line ministries assume relatively greater responsibility for resource allocation. This delegation of authority requires close working relationships between the two: line ministries use their superior knowledge of operational issues to determine the most efficient allocation of resources in their policy area but may require advisory and technical support from the Central Budget Authority to understand how programme spending will evolve over time and to develop expenditure projections.

Top-down budgeting marks a significant re-orientation of the budget process as compared to the traditional bottom-up approach (Table 6.1). Bottom-up budgeting is a reactive, expenditure-driven process that imposes no up-front constraints on ministerial requests. Total spending is determined as the residual sum of individual appropriations and remains unknown until the final stages of budget preparation. The detailed appropriations characteristic of bottom-up budgeting foster agency-specific programme ownership and make it difficult to reallocate in accordance with new policy priorities. Top-down budgeting, on the other hand, should encourage joint ownership of proposals across line ministries and create space to reallocate resources according to shifting priorities and economic conditions.

Table 6.1 **- Top-down budgeting vs. bottom-up budgeting**

	Top-down	**Bottom-up**
Primary Focus	Policy-driven process that aligns spending with key priorities (proactive)	Expenditure-driven process (reactive)
Role of Finance Minister	Set aggregate spending level based on fiscal management target and monitor compliance	Negotiate details of individual spending proposals to control detailed allocations
Role of Spending Ministers	Allocate financial resources to individual programmes within assigned spending ceilings	Submit budget requests and negotiate itemised appropriations
Economic Forecasting	Aggregate fiscal analysis that takes into account economic forecasts.	Ministry by ministry analysis that largely ignores economic forecasts
Efficiency	Streamlined process reduces inefficient practices and excessive requests	Inefficient and time-consuming negotiations process
Timeframe	Multi-year perspective	Annual appropriations process

Source: Adapted from Kim and Park (2006)

Some factors that have a bearing on budget flexibility are: the number and detail of budgetary line-items (i.e. the most detailed level of spending that is mandated by the Legislature); the use of lump-sum appropriations, which give government organisations a greater deal of flexibility to allocate public funds in order to maximise their performance; latitude to reallocate appropriations during the budget year, subject to certain restrictions; and latitude to carry over unused appropriations from one budget year to the next.

On this last point, the appropriateness of carry-over rights has been subject to debate. In general, for carry-overs to be most effective and to limit their misuse, budget systems should have a medium-term budget framework (see next section), devolved budget management powers, well-developed accounting and reporting systems, and sound internal control and external audit procedures.

Medium-term fiscal and expenditure frameworks

One of the major developments since the introduction of the OECD Best Practices on Budget Transparency in 2002 has been the increased focus on the multi-annual dimensions of budgeting. Medium-term expenditure fiscal frameworks (MTFFs) and expenditure frameworks (MTEFs) strengthen the ability of the government collectively, and the Ministry of Finance in particular, to plan and enforce a sustainable fiscal path. If properly designed, an MTEF should force stakeholders to deal with the medium-term perspective of budgeting and budgetary policies rather than adopt an exclusively year-by-year approach. MTEFs typically cover a period of three to four years and aim to improve the quality and certainty of multi-annual fiscal planning by combining prescriptive yearly ceilings with descriptive forward estimates. 'Estimates' in this context are calculations of how expenditure, revenue and the aggregate fiscal position will evolve under certain assumptions. By their very nature, high-level fiscal ceilings are set in a medium-term context. Ceilings are targets or limits set by the government regarding aggregate or policy area spending for each year of the multi-year frame of reference. The ceilings may be updated annually or fixed for a period. For the medium-term framework to work effectively, estimates and ceilings need to be reconciled within the context of a forward-looking approach to budgetary planning and policy formulation. Accordingly, a medium-term framework should state the government's medium-term fiscal objectives clearly in terms of high-level targets such as the level of aggregate revenue, expenditure, deficit/surplus and debt. It should also facilitate stakeholders in identifying the policy choices and trade-offs that will be necessary in light of the estimates of what would happen in the following 3-5 years based on unchanged policies. The level of detail of such frameworks varies from country to country, and a corresponding vocabulary describing the various forms of medium-term frameworks has developed.

MTEFs are increasingly relevant in a context where the multi-annual character and implications of certain policies need to be more clearly presented. Many policies require an extended time horizon, such as large capital projects, new programmes, and organisational reform and restructuring. The forward estimates make clear the medium-term implications of budget decisions. This is particularly important when: i) capital projects are launched with changing operating costs; ii) programmes come into effect late in the budget year, thus not exposing their full costs in the initial year; iii) programmes' spending implications are not fully reflected under the circumstances prevailing during the budget year, but will become so in out-years. These are all classic examples of budgeting 'games', which the medium-term frameworks aim to mitigate. From the point of view of managers, in-line ministries and agencies, medium-term frameworks put them in a better position to plan their policies and operations, to the extent that they have some level of visibility regarding the likely level of funding beyond the next budget. This is especially relevant in a context of fiscal consolidation. Many savings options involve more than one year in order to reap their full benefits. Prior to the advent of medium-term frameworks, such options were often not considered as the time horizon only extended to the next budget year.

Almost all OECD countries report to have a medium-term expenditure framework in place. Half of the OECD countries have enshrined the MTEF in law and most of the rest have established the framework in a policy or strategy decided by the government or through other arrangements.

Capital budgets and multi-year funding practices

Capital budgeting means different things in different countries. Capital budgeting can mean that the government has a divided budget, with one budget for investment and another for current expenditures. It can also mean that government accounts for investment and current expenditure separately, but then integrates them into a single budget with budget charges for depreciation and write-offs on capital assets. Alternatively it can mean separate decisions, which are then combined into a single budget. Two-thirds of OECD countries prepare separate capital and operating budgets, while most of the other countries have integrated capital and operating budgets.

Public-private partnership practices

Public-Private Partnerships (PPPs) are a way of delivering and funding public services using a capital asset where project risks are shared between the public and private sector. A PPP can be defined as a long term agreement between the government and a private partner whereby the service delivery objectives of the government are designed to be aligned with the profit objectives of the private partner.

Since the early 1990s and increasingly throughout the 2000s, there has been a significant increase in the use of PPPs by OECD countries. Countries such as Australia, France, Germany, Korea and the United Kingdom increasingly use PPPs to deliver services that they previously delivered through traditional public procurement. Given the complexity of PPPs and their somewhat infrequent use, critical skills to ensure value-for-money may need to be concentrated in a PPP Unit that is made available to the relevant authorities.

Value-for-money assessment

Value-for-money can be defined as what a government judges to be an optimal combination of quantity, quality, features and price (*i.e.* cost), expected (sometimes, but not always, calculated) over the whole of the project's lifetime. Thus, the value-for-money concept attempts to encapsulate the interests of citizens, both as taxpayers and recipients of public services. As such, value-for-money should, in principle, also be the driving force behind traditional infrastructure procurement. Therefore, any project, whether it is a PPP or a traditionally procured project, should be undertaken only if it creates value-for-money.

There are several techniques for assessing value-for-money. Cost-benefit analysis is a systematic process for calculating and comparing benefits and costs of a government policy. It has two purposes: *i)* to determine if it is a sound investment/decision (to assess the justification/feasibility); and *ii)* to provide a basis for comparing different government policies. It involves comparing the total expected cost of each option against the total expected benefits, to see whether the benefits outweigh the costs, and by how much. Cost-benefit analysis is related to, but distinct from cost-effectiveness analysis. In cost-benefit analysis, benefits and costs are expressed in monetary terms, and are adjusted for the time value of money, so that all flows of benefits and costs over time are expressed on a common basis in terms of their "net present value." Cost-effectiveness analysis is a form of economic analysis that compares the relative costs and outcomes (effects) of two or more courses of action. Cost-effectiveness analysis is often used in the field of health services, where it may be inappropriate to monetise health effects. Common measures include "quality-adjusted life years". Other relative analysis methods could be, for example, public sector comparators.

The extent to which these methodologies can and should be applied to areas of current expenditure, complementing their longer-established use in capital projects, is an active area of consideration in many OECD countries.

Performance-related budgeting

A further area where developments have progressed on substantially since the 2002 *OECD Best Practices on Budget Transparency* is the area of performance information and its use in the budget. The public sector has traditionally been held to account for compliance with rules and procedures, including accounting for financial appropriations. In more recent years, OECD and other countries have increasingly sought to develop a focus on the results achieved with the appropriations allocated through various approaches under the heading of 'performance budgeting'. This area is the subject of a lot of activity across many OECD countries at present, including revisions and re-assessments of established performance budgeting models, and there is currently no settled consensus on the optimal way of using performance information within the budgeting context. The issues arising range from *i)* the level of information being used (with a more recent focus on streamlining and focussing performance information, and retreating from a tendency to "over-engineer" performance budgeting products); *ii)* the problems inherent in measurement of public performance and *iii)* a broader question of whether the budgeting process lends itself well to performance monitoring, or whether other mechanisms of governance and accountability should play a more significant role.

Performance budgeting frameworks are widely found in OECD countries and are generally flexible in nature. In general, the different policy sectors mainly use performance information for setting allocations for programmes, line ministries and agencies, for strategic planning, for proposing new areas of spending, and for a reduction in spending. However, in some countries, performance information does play a limited role in the budget negotiations with the Central Budget Authority. A general finding is that when performance targets are not met, the consequences for managers of ministries can be limited - this suggests that performance information is not easily transformed into action.

A consistent finding is that countries have difficulty establishing performance information of sufficient quality, robustness and reliability to serve as a sound basis for informing resource-allocation decisions. While frameworks exist for the types of indicator that can be applied to various stages of the budget process (see Table 6.2), a settled consensus tends to be lacking – whether nationally or internationally – on the benchmark indicators that can be used to guide and assess progress on the achievement of public policy objectives.

Table 6.2 **- Types of performance measures**

	Types	Measures
Performance Measures	Input measures	What goes into the system? Which resources are used?
	Output measures	What products and services are delivered? What is the quality of these products and services?
	Outcomes measures	Intermediate: What are the direct consequences of the output? Final: What are the outcomes achieved that are significantly attributable to the output?
	Contextual measures	What are the contextual factors that influence the output (*e.g.* processes, antecedents and external developments)
Ratio Indicators	Efficiency	Cost / Output
	Productivity	Output / Input
	Effectiveness	Output / Outcome (intermediate or final)
	Cost-effectiveness	Input / Outcome (intermediate or final)

Source: Adapted from Streck et al. (2006)

Budget Transparency and Comprehensive Reporting

In line with the OECD Best Practices for Budget Transparency, a variety of government reports and related disclosures exist that are essential for appropriate openness and transparency. Key elements are summarised below:

- *Disclosure of underlying assumptions and publicly available budget documents:* A key aspect of transparency is the extent to which the Executive's budget discloses the underlying assumptions (macroeconomic and others) that set the fiscal framework within which government organisations formulate their spending proposals. Key assumptions include estimates of GDP growth, the current account, inflation and the interest rate. These estimates underlie forecasts for tax and non-tax revenues, and government debt-servicing obligations and requirements. Arguably there is no single factor more responsible for "de-railing" budget outcomes and projections of deficits or surpluses than the use of weak macroeconomic assumptions.

- *Comprehensiveness of budget documentation:* It is important that comprehensive information is presented in the budget to enable policy debate. In addition to the economic assumptions underlying the budget, the Best Practices on Budget Transparency states that the budget should include, among other things: a medium-term perspective; a detailed commentary on each revenue and expenditure programme; appropriations by administrative unit (*e.g.* ministry, agency); and non-financial performance data, including performance targets. Most OECD countries identify expenditure items that are considered as contingent liabilities. From a transparency perspective it is also important that those elements are disclosed in the budget documentation submitted to the Legislature and that the documentation is made publicly available.

- *In-year reporting:* Periodic in-year reporting on budget execution and revision of budget estimates helps to detect and manage the impact of economic developments on the budget in a timely manner. This includes information on tax and non-tax revenues and spending on programmes and public services. Such reports identify any changes in the assumptions underlying the budget, as well as other relevant events that have transpired during the fiscal year.

- *Year-end reporting:* The year-end report is a government's key accountability document. The Best Practices recommend that it should be audited by SAIs in accordance with generally accepted auditing practices, released within six months of the end of the fiscal year, and scrutinized by Parliament. All OECD countries have an institution mandated with auditing government accounts. There is, however, great variation within OECD countries as to the time by which the audited annual report is disclosed after the end of the fiscal year. For example, while Mexico and the United States produce an audited year-end report within 3 months of the end of the fiscal year, Germany, Greece, Portugal and the United Kingdom's year-end reports are published 11-12 months after the end of the fiscal year. Spain publishes the audited report 16 months after the end of the fiscal year (six months after the audit institution receives the accounts).

Ensuring an effective role for the Legislature

The OECD believes that an effective role for the Legislature is a key ingredient in establishing and maintaining fiscal discipline, while providing a necessary link with civil society and fostering accountability of the Executive. Legislatures are constitutionally mandated to hold governments to account, including with respect to the budget process. Indeed, the evolution of legislative "power of the purse" dates back to medieval times. Today's Legislatures scrutinise and authorise revenues and expenditures and ensure that the national budget is properly implemented. This is done through a variety of means, including committee review, plenary debates, and Parliamentary questions and interpellations. It is worth noting that the general trend in OECD countries in terms of committee structures for reviewing the budget appears to be a dominant Budget/Finance Committee responsible for budget review which coordinates varying levels of input from sectoral committees. Ideally, a strong Budget/Finance Committee promotes co-ordination and consistency in legislative budget action and facilitates fiscal discipline, while involving sectoral committees allows the Legislature to draw on its specific expertise (Schick, 2002).

Amendment powers

There is nevertheless great variation in legislative influence over the budget in OECD countries, as demonstrated by a Legislature's amendment powers. At one end of the spectrum, the Legislature in the United States has the power to rewrite the government's proposed budget; at the other end, Legislatures such as Greece or Ireland can only approve or reject the budget. In Australia, the Legislature can only make amendments on new policies.

Time available for legislative debate

The effectiveness of a given Legislature in the budget process is also influenced by the time available for legislative debate and the quantity of resources that the Legislature has at its disposal. It should be emphasized that the presentation of the budget and related documentation in the Legislature is normally the first opportunity for public scrutiny of the government's spending priorities. Legislative debate in both the plenary and committees facilitates public participation in the budget process.

Legislatures and their committees require an adequate amount of time to reflect upon and debate budget documentation prior to approval. This is particularly important in order to ensure that legislative committees (which exist in all OECD Legislatures and which provide the most in-depth scrutiny of the budget) have sufficient time to review, debate and propose amendments. The OECD (2002) *Best Practices on Budget Transparency* recommend that the Executive's draft budget should be submitted far enough in advance to allow for its proper review by the Legislature. This should be no less than three months prior to the start of the fiscal year, and the budget should be approved by the Legislature prior to the start of the fiscal year.

Analytical capacity

To engage meaningfully in the budget process rather than simply serving as a rubber stamp, Legislatures require reliable, unbiased information as well as strong analytical capacity. Strengthening research capacity, hiring adequate committee staff, and allowing committees to consult or employ experts all serve to enhance legislative effectiveness and redress the capacity imbalance between the Legislature and the Executive. Most Parliaments in OECD countries have access to several sources of technical capacity for budget analysis. Committee staff is perhaps the most commonly available resource. However, the number of staff available to assist the Budget/Finance Committee in undertaking specialised analysis of the budget and related matters varies widely.

There is a trend in OECD countries to establish specialised units that assist Legislatures with budget-related research and analysis. In some cases, these units are located within Parliament, often as part of Parliament's research services. In others, they are independent. Some larger Legislatures maintain a large unit (a "Parliamentary budget office" (PBO) or equivalent) to assist the finance committee on public finance work. Across the OECD, these bodies differ in size, constituents and core functions, but all help to simplify the budget, eliminate the Executive's monopoly on information in the budget process, and improve the budget's credibility and accountability. Key tasks may include analysis of the Executive's budget proposal or the estimates, costing of legislation, and economic forecasting.

Independent fiscal institutions

In parallel with the development of enhanced resources and institutions to facilitate Parliamentary engagement in the budget process, there is a clear trend within OECD countries to establish independent fiscal institutions (typically referred to as fiscal councils, although the definition sometimes also includes PBOs) as a means of enhancing independent oversight and accountability in regard to the fiscal performance of the Executive and/or to improve the credibility of budgetary forecasts. The role, structure and funding model of these bodies vary considerably across countries. Apart from a role in assessing or preparing official economic forecasts, typical tasks include analysis of the Executive's budget proposals, monitoring compliance with fiscal rules or official targets, costing of legislative proposals and analytical studies on selected issues.

A fiscal council's independence – real and perceived – is critical to its success. Independence is underpinned by a clear legal framework. The OECD's draft "Principles for Independent Fiscal Institutions" identifies several factors that can enhance independence.

The role of SAIs

On the basis of the analysis set out above, this section considers the opportunities for SAI engagement to enhance budgetary governance in line with the SBO's draft *Principles of Budgetary Governance* (PBG).

These draft principles aim to provide normative guidance to countries – within the OECD and further afield – in developing and reforming their budgetary frameworks to take account of recent experiences, good practices and innovative developments. The PBG (see Box 6.2 below) emphasise that budgeting and PFM are no longer a matter of basic financial allocations and appropriations; this area is now much more closely inter-twined with the broader themes of public governance, including support for the achievement of government-wide strategic objectives, open and transparent government, management of complex risks and public service innovation.

It is fitting to consider in this context to what extent the role of the SAI should also evolve, so that it can engage with these aspects of PFM and keep pace with budget policy-makers who are becoming increasingly active in these spaces. In particular, an over-arching theme is that the objective, professional perspective of an SAI should be capable of adding value and enhancing quality throughout the budget process by broadening the traditional understanding of their role in PFM oversight and accountability.

Accordingly, this section will assess the actual and potential roles of the SAI against these draft Principles and offer suggestions on how these roles could be put into practice. The experience of various countries in adopting a forward-looking approach to the role and contribution of SAIs will also have a bearing on the proposed approach. It should be borne in mind, however, that SAIs, like all public bodies, must prioritise their activities and areas of focus within their limited resources. Accordingly, SAIs will need to carefully weigh the question of whether and to what extent they should apply their resources beyond the traditional areas of activity (notably financial audit) and into other areas of public governance. The SAI's own assessment of the priority areas for improving budgetary governance, as well as the assessment of other key stakeholders will naturally be of fundamental importance in this regard.

It should also be noted that the SAI is one of the key institutions of national budgeting alongside the Parliament and the Executive. The relations between these institutional pillars are usually well established, and any initiatives to modernise and re-work these relations should, ideally, command the understanding and the support of all stakeholders. Managing the process and renewal, reform and modernisation may, in some circumstances, represent a significant implementation challenge for countries.

Box 6.2**.** **The draft *OECD Principles of Budgetary Governance***

1. Fiscal policy should be managed within clear, credible and predictable limits.
2. Top-down budgetary management should be applied to align policies with resources.
3. Budgets should be closely aligned with government-wide strategic priorities.
4. Budgets should be forward-looking, giving a clear medium-term outlook.
5. Budget documents and data should be open, transparent and accessible.
6. The budget process should be inclusive, participative and realistic.
7. Budgets should present a true, full and fair picture of the public finances.
8. Performance, evaluation and value-for-money should be integral to the budget process.
9. Longer-term sustainability and other fiscal risks should be identified, assessed and managed prudently.
10. The integrity and quality of budgetary forecasts, fiscal plans and budgetary implementation should be promoted through rigorous, independent quality assurance.

See *http://www.oecd.org/governance/budgeting/* for further information on the draft principles.

Budgetary planning and formulation

Accuracy of fiscal forecasts

- SAIs could assess whether adequate institutional procedures and safeguards are in place to ensure the quality and reliability of the technical economic and budgetary forecasts that underlie the budget and the medium-term projections. SAIs could then determine if these forecasts are consistent with budgetary constraints and objectives.

As discussed above, in recent years, there has been an increase in the number of independent fiscal institutions tasked with, among other functions, ensuring compliance with fiscal rules, assessing the accuracy of economic forecasts, and evaluating the appropriateness of the fiscal stance pursued by the government, whether by reference to fiscal rules (internal or external) or by reference to stated fiscal objectives of government. Given the specialist economic nature of this analysis, it is not apparent that the SAI should become directly involved in this area.

However, the accuracy and reliability of budget forecasts are of fundamental importance to the credibility and quality of the government's budgetary framework. To the extent that an SAI may have a legitimate role in assessing the integrity of the overall national fiscal framework, it may be appropriate for the SAI to consider what safeguards are in place to ensure the professional quality and character of such forecasting processes – e.g. whether through the establishment of an Independent Fiscal Institution (IFI) or through administrative assurances for the independence of forecasting units within ministries of finance.

Top-down budgetary management and planning; alignment with strategic priorities

- SAIs could assess whether the processes and procedures in place facilitate the alignment of the annual budgetary/resource-allocation process and with identification, prioritisation, resourcing and monitoring of governmental strategic objectives.

- SAIs could communicate key results from previous audits, evaluations and other assessments during the policy-formulation stages of the budget process and engage with administrative, political and Parliamentary counterparts in this regard.

The draft PBG emphasise the importance of an inter-connected, holistic and clear approach to budgetary planning and management, to ensure the quality of resource allocation and alignment with the policy priorities of government. What is envisaged in a policy-making cascade in which there is clarity from the outset about the level of resource availability for different sectors; there is a strong impetus within each sector to identify priorities so that resources can be targeted to best effect within each sector; and review / monitoring processes that form an integral part of the policy cycle so that messages about performance and delivery can feed back into subsequent resource-allocation phases.

At a general level, an SAI role can be identified in assessing whether such a coherent overall framework exists, so as to facilitate an effective, strategic and results-focussed deployment of limited resources. It should be noted that an alignment of this nature extends beyond the annual budget-formulation window and encompasses also the results of monitoring and evaluation.

More specifically, SAIs can play a role in the *ex-ante* policy formulation stage by ensuring that the results of previous financial audits, performance audits and other assessments are made available to policy-makers at an early stage. For it to be most effective, this approach requires a clear communication of key findings by the SAI in a manner that is comprehensible and relevant for policy-makers, as well as an appreciation on the part of policy-makers (both administrative and Parliamentary) of the value of the SAI contribution and its relevance for policy design. For example, the Federal Court of Audit in Germany is present in the initial discussions between the Federal Ministry of Finance and line ministries when discussing initial budget requests, and is also called upon by the Bundestag Budget Committee when debating the draft budget from the Federal Government. In this way its critical perspective and experience can be brought directly to bear on the budget negotiations.

Medium-term aspects of budgeting

- SAIs could assess whether there is in place an effective framework for guiding the annual process of resource allocation by reference to multi-annual budgetary constraints, fiscal plans and strategic priorities/objectives of government.

As discussed above, the multi-annual character of budgeting has moved to the forefront of budgetary practice over recent years, and the annual budgetary process has increasingly come to be viewed as an element within the longer time horizon during which public sector outcomes can most realistically be planned and assessed. A growing number of OECD countries have developed medium-term budgetary frameworks (MTBFs) and medium-term expenditure frameworks (MTEFs) to make the multi-annual aspects of budgeting explicit, and more directly manageable. These aspects relate both to compliance with fiscal constraints and to achievement of multi-year strategic objectives.

However, there is often a sharp distinction between the ostensible attributes of a MTEF (e.g. routine presentation of multi-annual projections) and the substantive effect of a MTEF (especially – whether the framework effectively guides and constrains multi-annual resource allocation, and how easily the expenditure ceilings can be varied from one year to the next). In assessing whether an effective MTBF or MTEF is in place, an informed, qualitative judgement is called for, and this is an area where an SAI could have a value-added role to play, and some already have. The Portuguese SAI identifies and assesses emerging trends – such as economic, social, technological, environmental – that have the potential to impact the public administration in the medium- to long-term. For example, it has identified demographic issues as being a key structural constraint to economic development and financial sustainability in Portugal, given its ageing population and the impact on the sustainability of its social security system and national health service.[12]

Capital budgeting

- SAIs could assess the effectiveness of the national framework for identifying, evaluating and prioritising capital investment projects by reference to the economic, social and environmental needs of the country.

- SAIs could assess whether there are sufficiently robust procedures and technical capacity in place to evaluate effectively the various modalities for procuring capital investment projects, including PPPs, and to ensure that the selection of modality is properly grounded on value-for-money considerations.

Capital budgeting is one particular dimension of multi-year budgeting with a distinct set of attributes. Capital budgeting is concerned with the creation of an asset with a multi-annual lifespan (typically of five years or more, although the lifespan can be much longer in the case of public infrastructure assets). This area of budgeting also corresponds closely with capital asset accumulation in the private sector, and a range of international norms have been established in areas such as appraisal (e.g. cost-benefit analysis) and depreciation.

Given the technical nature of the various appraisal methodologies and accounting decisions, and the potentially significant implications for the cost-effective use of public funds, this area represents a natural area of scrutiny by an SAI. Moreover, decisions about capital infrastructure need to be grounded in a comprehensive assessment of the economic, social and environmental needs of a country.

Finally, in this regard, over recent years there has been an increasing focus in many OECD and other countries on the potential application of PPPs and related non-traditional methodologies for procuring capital investment projects. Experience has shown that procedural faults and lack of technical professional capacity can have serious repercussions for the achievement of value-for-money from PPPs, whether through an institutional or political bias towards the use of PPPs, a misunderstanding of the use of the "public sector benchmark" or an under-appreciation of the potential contingent liabilities and other fiscal risks that a PPP may entail. To this end, SAIs can offer useful assessments of PPPs, identifying risks associated with them, as the SAI of Poland did in a 2012 audit regarding the implementation of PPPs.[13]

Budgetary openness, transparency and inclusiveness

- SAIs could publish the results of key audit findings and of other technical assessments in a format and in language that is accessible to citizens, including through simple publications and on-line media.

- SAIs could engage directly with citizens, NGOs and Civil Society Organisations (CSOs), including through the use of "expert panels" in some circumstances, where this can provide additional useful evidence in support of an audit or assessment of programme efficacy.

- SAIs could maintain a close working and reporting relationship with Parliament or a key committee of Parliament to ensure two-way communication with public representatives on audit findings and policy implications.

The OECD has long advocated budget transparency and openness in the interests of ensuring that citizens and their representatives in Parliament can understand and engage with a budgetary process that is in their interests. The OECD Best Practices on Budget Transparency provide clear and practical guidance in this regard, and could form the basis for a qualitative assessment by the SAI (see also under "Comprehensiveness of budgetary information and accounting" below).

Given the role of the SAI as one key actor in the budget process, one way in which the SAI can contribute to budget transparency is by ensuring that the key results of audit reports and other technical assessments are made available to citizens generally in a format and in language that are accessible. In many advanced OECD countries, accessibility can be achieved through on-line media; in more developing countries with populations that are poorly-connected to the internet, accessibility can mean making a simple publication available in local citizen centres or through public libraries. For example, the Comptroller & Auditor General of India publishes short, non-technical, user-friendly summaries of its audit reports (sometimes referred to as "noddy books") aimed at a general audience.

In addition, the SAIs of some countries have developed innovative approaches to engaging directly with citizens, with a view to improving the quality and the evidence base for the audit process – in particular through accessing local knowledge and experience that is not normally available to an SAI. Such a direct citizen-centric engagement may also have intangible effects in terms of promoting trust in government as a whole. For example, the SAI of the Philippines has pioneered a "citizen participatory audit" process which engages with civil society organisations – on the basis of a formal memorandum of agreement – as partners in the auditing of particular infrastructure projects, beginning with projects aimed at providing protection from flooding. In Brazil, a country with a tradition of mobilising citizens in various aspects of the budget process, the SAI has developed representative "expert panels," which help to inform the SAI of how to engage with citizens. This practice has now been institutionalised as part of the SAI's manual for the conduct of performance audits.

Of course, the primary means of ensuring that citizens' viewpoints are taken into account via elected representatives in Parliament. A close working relationship between the SAI and the Parliament, or a dedicated committee of Parliament, is therefore a hallmark of an effective SAI in many OECD countries.

Comprehensiveness of budgetary information and accounting

- SAIs could assess whether the budget document provides a true, full and fair account of the position of the public finances, including by reference to the treatment of off-budget items, security information and the enumeration/quantification of fiscal risks.

- SAIs could audit whether the budgetary information conforms with stated accounting standards and communicate the resource-management and policy implications of the accounting information in particular areas, where this may not be obvious.

- SAIs could assess whether the existing public accounting framework is fit for purpose in informing citizens, Parliament and key stakeholders of the true position of the public finances, and providing expert advice – including by reference to international standards and practices – on how the national accounting framework might be modified and improved.

As outlined above, the OECD Best Practices on Budget Transparency provide useful guidance on the information that should be listed in the budget documentation. As underlined also in the draft PBG, the budget documentation should include a comprehensive account of all expenditures and revenues, and no figures should be omitted or hidden. The SAI, in the context of an over-arching qualitative assessment of the soundness of the budget framework, would be in a position to provide an informed view in this regard. This is particularly important in those areas where there is a marked asymmetry of information between the government and citizens, and where assurances from technically competent and independent experts such as those in the SAI can play a key role in underpinning trust, such as: the fair treatment of off-budget items; appropriate (and not excessive) recourse to security restrictions on budget transparency; proper quantification and listing of the likely costs and benefits associated with PPPs. In addition, an assessment and quantification of contingent liabilities and other fiscal risks (as discussed in more detail below) would also be relevant in this overall context.

In addition, a number of countries have committed themselves to moving from traditional cash-based budgeting and public accounting methodologies toward more accrual-based approaches such as those laid down by IPSAS. While accrual-based approaches can have some advantages in making explicit the full longer-term financial implications of budget decisions and policy programmes. A potential disadvantage is the increased complexity relative to simple cash-based approaches for public finance non-specialists. Accordingly, there is an important role for the SAI in assuring non-specialists of the accuracy and reliability of budgetary accounting, and indeed of communicating the implications of these accounts in understandable terms.

Related to this point, SAIs could potentially have a role to play in informing the national debate on the choice of accounting standards to use, as they are doing in Europe around the possible implementation of European Public Sector Accounting Standards. SAIs are uniquely well-informed in assessing whether an existing traditional accounting framework is "fit for purpose" in informing the citizens and stakeholders about the real position of the public finances, and in providing recommendations – tailored to national circumstances – on what elements of the accounting framework might be modified, perhaps, to reflect international experience or to conform with international accounting standards.

Ensuring quality of budgetary implementation and delivery

- SAIs could assess the effectiveness of the procedures in place for managing, monitoring and overseeing financial allocations, by reference to budgeted appropriations during the phase of budget execution; and the appropriateness of mechanisms in place to facilitate budget flexibility during this phase.

- SAIs could assess whether there are adequate mechanisms in place to generate and capture quality performance information during the phase of budget execution, and advise on how these mechanisms could be improved.

Once resources are allocated and made available for use, it is a matter for budget managers *(a)* to ensure that resources are allocated to the areas authorised *(b)* to ensure that the resources are properly deployed in pursuit of the objectives specified and *(c)* to observe the principles of economy and efficiency in so doing. In most OECD countries, the oversight of budget execution is primarily the responsibility of a central financial office or coordinating unit within a line ministry (vis-à-vis its implementing agencies) or of units within the ministry of finance, which "shadow" the spending of the line ministries.

Monitoring of budget execution is a basic budgetary function not just in terms of keeping account of financial outlays, but also in assessing whether appropriate activities are being generated and objectives achieved. Among the tools at the disposal of budget managers, in responding with agility to the issues arising during the implementation phase, are *virement* (the latitude to switch funds from one budget line to another) and *carry-over* (the ability to bring unspent funds from the budget year forward into the following year). While these tools have the potential to promote better value-for-money, e.g. by discouraging managers from using up all of the allocation when it might be used elsewhere (or in a different time period) to better effect, they are also open to misuse and need to be regulated carefully.

Moreover, the budgetary implementation phase is also the phase when much useful non-financial information could – or should – be generated to assist in the process of management reporting and performance evaluation, as outlined in more detail in the foregoing section. Traditionally, these aspects have not been highlighted during the implementation phase, which has been characterised by a focus on financing service activity. As outlined previously, modern budgeting practice envisages a policy-making cycle in which the data generated during the budget execution phase are used in ongoing evaluation and review work, which in turn feeds into the subsequent round of resource allocation and prioritisation. In each of these areas, there is a potential value-added role for the SAI in assessing the extent to which the basic/traditional and more advanced/modern governance aspects of budgetary implementation are being put in place.

Identification and management of longer-term sustainability and other fiscal risks

- SAIs could assess the integrity and quality of the systems in place for assessing long-term fiscal sustainability, including the effectiveness of these systems for identifying clear policy messages of relevance for the policy-making process.

- SAIs could assess the overall risk-management system within system of public and budgetary governance – including as regards the identification, management and mitigation of fiscal risk.

As outlined above, the management of fiscal risks is an area of budgetary practice that is receiving increased attention in the light of the experiences of the global economic and financial crisis. Related to this is the question of longer-term fiscal sustainability (see above) taking account of demographic and other trends.

In several OECD countries, independent fiscal institutions (IFIs) such as fiscal councils are assigned a role in assessing long-term sustainability; in other countries, such an assessment may be carried out by the ministry of finance or its equivalent. It will normally be beyond the remit of an SAI to conduct such an assessment on its own capacity. However, one common shortcoming in national processes for assessing long-term sustainability is the weak connection between longer-term fiscal issues and the full range of near-term policy messages. In the context of an overall assessment of the quality and soundness of a national fiscal framework, an SAI with foresight capability may be in a position to assess whether the overall approach for identifying long-term sustainability issues (a) is institutionally robust and (b) allows for the discernment of near-term policy signals.

In regards to fiscal risks more generally, including shorter term risks: the assessment of risk-management frameworks should fall within the normal range of activities of an SAI; and in the context of quality budgetary governance, it is natural to consider whether such risk assessment such extend beyond traditional areas of financial management to include broader fiscal risks. This area is related to the question of comprehensive, full and fair budget accounting, which in modern budgeting goes beyond the central government sector to include the full spectrum of assets, liabilities and risks arising from all public agencies, state-supported companies and indeed private bodies in strategic sectors of the economy.

Promoting integrity and quality in budgetary management

- SAIs could audit the annual public accounts of public bodies and of the government as a whole, as to their accuracy, and probity and the effectiveness of the public financial management systems in place.

- SAIs could maintain a public log of the key audit findings and recommendations in respect of each public body and of the government as a whole, and update the log in reference to the actions taken to address the issues arising.

- SAIs could assess the soundness and quality of the overall national framework of budgetary governance in promoting optimal resource allocation, implementation, evaluation and review, including by reference to international norms and practices; and providing advice on how the overall framework might be improved.

The core traditional role of the SAI is of fundamental importance in ensuring the financial probity of the public budgeting system, the accuracy and reliability of public accounts, and the effectiveness of internal governance arrangements including internal audit. This primary quality-assurance role should not be undermined or displaced in any move to extend the breadth of the SAI involvement in public budgeting.

One way of ensuring that audit findings and recommendations have a heightened visibility and impact is by maintaining a log of the key audit findings and tracking/updating the progress made by public bodies in addressing these issues. This practice, adopted for example by the Montenegrin SAI, has proven effective in leveraging the high public standing of the SAI and maintaining pressure on the system of public administration to address issues arising. This issue is also relevant in promoting the transparency of the budget framework (as discussed above), of which the SAI is an integral part.

As outlined in the preceding sections, there is also an over-arching potential role for the SAI beyond core PFM issues, in providing an informed critique of the quality of the overall budgeting framework of budgetary governance, based on the modern understanding of how the elements of budgetary governance are inter-related.

Performance, evaluation and value-for-money

- SAIs could audit the performance of particular programmes as to their effectiveness, efficiency and economy.

- SAIs could assess the quality of performance information used in performance-related budgeting processes, as to its quality, availability and auditability; and advise on how this information could be improved.

- SAIs could assess the soundness of the programme logic models (including Key National Indicators and similar models where these are used) as to their effectiveness in making linkages between resources, results and strategic objectives; as to their evidential basis; and in place in performance-related budgeting processes, as to their evidential basis, and as to the quality of processes in place for developing such models.

SAIs have an established tradition of conducting value-for-money audits and performance audits, and, indeed, INTOSAI has developed standards and principles in this area (ISSAI 3000, 3100). When done effectively, performance audits can generate useful and relevant information that bears directly on the resource allocation process. Traditionally, performance audits have focussed upon issues of economy (i.e. minimising resources consumed), efficiency (i.e. getting the most out of the limited resources available) and effectiveness (i.e. achieving the intended policy objectives).

The challenges faced by an SAI in conducting a performance audit are the same as those faced by public administrations generally in this regard: namely, identifying clearly the objectives of a public programme, identifying and obtaining performance information that is useful and relevant in assessing whether these objectives are being achieved, and gauging whether the proximate objectives (outputs) of a policy programme are logically and efficiently connected to the higher-order objectives (outcomes) of public policy.

As outlined above, countries tend to have difficulty establishing performance information of sufficient quality, robustness and reliability to serve as a sound basis for informing resource allocation decisions. It seems likely that, due to resource and other constraints, and to issues of prioritisation within the legislative mandate, SAIs have not in the past been able to devote the same level of attention to the performance-related aspects of budgeting as to the core financial management aspects. As a result, the discipline and rigour that the audit perspective has instilled in the financial area has not been matched by corresponding levels of quality in the performance sphere. In other words, there has not up to now been the same pressure on administrations to make performance information ‘auditable’ – available, measurable, consistent over time, clearly related to financial allocations and attributable to policy objectives etc. On this theory, a stronger engagement by the SAI on performance-related aspects of budgeting should contribute to higher levels of quality and robustness of performance information frameworks, and thereby increase its relevance and usefulness to policy-makers. For example, the French SAI takes performance, evaluation and value-for-money into account in most of its reports, and in particular, produces an annual report (*Résultats et gestion budgétaire de l'Etat*) on the results and management of the state budget execution that includes an assessment of programmes and policies matched against objectives and performance criteria. It also contains a set of recommendations as well as tracking progress in implementing previous years' recommendations.

Apart from conducting performance audits on the traditional model, an enhanced role for SAIs in promoting quality in this area of budgeting would involve a more fundamental, critical assessment of whether the performance indicators chosen correspond properly to public policy objectives. In other words, the "programme logic model" – the rationale for linking financial inputs for given activities, production of certain outputs and achievement of desired outcomes – should it be criticised about its evidential basis and robustness. In several countries, Key National Indicators have been laid down as a basis for setting and monitoring overall development and strategic objectives of government, and INTOSAI has been actively considering ways in which SAIs can support the quality and impact of the Key National Indicators model. The technical capacity within ministries and agencies to develop such models is also of critical importance: in the absence of robust professional capacity, there will inevitably be a risk that programmes may be designed and justified by reference to prejudices or populist appeals rather than by reference to evidence.

Moreover, all of the above observations apply with equal force to tax expenditures as they do to programme expenditures. Indeed, as set out in the *OECD Best Practices on Budget Transparency* (section 2.2, OECD, 2002), analysis and discussion of tax expenditures should in principle be 'mainstreamed' as part of a discussion of resources in a particular sectoral area. SAIs could play a role in monitoring and, in appropriate cases, challenging whether this principle is being observed satisfactorily in the interests of an informed overall discussion of resource allocation. In the case of Brazil, its SAI has increased its efforts to improve the quality and effectiveness of its engagements in this area, in recognition of its fundamental role in the external control of tax collection policies in Brazil (TCU, 2011).

Notes

[12] Information provided by the SAI of Portugal through a peer review process, May 2014.

[13] Ibid.

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7. REGULATORY POLICY

Effective regulatory governance seeks to maximise the influence of regulatory policy to deliver regulations that will have a positive impact on the economy and society, and which meet underlying public policy objectives. Regulations are indispensable to the proper functioning of economies and societies. They create the "rules of the game" for citizens, businesses, government and civil society. Regulations underpin markets, protect the rights and safety of citizens and ensure the delivery of public goods and services. At the same time, regulations are not costless. Businesses complain that red tape holds back competitiveness while citizens complain about the time that it takes to fill out government paperwork. Regulations can also have unintended costs, that arise when they become outdated or inconsistent with the achievement of policy objectives, for example.

This section focuses on how an SAI can add value to regulatory governance by placing a specific focus on economic regulation. The discussion is guided by the 2012 *Recommendation of the OECD Council on Regulatory Policy and Governance* as well as various International Standards of Supreme Audit Institutions – including ISSAI 5230 *Guidelines on Best Practice for the Audit of Economic Regulation.* The analysis could equally be broadened to focus on other types of regulation (e.g. environmental and social). Indeed, the INTOSAI Working Group on Environmental Auditing (2012) *Improving National Performance: Environmental Auditing Supports Better Governance and Management* is explicit that SAIs can play a role in "providing practical, objective, and rigorous examinations of how environmental and sustainability programs, laws, regulations, and targets are managed, implemented, and monitored at the national and international levels."

This section compliments INTOSAI standards by drawing upon the 2008 OECD indicators of regulatory management systems (OECD, 2009) and a 2012 OECD survey of regulatory policy evaluation, which included specific attention to the role of SAIs in evaluating the performance of regulatory management tools and programmes.[14] The data are supplemented by desk research of publically available audit reports on SAI websites and informal consultation with the SAIs of Brazil, the United Kingdom and the United States.

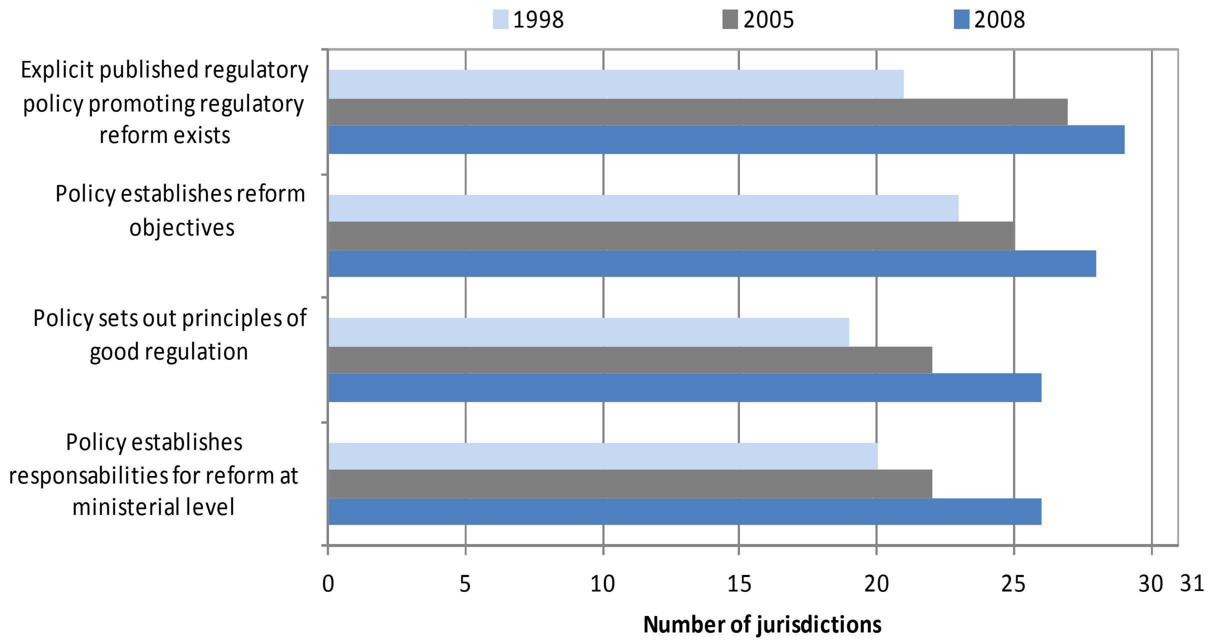
Regulatory governance

The OECD model of regulatory governance is founded on the view that assuring regulatory quality requires an integrated and dynamic approach to the deployment of regulatory institutions, tools and processes. Governments must be actively engaged in assuring the quality of regulation, not reactively responding to its failures. It is often founded in an explicit regulatory policy that there is a permanent need to ensure that regulations and regulatory frameworks are justified and achieve policy objectives. It helps policy makers to reach informed decisions about what to regulate, whom to regulate and how to regulate. Such a policy needs to be adopted at the highest political level, and its importance should be adequately communicated across the administration and to lower levels of the government. Regulatory governance also recognises the roles of a wider domain of players including the Legislature, the judiciary, sub-national and supranational levels of government and international standard setting activities, including those of the private sector.

Attempting to neatly classify any approach to governance is a challenge. The OECD has developed and reassessed principles on regulatory policy and governance, drawing on over twenty years' experience. These principles – the 2012 *Recommendation of the OECD Council on Regulatory Policy and Governance* – represent aspirational goals for governments to pursue. The principles are the results of careful assessments of best practices identified by the Regulatory Policy Committee through two decades of policy dialogue. The Recommendation builds upon previous OECD instruments on regulatory policy, including the 1995 *Recommendation of the OECD Council on Improving the Quality of Government Regulation*, (1997) "Policy Recommendations on Regulatory Reform", and (2005) *Guiding Principles for Regulatory Quality and Performance.* The principles and guidelines aim to share the results of the OECD experience, and to foster good practices in terms of processes for preparing and issuing new regulations as well as tools and policies to improve the stock of existing regulations (Box 7.1).

A growing understanding of the need for effective regulatory governance has led OECD members and many other countries to articulate their own regulatory policies (Figure 7.1). However, while indicators reveal the broad lines of regulatory policy development, closer examination reveals that a country's regulatory policy often consists not of one but of a series of often disjointed regulatory policies. For example, policies to tackle administrative burdens in existing regulations may not be fully joined up with policies for the *ex-ante* impact assessment of new regulations.

Figure 7.1**. Adoption of explicit regulatory policy in OECD member countries and EU**



Notes: The sample includes 31 jurisdictions for 2008 and 2005. For 1998, 27 jurisdictions are included as no data were available for the EU, Luxembourg, Poland and Slovak Republic.

Source: OECD (2009), *Regulatory Policy Committee, Indicators of Regulatory Management Systems, 2009 Report*, OECD, Paris. www.oecd.org/gov/regulatory-policy/44294427.pdf

Box 7.1. **2012 *Recommendation of the OECD Council on Regulatory Policy and Governance***

The Council recommended that Members:

1. Commit at the highest political level to an explicit whole-of-government policy for regulatory quality. The policy should have clear objectives and frameworks for implementation to ensure that, if regulation is used, the economic, social and environmental benefits justify the costs, the distributional effects are considered and the net benefits are maximised.
2. Adhere to principles of open government, including transparency and participation in the regulatory process to ensure that regulation serves the public interest and is informed by the legitimate needs of those interested in and affected by regulation. This includes providing meaningful opportunities (including online) for the public to contribute to the process of preparing draft regulatory proposals and to the quality of the supporting analysis. Governments should ensure that regulations are comprehensible and clear and that parties can easily understand their rights and obligations.
3. Establish mechanisms and institutions to actively provide oversight of regulatory policy procedures and goals, support and implement regulatory policy, and thereby foster regulatory quality.
4. Integrate Regulatory Impact Assessment (RIA) into the early stages of the policy process for the formulation of new regulatory proposals. Clearly identify policy goals, and evaluate if regulation is necessary and how it can be most effective and efficient in achieving those goals. Consider means other than regulation and identify the trade-offs of the different approaches analysed to identify the best approach.
5. Conduct systematic programme reviews of the stock of significant regulation against clearly defined policy goals, including consideration of costs and benefits, to ensure that regulations remain up to date, cost justified, cost effective and consistent and deliver the intended policy objectives.
6. Regularly publish reports on the performance of regulatory policy and reform programmes and the public authorities applying the regulations. Such reports should also include information on how regulatory tools such as RIA, public consultation practices and reviews of existing regulations are functioning in practice.
7. Develop a consistent policy covering the role and functions of regulatory agencies in order to provide greater confidence that regulatory decisions are made on an objective, impartial and consistent basis, without conflict of interest, bias or improper influence.
8. Ensure the effectiveness of systems for the review of the legality and procedural fairness of regulations and of decisions made by bodies empowered to issue regulatory sanctions. Ensure that citizens and businesses have access to these systems of review at reasonable cost and receive decisions in a timely manner.
9. As appropriate, apply risk assessment, risk management, and risk communication strategies to the design and implementation of regulations to ensure that regulation is targeted and effective. Regulators should assess how regulations will be given effect and should design responsive implementation and enforcement strategies.
10. Where appropriate, promote regulatory coherence through co-ordination mechanisms between the supranational, national and sub-national levels of government. Identify cross-cutting regulatory issues at all levels of government, to promote coherence between regulatory approaches and avoid duplication or conflict of regulations.

Box 7.1. **2012 *Recommendation of the OECD Council on Regulatory Policy and Governance*** (*cont.*)

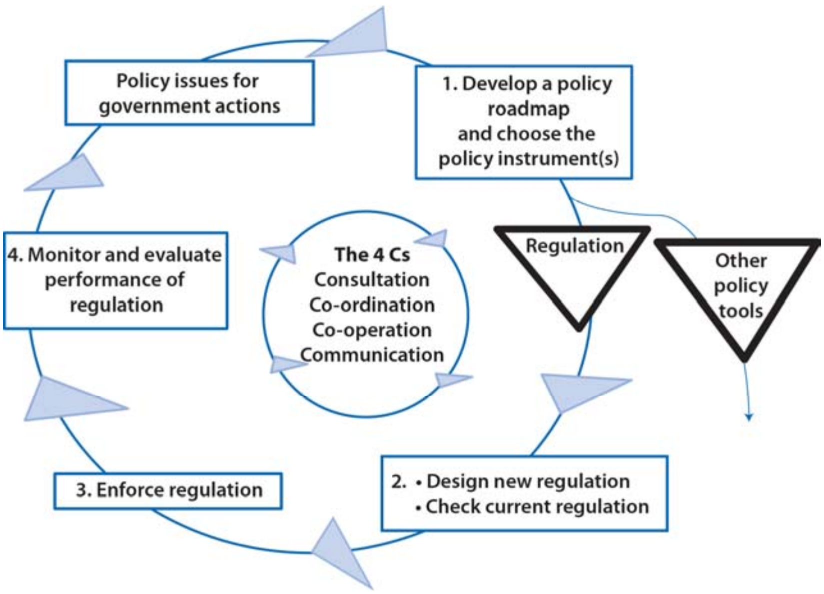
11. Foster the development of regulatory management capacity and performance at sub-national levels of government.
12. In developing regulatory measures, give consideration to all relevant international standards and frameworks for co-operation in the same field and, where appropriate, their likely effects on parties outside the jurisdiction.

Source: OECD (2012), *Recommendation of the Council on Regulatory Policy and Governance*, C(2012)37, 22 March 2012, www.oecd.org/gov/regulatory-policy/49990817.pdf

The regulatory governance cycle

Effective regulatory governance involves the co-ordination of regulatory actions, from the articulation of policies and the design of regulations, to their implementation and enforcement, to closing the loop with monitoring and evaluation in order to inform the development of new regulations and the adjustment of existing regulations. Figure 7.2 depicts an ideal state in which the different actions of effective regulatory governance are co-ordinated. It highlights a number of critical points: (i) policy making is closely linked to regulatory design but the two are not synonymous with one another; (ii) regulatory governance is a dynamic and continuous process; and (iii) integrating and joining up the various functions in not just a matter of processes, but of institutions.

Figure 7.2**. The regulatory governance cycle**



Note: Different jurisdictions may use different vocabulary to express the functions depicted in the figure, which are not always easily translatable. They are so closely associated with the country context that some terms take on a country specific meaning. For example, in Europe, enforcement may also be referred to as supervision, inspection or execution

Source: OECD (2011), *Regulatory Policy and Governance: Supporting Economic Growth and Serving the Public Interest*, OECD Publishing.

Of particular significance in the depiction of the policy cycle in other parts of this framework is the difference between policy formulation and regulatory design. Indeed, there are two distinct steps: defining which policy instrument is appropriate and, if regulation is the policy option that offers the greatest net benefit, providing the attention to assure necessary regulatory quality.

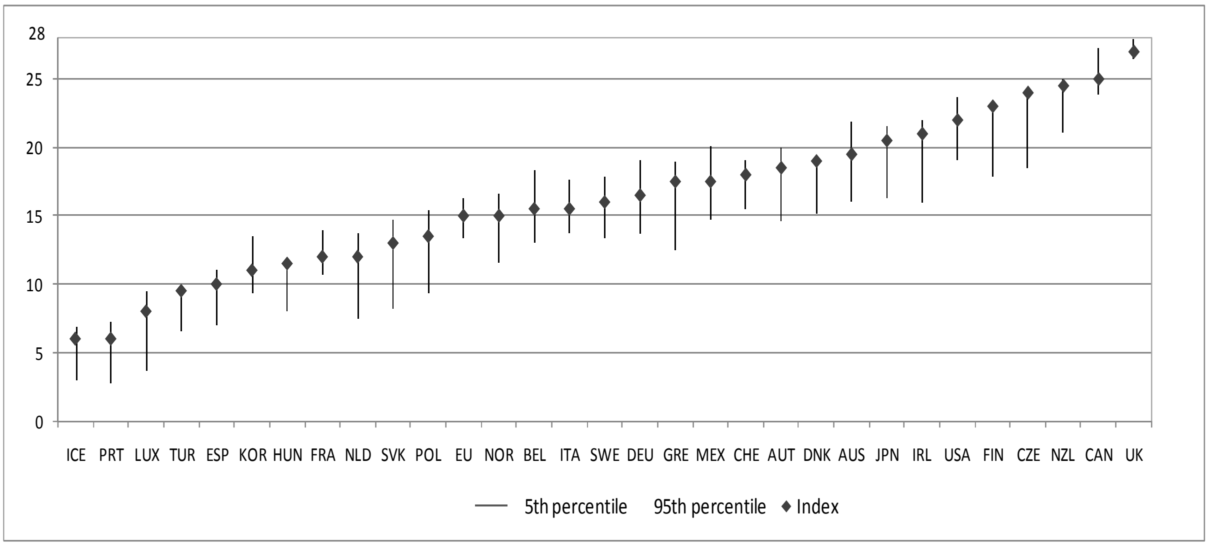
Not every policy issue can be solved by government. The government should only intervene if there is a genuine need for it to take responsibility for the problem. There are a number of situations that justify direct government intervention such as market failure (e.g. imbalance in market power generating inefficient outcomes or where information is inherently asymmetric) where there are externalities emerging from the economic activities of one organisation on another. However, government policy may be more effectively achieved through no regulatory action whatsoever (e.g. information and education campaigns, market-based instruments including taxes and tradable permits), or even the better enforcement of existing regulation. Where regulation is the best solution, there are multiple approaches such as quasi-regulation (e.g. codes of practice, guidance notes, accreditation schemes), co-regulation (i.e. where industry develops and administers its own arrangements and the government provides the underpinning regulation to enforce it) or explicit government regulation – though each option is not able to acceptably manage risks in public policy making.

Regulatory design refers to the explicit design of regulation, i.e. once a decision has been taken that regulation is the policy option that offers the greatest net benefit. Regulatory design ensures that regulation is most effectively, and cost-effectively, designed to support the policy objective, and that a clear implementation and evaluation plan is established from the outset. Regulatory cost-effectiveness relates to all of the costs attributable to the adoption of regulatory requirements. Among these costs, specific attention often focuses on what compliance costs are, i.e. those incurred by business or other parties at whom regulation may be targeted in undertaking actions necessary to comply with regulatory requirements (OECD, 2014). A clear implementation and evaluation plan ensures that there is a shared understanding of how the governments will ensure compliance and enforce the regulation, and how the continued relevance of government regulation will be assessed.

Challenges affecting regulatory governance

Reviews, surveys and roundtables on regulatory reform have confirmed that the 2012 *Recommendation of the OECD Council on Regulatory Policy and Governance* is very much aspirational and that there is much heterogeneity of a country's achievement of the spirit of this recommendation. The scope for improvement in adopting good practices, in terms of processes for preparing and issuing new regulations as well as tools and policies to improve the stock of existing regulations, is illustrated by the OECD's periodic surveys of indicators of regulatory management systems. The most recent survey, in 2008, demonstrated that there had been progress but also that there remained much that could be done (OECD, 2009), for example in the extent of regulatory impact assessment (Figure 7.3), the use of *ex-post* review and evaluation (Figure 7.4) and the mechanism for coordination of regulatory policy between different tiers of government (Figure 7.5).

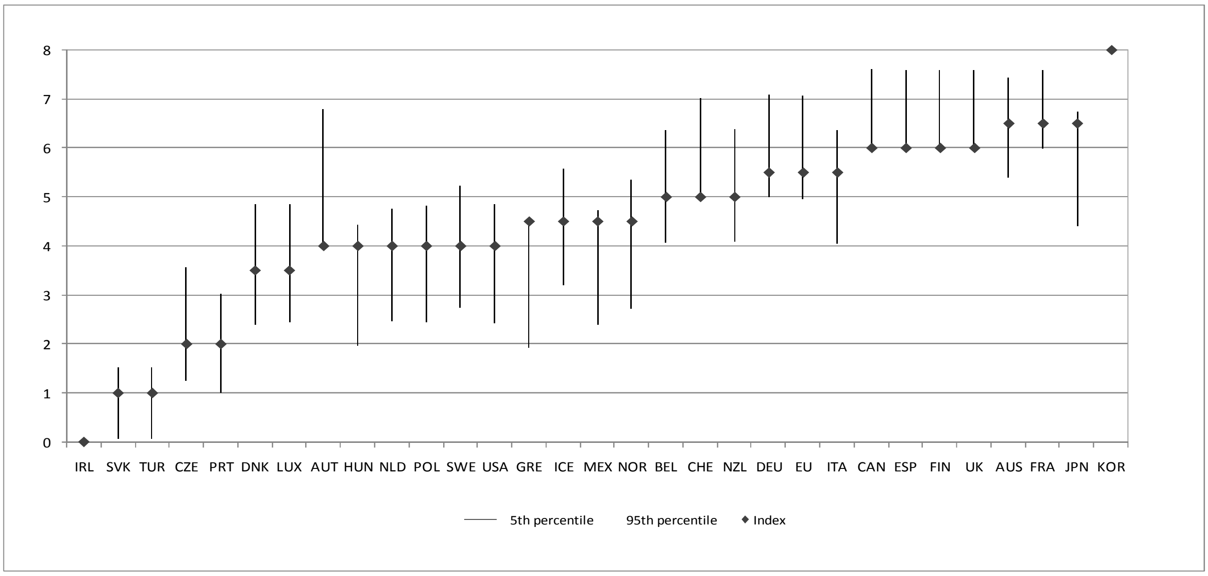
Figure 7.3. **Extent of regulatory impact assessment processes in OECD member countries and in the EU (2008)**



Notes: This graph summarises information about the extent of RIA processes in OECD member countries. It does not gauge whether these processes have been effective. The vertical scale is a composite on a scale of 0 to 28 of a range of measures of aspects of the regulatory impact assessment system in each country.[15]

OECD (2009), *Regulatory Policy Committee, Indicators of Regulatory Management Systems, 2009 Report,* OECD, Paris. www.oecd.org/gov/regulatory-policy/44294427.pdf

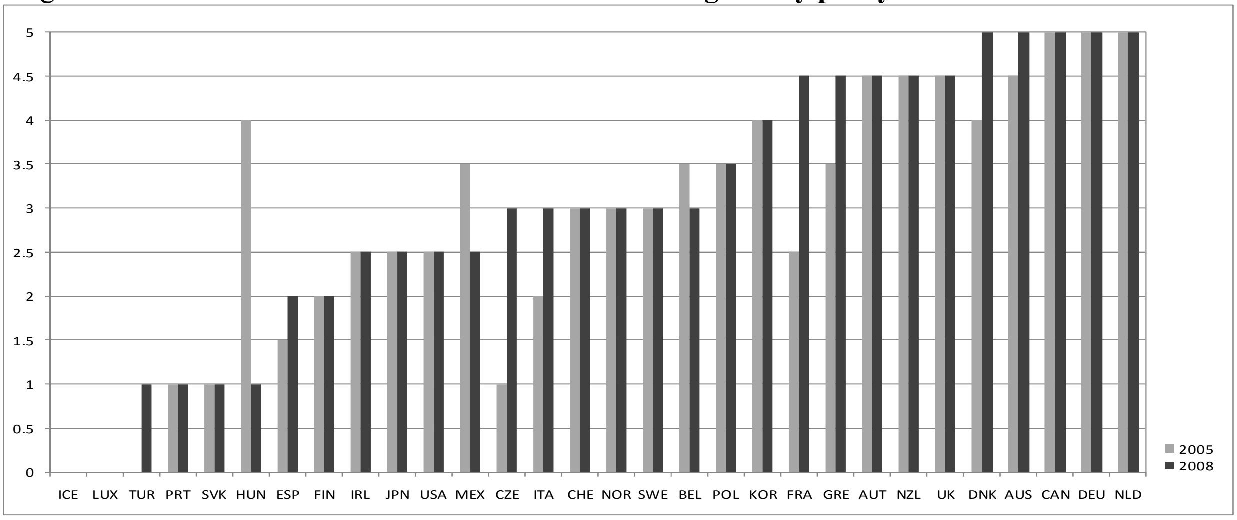
Figure 7.4. **Mechanisms for *ex-post* regulatory review in OECD member countries and in the EU (2008)**



Notes: This graph summarises information about dynamic processes of update and evaluation of existing regulations in OECD jurisdictions. It does not gauge whether the efforts made by these countries have been effective. The vertical scale is a composite on a scale of 0 to 8 of a range of measures of the *ex-post* regulatory review mechanisms in each country.[16]

OECD (2009), *Regulatory Policy Committee, Indicators of Regulatory Management Systems, 2009 Report,* OECD, Paris. www.oecd.org/gov/regulatory-policy/44294427.pdf

Figure 7.5. **Multi-level co-ordination mechanisms for regulatory policy in OECD member countries**



Notes: This figure summarises information about the existence of formal co-ordination mechanisms between national/federal and state/regional governments with respect to regulatory policy. It does not provide information on their effectiveness. Vertical scale is a composite on a scale of 0 to 5 of a range of measures of aspects of the formal co-ordination mechanisms in each country. This question is not applicable to the European Union.[17]

OECD (2009), *Regulatory Policy Committee, Indicators of Regulatory Management Systems, 2009 Report,* OECD, Paris. www.oecd.org/gov/regulatory-policy/44294427.pdf

Assessing indicators on the implementation of regulatory policy programmes and tools over time can provide an overview of the progress made towards full implementation of a coherent and effective regulatory policy. Indicators can also help to demonstrate measurable improvements that can be attributed against particular activities, and help highlight areas for improvement. While half of OECD members publish performance indicators on administrative simplification and burden reduction programmes (17) and one-third on the performance of RIA (11), only five countries have indicators for consultation (Table 7.1). However, a number of countries indicated that they have performance indicators for several regulatory tools and programmes available internally only. Most of these internally available indicators refer to the functioning of RIA (9) and consultation (9), some to administrative burden reduction/simplification programmes (8), and only very few to *ex-post* analysis (3).

Table 7.1. **Countries publishing indicators by policy tools and programme in OECD countries and the EU (2012)**

	Publicly available indicators on the functioning of:			
	Regulatory Impact Analysis (RIA)	Consultation practices on draft regulations	Ex-post analysis/reviews of existing regulation	Administrative simplification and burden reduction programmes
Australia	●	❍	●	❍
Austria	❍	❍	❍	●
Belgium	●	❍	❍	●
Canada	❍	❍	❍	❍
Chile	❍	❍	❍	❍
Czech Republic	❍	❍	❍	●
Denmark	❍	❍	❍	●
Estonia	❍	●	❍	❍
EU	●	●	❍	●
Finland	●	❍	❍	●
France	❍	❍	❍	❍
Germany	❍	❍	❍	❍
Greece	❍	❍	❍	❍
Hungary	❍	❍	❍	❍
Iceland	❍	❍	❍	❍
Ireland	❍	❍	❍	❍
Israel	❍	❍	❍	❍
Italy	●	❍	❍	●
Japan	❍	●	❍	❍
Korea	❍	❍	❍	❍
Luxembourg	❍	❍	❍	❍
Mexico	●	❍	❍	●
Netherlands	❍	❍	❍	●
New Zealand	●	❍	❍	❍
Norway	❍	❍	❍	❍
Poland	❍	❍	❍	●
Portugal	❍	❍	❍	●
Slovak Republic	❍	❍	❍	●
Slovenia	●	●	❍	❍
Spain	❍	❍	❍	❍
Sweden	●	❍	❍	●
Switzerland	●	❍	❍	●
Turkey	❍	●	❍	●
United Kingdom	●	❍	❍	●
United States	❍	❍	❍	●
OECD34+EU	**11**	**5**	**1**	**17**

● - Yes
❍ - No

Source: OECD Survey on Regulatory Policy Evaluation (database).

More broadly, beyond tools and processes, emerging themes and challenges of regulatory policy appear to centre on four essential areas:

- Closing the regulatory governance cycle: regulatory implementation and enforcement remain the weakest link in regulatory governance. There is still large potential to improve inspections and use new approaches to regulatory design – such as behavioural economics – to foster better compliance.

- Empowering the players of regulatory governance: the landscape of regulatory players is rich and there is no blueprint or ideal institutional arrangement for regulatory reform. However, there are missed opportunities in the institutional set up of countries to promote regulatory reforms. There is untapped potential of traditional actors and the emerging state and non-state actors, including at the international level.

- Promoting evidence-based policy: many countries are still in the process of developing the tools that can support the identification of the trade-offs, costs and benefits of alternative regulatory reforms upon which countries can base their societal choices. The evidence on the impact of using alternative regulatory policy tools and approaches remains very elusive.

- Addressing better regulation beyond the border: regulators cannot afford to act in isolation anymore. They are impacted by the regulatory activity of other jurisdictions. Their own activity may have direct or indirect effects on trade and investment flows. However, ensuring efficient regulatory policy in an interconnected world remains a challenge, and one also related to the limited spread of regulatory policy beyond a handful of OECD countries.

The role of SAIs

A wide range of actors are involved in the regulatory governance cycle, including Legislatures, regulatory oversight bodies, regulatory bodies, and other tiers of government as well as non-government actors (e.g. private sector and civil society). However, SAIs are not typically considered by the Executive as a key actor at any particular stage of the regulatory governance cycle. The Executive from only five out of 24 OECD member countries considered that SAIs have a role in evaluating regulatory governance (Table 7.2). The notion that SAIs are only involved in the evaluation stage of the regulatory governance cycle would most likely be reasserted by SAIs themselves. SAIs do not normally have a role in deciding questions of policy and design, which are matters for the Executive and legislative branches that have the electoral mandate to do so. Moreover, SAIs are also often concerned that to advise on matters of policy, design and implementation might affect their real or perceived independence when conducting evaluation.[18] The potential role of SAIs may also be affected by the existence of other types of oversight bodies focussed on regulatory policy.

Table 7.2**. The reported actors at each stage of the regulatory cycle in OECD member countries**

24 responding OECD member countries

Number of countries reporting involvement of actors at the stages				
	Stage 1: Set policy	Stage 2: Design	Stage 3: Enforce/ implementation	Stage 4: Evaluate
Parliament	7	6	2	4
Government collectively (e.g. cabinet or president)	19	6	4	6
Individual ministries acting within their policy areas	15	20	14	15
National government body co-ordinating or overseeing regulatory proposals	17	20	6	10
Regulators	3	9	17	9
Supreme audit institution (SAI)	0	0	0	5
Other (subnational) tiers of government	4	7	7	5
Civil society (business, citizens, etc.)	3	8	0	3

Source: OECD (2013), "The Institutions and Key Players of Regulatory Reform: Survey of OECD Members - Results and Analysis," Roundtable on Regulatory Reform for Inclusive Growth, GOV/RPC(2013)11, 12 November 2013

A further reason why SAIs may not be perceived to have such a prevalent role in the regulatory governance cycle is because not all of these actors are subject to audit by the SAI. For example:

- SAI audit work is normally focussed on the activity of the Executive branch. Decision making by the Legislature and civil society is not normally within the scope of an SAI's review.

- Regulatory enforcement is often the responsibility of a body separate from the ministries that develop policy, and design and evaluation is often a joint activity between both ministries and regulators. This separation can reflect a deliberate intention to ensure regulators are independent of government, for example in the case of economic regulators of infrastructure industries.

- Independent national regulators may be set up in a form that means that they are not subject to audit by the SAI. For example, in the UK, the statutory regulators of professionals working in health services are not supported by public funds and appoint their own commercial auditors.

- Depending on the public audit arrangements in place, public bodies in sub-national tiers of government may not be audited by the SAI. This is frequently the case in federal countries (e.g. Australia, Canada, Germany, Mexico and the United States).

However, in relation to the issue of sub-national tiers of government, the absence of an SAI mandate need not be a limitation on appropriate scrutiny. SAIs need to be alive to the constitutional implications of scrutinising, on behalf of the national Legislature, the exercise of power by sub-national tiers of government. Typically, alternative forms of audit, and accountability to an elected body, have been provided at the sub-national level. Often, however, sub-national tiers are implementing regulation designed to a greater or lesser degree by national bodies. Where this is the case, the sub-national tiers concerned may have the information needed to make an assessment of the performance of the national bodies – for example, its design of the regulations concerned and the policy choices made when they were designed. Accordingly, SAIs will need to be able to engage with sub-national tiers of government and their auditors, even when they are not the auditors themselves.

Ultimately, the role of SAIs in contributing to the regulatory governance cycle will depend on their mandate. The 2012 OECD survey on regulatory policy evaluation found that around half of the countries reported that their SAIs had a mandate to review regulatory management tools or programmes and just over a third reported that their SAIs had done so (Table 7.3).

SAIs mandates not only cover the scope of their audit powers but the types of audit and non-audit engagements. Where regulatory bodies[19] are subject to financial and compliance audit, engagement is likely to be regular and routine. Through these audit assignments, the governance of the regulatory body may potentially be a part of the audit subject matter – for example, as a way of checking whether expenditure is in accordance with relevant authorities. However, regulatory governance – the processes governing the formulation of regulatory policy and practice – is likely to be germane only to the extent that it gives rise to public expenditure.

Table 7.3 **Mandate and activities of audit offices in relation to regulatory policy (2012)**

	The audit office has...		
	the mandate to review regulatory management tools and/or programmes	actually undertaken a review of regulatory management tools and/or programmes	actually undertaken a review of the performance of regulators or inspection authorities
Australia	1	1	1
Austria	1	1	0
Belgium	0	0	0
Canada	1	1	0
Chile	0	0	0
Czech Republic	0	0	0
Denmark	1	1	0
Estonia	1	1	0
EU	1	1	1
Finland	1	1	0
France	1	1	1
Germany	1	1	0
Greece	0	0	0
Hungary	0	0	0
Iceland	0	0	0
Ireland	0	0	0
Israel	0	0	0
Italy	1	0	0
Japan	0	0	0
Korea	0	0	0
Luxembourg	0	0	0
Mexico	0	0	1
Netherlands	1	1	0
New Zealand	1	0	1
Norway	1	0	0
Poland	0	0	0
Portugal	-	-	-
Slovak Republic	0	0	0
Slovenia	1	1	1
Spain	0	0	0
Sweden	1	1	1
Switzerland	1	1	0
Turkey	-	-	-
United Kingdom	1	1	1
United States	0	0	0
OECD34+EU	**17**	**14**	**8**

Notes: 1 = Yes, 0 = No. Answers from Portugal and Turkey not available.

Source: Adapted from OECD Survey on Regulatory Policy Evaluation (database).

Performance audit involves a greater degree of judgement and flexibility on the part of the audit, and it is possible to identify at least three ways in which it can examine regulatory issues:

- Performance audit of regulatory policy and governance (e.g. use of impact assessment, administrative burdens reduction programme, etc.);

- Performance audit of regulators (e.g. performance of regulatory in achieving their operational objectives, having regard to public sector resources consumed); and

- Performance audit of regulations (e.g. considering also, or instead, achievement of the benefits sought through the adoption of the regulations, and taking into account the consumption of non-public sector resources, such as compliance costs – the cost to regulated entities and others of complying with the regulations).

In addition, various SAIs have mandates to perform a range of other work. ISSAI 100 recognised that SAIs may carry out audits or other engagements on any subject of relevance to the responsibilities of management and those charged with governance and the appropriate use of public resources. These engagements may include reporting on the quantitative outputs and outcomes of the entity's service delivery activities, sustainability reports, future resource requirements, adherence to internal control standards, real-time audits of projects, or other matters (INTOSAI, 2013). SAIs continue to acquire such responsibilities as in Australia, for example. In December 2011, amendments to the 1997 Auditor-General Act provided the Auditor-General with the explicit authority to conduct audits of the appropriateness of agencies' key performance indicators and the completeness and accuracy of their reporting. Given the number of countries publishing indicators on the implementation of regulatory policy programmes and tools (Table 7.1), SAIs could also potentially audit the reliability of this information.

In 2001, INTOSAI adopted ISSAI 5230 *Guidelines on Best Practice for the Audit of Economic Regulation.* It followed recognition by the XVI INCOSAI that economic regulation of both privately and publicly owned businesses was a growing area of importance for governments and citizens. ISSAI 5230 defines economic regulation as the exercise by the state, either directly or indirectly, of control and influence over publicly and privately owned suppliers of services to consumers. Economic regulation addresses a number of objectives, some of which are in competition with one another. This could include, for example, protecting consumers from abuse by monopoly suppliers while seeking to ensure that suppliers are able to finance the provision of essential services, such as utilities, public transport and financial services, to specified standards. In the case of competitive markets, the economic regulator's attention is focussed on securing adequacy and transparency in the provision of information by suppliers to assist consumers in making informed choices, monitoring the financial standing of suppliers and acting against anti-competitive practices. The range of business activities covered by economic regulators is vast, directly affecting the vital interests of all citizens (INTOSAI, 2001).

ISSAI 5230 highlights a series of key questions that SAIs are likely to need to address when examining the efficiency and effectiveness with which economic regulators set about their tasks. In recommending these guidelines, INTOSAI's working group recognised that economic regulation was an evolving concept, practised in a variety of ways in different countries with different constitutions and at different stages of development. The working group, therefore, advised that the guidelines may need to be applied with regard for the particular circumstances of different countries with appropriate modifications to take account of the state of development there (INTOSAI, 2001). However, compliance with ISSAI 5230, and ISSAIs more broadly, is "voluntary" given that SAIs operate under different mandates and models, which are matters for each country to determine - though ISSAI 12 encourages SAIs to apply the ISSAIs and to assess their compliance with such provisions in a manner that is most appropriate for their respective environments (INTOSAI, 2013).

This section is based on a review of available information of work on regulatory issues carried out by SAIs in recent years. The examination focusses mainly on performance audit and distinguished between two main categories of audit:

- Audits of regulatory policy and governance. As regulatory policy and governance is usually formulated at a government level and applied across most or all of central government bodies, such audits tended to look across government as a whole. In some cases, audits focus detailed examinations on only a small number of ministries, for example, to reduce the cost of the audit.

- Audits of regulators or regulations. In most cases these concentrated on a single public body – typically the regulator – but some examined several, for example, when they needed to work together in the operation of the regulatory system.

In addition, this section reviews other work carried out by SAIs with a bearing on regulatory management such as good practice guidance, counselling work and testimony in Parliament, among others. The examination subsequently assesses the extent to which SAIs' work addresses each of the 12 principles set out in the 2012 *Recommendation of the OECD Council on Regulatory Policy and Governance* and to the different phases of the regulatory governance cycle.[20]

Audits of regulatory policy and governance

Examination of SAIs' websites identified 12 SAIs that had examined aforementioned regulatory issues since 2005, two of which[21] had published reports on the subject within the last year.[22] The 12 SAIs identified largely corresponded to the 13 SAIs reported in the 2012 OECD survey but the overlap was not complete. As can be seen from Table 7.1, most of the reports were in the areas of *ex-ante* impact assessment or *ex-post* administrative simplification. In addition, the most recent work by the SAI of the United States examined regulatory impacts, but the GAO had also examined international regulatory co-operation earlier in the year (GAO, 2014) and has built up a large and varied body of work on regulatory governance and policy over the years. In 2005 the Netherlands' SAI had examined regulatory enforcement, and both SAIs also have done earlier work in either Impact Assessment or administrative simplification. Between 2008 and 2010 the United Kingdom's NAO worked with the United Kingdom's Better Regulation Executive to publish 12 reports on different regulators' implementation of the recommendations of the 2005 Hampton Report on regulatory inspection and enforcement.

Audits of regulators or regulations

Some evidence on the extent of SAIs' work on regulators is available from discussions at the VIII Congress of the EUROSAI in Lisbon in 2011. Prior to the Congress, a survey had been conducted of European SAIs. The survey focussed on SAIs' work on economic regulators, such as competition authorities, financial regulators and regulators of infrastructure industries. Four key points of the survey are detailed below.

- All 23 SAIs responding reported that they had a mandate to conduct financial audits of regulators. But some restrictions were imposed on performance audits in the countries where the central bank has regulatory functions. In two countries the SAI was not allowed to audit the central bank at all, and in two others only the financial management could be audited.

- Financial audits were the most frequent types of audits of regulators but more than half of SAIs responding had conducted performance audits of regulators, reporting that SAIs had conducted a total of 50 audits between 2008 and 2010.

Box 7.2. **Summary of recent SAI audit reports on regulatory policy and governance between 2005-2014 based on an Internet search**

Austria (Rechnungshof – Court of Audit): *Verwaltungsreforminitiative - Register der Bundesverwaltung* [Administrative Reform Initiative - the Federal Register]. Published in May 2012.

Belgium: *La stratégie de simplification administrative en Région wallonne* [The Administrative Simplification Strategy in the Walloon Region]. Published in May 2014.

Denmark (National Audit Office of Denmark): *The Impact of Better Regulation and Simplification*. Published in February 2007.

Estonia (Riigikontroll – National Audit Office of Estonia): *The State of Affairs with the Legislative Impact Assessment - Does a Legislator Know What the Consequences of its Decision are?* Published October 2011.

European Court of Auditors (ECA): *Impact Assessments in the European Union Institutions: Do They Support Decision-making?* Published September 2010.

European Court of Auditors (ECA): *Are Preferential Trade Arrangements Appropriately Managed?*

Finland (*Valtiontalouden Tarkastusvirasto - Valtiontalouden Tarkastusvirasto*): *Evaluation of the Economic Impacts of Legislative Projects*. Published 2011.

Germany (Bundesrechnungshof - Court of Audit, Germany): *Report by the Federal Performance Commissioner: Opinion on Steps Taken to Enhance Regulation and Improve Legislation in Place.* Published November 2010.

Korea (Korean Board of Audit and Inspection): Regulatory Reform Policy 1125/2009

Korea (Korean Board of Audit and Inspection): Economic Regulation Reform 0813/2007

Netherlands (Algemene Rekenkamer - Court of Audit): *Reducing the Administrative Burden on Business*. Published June 2006.

Norway: *The Office of the Auditor General's Investigation of State Supervisory Activities*. Published March 2014.

Sweden (Riksrevisioner - Swedish National Audit Office): *Simplifying Company Regulations – the Government Still has a Long Way to Go*. Published March 2012.

United Kingdom (National Audit Office): *Delivering Regulatory Reform.* Published February 2011.

United States (Government Accountability Office): *Regulatory Review Processes Could Be Enhanced*. Published March 2014.

- Most performance audits had been of infrastructure regulators, followed by competition and consumer protection regulators. Audits of financial regulators had been least common, possibly because of the limited mandate for SAIs in some countries to audit central banks which have regulatory functions.
- Due to the specialised issues audited in regulatory authorities, some SAIs reported that they had contracted out the audits or used the services of external experts. A methodological challenge, also highlighted by some regulators, was that of determining indicators of outcomes that reflected regulators' statutory or other duties; and recognising the fact that outcomes are usually influenced by other factors as well as the regulator's actions (EUROSAI, 2011).

In the 2012 OECD survey on regulatory policy evaluation, seven countries reported that their SAIs had carried out reviews of the performance of regulators or inspection authorities (Table 7.3). However, the website search found a number of others as having done so in recent years (Table 7.4). Examination of SAIs' websites identified a total of 21 SAIs that had published information on reviews since 2005 either of regulators, or of policies in which regulation played a significant part (Table 7.4), of which 10 had done so in the last year. The subject matter of these reviews varied considerably, reflecting the wide range of activities that governments seek to influence through regulation. Table 7.5 shows the subjects addressed by the 10 SAIs having produced such reports in the last year – and of course over longer periods the variety is even greater.

Table 7.4. **Supreme Audit Institutions (SAIs) auditing regulators or regulations since 2005**

Australia	Finland	Netherlands	Slovenia
Austria	Germany	New Zealand	Sweden
Belgium	Greece	Norway	Turkey
Brazil	Hungary	Poland	United Kingdom
Canada	Ireland	Portugal	United States
European Union			

Source: OECD desk research

Table 7.5. **Subject matter of Supreme Audit Institution (SAI) audits of regulations or regulators in last year**

Country	Title of report
Australia	Administration of the Improving Water Information Program The Regulation of Tax Practitioners by the Tax Practitioners Board
Belgium	The functioning of the Belgian Gaming Commission
Canada	Canada's Food Recall System Oversight of Rail Safety—Transport Canada
France	Labor market: faced with high unemployment, better target policies
Hungary	Audit on the operation and financial management of the Hungarian competition authority
Netherlands	Supervision of the Netherlands food and consumer product safety authority following the merger Wadden area: nature protection, nature management and spatial planning Coordinated audit on the enforcement of the European Waste Shipment Regulation – (Joint report based on eight national audits (including by SAIs of 6 other OECD members) Quality control in higher education in the Netherlands and Flanders: follow-up audit 2013 (in conjunction with Belgium) Sustainable intensive livestock farming: follow-up audit 2013 Quality Indicators in the Care Sector
Poland	Civil Aviation Office
Portugal	Regulation of PPP in the Sector of Water
Slovenia	Trans-boundary Movement of Waste
Sweden	The government and the telecom market The State in the Electricity Market – Interventions for a Functional Electricity Transmission System
United Kingdom	Regulating financial services 4G radio spectrum auction: lessons learned The regulatory effectiveness of the Charity Commission The Levy Control Framework Infrastructure investment: the impact on consumer bills
United States*	Countries' Regulatory Bodies Have Made Changes in Response to the Fukushima Daiichi Accident Energy Infrastructure Risks and Adaptation Efforts Drinking Water: EPA Has Improved Its Unregulated Contaminant Monitoring Program, but Additional Action Is Needed Fair Labor Standards Act: The Department of Labor Should Adopt a More Systematic Approach to Developing Its Guidance Clean Water Act: Changes Needed If Key EPA Program Is to Help Fulfill the Nation's Water Quality Goals Air Emissions: Status of Regulatory Activities and Permitting on Alaska's Outer Continental Shelf - Jan 2014

Notes: Data for the United States is limited to a review of three months only because of the volume of reports produced.

The economic regulators of utilities are a common subject of such reports, reflecting the significance of their activities both for economic performance and development, and for issues such as the environment and national energy security. Several of the audits reported in Table 7.5 touch on the work of such regulators. Since the early 2000s, the SAI of Brazil has had a particularly large programme of work on such issues, focussing particularly on energy, telecoms and roads (Box 7.3).

Box 7.3. **Audits of infrastructure regulation by the supreme audit institution (SAI) of Brazil**

Articles 70 and 71 of the Federal Constitution provide for oversight of regulatory agencies by the SAI of Brazil, the Tribunal de Contas da União (TCU). Pursuant to these articles, the TCU undertakes performance audits and renders accounts of those who manage public goods and values. The oversight of regulated sectors aims to verify regularity, efficiency, transparency and improvement of federal infrastructure sector management. This improvement may derive from the regulatory agencies and from bodies that develop public policies and plan services expansion and operation.

Some recent activities of the TCU are discussed below.

The oil and gas sector

The TCU assesses the management of regulatory agencies and entities in the oil sector. Through audits, it also evaluates their performance and monitors compliance with applicable legal standards.

TCU oversees all public bids granting oil and gas exploratory blocks, held periodically by the National Petroleum, Natural Gas and Biofuel Agency (ANP). TCU monitors, under the guidelines provided in Internal Rule nº 27/1998, the adequacy of studies of economic and financial feasibility, which establish signature bonuses. It also monitors contract compliance which should be inspected by the respective regulatory agency and concessions of gas transportation and storage. TCU approval is not required for the bidding process to proceed but involvement at this stage means the TCU can alert government to any deficiencies while there is still time to rectify them. Amongst this work, TCU oversaw the auction of the largest oil field in the so-called pre-salt area, in which the subscription bonus for this field reached USD 7 billion.

Reviews and readjustments of electric power distribution tariffs

The TCU monitors the periodical tariff reviews of concession contracts for power distribution. The main purpose of this oversight is to verify consistency in the methodological criteria used, considering regulation principles such as moderate tariffs. It involves the evaluation of methodology, studies and procedures uniformly applied by the National Electric Energy Agency (Aneel) to all concessionaires during a review cycle (four years). TCU also monitors, on a yearly basis, the use of this methodology in some specific tariff review processes.

Following its oversight of tariff reviews during the first cycle, between 2003 and 2006, the TCU issued recommendations and determinations to Aneel. Those were related to an early stage of the tariff review process and the issues raised at the time were addressed with the introduction of new methodologies.

From the second cycle, between 2007 and 2010, TCU recommended that Aneel improve the criteria used in the valuation of surplus power purged from the balance sheet in order to increase efficiency, boost low tariffs and improve concessionaires' management of power purchase contracts. TCU also recommended Aneel to establish mechanisms for periodic monitoring of actual revenue reported by concessionaires and to improve ways on informing population about average increase or decrease of tariffs. In the third cycle of reviews, conducted between 2011 and 2014, the TCU evaluated major enhancements to the methodology used.

Box 7.3. **Audits of infrastructure regulation by the supreme audit institution (SAI) of Brazil *(cont.)***

The TCU does not perform systematic monitoring of annual tariff adjustment. However, this issue was the subject of a specific audit, following a request from the Committee of Mines and Energy of the Chamber of Deputies. In the audit the TCU found that the adjustment formula contained distortions which revealed undue gains by the concessionaires since 2002. In response, Aneel discussed the issue with distribution concessionaires and in 2010 contractual amendments were signed changing the criteria for adjustment.

Quality of telephone service provision

In 2006 the TCU conducted an audit to evaluate the performance of the National Telecommunications Agency (Anatel) in monitoring and assuring quality in the provision of telephone services. The work was proposed based on the observation that, although privatisation of telecommunications in Brazil has allowed significant growth in the number of accesses to telephone services, the quality of these services has been subject of complaints to Anatel by users, representative organisations, consumer protection agencies and by other organisations that protect user's rights.

The TCU found that fundamental aspects of quality were not being properly addressed by the Regulatory Agency. There were gaps in quality regulations, weaknesses in the monitoring procedures developed by the agency and lack of effectiveness of the sanctions imposed on service providers. The regulating process of Anatel did not adequately consider the demands of society for improvement in services. In addition, the audit found a very low rate of user participation in the regulatory processes.

Source: Review of TCU documentation and email correspondence.

Other work on regulatory management

Providing **advice** and sharing knowledge acquired from audit work is a common feature of SAIs' strategies. For example, the strategy of the SAI of the Netherlands recognises that the insights provided by the SAI's audits may have wider application than to just the individual auditees, aiming to disseminate knowledge and improve access to audit findings, and to improve the learning ability of public administration. Similarly, the Danish SAI, the Rigsrevisionen, has the aim of communicating and sharing its knowledge and experience in various fora, and acting as a knowledge partner and sounding board for both clients and other auditors operating in the public sector.[23]

In addition to its performance audit reports for the House of Commons Public Accounts Committee, the United Kingdom SAI also provides **briefings** at the request of other Select Committees of the House of Commons from time to time. These can cover regulatory issues, such as a July 2013 briefing provided to the Environmental Audit Committee on carbon budget management (NAO, 2013b). Other outputs beyond its normal performance audit output include a paper on setting out principles to guide public bodies purchasing services in markets (where public bodies can possess market power as the only or principle buyers of the services) and a review at the request of the Food Standards Agency of the efficiency of the Agency's delivery of meat hygiene official controls (NAO, 2012; 2013c).

In 2007, the ANAO published a **Better Practice Guide** on administering regulation (ANAO, 2007). This provided a framework to assist Australian Government regulators in assessing the quality of their administrative practices and identifying improvements that could, and should, be made. Examples of how regulators were currently employing better regulatory practice were provided throughout the Guide.

Further analysis of regulatory governance

Extent to which the audits address the principles set out in the Recommendation of the OECD Council

The Recommendation of the OECD Council was issued in March 2012, so the great majority of the audit reports identified were planned or published before its publication, and none of the reports mentions it. However, the principles set out in the Recommendation are of enduring importance and, while the Recommendation has succeeded in bringing them together and codifying them, the issues that they highlight were potentially available for SAIs to examine them at any time. Accordingly, Table 7.6 analyses the extent to which the reports produced by SAIs addressed each of the 12 principles in the OECD Council Recommendation. In view of the small number of reports on regulatory governance and policy produced in the last year, the analysis focuses on two groups:

- The reports on regulatory governance and policy in Table 7.4 – i.e., the most recent reports published since 2005 by those SAIs having reported on regulatory governance and policy in this period.

- Reports on regulators or regulations published in the 12 months to the end of March 2014 – i.e. those listed in Table 7.5.

Table 7.6 shows a clear difference in the pattern of the two types of examinations. It shows that reports on regulatory governance and policy have focussed very largely on questions around regulatory policy, communication and engagement, the work of regulatory oversight bodies and the implementation of regulatory impact assessment. Reviews of the stock of regulation have also been featured, especially in audit reports on administrative simplification programmes. In contrast, reviews of regulations and/or regulators have focussed far more on operational matters, such as the organisation of regulatory agencies. Risk has also featured heavily in the latter group, and has done so in two main ways:

- Discussion of regulators' use of assessment of risk as a means of targeting regulatory effort where it can be most valuable.

- Discussion of the hazards that regulation is seeking to control – a common indicator of the performance the regulatory regime, being how successful it is in managing the risks presented by these hazards.

It is interesting to note that neither type of report addressed Principle 8 (access to systems of administrative or judicial review). In addition, few addressed questions of sub-national tiers of government. The reason for the low emphasis on sub-national tiers is generally not explained, but in one case (Canada) the wording used suggests there may have been a concern to respect the autonomy of other tiers of government within a federal system of government.

Table 7.6. **Surveyed Supreme Audit Institution (SAI) audit reports mapped to the 12 Principles of the 2012 *Recommendation of the OECD Council on Regulatory Policy and Governance***

Principle	Number of reports including coverage of this principle, either in the evidence examined or in recommendations	
	Reports on reg. governance and policy (base 10*)	Reports on regulators or regulations (base 27)
1: Explicit Policy on Regulatory Quality	10	2
2: Communication, Consultation and Engagement	10	15
3: Regulatory Oversight	9	2
4: Integrated Regulatory Impact Assessment	9	5
5: Reviews of the Regulatory Stock – *ex-post* Regulatory Evaluation	7	3
6: Reviewing Performance of Regulatory Reform Programmes and Regulatory Policy	6	5
7: The Organisation of Regulatory Agencies	3	13
8: Administrative and Judicial Review	0	1
9: Risk and Regulation	1	16
10: Regulatory Coherence across Levels of Government	4	13
11: Regulatory Management Capacity at Sub-national Level	2	1
12: International Regulatory Co-operation	3	3

* Base omits two reports (Austria, France, Germany and Korea) for which English summaries were not available.

How they address the different phases of the regulatory governance cycle

As illustrated by Table 7.2., the Executive considers the contribution of SAIs exclusively at the evaluation stage of the regulatory governance cycle. However, analysis of the reports listed in Box 7.2 and Table 7.7 suggests a more complicated picture. Both types of report included examples where there was some examination of the policy-making process. With only one exception, all reports in the first group included at least some examination of policy development, but so too did around a quarter of the second group. For example, an examination of Transport Canada's regulatory framework formed part of the Canadian SAI's examination of the oversight of rail safety regulation in Canada (OAG, 2013), while the Dutch SAI's review of nature conservation, nature management and spatial planning in the Wadden Sea area[24] included examination of the central government's supervision and coordination of Wadden Sea policy and difficulties that had resulted from it.

Table 7.7. **Surveyed Supreme audit institution (SAI) audit reports mapped to the different phases of the regulatory governance cycle**

	Number of reports including coverage of this phase of the regulatory governance cycle	
	Reports on regulatory governance and policy (base 10*)	Reports on regulators or regulations (base 27)
Develop	9	7
Design	10	21
Enforce	5	23
Monitor	7	23

* Base omits two reports (Austria, France, Germany, Korea) for which English summaries were not available.

Nonetheless, there was a broad pattern of the first type of report focussing mainly on the "upstream" side of regulation, while the second type focussed mainly on the "downstream" elements of design, enforcement and monitoring. It is suggested that this might reflect a number of factors:

- As already noted, SAIs are frequently limited in the extent to which they can or wish to engage with policy development – for example, they may not have the mandates to do so. They may also face technical challenges in developing criteria for evaluation which would allow them to examine policy development, without crossing the line into examining policy itself. The 2012 *Recommendation of the OECD Council on Regulatory Policy and Governance* was not cited in any of the SAI reports reviewed, but is potentially a major help to SAIs because it sets a clear and internationally recognised benchmark for evaluating these processes as they apply to regulation.

- In many countries there is often a division between regulatory policy making by government ministries and regulatory implementation by arm's-length regulators. Inevitably, therefore, examinations of regulators will tend to focus particularly on the "downstream" side of regulation, since that is predominately what these bodies do.

Considerations in shifting SAI engagement

SAIs have a key role in supporting high standards of public sector governance – including regulatory policy. Their work is most evident and has the longest history in the field of public financial management and accountability. However, during the previous decade there has been growing attention by INTOSAI to the role of SAIs in supporting good public governance. This included, in the early 2000s, the development of "Guidelines on Best Practice for the Audit of Economic Regulation". However, compliance with these guidelines is "voluntary" in the sense that INTOSAI as an organisation has neither the intention nor the means to attempt to enforce their application. At the same time, understanding of regulatory policy and governance in OECD has advanced substantially during the past decade, as captured by the 2012 *Recommendation of the OECD Council* on this subject (Box 7.1).

The above analysis shows that many SAIs are seeking to contribute to good regulatory governance through their audit work. Practice in a number of countries demonstrates that SAIs are examining the performance of regulatory programmes and tools, as well as the performance of regulators. SAIs' mandates frequently permit them to undertake audits related to regulatory governance but do not require them to do so, given that this audit work is conducted as a performance audit. Although only a very small proportion of SAIs' performance reports are related to issues of regulatory governance, such reports nonetheless are a periodic feature of many SAIs' outputs. Whilst spending programmes are likely to remain the main focus of SAIs' performance audits for the foreseeable future, the economic significance of regulation, and the importance of some of the policy objectives it is used to achieve, suggests that SAIs could increase their work in this area.

In this regard, the 2012 *Recommendation of the OECD Council on Regulatory Policy and Governance* offers considerable potential as a benchmark for SAIs to use for such work. The Recommendation is an internationally agreed standard, based on many years' assessment and experience of what works. As such, it provides SAIs with a valuable resource to draw on when developing evaluative criteria for performance audits, and a basis for putting national performance in the context of international best practice. For example, the Recommendation could be used by SAIs when they conduct performance audit of regulatory impact analysis and *ex-post* review of regulations, which have been a common theme in surveyed audit reports. However, SAIs need also to look at i) the extent to which their existing audit programming may be predisposed to measure materiality and risk based on government spending, including through failing to understand the significance of the regulatory costs; and ii) the maturity of their country's regulatory governance systems (which existing OECD regulatory management systems indicators can help provide information).

SAIs may also draw insight from the emerging themes and challenges that have been identified by the Executive branch in OECD countries as a means of contributing to good public governance. These challenges include closing the regulatory governance cycle, empowering the players of regulatory governance, promoting evidence-based policy and addressing better regulatory beyond the border. In many respects, an SAI's work is predisposed to addressing these challenges because of their emphasis on evidence and providing recommendations to the heads of public entities, thus supporting efforts to close the governance cycle, empower different plays in regulatory governance and emphasising regulatory policy. Some SAIs surveyed in this section are also addressing issues across the border (such as the ECA and United States GAO).

Nevertheless, there a number of institutional factors that can support and/or prevent SAIs addressing issues of regulatory governance in their audit work, and that warrant further attention. These factors include i) the SAIs mandate (levels of government, types of public bodies) and composition of audit portfolio (i.e. financial, compliance, performance); ii) the availability of alternatives forms of scrutiny (e.g. independent regulatory oversight bodies); iii) the relationship between the SAI and the Legislature and its committees (e.g. if the SAI is considered a body of the Legislature); iv) whether the SAI reports primarily to a single committee and/or multiple committees and whether there is a specific committee responsible for regulatory policy; v) the allocation of responsibility for regulatory reform between functional ministries and ministries with cross-cutting responsibilities (e.g. role of oversight bodies); and vi) other contextual factors such as national legal systems (i.e. civil versus common law), state structure (i.e. federal versus unitary states).

Notes

14 Two caveats should be acknowledged. First, the 2012 OECD survey was sent to the Executive branch and, although survey recipients were encouraged to co-ordinate within their respective government, there is no guarantee that SAIs were explicitly consulted. Although desk research of publically available audit reports through SAI websites largely corresponds to the results of the 2012 OECD survey, the overlap was not complete. Second, the analysis draws heavily on a desk review of audit reports carried out in English. The analysis is likely to understate the full extent of work by SAIs, particularly among those SAIs that do not publish information on their work in English.

15 The vertical scale is a composite on a scale of 0 to 28 of a range of measures of aspects of the regulatory impact assessment system in each country. The questions and their corresponding weights are shown in the table below:

Questions:	Weights:
d(ix) Is the RIA required to include assessments of other specific impacts: Impacts on the budget, impacts on competition, impacts on market openness, impacts on small businesses, impact on specific regional areas, impact on specific social groups, impact on other groups (not for profit sector including charities), impact on the public sector	d(ix), Impacts on the budget, competition, market openness, small businesses, specific regional areas, specific social groups, the public sector: if no=0, in other selected cases=1, only for major regulation=1, always=2 d(ix), Impact on other groups (charities, not for profit sector): if no=0, in other selected cases=0.5, only for major regulation=0.5, always=1
e) Is risk assessment required when preparing a RIA?	e) if no=0, in other selected cases=1, only for major regulation=1, always=1
For all regulation, for health and safety regulation, for environmental regulation?	if yes, weight=1
If “yes”:	
Does the risk assessment require quantitative modelling?	
f(i) Does the RIA require regulators to explicitly consider compliance and enforcement issues when preparing new regulation?	f(i) if yes, weight=1
f(ii) Are reports prepared on the level of compliance with the above RIA requirements?	f(ii) if no=0, *ad hoc* basis=1, regularly=2
f(iii) Are these reports published?	f(iii) if yes, weight=2

16 The vertical scale is a composite on a scale of 0 to 8 of a range of measures of the *ex-post* regulatory review mechanisms in each country. The questions and their corresponding weights are shown in the table below:

Questions:	Weights:
Is periodic *ex-post* evaluation of existing regulation mandatory?	No=0, For specific areas=1, For all policy areas=2
Are there standardised evaluation techniques or criteria to be used when regulation is reviewed?	No=0, Yes=1
Are reviews required to consider explicitly the consistency of regulations in different areas and take steps to address areas of overlap/duplication/inconsistency?	No=0, Yes=1
Are there mechanisms by which the public can make recommendations to modify specific regulations?	No=0, Yes=1
If the answer is “yes”, please specify:	
- Electronic mailboxes	If yes, weight=0.5
- Ombudsman	If yes, weight=0.5
Is sunsetting used for primary laws?	No=0, Yes=0.5
Is sunsetting used for subordinate regulations?	No=0, Yes=0.5
Do specific primary laws include automatic review requirements?	No=0, Yes=0.5
Does subordinate regulation include automatic review requirements?	No=0, Yes=0.5

17 The vertical scale is a composite on a scale of 0 to 5 of a range of measures of aspects of the formal co-ordination mechanisms in each country. The questions and their corresponding weights are shown in the table below:

Questions:	Weights:
Are there formal co-ordination mechanisms between National/Federal and State/regional governments? (in Federal or quasi-federal countries, between national and regional/local governments in unitary countries)	No=0, Yes=1
	No=0, Yes=1
Do any of these mechanisms impose specific obligations in relation to regulatory practice?	No=0, Yes=1
Are any of the following regulatory harmonisation mechanisms used? - Mutual recognition? - Regulatory harmonisation agreements? - Strict regulatory uniformity agreements?	If not at all, weight=0; if sometimes, weight=0.5; if widely, weight=1

[18] In a small number of jurisdictions, SAIs may have a role to play in a before-the-fact review of administrative or financial activities – known as a pre-audit (or *ex-ante* or *a priori* audit). However, *ex-ante* audit of legality function does not exist in the majority of benchmark SAIs while in the few where it is present, the scope is limited, either functionally (e.g. Italy) or financially (e.g. Portugal).

[19] The term "regulatory body" is used in this paper to cover all bodies exercising regulatory functions that are subject to audit by SAIs – including potentially both ministerial departments and arms-length bodies – and any sub-national bodies subject to SAI audit.

[20] The analysis in this part draws heavily on a review of SAIs' websites carried out in English. The search examined the websites of the SAIs of the 34 OECD members, the European Union (a permanent observer to the OECD) and two key partners (Brazil and South Africa). Of these 37 websites, 8 provided full information in English;[20] a further 21 provided at least a listing of reports in English, but normally only of a selection of the reports published by the SAI. Some gaps in coverage could be filled using information provided in other surveys, for example carried out by OECD and by EUROSAI (European Organisation of Supreme Audit Institutions – a regional grouping of INTOSAI). Nevertheless, as mentioned in the introduction, it should be noted that the analysis is likely to understate the full extent of work by SAIs, particularly among those SAIs that do not publish information on their work in English.

[21] Belgium and the United States.

[22] In addition, Canada and the Netherlands had published such reports before 2005.

[23] http://uk.rigsrevisionen.dk/about-us/strategy-and-performance-targets/mission-and-strategic-objectives/strategic-objective-no-3/

[24] http://www.courtofaudit.nl/english/Publications/Audits/Introductions/2013/11/Wadden_area_nature_protection_nature_management_and_spatial_planning

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8. THE CENTRE OF GOVERNMENT

Strengthening the role and performance of governments is crucial to sustainable economic development. Strong government and effective implementation require a strategic and forward-looking state with commitment to and capacity for policy implementation and compliance. This cuts across all aspects of policy and needs to be integrated into policy responses across the whole-of-government. The Centre of Government, which comprises the core institutions that support decision making by the head of government, plays a pivotal role in ensuring that this vision of a more strategic state is translated into better and more coherent policies on the ground.

Centres of Government are expected to fulfil their traditional role of serving the head of government and cabinet from a procedural perspective but are also, in many countries, engaging much more actively in policy and budget development, and in steering of implementation across government. The Centre is expected to lead ever more complex policy agendas and coordinate responses in a manner that come as close as possible to a whole-of-government perspective. The Centre also plays a role in driving reform of the public sector in order to improve implementation capacity and, in some countries, works with ministries of finance to monitor spending and outcomes.

Governments are facing increasing pressures in addressing more complex and interconnected economic, social and political challenges. In a strategic and open state, the government identifies and addresses internal and external challenges to policy implementation through evidence-based decision making and strategic foresight, strengthens efficiencies in policy design and service delivery to meet these challenges and mobilises actors and leverages resources across governments effectively. This requires leadership and stewardship from the Centre of Government.

In view of expanded mandates, the question for Centres of Government across the OECD and in non-member countries is about how can the Centre be structured, resourced differently, or linked in to networks of relevant expertise in order to better accomplish its key tasks. Meeting new challenges has, on the one hand, highlighted the need for a strong Centre but has also, on the other hand, exposed the limited resources at its disposal. Some central analysis units employ only a handful of people, which means they are wholly dependent on data and assessments from line ministries and agencies themselves which, in some cases, are interested parties and thus not fully objective. This suggests a need for the Centre to draw on information and analysis from independent and objective sources, external to the Centre. SAIs may be well-placed to help fill this gap as external and independent actors with a view across government institutions. However, it is important to note that SAI activity in assisting the Centre with its work must not compromise the external auditor's institutional independence.

Defining the Centre of Government

To understand how SAIs could enhance their positive impact on policy making through the Centre of Government, it is important to define what is meant by the Centre of Government. Various definitions are possible to establish, but the one that the OECD appeals to for its work on Centres of Government is as follows:

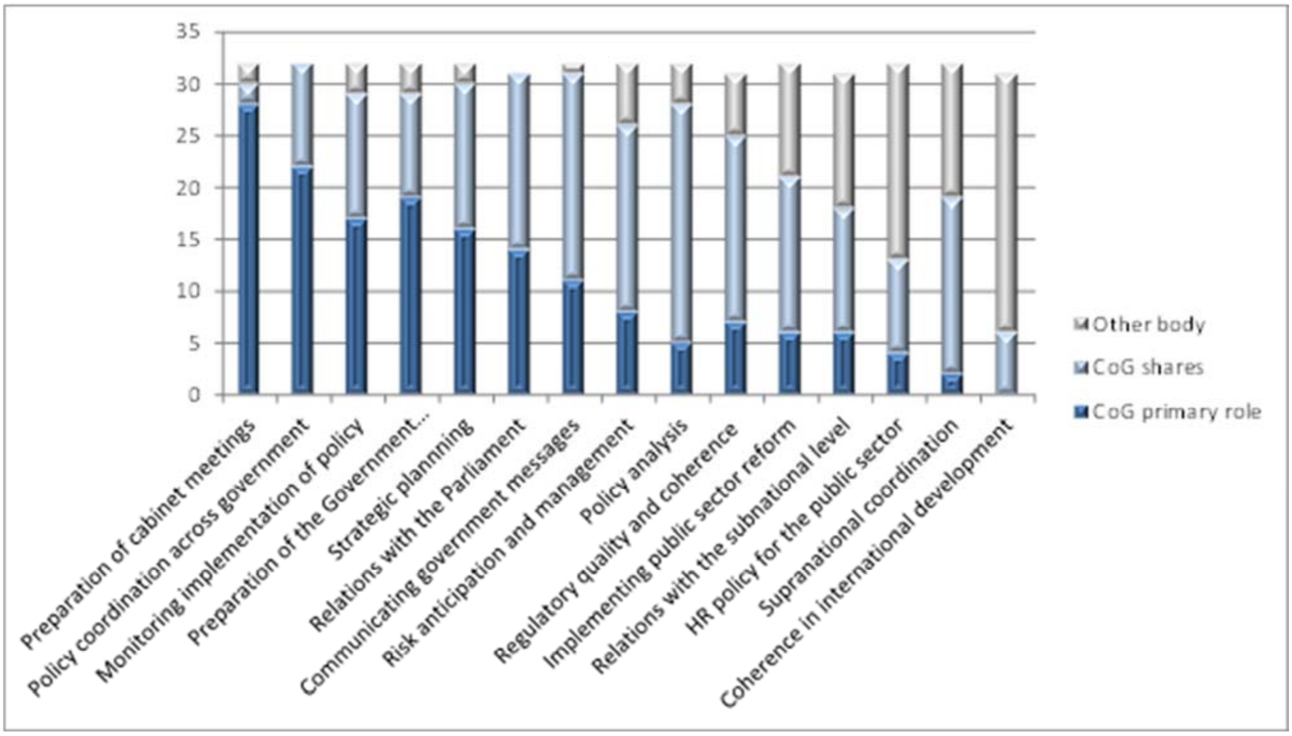
The Centre of government is the administrative structure that serves the Executive (President or Prime Minister, and the Cabinet collectively). This definition does not cover other units, offices, and commissions (e.g. offices for sport or culture) that may report directly to the President or Prime Minister but are, effectively, carrying out line functions that might equally well be carried out by line ministries. The Centre of Government has a great variety of names across countries, such as General Secretariat, Cabinet Office, Chancellery, Office/Ministry of the Presidency, Council of Ministers Office, etc. In many countries the Centre is made up of more than one unit, fulfilling different functions.

There are some differences between Centres of Government in Parliamentary systems and those in presidential systems. In Parliamentary systems, the goal of the Centre's leadership is to provide guidance and co-ordination to Ministers and their civil servants on strategy setting and implementation to ensure that the government can demonstrate accountability to Parliament. In a presidential system, the purpose of the Centre is to generate and sustain institutional accountability across the government while ensuring that the government can demonstrate accountability to the Head of State to whom it is responsible (OECD, 2013b).

In the past, commentators have often emphasised that the Centre of Government is a product of diverse historical, cultural and political forces and has developed incrementally, and often haphazardly. As such, it was also assumed that this heterogeneity made comparative analysis difficult. However, a recent OECD survey found that the aforementioned OECD definition was recognised as usable for their own Centre of Government in most of the 24 countries surveyed (OECD, 2013a).[25] This suggests commonalities across very diverse constitutional forms. At the same time, the geometry can vary widely, with some countries noting that units in several ministries (notably Finance, but also Foreign Affairs, Justice and Interior) manage functions that come under the notion of the Centre of Government. In some cases, formal institutions (such as the Political Committee in Chile or New Zealand's Corporate Centre) give some shape to a broader definition of the Centre while, in others, informal groupings according to topic or objective develop to act as the *de facto* Centre of Government for that issue or function. More rarely, the notion of collective action is used to describe a concept in which all ministries contribute in different ways to and therefore constitute the "centre". Nonetheless, a large majority recognise an entity that can be delimited that plays a set of core functions.

The OECD survey found that the primary roles fulfilled by the Centre include preparation of cabinet meetings, policy coordination, monitoring implementation of policy, preparing the government's programme, strategic planning and overseeing the relationship with the Legislature (Figure 8.1). Secondary roles include communicating government messages, risk anticipation and management, and policy analysis.

Figure 8.1. **Allocation of responsibility by function - overview**



OECD (2013a), *Centre of Government Survey* (unpublished), OECD Public Governance and Territorial Development Directorate.

Three particular functions of the Centre stand out: 1) promoting quality decision making, 2) strategic planning, and 3) coordination and monitoring of policy implementation.

Quality decision making at the Centre

The OECD Centre of Government survey underlines the role of the Centre in driving evidence-based, inclusive and effective decision-making, and in leading whole-of-government strategy setting, implementation and performance monitoring. This means demonstrating strong leadership, playing the challenge function effectively and advising Ministers strategically about government priorities, as well as managing communications with both internal and external audiences.

While there are numerous channels available to a head of government for policy-related decision making, the Cabinet remains the principal vehicle. As such, the role of the Centre in co-ordinating Cabinet meetings and the discussion of agenda items has an important influence on reaching the right outcome.

Box 8.1. **Summary of survey results – cabinet meeting coordination**

- In 17 out of 24 countries, the Cabinet is the principal channel for decision making by the head of government;
- In all countries, the Centre reviews agenda items;
- In 22 out of 23 countries, the Centre coordinates discussion of agenda items in advance of cabinet meetings;
- In half of the countries, the Centre organises pre-meeting briefing sessions with relevant senior ministry officials and uses these occasions to mediate possible differences of opinion and comments on evidence and supporting material.

The function of the Cabinet or Council of Ministers itself varies greatly. In some cases, the Council of Ministers is the key locus of decision-making while, in others, it acts to ratify decisions taken by the head of government in consultation with key Ministers. In presidential systems, the ministerial team might not meet regularly and its participation in policy meetings with the head of government will depend on the topic. Yet, in all cases, whether a full Cabinet of twenty or more Ministers or a bilateral or trilateral discussion with the head of government on a more narrow topic, the Centre has a crucial role in controlling the quality of evidence, objectivity and inclusiveness of options presented, and ensuring procedures are respected, to ensure quality decision making.

Table 8.1. **How are the items submitted to Cabinet reviewed?**

Review criteria	Centre of Government reviews		CoG has the authority to return items to Ministry for additional work if criteria are not satisfied		This is reviewed by another body	
That procedures for preparation and presentation are respected	16	(66.67%)	19	(79.17%)	0	(0.00%)
Quality of legal drafting and legal conformity	10	(41.67%)	13	(54.17%)	13	(54.17%)
That a regulation meets regulatory quality standards (public/economic benefits, that benefits outweigh costs, that an impact analysis has been carried out, etc.)	8	(33.33%)	14	(58.33%)	10	(41.67%)
That the item is in line with the Government Programme	12	(50.00%)	13	(54.17%)	4	(16.67%)
That relevant ministries and other stakeholders have been consulted as required	12	(50.00%)	16	(66.67%)	3	(12.50%)
That adequate costing has been carried out	10	(41.67%)	13	(54.17%)	12	(50.00%)

One important objective of the management role of the Centre of Government, with respect to high-level government meetings, is to ensure that harmonised consultation processes have been followed and that appropriate analytical tools have been used. These twin streams aim to ensure that basic issues regarding the usefulness and cost-benefit analysis of a particular action can be judged easily by the Head of Government and Cabinet. This analysis and consultation process usually extends beyond the sectoral perspective of the sponsoring agency or department and, as such, the analytical tools and consultation processes must also be broader. The resulting presentation of information to the government should enable political leaders to understand the need for, and consequences of, proposed policy interventions. This includes understanding their costs and benefits, including weighing up evidence on the likely impacts of such interventions, and anticipating risks and resistance to the policy. While individual departments might focus on their own evidence-gathering sometimes, through large internal research units, the Centre is obliged to canvass opinion and analysis more widely. This process must be to some extent formalised so that the Centre is able to justify how it has selected the evidence that is presented. In other words, the Centre needs a system that makes best and transparent use of available evidence. Given the relative size of Centre of Government research units and the volume of material that needs to be passed to Cabinet, the ability of most Centres to undertake this rigorous analysis is limited.

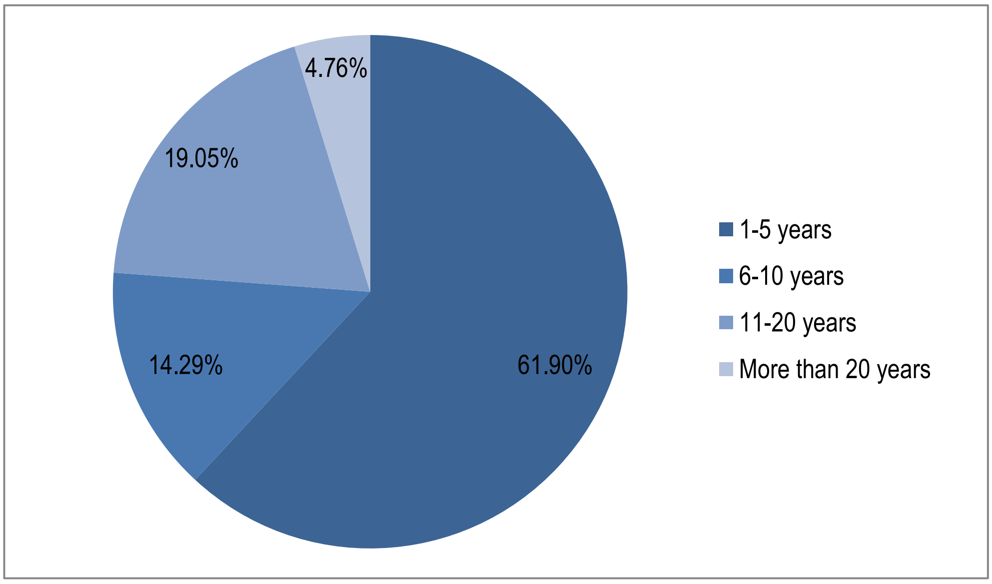
Strategic planning and foresight

Governments have an obligation to minimise uncertainty in the economic, social and political spheres of society. This is particularly true with respect to external events over which citizens have limited or no control, such as disasters or economic crises. This, in turn, implies (i) that the State acts as the steward of the public interest, with foresight capacity and (ii) that its actions are consistent and predictable. The financial crisis was a severe test of the ability of governments to play this important stewardship role, raising a number of important questions that have implications for trust in government:

- Is the government able to identify challenges and assess risks for society? Does the government have mechanisms to mitigate such risks?
- Are the strategies of public bodies aligned to a more general strategy that takes into account challenges and risks?
- Does the public service have the competencies to deliver programmes and services effectively, efficiently and economically?

The OECD survey of Centres of Government confirms that this strategic planning role is seen as an important task in many countries. However, strategic planning has not always been a priority, is not always clearly separable from other shorter term activities and does not result in the creation of a genuine, long-term, strategic vision document. It appears that few countries have a specific strategic planning unit. While such units were more common in the past, they lost their prominence over time and saw their resources decrease. The reasons for this vary from country to country, but relatively long periods of robust economic growth may have been a motive for governments to downplay the need for horizon scanning and contingency planning. In countries where the Centre of Government is involved in preparing or co-ordinating a strategic document for the government, it is often a relatively short-term vision statement: for 60% of the countries surveyed, the document has a time horizon of between 1 to 5 years, which appears to cover little more than the government's term in office. The government's work programme, prepared or updated on an annual basis, is clearly different from "foresight". In the aftermath of the crisis, which exposed the low priority that had been given to strategy and anticipation, this is an area of work that preoccupies many governments.

Figure 8.2. **How far into the future does the strategic vision document cover? (21 responses)**



OECD (2013a), *Centre of Government Survey* (unpublished), OECD Public Governance and Territorial Development Directorate.

The role of the Centre in strategic planning includes diverse elements that range from direct contribution to foresight studies and risk assessments, to “mainstreaming” of strategic priorities in operations, notably:

- ensuring that the government’s deliberations on its strategic priorities take place with the benefit of a broad assessment of the current and anticipated economic, political and social situation;
- ensuring that the strategic priorities are harmonised with other strategic documents of the government, such as economic and fiscal strategies, and other key policy and reform strategies;
- ensuring that the budget preparation process and ministry work plans take account of, and reflect, strategic priorities; and
- ensuring that the Prime Minister, President or Cabinet is regularly briefed on new developments affecting the strategic priorities and annual work plan, and possible responses or adjustments where warranted.

Centres of Government provide advice and guidance to the Prime Minister, President or Cabinet. As such, their strategic thinking feeds directly into decision making at the highest level. In most cases, the contribution of the Centre to the analysis underlying the strategic vision is limited. However, their role in ensuring political buy-in for strategic priorities, and ultimately allocation or reallocation of resources to align with priorities, means that they need to be fully convinced by the evidence.

Policy coordination, implementation and monitoring

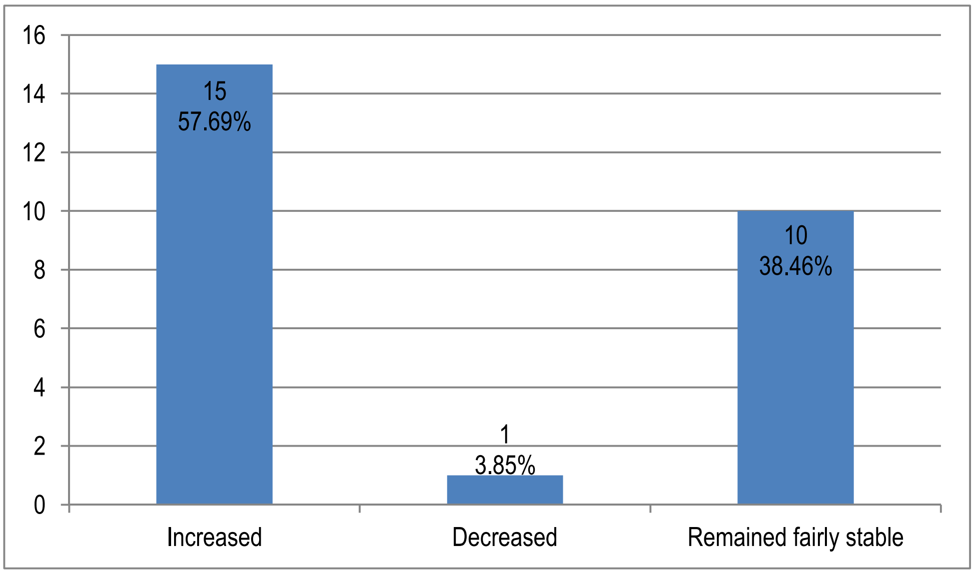
Another key role of the Centre of Government is to ensure coherence in the way the government manages horizontally across its departments and agencies. Governments are subject to divergent policy tensions, often epitomised in the occasionally conflicting sectoral interests of line ministries, while the budget ministry characteristically seeks to control outlays. In all countries, important trade-offs between diverging interests usually have to be made at the highest level. The Centre of Government helps to facilitate this arbitrage. Inconsistent policies can lead to a higher risk of duplication, inefficient spending, a lower quality of service, contradictory objectives and targets and, ultimately, a reduced capacity to govern. At the same time, the task of the Centre is to balance this ideal against the political and practical limits on coherence in the real world.

The need to do more with less has led to a new emphasis on monitoring policy outcomes and ensuring that government programmes are being implemented effectively and in a co-ordinated manner. This coincides with the new public management trend towards better benchmarking policy and programme performance against value-for-money. What is new is that the effort puts more emphasis on policy alignment and impact than only on tracking expenditures. In the past, monitoring of spending by departments has been the responsibility of the Ministry of Finance, with the departments themselves tracking their own spending for accountancy/reporting purposes. Today, the Centre of Government seems to play a more direct role in following the implementation of the policies themselves and ensuring good coordination, particularly in the increasing number of cross-disciplinary policy initiatives. Institutional coherence in the Centre of Government aims at explicitly linking budget and strategy, and linking budget and strategy to performance, or achieving strategic results through effective and efficient management of the government’s fiscal and human resources.

Co-ordinating complex policy strategies now constitutes a key function of the Centre of Government. The OECD survey found that the number of cross-departmental policy initiatives has increased in most countries (Figure 8.3). They play this role in several ways:

- promoting co-ordination of activities directly included in the government's direction;
- a facilitation role in bringing ministries together at the senior level (minister, state secretary, director);
- supporting the work of specialised co-ordination bodies established to cover a particular policy field (economic advisory bodies); and
- specifying the follow up and cross-departmental roles in actions approved in Cabinet decisions.

Figure 8.3. **From 2008-2012, did the number of cross-governmental policy initiatives increase, decrease, or remain fairly stable? (26 responses)**



OECD (2013a), *Centre of Government Survey* (unpublished), OECD Public Governance and Territorial Development Directorate

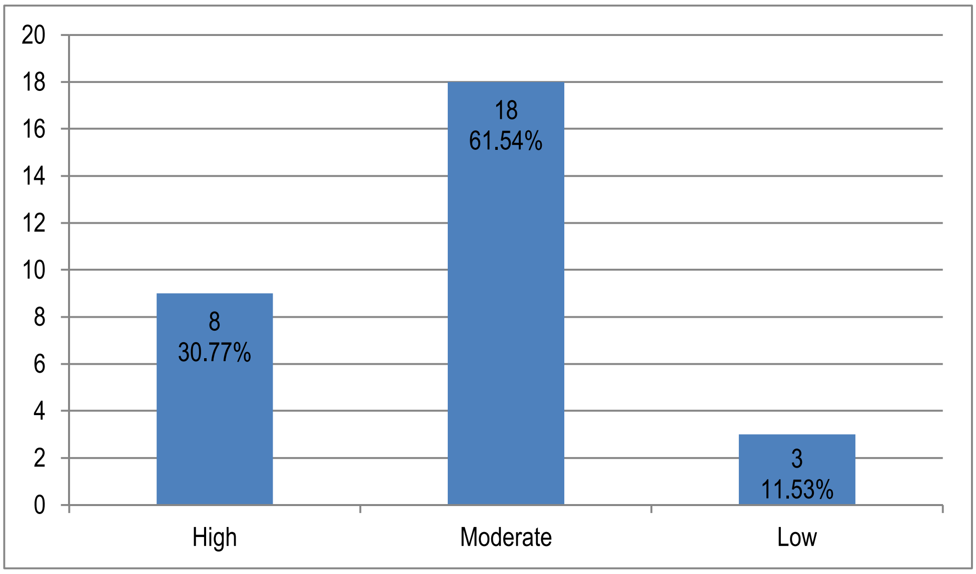
A key issue for the Centre regards the ability to set agendas and work with other government institutions. This often involves applying rules in the name of the Head of Government. The survey indicates that most Centre of Government officials consider that they exert only a moderate degree of influence over ministries to promote co-ordination (18 countries, moderate influence; 9, high influence; and 3, low influence) (Figure 8.4). This is partly a result of the general institutional problem of coordination in any large organisation. However, in some cases this might also derive from information asymmetries.

The need for the Centre to provide accurate information to the political level on progress with implementation assumes some mastery of the detail of spending and results across a large range of policy areas. While most departments have relatively large units to track spending, this is a relatively new task for the Centre of Government and the resources available are limited. Despite some progress related to digital governance, some problems Centres have to do with the following:

- The flow of information becomes too great and transaction costs are larger than the benefit to policymakers
- There is a knowledge asymmetry between large teams in departments who provide the data and the non-specialist teams in the Centre that try to process it

- The information delivered might not be entirely objective given that departments know that their performance – and possibly resources -- will be judged on the basis of it

Figure 8.4. **How much influence can the Centre of Government exert over line ministries to encourage them to co-ordinate with each other? (30 responses)**



OECD (2013a), *Centre of Government Survey* (unpublished), OECD Public Governance and Territorial Development Directorate

As comprehensive audits are beyond the Centre's capacity, better use of information generated through an independent body may be useful. This is the case for SAIs, which already evaluate spending at the ministry level to verify conformity with accounting rules as well as, increasingly, benchmark outcomes against targets.

The role of SAIs

Given the need for objective government-wide information and a well-functioning Centre, three opportunities for SAI engagement with the Centre of Government emerge:

1) SAIs could provide valuable information at a whole-of-government level for the Centre's oversight and co-ordination functions, to enable quality policy formulation, policy coordination and monitoring.

2) In conjunction with Section 6 on budgeting, SAIs could provide the Centre with useful information about risks, implementation challenges and performance, which can feed into the budgeting process, thereby allowing the Centre to guide budgeting decisions with helpful, objective information.

3) The Centre could itself become the subject of assessment by SAIs to ensure that it is well-positioned to guide governments in achieving strategic objectives and responding effectively to government-wide challenges. To this end, SAIs can examine the institution(s) at the Centre to determine whether they are well structured, have effective processes and are contributing to overall good governance across the whole-of-government.

While SAIs are well-positioned to provide these assessments, in theory, many do not currently have a systematic approach to supporting or assessing the Centre, as it may fall outside of their traditional remit. To the extent that SAIs have been engaged with the Centre, it has been on an *ad-hoc* basis. Nevertheless, as the following examples demonstrate, some SAIs are able to provide valuable whole-of-government assessments, which could form the basis of further development of SAI work.

Generating information at the whole-of-government level

Through taking a whole-of-government approach, SAIs can provide Centres of Government with a bird's eye perspective on the effectiveness of governance mechanisms and on policy performance so that Centres can use this credible and objective information to better inform their budgeting, policy planning, implementation and evaluation processes.

The SAI of the Netherlands has taken a whole-of-government approach to auditing the performance of the central government. Recent audits published in May 2012 and a follow up report in June 2013, looked across ministries to their evaluations of policy effectiveness (Algemene Rekenkamer 2012; 2013). These audits focussed on investigating whether ministries evaluated the effectiveness of policies with a social objective.

The 2012 audit focussed on evaluations of policies amounting to €51 billion (or 46% of government expenditure in 2010) that was spent to achieve social objectives. While the audit did not focus on the quality of the evaluations, it recommended that ministries should improve their scans of policy effectiveness and that a comprehensive programme of policy scans should be introduced in line with budget regulations. By way of follow up, the SAI published the Minister of Finance's response on its website stating where the government agreed with its recommendations and undertook to make improvements, as well as where the Minister did not respond. The non-response related to ensuring there are comprehensive advance evaluation programmes in place, which led the SAI to note that this poses a risk as it may leave the Legislature without adequate information.

In 2013, the SAI of Netherlands conducted a follow-up audit after finding that the effectiveness of half of the government's policy expenditures relating to social objectives in 2006-2010 had not been evaluated. The 2013 conclusions highlighted areas that were still of concern, particularly in light of spending cuts that were underway. The SAI found that policy effectiveness was not evaluated in many policy fields, including in areas where the government was cutting expenditure, which meant that the impacts of the cuts could not be determined. It impressed upon the need not to evaluate the effectiveness of all policy at all times, but to have a reasoned evaluation programme in each Ministry that specifies what kinds of evaluation are to be carried out, when and what kinds have the most added value. By providing this type of whole-of-government perspective, the SAI is able to inform the Centre of the weakness that exist across ministries in specific policy areas so that it can address the problem in a horizontal and co-ordinated manner.

Another example of a whole-of-government approach taken by the Dutch SAI pertains to government personnel strategy and planning. In May 2012, the SAI published its audit on the strategic personnel plans of the central government in anticipation of over 60% of its personnel retiring within ten years (Algemene Rekenkamer, 2012). It found that the majority of government institutions do not have a plan in place to deal with this outflow of personnel, which poses a risk to government performance in the long-term, particularly given the ongoing spending cuts that include to personnel. It concluded that the government's requirement of having a plan in place by the end of 2012 was not realistic for a number of reasons, and made recommendations on how to approach issues of planning. By providing this type of objective assessment, governments are better positioned to respond using a whole-of-government approach.

In 2012 the Polish SAI performed an audit on the preparation of government strategic documents in relation to the government's preparedness to use its EU financial resources of 2014-2020. The audit also included reviewing elements of national development policy, strategic planning and covered innovation and efficiency of economy, transportation development, energy and environment, regional development, human and social capital development, sustainable development of rural areas, agriculture and fisheries and the efficiency of state and national security.[26]

Feeding into the budgeting process

Another area in which SAIs are supporting government-wide planning is in budgeting. The Brazilian SAI uses performance and compliance audits to evaluate the whole-budget process, and subsequently reports on quality, gaps and issues to be addressed (OECD, 2014).

Every two years, the SAI of the US carries out a risks assessment before a budget cycle to provide the government with insights on performance and vulnerabilities (GAO, 2013). Following a government-wide scan, the SAI highlights programmes that are high risk due to their vulnerabilities to fraud, waste, abuse and mismanagement, or those that are in need of transformation. The SAI's 2013 high-risk list includes areas for strengthening specific programmes' efficiency and effectiveness, ensuring public safety and security, managing contracts more effectively and modernising and safeguarding insurance and benefit programmes. The report contains the SAI's views on progress made and what remains to be done to bring about lasting solutions for each high-risk area. The report is targeted at the Executive branch to implement its recommendations, recognising that the continued oversight by the Legislature is essential to achieving progress.

Assessing the Centre of Government

Given the large differences in structures of Centres of Government, the mandate for and scope of SAIs' assessments of institutions within those structures would largely depend on country-specific set-ups. Where possible, as a starting point, SAIs could examine the functions fulfilled by the Centre in relation to other bodies to assess synergies and overlaps as a way to understand how effectively the Centre is functioning in terms of advancing the government's policy agenda.

OECD research suggests that despite significant diversity in institutional structure, the Centre of Government can be assessed on the basis of its effectiveness in carrying out its core functions. The "output" of the Centre can be difficult to quantify, particularly identifying performance targets for the Centre. However, SAIs generally have experience in assessing outcomes that are difficult to measure. Thus, SAIs' assessments could help to "demystify" the Centre, which often lies outside the usual scope of performance measurement because of the somewhat intangible nature of its output.

In this regard, the added value that an SAI could bring would be in reviewing the responsibilities of the Centre of Government institutions to verify that they are clear and understood, that all key functions are covered with no significant gaps, and that the processes that govern the functioning of the institutions at the Centre are codified in some way, either through legislation or rule of government procedure. SAIs could review the clarity of the Centre's institutional architecture, the application of important procedures in practice, including respect by others for the Centre's role and its own adherence to its principles, and also assess the outcomes of major initiatives led by the Centre.

Assessing the Centre through the three stages of the policy cycle would be a helpful way of determining the value added by the Centre in contributing to good governance. While overlapping, these stages include some discrete tasks that should be identifiable within the institutional structure of the Centre and to which assessment criteria could be assigned. This includes evaluation of its prioritisation among tasks and the allocation and efficient use of resources to achieve these tasks. Among the core functions, SAIs could assess the Centre's role in **policy formulation**, including in:

- co-ordinating the appraisal of policy proposals from ministries and ensuring appropriate citizen-engagement;
- performing a solid challenge function on policy proposals from ministries and their associated programme designs in terms of coherence, affordability, risk and expected results;
- ensuring conformity of policies with the government's strategic plan and legal frameworks;
- co-ordinating the preparation and approval of the government's strategic priorities and work programme, including the associated budget; and
- co-ordinating preparation of the sessions of government and supporting Cabinet decision making.

SAIs could assess the Centre's role in **policy implementation**, including in:

- ensuring programmes are implemented consistently with their programme design; and
- ensuring integrity in programme delivery, such as in the award of contracts.

SAIs could assess the Centre's role in **monitoring** and **evaluation**, including in:

- advising ministries with respect to monitoring and evaluation good practices;
- actively monitoring programme implementation across ministries;
- having a whole-of-government understanding of the results of programme evaluations;
- taking a whole-of-government approach to policy performance and achieving key objectives, and linking these with the government's overall strategic plan; and
- overseeing the government's communications strategy, including the relationship with key stakeholders including Parliament, sub-national governments, private actors and the public.

Assessing the Centre's policy making can also lead to developing guidance for effective policy-making. For example, the Brazilian SAI has developed a framework for assessing the governance of sectoral public policies in general, which has included discussions with the Centre of Government and the Legislative Branch. In its work, it was clear that the SAI's role was to help improve the framework for the policy-making process without entering into a discussion to the merits of public policies. The framework is comprised of eight elements: Institutionalisation, Plans and Objectives, Participation, Organisational Capacity and Resources, Coordination and Communication, Monitoring and Evaluation, Risk Management and Internal Control and Accountability.

Notes

25 OECD (2013), Centre of Government Survey (unpublished) Country's surveyed: Austria, Belgium, Brazil, Canada, Chile, Denmark, Finland, Germany, Iceland, Japan, Korea, Latvia, Lithuania, Morocco, New Zealand, Norway, Portugal, Slovak Republic, Slovenia, South Africa, Sweden, Switzerland, United States, European Commission.

26 Information provided by the SAI of Poland through a peer review process, May 2014.

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9. INTERNAL CONTROL

Within the public sector, effective internal control is a critical element in maintaining public confidence in a government's ability to manage public resources, meet its public policy objectives and deliver public services. For the purposes of this study, internal control refers to the processes through which governments can reasonably assure the effectiveness and efficiency of their operations, the reliability of financial reporting and compliance with applicable laws, regulations and policies such that they deliver on their mandates.[27] Internal control includes mechanisms for safeguarding public resources against loss, misuse and damage, including fraud and corruption (INTOSAI, 2004; UN, 2004).

INTOSAI asserts that the objective of internal control is to execute orderly, ethical, effective, efficient and economical operations that are consistent with the organisation's mandate (INTOSAI, 2004). Part of this is ensuring that resources are used judiciously, meaning that the least possible effort and expenditure deliver the greatest output and secure desired outcomes in achieving the objectives of the organisation. Organisations should balance detective and preventative controls, and take corrective actions when necessary to achieve objectives (INTOSAI, 2004).

Organisation and components of internal control

Internal control systems of government can be structured in two main ways. In some countries, special internal control institutions exist that are independent from those that they monitor. They have a role in evaluating internal control systems, meaning that internal control assessment functions are centralised. In others internal control assessment is decentralised, and is the responsibility of respective line ministries. In this case, the internal control system is an integrated, yet independent, part of the administration. In all cases, establishing, maintaining and reforming the internal control system is the responsibility of senior management. In contrast, the role of auditors, both internal and external, is to provide independent and objective advice on and assessment of the efficiency and effectiveness of the internal control system.

The international industry standard on internal control, as espoused by the *Committee of Sponsoring Organisations of the Treadway Commission* (COSO), articulates the components of effective internal control as involving the following elements: the control environment, risk assessment, control activities, information and communication, and monitoring activities (Box 9.1) (COSO, 2013). All these elements are essential and must be able to operate seamlessly together for an effective internal control system.

Box 9.1. **The components and principles of effective internal control processes**

Component	Principles
1. Control Environment • Established by senior management • Set of standards, processes and structures • Represents integrity and ethical values of the organisation • Enables management oversight • Processes to ensure a competent workforce • Performance measures, incentives and rewards	1. Demonstrates commitment to integrity and ethical values 2. Exercises oversight responsibility 3. Establishes structure, authority and responsibility 4. Demonstrates commitment to competence 5. Enforces accountability
2. Risk Assessment • Dynamic and iterative process • Establishes risk tolerance against clear organisational objectives	6. Specifies relevant objectives 7. Identifies and analyses risk 8. Assesses fraud risk 9. Identifies and analyses significant change
3. Control Activities • Performed at all levels of an entity • May be preventative or detective	10. Selects and develops control activities 11. Selects and develops general controls over technology 12. Deploys through policies and procedures
4. Information and Communication • Using relevant quality information to carry out internal control responsibilities • Continual, iterative process of providing, sharing and obtaining necessary information	13. Uses relevant information 14. Communicates internally 15. Communicates externally
5. Monitoring Activities • Scope and frequency partly depends on assessment of risks and management considerations	16. Conducts ongoing and/or separate evaluations 17. Evaluates and communicates deficiencies

Source: Adapted from COSO's *Internal Control – Integrated Framework, Executive Summary*, May 2013 http://www.coso.org/documents/990025P_Executive_Summary_final_may20_e.pdf; COSO, *An Update of COSO's Internal Control – Integrated Framework*, May 2012 http://www.coso.org/documents/cosoicifoutreachdeck_05%2018%2012.pdf

Regardless of whether in a centralised or decentralised internal control assessment system, internal control processes should permeate an entire ministry's operations and is most effective when integrated into the infrastructure of the ministry's activities, management frameworks, information technology infrastructure and decision-making processes as a means of strengthening public governance.[28]

Internal control activities span all stages of the public policy cycle, and are particularly useful during the policy implementation phase. As internal control policies and procedures are designed to manage risks to achieve an organisation's objectives, it is important that programme design and implementation takes into account controls that ensure that public resources are used efficiently and properly. This can be done through internal control activities such as appropriate authorization and approval procedures, clear codes of conduct for officials, adequate verification processes, reviews of operations and procedures and sufficient supervision.

Using a risk-based approach

Strong internal control processes require a risk-based approach to exercising control functions in order to achieve a ministry's objectives. In other words, internal control processes should be tailored to reduce risks to an acceptable level within the specific contexts of the organisations in which they are situated.

Risk can be defined as the probability of a negative outcome that would adversely affect the achievement of organisational objectives. Risks can be considered qualitative in nature (e.g. reputational risk) or quantitative (e.g. financial risks). Risk management is thus the identification, evaluation and mitigation of risks such that the government's objectives are still achieved.

According to INTOSAI, risks must be identified comprehensively against key organisational objectives, from which key risks can be isolated and prioritised for mitigation (INTOSAI GOV 9100). Objectives can be classified in three ways: operational, reporting, and compliance. According to COSO, these can be understood as follows (COSO, 2013):

- *Operational Objectives* pertain to effectiveness and efficiency of the entity's operations, including operational and financial performance goals, and safeguarding assets against loss.

- *Reporting Objectives* pertain to internal and external financial and non-financial reporting and may encompass reliability, timeliness, transparency or other goals as set forth by regulators, recognized standard setters, or the entity's policies.

- *Compliance Objectives* pertain to adherence to laws and regulations to which the entity is subject.

An additional set of objectives according to INTOSAI is considering *strategic objectives*, which are the high level goals linked with the organisation's mission (INTOSAI, 2007).

Prioritising risks includes taking factors such as the likelihood and severity into consideration, and rating them (for example, as high, medium or low) in order to highlight key exposures and focus the attention of managers. Prioritisation includes weighting the probability of a negative event occurring against the impact it would have on the organisation, programme or ability to achieve the government's objective. Specific risk management actions can then be planned to mitigate the key risks, in line with the appetite for risk acceptance within the organisation. Risk management is also geared towards ensuring that the mitigation measure is proportionate to the costs associated with risk itself (INTOSAI, 2004). Risk appetite is essential to consider before establishing how risks can be addressed as it sets out the level of risk that is tolerable and justifiable should they materialise. It is the senior management's responsibility to set and evaluate the risk appetite for the entire organisation.

Recognising that all risks cannot be eliminated, risk management within ministries aims to provide reasonable, but not absolute, assurance against the probability of an untoward risk materialising. Effective risk management can lead to better delivery of programmes and services, more efficient use of resources, and overall performance enhancement, while reducing exposure due to factors such as waste, fraud and corruption.

Consideration also needs to be given to the costs associated with putting in place control processes. This helps to ensure that the cost of internal control does not exceed the derived benefit (INTOSAI, 2004). A cost-benefit analysis is required to determine the optimal level of control processes that can facilitate achieving a ministry's objectives in delivering its services. This analysis should not just focus on financial costs, but should take into account the risk of fraud, waste and abuse, as well as the impact on those whom the government serves. This is an important balance, as excessively burdensome controls can lead to a greater risk of circumvention of control processes, inefficiencies or unnecessary delays in delivering public services.

Leadership is required to create a culture of risk management that is focussed on prevention rather than as a means to assign blame. In order to be effective, risk management must be an ongoing, iterative process, requiring risk profiles and related controls to be regularly revisited and reconsidered to ensure risk profiles remain relevant and that responses and risk mitigation measures continue to be appropriate and effective (INTOSAI, 2004).

Oversight over an internal control system is key, and requires a clear delineation of roles and responsibilities for risk management to avoid duplication or redundancies. All members of an organisation must know their role and the limits of their authority, with senior management providing direction and oversight (INTOSAI GOV 9100). The Institute of Internal Auditors (IIA) take the position that risk management is strongest when there are separate and clearly identified actors and roles. The IIA promulgates a *Three Lines of Defence Model*, which provides a simple and effective way to enhance communications on risk management and control by clarifying essential roles and responsibilities (IIA, 2013a). In this model, management control is the first line of defence in risk management. The various risk control and compliance oversight functions established by management are the second line of defence. Independent assurance, typically through internal audit, is the third. Each of these three "lines" plays a distinct role within the organization's wider governance framework:

4. **First Line of Defence – Operational Management:**

   As the first line of defence, operational managers own and manage risks. Operational management is responsible for maintaining effective internal controls and for executing risk and control procedures on a day-to-day basis. Operational management identifies, assesses, controls and mitigates risks, guiding the development and implementation of internal policies and procedures while ensuring that activities are consistent with goals and objectives.

5. **Second Line of Defence – Risk Management and Compliance Functions:**

   Management establishes various risk management and compliance functions to help build and/or monitor the first line of defence controls. The specific functions may vary by organisation, but typical functions in the second line of defence include a risk management function (and/or committee), a compliance function and a controllership function.

6. **Third Line of Defence – Internal Audit:**

   Auditors provide the governing body and senior management with assurance regarding performance assertions made by management based on the highest level of independence and objectivity within the organization. This high level of independence is not available in the second line of defence. Public sector auditors provide assurance on the effectiveness of governance, risk management and internal controls, including the manner in which the first and second lines of defence achieve risk management and control objectives.

The IIA recommends that these lines of defence be coordinated to ensure effectiveness and efficiency, including by sharing information, to assist all functions in accomplishing their goals (IIA, 2013a).

To be effective, risk management frameworks must be applied throughout the organisation, and not conducted in silos or limited to discrete parts of an organisation. Governments have developed integrated risk management frameworks to be applied within ministries, such as Canada's *Framework for the Management of Risk* (TBS, 2010). It is a policy instrument that contains a principles-based approach to risk management for all federal ministries and is complemented by numerous guides and tools to enable its application. For example, there is a guide on integrated risk management that provides guidance on designing, implementing, practicing and continuously improving risk management approaches and processes. They have also developed a corporate risk profiles guide addressing how to manage corporate risks and inform decision-making.

The UK SAI has developed a guide to managing risks in government, which includes six principles to influence departments to embed good practice approaches to risk management to promote better decision-making (Box 9.2) (NAO, 2011).

Box 9.2. **UK National Audit Office's Principles of Risk Management**

1. An engaged Board focuses the business on managing the things that matter
2. The response to risk is most proportionate when the tolerance of risk is clearly defined and articulated
3. Risk management is most effective when ownership of and accountability for risks is clear
4. Effective decision-making is underpinned by good quality information
5. Decision-making is informed by a considered and rigorous evaluation and costing of risk
6. Future outcomes are improved by implementing lessons learnt

Source: NAO (United Kingdom National Audit Office) (2011), Good Practice: Managing risks in government, *http://www.nao.org.uk/wp-content/uploads/2011/06/managing_risks_in_government.pdf*

The role of internal audit

Internal auditors are a critical part of an organisation's internal control structure (INTOSAI, 1997). Internal audit is concerned with the effectiveness, efficiency and economy of the internal control system. Within government organisations, the internal audit function should be established as an independent, objective assurance and consulting activity designed to add value and assist the organisation in achieving its objectives by bringing a systematic and disciplined approach to evaluating risk management, control and governance processes.[29] Governing bodies and senior management rely on internal auditing for objective assurance and insight on the effectiveness and efficiency of governance, risk management and internal control processes.

Within ministries, internal auditors provide reasonable assurance that these processes are functioning in a manner that minimizes the probability of errors, inefficiencies and uneconomic practices, and fraud.[30] Internal auditors can assess the adequacy of controls in the overall internal control system and should, based on globally recognised standards, conduct their work in line with the organisation's risk-based approach (INTOSAI, 2010). To be most effective in the fulfilment of their mandate, internal auditors should provide reasonable assurance and advice to leadership on the adequacy of risk management and the sufficiency of control to mitigate risk.

As with SAIs, the independence of the internal audit unit from the rest of the ministry is paramount to its ability to carry out its function effectively. Additionally, internal audit's activities and outputs are expected to be objective and unbiased. Core internal audit roles with respect to risk management are (IIA, 2009):

- to review the management of key risks;
- to evaluate the reporting of key risks;
- to evaluate risk management processes;
- to give assurance that risks are correctly evaluated; and
- to give assurance on the risk management processes and activities.

Oversight of internal control processes

A number of bodies can play a role in providing oversight of internal control, including SAIs, audit committees and the Centre of Government.

Audit committees are comprised of members who are independent from the controlled ministry's senior management. They are responsible for the independent oversight of internal control, risk management and the internal audit function, and enhance the independence of the internal audit function insofar as internal audit units report to the audit committee. The existence of an audit committee can strengthen the independence of internal audit and the overall transparency of an organisation. The audit committee represents an important oversight body interested in ensuring that integrated risk management and control processes are effective in order to assist the management's overall governance duties. The IIA recommends that to be effective, audit committees should have at least three members, the majority of whom should be independent from the ministry, including the chair. Also, members should collectively possess relevant public sector, risk management, financial, and audit competencies, and their remuneration should be commensurate with audit committee workload, experience and personal exposure (IIA, 2013b).

Audit committees' functions should enhance organisational independence of internal audit through activities such as: making recruitment, remuneration and dismissal decisions pertaining to the chief audit Executive; determining the scope and budget of internal auditing on the recommendation of the head of audit; considering key issues raised by internal auditors, concurrently with senior management; and meeting with the head of audit without the presence of management (IIA, 2013b). The audit committee can also play an important role in the inter-relationship between internal auditors and external auditors from SAIs, by being a point of contact for both (Gilchrist et al, 2013).

Countries differ in how their internal control and audit functions are set up. The following table provides data on institutional arrangements for internal audit in selected countries. It shows that most countries surveyed have internal audit units, but most do not have a formal audit committee. In some countries, such as in Chile, Costa Rica, Denmark, Korea and Peru (Table 9.1), their respective national SAI provides an oversight role over internal audit functions.

Table 9.1. **Oversight of internal audit in the public sector in selected countries**

Country	Existence of internal audit units	Existence of audit boards/ committees	Internal audit co-ordination body
Australia	Yes	Yes	None
Brazil	Centralised within the Office of the Comptroller General; individual audit units exist for indirect administration	No	Secretariat of Federal Internal Control, Office of the Comptroller General of the Union (CGU)
Chile	Yes, internal audit units	No	Office of the Comptroller General of the Republic (CGR); Council of Government's General Internal Auditors (CAIGG)
Costa Rica	..	No	Office of the Comptroller General of the Republic
Denmark	Yes, but only in some public entities	No	National Audit Office of Denmark
Israel	Every public body	No	..
Italy	Yes, provided by independent performance evaluation bodies	No	Independent Commission for the Evaluation, Integrity and Transparency of Public Administration (CIVIT); Ministry of the Economy and Finance; State General Accounting Department
Korea	Internal audit units	No	Board of Audit and Inspection
Mexico	Internal control offices	No	Ministry of Public Administration
Peru	Yes, institutional control bodies – some in the Office of the Comptroller General and in some public entities	No	Office of the Comptroller General of the Republic
Portugal	All ministries and most of the public sector, except for smaller entities	No	Internal Audit Co-ordination Council
South Africa	Yes	Yes	..
Spain	Yes	No	General Control and Audit Office (IGAE)

Note: … = not available

Source: Adapted from "Chile's supreme Audit Institution: Enhancing strategic agility and public trust", OECD, 2014.

A 2011 OECD survey on internal control collected data from 73 ministries across 12 countries[31] to examine how professional standards, internal control standards and internal audit activities help strengthen accountability and integrity in the public sector (OECD, 2011). One key finding was that 91% of respondents reported having adopted an internal control framework comprising control activities, control environment, risk assessment and monitoring. The existence of a formal and comprehensive internal control framework was ranked as being most important for the enhancement of internal audit contribution to preventing, detecting and reporting fraud and corruption.

Three-quarters of respondents stated that internal audit units within their ministries report to the highest authority within the ministry, which is intended to enhance their independence in terms of defining their work plan, the execution of their work and transparency of their reports. These internal audit units also facilitate prevention, detection and reporting of fraud and corruption within ministries.

The survey also found that the involvement of management is a key component of countries' internal control and risk management systems. For 87% of respondents, management is assigned responsibility for internal control, 84% for risk management and only 75% for the prevention of fraud and corruption. Thus internal audit has a key role to play in advocating the formalisation of an internal control and risk management framework applying not only to purely financial controls, but also to the wider environment including codes of ethical conduct, and fraud and corruption prevention plans.

In line with the previous discussion on the Centre of Government, central government agencies can play an important overarching role in ensuring coherence across ministries internal control systems. Recognising the need for organisation specific particularities, central agencies are well placed to advise line ministries on best practices with respect to internal control, internal audit and risk management.

For example, the aforementioned Canadian *Framework for the Management of Risk* was developed by the Treasury Board Secretariat, a central government agency, to be used by all federal government organisations. This type of framework informs ministries' structures and processes around risk management while, in turn, helping the central agency to carry out its management, enabling and oversight roles over federal entities.

Internal control systems have seen changes over the past 10 to 15 years in various countries. In Europe, internal control reforms have led to increased attention being placed on objectives and performance management and risks as well as governance as a whole, including accountability and the quality of service delivery and cost efficiency (SIGMA, 2012). The functional independence of internal auditors has increased, and the programme of audit work has developed, focussing more on effectiveness, efficiency and economy and on the provision of information and assurance with regard to system operations. Practitioners of internal control, including internal auditors, have become, or are becoming, a professional category of staff with formal qualifications and special, long-term training programmes.

The role of SAIs

SAIs have the responsibility to conduct the external audit of the ministries or public entities in which internal control processes are embedded and over which internal control systems preside. Given that SAIs interact with internal control at these two levels, SAIs can contribute to more efficient and effective internal control processes at the ministry level, as well as at the whole-of-government level.

Collaborating with internal auditors

A constructive, professional and mutually beneficial relationship between SAIs and internal audit units within line ministries can lead to a more coherent contribution from public sector audits to public governance, as is recognised in INTOSAI's standards relating to *Coordination and Cooperation between SAIs and Internal Auditors in the Public Sector* (INTOSAI, 2010). External and internal audit functions perform a full range of audits, while offering distinct insights. SAIs also have the responsibility to evaluate the effectiveness of the internal audit function, as their external audit relies on internal audit units to provide credible and reliable information as inputs to their work.

Although internal auditors and SAIs report to different entities, the INTOSAI standards set out guidance on how SAIs and public sector internal auditors can coordinate and collaborate while performing their distinctive functions towards their collective goal of promoting good governance. There is recognition that co-ordination and co-operation between internal and external auditors can increase efficiency in their work through an exchange of knowledge and by minimising duplication of work (INTOSAI, 2010). In particular, dialogues on the risks facing the organisation can help to focus respective audit work, resulting in more useful recommendations and more effective audits (INTOSAI, 2010). Mutual benefits derived from a professional relationship can be achieved in a number of ways, and determining the appropriate modes of co-operation is case specific. These modes may include holding joint planning sessions, developing mutual consultation procedures, communicating audit reports, having common training programmes or seconding staff across audit functions (INTOSAI, 2010).

In most EU member states, internal and external audit entities have working relationships, including internal audit providing audit plans and reports to the SAI, audit organisations cooperating on methodological and training matters, and the SAI having the possibility, as an advisor or observer, to take part in regular meetings of the heads responsible for internal audit (SIGMA, 2012). Half of the European SAIs recently reported that they experienced the following benefits of coordination and cooperation between SAIs and internal auditors (Table 9.2).

Table 9.2. **Benefit of coordination and cooperation between SAIs and internal auditors**

Benefit of coordination and cooperation between SAIs and internal auditors	Responding SAIs %
More efficient audits based on better coordinated internal and external audit activity resulting from coordinated planning and communication; refined audit scope for SAIs and internal auditors	90
Reducing the likelihood of unnecessary duplication of audit work (economy)	85
Improving and maximising audit coverage based on risk assessments and identified significant risks	85
Mutual support on audit recommendations which may enhance the effectiveness of audit services	80
Minimising disruption to the audited entity	75

Source: EUROSAI-ECIIA Joint Paper, *Coordination and Cooperation Between Supreme Audit Institutions and Internal Auditors in the Public Sector*, May 2014

The Australian SAI has developed a "Better Practice Guide" for public sector internal audit, which recognises that a professional relationship between internal audit and external audit creates mutual benefits. For example, internal auditors can often be the primary liaison with the SAI and coordinate to ensure the SAI's work is facilitated when auditing that ministry. Furthermore, the guide encourages internal and external auditors to consult with each other during the work-planning phases, for both financial audits and performance audits. However, it also reiterates the importance of SAI's evaluation of the adequacy of internal auditors' work for both internal control processes and as inputs to external audit (ANAO, 2012).

Assessing internal control processes

SAIs can have a greater impact on good governance by taking a whole-of-government approach in evaluating internal control and in providing guidance on effective and efficient internal control systems and activities. This would entail broadening the scope of current SAI internal control assessments, which, according to 64 SAIs that responded to an INTOSAI survey, are primarily focussed on assessing compliance with applicable laws and regulations, cases of fraud and corruption and reliability of financial statements. About half analyse the effectiveness of the implementation of objectives and tasks set by the organisation (INTOSAI, 2013).

From a bird's-eye view, SAIs can identify systemic areas for improvement in the design and formulation of internal control systems and can highlight practices and procedures that are working well so that all ministries can benefit from the SAI's review. By taking a government-wide approach to systematically and periodically evaluate the robustness and adequacy of internal control functions and procedures put in place by the Executive SAIs could:

- provide credible and relevant information on the roll-out of internal control processes at the ministry level, particularly on risk management and internal audit good practices, with reference to achieving government objectives;

- provide insights on the Executive's current and future internal control strategies and oversight; and
- contribute to the government's internal anti-corruption and anti-fraud activities.

In evaluating the robustness and adequacy of internal control processes, SAIs could also assess the adequacy of the oversight mechanisms over internal control and internal audit across government. Where audit committees exist, SAIs could evaluate the level of independence of such committees including whether there is a majority of audit committee members recruited from outside the ministry and, ideally, some from outside the public administration. They could also review an audit committee's mandate to see whether it covers the monitoring of risks exposure, including those relating to fraud and corruption, and to check if there is periodic reporting of cases of fraud and corruption to the audit committee.

The South African SAI's analysis of internal control systems includes discussion on root causes of weaknesses, such as senior management vacancies, lack of training and a lack of consequences for non-compliance with laws. This root-cause analysis is more effective in clarifying the situation, which gives impetus to addressing the issues by the government.

SAIs could follow up on these audits to report on progress and highlight areas of risk as a way to ensure accountability and enhance good governance. For example, the 2013 Fall Report of the Auditor General of Canada included an audit on internal controls over financial reporting that was a follow up to a 2011 audit on financial management and control and risk management (AGC, 2013). In the follow up report the Auditor General concluded that the majority of entities that were audited in 2011 had made unsatisfactory progress in response to the 2011 recommendations. It also commented on the entities that had fully addressed the recommendations.

Providing information and guidance

Government-wide assessment audits on internal control can be used to inform the Centre of Government on the effectiveness of internal control across the government. Internal control should be a dynamic rather than a static process that adapts in order to address adequately changing risks to an entity's objectives. Thus, from a bird's-eye view, SAIs can draw upon their knowledge of internal control processes to bring coherence and effectiveness to the public sector's internal control activities on an on-going basis. Depending on the context, SAIs may simply package the information in a way that is useful for those who are responsible for coherence, namely the Centre of Government.

Based on COSO's elements of effective internal control processes (Box 9.1), a synthesis of information can support **planning** of effective internal control processes by using its information to construct good practices on:

- control environments, so that the standards and structures that are necessary for effective internal control at the ministry level are put in place; that management oversight and clear responsibilities are established; and that processes are in place to establish a competent workforce;
- processes for establishing risk tolerance, prioritisation and criteria; and
- planning of control activities of specific policies and procedures.

The information that SAIs generate could also be used to support effective **implementation** of internal control processes by informing on good practices related to the conduct of risk assessment and by adding to the accumulation of relevant and quality information needed to conduct control activities. By auditing ministries and evaluating internal audit, SAIs are part of the **monitoring** and **evaluation** stage of internal control processes, as per the fifth COSO element.

The Centre, assuming it is adequately resourced, would then be better equipped to guide ministries' internal control systems in a coherent, whole-of-government manner. In addition to the Centre's guidance, or in place of it where it is absent, SAIs can develop good practice guides, as the SAIs in Australia and the United States have done.

The Australian example above demonstrates that SAIs can synthesise findings of evaluations and audits in order to identify good practice and trends in internal control processes, as well as to detect risks to internal control systems more broadly. By being cognisant of this potential and of its usefulness, SAIs could package the information that it gathers through audits in such a way that it strengthens the government's formulation, implementation and monitoring and evaluation of more effective internal control processes.

The SAI of the United States is in the process of updating its standards for internal control for federal agencies, which were first drafted in 1983 (GAO, 2013). The standards are intended to provide management criteria for designing, implementing, and operating an internal control system and to reinforce management's accountability for internal control.

Officials in the Executive should consider welcoming SAI advice and guidance on internal control matters. Almost half of the ministries surveyed by the OECD in 2011 indicated that it would be useful for SAIs to make recommendations for specific controls to better address the risks of fraud and corruption. To this end, SAIs could evaluate the design, implementation, and effectiveness of an organisation's ethics-related objectives, programmes and activities, and determine whether they include effective ethics awareness and training. SAIs could perform periodic audits of the design and quality of anti-corruption and anti-fraud frameworks and make recommendation for establishing and strengthening the field of ethics and integrity and conflict-of-interest policy.

SAIs could also play a formal role in the development of national anti-corruption strategies, as they do in Brazil, Chile, Costa Rica, the European Union, Italy and South Africa (OECD, 2014). In Brazil, the National Strategy for Combating Corruption and Money Laundering involves approximately 60 public entities and civil society organisations, directly or indirectly, in preventing and combating corruption and money laundering. The Brazilian SAI is an active member of the National Strategy for Combating Corruption and Money Laundering and is responsible for, or participates in, several actions. In Costa Rica, the Comptroller General of the Republic, the Office of Ethics and the Costa Rican Institute on Drugs have an anti-corruption agreement that defines the national strategy on the topic. One of the European Court of Auditors' tasks is to screen major anti-fraud and corruption legislation and systems to ensure that they provide adequate protection against fraud and corruption and do not open up opportunities for fraud within the EU.

Notes

27 Adapted from the Committee of Sponsoring Organisations of the Treadway Commission (COSO) definition of Internal Control. www.coso.org

28 In part from INTOSAI GOV 9100.

29 Derived in part from IIA definition of Internal Auditing.

30 Formulated from INTOSAI definition contained in ISSAI 9150, 3.2.1.

31 Australia, Brazil, Bulgaria, Canada, Finland, France, Japan, the Netherlands, South Africa, Sweden, the United Kingdom and the United States.

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