

# *New focuses in the relationship of the World Bank and the supreme audit institutions*

## *Lessons learned from a World Bank seminar*

The World Bank and the audit offices, as well as INTOSAI, the international organisation comprising the latter, have been converging for years. This convergence has been based on the sense of responsibility shown by both systems of institutions in the proper and efficient application of public funds, good financial direction, effective accomplishment of public administration activities, and supplying information to the state control authorities and the general public through objective reports.

For the World Bank and the donor countries, this cooperation is made directly valuable by the fact that the activity of audit offices may significantly facilitate the application of subsidies towards the goals. This has also motivated the World Bank to develop a strategy: to see how it is capable of supporting and reinforcing the activity of audit offices.

The importance of implementing these efforts and the Millennium Development Goals was suggested by the World Bank's Vice-President *James Adams* in his opening address at the seminar entitled 'Developing the capacity of state audit offices: opportunities and challenges'<sup>1</sup> to the participants from the World Bank and a few experts invited to give lectures. The Vice President also mentioned on a critical note that the World Bank had spent millions of US dollars in the past ten years on developing

direction systems for public funds in developing countries – primarily in Africa –, but the desired results had not been achieved.

On behalf of the World Bank, the principal goals of the seminar were summarised by the Bank's chief expert of financial direction, *Rafika Chaouali* in four points:

- it is a fundamental part and manifestation of cooperation pursued with the audit office;
- it is an opportunity for the World Bank staff to familiarise themselves with the audit offices' progressive experience with reforms;
- an exchange of experience is to be carried out on the challenges involving public funds direction systems, and
- to understand where and what cooperation can be expected by the World Bank, and from whom, under an efficient partnership.

## A REVIEW OF THE REGIONS

For meeting these goals, good starting points were provided by the World Bank's experts in their presentations giving a diagnosis of World Bank regions. As in almost every respect, regions show a great deal of diversity also in terms of audit office features. This report will only allow for mentioning but a few.

In the *African region*, the performance capaci-

ties of audit offices differ widely, and development programs are in many case in the planning phase only. Implementation is hindered almost everywhere by a shortage of resources and experts. Another problem is that the relationship between the audit offices and the parliaments is insufficient both in terms of quality and intensity. This is also related to an undesirable phenomenon whereby new audit organisations are often established, weakening the role of existing audit offices.

In a number of countries in the *European and Central Asian region*, the establishment of legal and institutional frameworks necessary for audits, independence of operation and the improvement of relations with legislators still pose a challenge. Within this region, the best audit office performance is produced by the EU8 countries. Among these – according to the expert requested to organise this seminar, former chief auditor of the French audit office and the president of OECD's External Audit Committee, *Patrick Mordacq* – Hungary and Poland lead the way.

The countries of *Latin America and the Caribbean region* have achieved significant development in improving the legal and independence statuses of audit offices; however, independence in terms of finance and operations, as well as the size of actually available financial resources are still not sufficient for efficient external auditing. Another general problem is that the opinions and recommendations made by audit offices are utilised to a small extent.

The auditing practice of the *Middle Eastern and North African region* is characterised by a high degree of diversity: supervision over court and common law audit offices ranges from the government through the head of state to the parliament. Capacity development is highly required, however, the relation maintained by some countries with donor countries is unsatisfactory. Audit offices do not audit World Bank projects.

In the *South Asian region*, auditing culture has considerable traditions. Difficulties are caused by low levels of administrative independence, and the

associated frequent interventions by the ministry of finance. Unsatisfactory are the facilities of familiarisation with audit results, and it is also typical here to have a low level of accepting and enforcing audit office opinions and suggestions. The audit offices also audit most World Bank projects.

Within the *East Asian region*, in China, audit also extends to subsidised projects, in addition to the ones with domestic funding. Mongolia focuses on adopting international standards, while Vietnam and Cambodia on developing internal audit. In Indonesia, enhancement of auditing capacity is emphasized.

## TRENDS IN AUDITING

Based on this diagnosis – illustrated with examples – and the experience presented by the invited experts of developed countries, some statements can be made on the courses of development typical of the activities of state audit offices.

■ Experience shows that the legal operating environments of audit offices and the direction features of public funds systems vary. However, there was an agreement in the seminar that an obstacle to assisting public funds reforms more efficiently was – while a slow progress was seen – that the independence of the audit office was not enforced properly. Out of the five elements influencing it, – legal, operational, financial, management/administrative independence and free information –, it is most frequently financial independence and the election of the management for political considerations that hinder the enforcement of management/administrative independence most. In addition to this, as pointed out by Canada's chief auditor *Sheila Fraser*, the most critical point – even in developed countries – was to achieve financial independence.<sup>2</sup> The importance (severity!) of this issue is indicated by the fact that in Canada a Charta is being produced on independence.

■ Another major obstacle to the activity of audit offices is – as seen with the regions – the shortage of audit capacities. This is primarily manifest in the low standards of auditors' professional competence. More efficient auditing is also hindered by the fact that information obtained by auditors is restricted, for example, important budgetary expense items are considered to be beyond their mandates, and the establishment of efficient working relations with the ministries of finance, other ministries and government organisations are impeded. For this reason, development of audit capacities is a high priority task with resolution especially urging in the emerging countries. Denmark's chief auditor, *Henrik Otbo* highly appreciated the World Bank's initiative to have directed attention to this important area with this seminar. In this context, the chief auditor of the United States of America, *David Walker* emphasised that the quality standard of audits needed to be raised, and the closest possible international cooperation was indispensable to achieve this – highlighting the role of the World Bank. Both pointed out that audit offices deserved confidence. The chief auditor of the US also supported it with personal experience, stating that – at more developed levels of activity – the professional standard of state audit offices does not fall behind that of private audit/consultancy companies.

■ In the world – experts unanimously stated – familiarity with and utilisation of audits performed by audit offices are unsatisfactory. Experience gained through auditing is not widely known to citizens, and this restricts their control over the process of modernising the public funds system, and also plays a role in the fact that audit offices do not, or hardly use the method of risk analysis in their activity. An obstacle is, for instance, that decision-making governments often fail to show sufficient will to implement the recommendations of audit offices, and the working relationship between parliaments (the committees) and the audit offices is inappropriate.

This shortcoming has been termed by Patrick Mordacq as an “expectation gap” towards audit offices. For emerging countries and countries in transition, he raised the issue that auditors often set up a narrow scope of activity for themselves, and in this way they are merely “auditors” instead of “helpers” of financial reforms. This is the transformation that should be facilitated by reinforcing the capacity of audit offices – through more thorough training, a better level of organisation, application of more recent methodologies, elimination of the formality of audits, etc. –, as well as a bolder attitude to taking on any potential errors (risks) of forward-looking consultancy.

Out of the methods aiming at unfolding this latter activity, considerable attention has been directed to the Canadian and Hungarian practises. In Canada, an organisation working as an independent and neutral forum, the Canadian Comprehensive Auditing Foundation, provides assistance in improving the efficiency of the audit office's activity by serving auditors, government managers and elected MPs, as well as by cooperating with them as a partner. This service embraces activities, starting from reinforcing accountability through research to training. Under research activities – for example – principles have been developed for reports on the performance of the public sector, by conducting diverse consultations with the representatives of the abovementioned three target groups of partnership. Another example: the Foundation summarises the major recommendations of the auditors in publications for the parliamentary committees.

A similar activity characterises the Hungarian practice. The Institute for Development and Methodology of the State Audit Office, in addition to presenting best international practises and experience, issues summarising and analysing studies to assess the development tendencies related to public finance, and pays particular attention to presenting the reasonable courses of reforms necessary in the public finance system.

However, development of forward-looking consultancy of audit offices cannot be considered a boundless process. By multiple considerations of each country's capabilities, – as the chief auditor of the US, David Walker put it – one can palpate the limit that ought not be crossed.

■ Today, perceivable convergence is being implemented in the public funds direction systems. This globalisation-related change also has an impact on financial auditing activity.

Based on the presentations and discussions of this seminar – with some courage – an attempt can be made at briefly reviewing the changes and trends perceived in financial auditing.

- Financial/compliance audits are indispensable but insufficient to achieve a sustainable fiscal position. Performance audits need to be placed in the foreground, to be used as the principal value in the audit office's activity.
- With the extending role of performance audits, the decentralised nature of audits is intensified, which requires different auditor capabilities and information. (Decentralisation is progressing also in internal audits.) The progressive practice of programme budgets also needs to reinforce decentralisation – even if with a new attitude.
- Also related to some extent to the increasing role of performance audits ex post audits gain increasing significance as opposed to ex ante audits.
- For good governance, transparency and accountability are becoming increasingly important requirements. A prerequisite to

accountability is transparency; consequently, these two criteria are inseparable.

- In financial auditing, the functions and tasks of internal control mechanisms and independent internal audits are reasonably established in harmony with each other, using approaches and methods typically used in audit office audits and methods.
- The supply models of public services are changing to include a growing role of background institutions, outsourcing, and projects implemented with public private partnership (PPP). The capacity enhancement of state audit offices needs to be implemented in a way that provides them with the ability to meet challenges concomitant with these changes.

■ The work performed in this seminar has also proved: state audit offices are not island-like, standalone institutions, but important parts of the public funds direction system. For this reason, the World Bank's expert staff intend to maintain even closer and more efficient cooperation with state audit offices in the future. A strategic cooperation between the World Bank and the audit offices provides powerful support to INTOSAI's strategic and renewal plan for the years 2005–2010, and facilitates implementation of the first two of the four major objectives laid down in the strategy, namely, enforcement of professional standards and accountability, as well as institutional capacity development. In summary of the above, it can be stated that the seminar met its objective in all respects.

*Gusztáv Báger*

## NOTES

1 This seminar was held on 3rd and 4th May 2006 in Washington. The World Bank invited lecturers for panel discussions in recognition of their performance at audit offices, i.e. representatives of the respective audit offices in Australia, France, Denmark, Canada, Poland, Hungary, Great Britain and the United States of America were present.

2 In Hungary, the SAO's financial independence has particularly been enforced since 2004, considering that it has submitted its draft budget directly to Parliament.