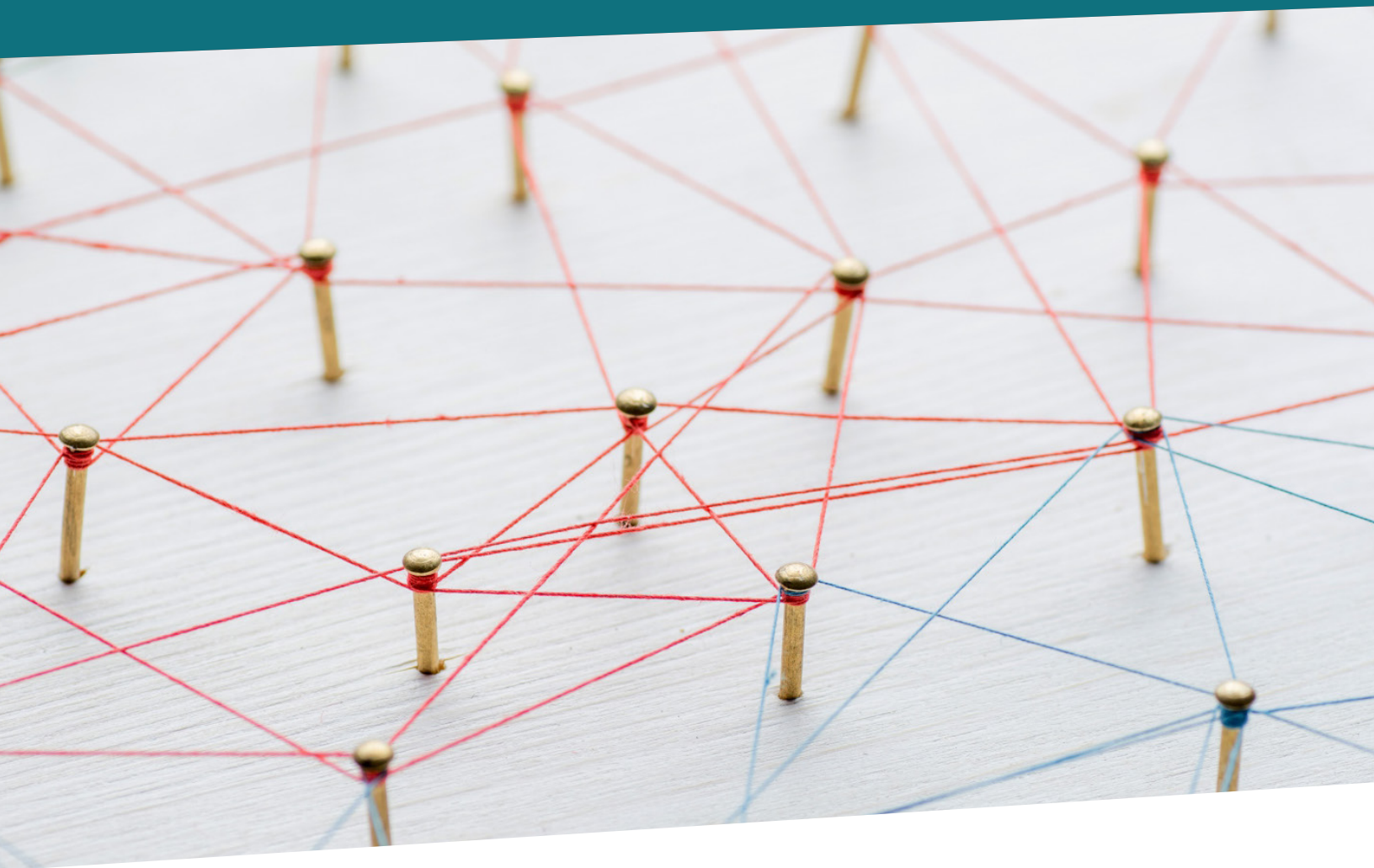


# Strengthening Budget Credibility through External Audits

**A Handbook for Auditors**



**United  
Nations**

Department of  
Economic and  
Social Affairs



**International  
Budget  
Partnership**

# Strengthening Budget Credibility through External Audits

A Handbook for Auditors

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Comments and feedback: [info@internationalbudget.org](mailto:info@internationalbudget.org); [dpidg@un.org](mailto:dpidg@un.org)

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- ii. It facilitates the negotiations of Member States in many intergovernmental bodies on joint courses of action to address ongoing or emerging global challenges; and
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The International Budget Partnership partners globally with budget analysts, community organizers, and advocates working to advance public budget systems that work for people, not special interests. Together, we generate data, advocate for reform, and build the skills and knowledge of people so that everyone can have a voice in budget decisions that impact their lives.

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**Lead coordinators:** Aránzazu Guillán Montero (UNDESA/DPIDG), Claire Schouten (IBP)

**Editor:** Debby Friedman

**Layout:** Damilola Ogundipe, Segun Adeniyi

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aspects of this work.

*The authors of this handbook include:*

**Chapters 1 and 2:** Aránzazu Guillán Montero (UNDESA/DPIDG), with contributions from Maximiliano Castillo Carrillo (Office of the Auditor General of the Nation of Argentina);

**Chapter 3:** Martin Bamulumbye and Peter Oyo Mugenyi (Office of the Auditor General of Uganda), with contributions from the SAIs of Argentina, Brazil, Georgia, Indonesia, Morocco, the Philippines, and Zambia;

**Chapter 4:** Winarno, Thopan Aji Pratama, Ramadhan Nugraha Putra, and Anisa (Audit Board of The Republic of Indonesia), with contributions from Cynthia Grace Matimba, Ngawa Mphande, and William Chibesa (National Audit Office of Zambia);

**Chapter 5:** Neemias Albert de Souza and Roberto Santos Victor (Federal Court of Accounts of Brazil), with contributions from the SAIs of Argentina, Georgia, Morocco, the Philippines, and Uganda;

**Chapter 6:** Cora Lea A. Dela Cruz, Josephine B. Manalo, and Paul Jonel Pollicar (Commission on Audit of the Philippines), with contributions from the SAIs of Argentina, Brazil, Georgia, Indonesia, Morocco, and Zambia; and

**Chapter 7:** Maximiliano Castillo Carrillo and Anibal Kohlhuber (Office of the Auditor General of the Nation of Argentina), with contributions from the SAIs of Georgia, Indonesia, and the Philippines.

Additional SAI contributors included Mouhcine Hanoun and Abedaali Ouissole (Court of Accounts of the Kingdom of Morocco); Tsotne Karkashadze and Lasha Kelikhashvili (State Audit Office of Georgia); Parishka Bhana (Auditor-General of South Africa); Aurich Champagnie (Auditor General's Department of Jamaica); and Jeff Arkin (US Government Accountability Office).

*Providing critical feedback towards the final product, the peer reviewers were:*

**Chapters 1 and 2:** Lawrence Ayagiba (Ghana Audit Service), Mary Ann Curet (Court of Audit of Aruba), Lorena Rivero del Paso (International Monetary Fund), and Sally Torbert (International Budget Partnership);

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**Chapter 5:** Lasha Kelikhashvili (State Audit Office of Georgia), the Board of Audit and Inspection of Korea, and Sébastien Lepers (French Court of Audit);

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## List of acronyms

AFROSAI	African Organisation of Supreme Audit Institution
AFROSAI-E	African Organisation of English-speaking Supreme Audit Institutions
ARABOSAI	Arab Organization of Supreme Audit Institutions
ASOSAI	Asian Organisation of Supreme Audit Institutions
BDA	big data analytics
BiH	Bosnia and Herzegovina
BOOST	although written out in all caps, this budget data portal is not a classic acronym, but rather is meant to emphasize the momentum that comprehensive disaggregated quality budget data can bring to a country.
BPK RI	Audit Board of the Republic of Indonesia
CA	compliance audit
CAROSAI	Caribbean Organisation of Supreme Audit Institutions
CEPA	United Nations Committee of Experts on Public Administration
ECA	European Court of Audit
EUROSAI	European Organisation of Supreme Audit Institutions
FA	financial audit
FGD	focus group discussions
GAO	U.S. Government Accountability Office
GDP	Gross domestic product
GFSM	Government Finance Statistics Manual
GIFT	Global Initiative for Fiscal Transparency
HLPF	High-level Political Forum
IBP	International Budget Partnership
ICT	Information and communication technology
IDI	INTOSAI Development Initiative
IFI	independent financial institution
IFMIS	integrated financial management information system
IMF	International Monetary Fund
INTOSAI	International Organization of Supreme Audit Institutions
IPSAS	International Public Sector Accounting Standards
iSDG	Integrated Sustainable Development Goals (modeling tool)

ISO	International Organization for Standardization
ISRE	International Standard on Review Engagements
ISSAI	International Standards of Supreme Audit Institutions
IT	information technology
MDA	ministries, departments, and agencies
MoF	Ministry of Finance
NDP	National Development Plan
OBS	Open Budget Survey
OECD	Organisation for Economic Co-operation and Development
OLACEFS	Organization of Latin American and Caribbean Supreme Audit Institutions
PA	performance audit
PASAI	Pacific Association of Supreme Audit Institutions
PEFA	Public Expenditure and Financial Management
PFM	public financial management
SAI	Supreme Audit Institution
SDG	Sustainable Development Goals
SOE	state-owned enterprise
TCU	Tribunal de Contas da União (SAI Brazil)
UK NAO	National Audit Office of the United Kingdom
UNDESA	United Nations Department of Economic and Social Affairs
UNDP	United Nations Development Programme
UNICEF	United Nations Children's Fund
VNRs	Voluntary National Reviews



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# Introduction

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**The budget is one of the most important public documents produced by a government, expressing its priorities and commitments. It is the place where a government proposes how much revenue it plans to raise and how it plans to use these funds to meet the nation's competing needs, from bolstering security to improving healthcare to alleviating poverty. Given its wide-ranging implications for a nation's citizens, the budget should be the subject of widespread scrutiny and debate.<sup>1</sup>**

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National budgets are meant to provide a roadmap to the effective delivery of public services and to the achievement of long-term national objectives such as the Sustainable Development Goals (SDGs). When the government implements its revenue and spending plans as approved by the legislature, its budget is considered "credible."<sup>2</sup> But when that is not the case and budgets are not credible, trust in public institutions diminishes, the integrity of public funds is jeopardized, and the risk of corruption rises. In recognition of the importance of budget credibility for effective, accountable, and transparent institutions, a dedicated indicator – 16.6.1 – is included in the global framework of indicators to monitor progress on the SDGs at the global level.<sup>3</sup>

Recent research indicates national budgets veering off course is a widespread and significant problem and impedes progress on key social and economic priorities. Several factors contribute to budget credibility challenges. In addition to technical issues - such as faulty revenue forecasting, weak procurement systems, or inadequate policies to control the shifting of funds - the role of external financing as well as political and institutional considerations are relevant in many countries.

Confounding the problem, when budget deviations do occur, often they are not properly accounted for. Many countries either do not provide explanations or provide too few essential details.<sup>4</sup> Repeated budget deviations in the absence

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<sup>1</sup>Joel Friedman, 2006. A Guide to Tax Work for NGOs. International Budget Partnership (IBP).

<sup>2</sup>See Chapter 1, section 1.1, and Chapter 2, section 2.1, on the standard definition of budget credibility

<sup>3</sup>Indicator 16.6.1 measures primary government expenditures as a proportion of the originally approved budgets (by sector, budget codes, or similar). See <https://unstats.un.org/sdgs/metadata/files/Metadata-16-06-01.pdf>

<sup>4</sup>Jason Lakin and Guillermo Herrera, 2019. "Explain that to us: how governments report on and justify budget deviations" IBP, <https://internationalbudget.org/publications/how-governments-report-and-justify-budget-deviations/>



of adequate justifications further undermine confidence in the ability of a government to make realistic plans and adhere to commitments.<sup>5</sup>

Given their essential role in auditing government finances, Supreme Audit Institutions (SAIs) are uniquely positioned to assess budget deviations, point to their consequences, and record any justifications. However, the literature on public financial management (PFM) is sparse on how SAIs contribute to understanding and assessing budget credibility. This handbook aims to fill this gap by offering a practical overview of existing audit work related to budget credibility in different regions among various SAI models and by providing specific guidance and practical examples to support SAIs to further advance these efforts.

## The importance of auditing budget credibility

SAIs have an important role to play in strengthening the implementation of the SDGs and ensuring that a country's budget is on track. Checking and reporting on the legality and accuracy of public accounts, as well as the credibility of budgets, can be instrumental in governments delivering on their sustainable development promises. Audits can improve budget credibility in several ways:

- **Audits help assess the fulfillment of international commitments and standards**

**and improve public financial management (PFM) systems.** As reflected in SDG16 and existing international budget standards, governments have made commitments related to the credibility of their budgets. These commitments entail taking action at the national level, including enacting legislation, defining responsibilities, and strengthening PFM systems. Because these actions occur at the national level, it is within SAIs' mandate to assess governments on these issues.

- **Audits help to identify and examine the causes and impacts of budget credibility problems.** Government budgets significantly affect people's lives, especially those most in need. Budget deviations can have an adverse impact on achieving long-term policy and national objectives and on the quality of service delivery. Citizens have an expectation that governments will deliver on their commitments. Audits can help determine why breaches of contract occur, whether the reasons are justified, and discern the differential impacts that these deviations may have on different groups and /or across policy areas.
- **Audit recommendations can lead to improvements in the budget process and in the execution of budget resources at both the aggregate and the sectoral levels.** Budget deviations – both at aggregate levels of spending and in the composition of spending – happen for a variety of reasons. An audit report, as the summary of an independent and

<sup>5</sup>Jason Lakin, 2018. "Assessing the quality of reasons in government budget documents" IBP, <https://internationalbudget.org/publications/assessing-reasons-in-government-budget-documents/>

<sup>6</sup>This activity has been particularly significant in the context of the pandemic, given the volume of public resources mobilized through relief packages and recovery plans. For examples of SAI oversight responses during this period, see IBP, 2021. Managing COVID funds. The accountability gap, Washington DC, IBP, May, at <https://internationalbudget.org/covid/> and UN-INTOSAI, 2021. Working during and after the pandemic: building on the experience of SAIs for strengthening effective institutions and achieving sustainable societies, 25th UN-INTOSAI Symposium, June 2021, at [https://www.intosai.org/fileadmin/downloads/news\\_centre/events/un\\_int\\_symposia/reports\\_un\\_int\\_symp/en/EN\\_25\\_Symp\\_2021\\_report.pdf](https://www.intosai.org/fileadmin/downloads/news_centre/events/un_int_symposia/reports_un_int_symp/en/EN_25_Symp_2021_report.pdf)

evidence-based assessment, can shed light on what is creating budget credibility risks, and include recommendations for governments to address them. The implementation of these recommendations is crucial for improving budget execution and credibility.

- **Audit reports can raise awareness of budget credibility both within and outside government** and convey how it affects the achievement of national goals and policies, service delivery, and the performance of the PFM system. Audit reports – which should be made publicly available – can also highlight the strengths and challenges of governments and specific public entities in enhancing budget credibility.

## Current status of audit work on budget credibility

Budget credibility has gained increased attention in recent years but is still a new topic. More research, both across countries and through in-depth case studies, is needed to better understand its drivers so as to ensure critical and effective service delivery. More external audits – especially those that explicitly address credibility issues and disseminate findings to government entities, parliaments, experts, the media, civil society, and the general public – will bring increased attention to the credibility of government budgets. This can help assess ongoing government action and encourage course correction, as needed.

SAIs are aware of budget credibility problems – 74 percent of 27 respondents to a 2021 SAI survey identified it as a significant problem in their countries<sup>7</sup> – and many address related issues in their work (82 percent of respondents in the same survey).<sup>8</sup> In several countries, SAIs already produce a variety of audit reports that help understand budget credibility in specific government entities and programs and the extent and causes of budget deviations. SAIs' work in this area also helps analyze wider trends in PFM systems that create risks to budget credibility.

However, SAIs do not systematically conduct comprehensive assessments of budget credibility, particularly at the aggregate level. While audits often identify common factors associated with budget credibility risks, they do not necessarily link them with aggregate budget deviations. Also, some audits merely identify overruns or under-expenditures without additional analysis to understand their impact on the achievement of policy objectives and development outcomes.<sup>9</sup>

Several things may explain these findings:

1. a limited understanding of what budget credibility means for an SAI and how it can be operationalized for auditors;
2. lack of awareness on how the traditional work of an SAI supports budget evaluation, and what it means to conduct a budget credibility assessment;
3. the absence of audit standards on budget credibility assessments;
4. inadequacy of or lack of access to relevant budget information in a timely manner; and

<sup>7</sup>This 2021 survey (27 respondents) was conducted for an earlier report (see footnote 7) and the year before the 2022 UNDESA/IBP SAI survey (38 respondents) which provided yet additional key information for this handbook.

<sup>8</sup>Aránzazu Guillán Montero, 2021. Upholding commitments. How supreme audit institutions can strengthen budget credibility through external audits, Washington DC, IBP. (<https://www.internationalbudget.org/wp-content/uploads/sai-budget-credibility-march-2021.pdf>)

5. the different timing and processes of diverse audit practices (given budget credibility issues cut across different types of audits) make it difficult to combine audit information into an assessment of budget credibility at the national level.

Generally, SAIs identify they have the mandate to audit budget credibility, according to a 2022 survey of INTOSAI members.<sup>10</sup> However, the choice of whether and how to incorporate budget credibility into the annual audit plan will be influenced by the SAI's particular mandate, institutional structures, priorities, and resources.

Acknowledging the differences among SAI circumstances, this handbook explores different approaches to auditing budget credibility and draws on SAIs' experience in different countries. Each approach has implications on audit methodology, including the type of audit practice, the definition of audit objectives, criteria, and specific audit tools to be used.

## Outline of the handbook

This handbook is intended to support SAIs in identifying whether and how an audit related to budget credibility is relevant and manageable in their respective context. To that end, the handbook presents an array of approaches and examples that can serve as a reference for auditors and help advance efforts to strengthen SAIs' contribution to budget credibility.

The first two chapters present the conceptual and analytical framework of the handbook:

- **Chapter 1** introduces the concept of budget credibility in the context of the wider public financial management (PFM) system and highlights relevant international standards and tools.
- **Chapter 2** operationalizes the concept of budget credibility from an SAI perspective and identifies relevant dimensions that can help delimit the scope of the concept for auditors, considering differences across countries. The chapter reflects on the strategic considerations for selecting budget credibility as an audit topic and provides an overview of audit standards and processes to audit budget credibility. Annex 2.1 provides examples of credibility-related issues and risks examined by SAIs.

The next several chapters cover different approaches SAIs may follow to audit budget credibility and draw on the experiences of SAIs from different regions to help auditors understand what the work entails:

- **Chapter 3** provides guidance on how to identify and assess budget credibility risks across the budget cycle at the whole-of-government level. Annex 3.1 offers questions to probe budget credibility risks at the whole-of-government level.
- **Chapter 4** focuses on SAIs' experience in

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<sup>9</sup>Ibid.

<sup>10</sup>Eighty-two percent of the 38 SAIs responding to the 2022 UNDESA/IBP survey indicated they had the mandate to audit budget credibility.

auditing the performance of the PFM system. These audits rely on a performance and/or compliance approach. Annex 4.1 and Annex 4.2 offer examples of the RIAS (risk, impact, auditability, significance) method and an audit design matrix, respectively, for planning an assessment of the PFM system's performance.

- **Chapter 5** provides guidance on auditing the state budget or year-end accounts on a regular basis. These recurring audits apply a financial and compliance focus to the annual budget cycle. They can include analysis at the program and entity level and, in a few examples, can also incorporate performance elements. Annex 5.1 provides a sample audit planning matrix, a useful tool when organizing an audit examining budget credibility.
- **Chapter 6** examines auditing of budget credibility risks at the entity or program level. These audits are of the performance, financial, and/or compliance type and are conducted

separately from the audits of the execution of the state budget. Annex 6.1 suggests selection criteria for auditing budget credibility and Annex 6.2 provides a self-checklist to guide auditors assessing budget credibility risks at the program/entity level.

The concluding chapter complements the analysis presented in the previous chapters by focusing on a specific and crucial phase of the audit process:

- **Chapter 7** focuses on the monitoring and follow-up to audit recommendations, illustrating different ways SAIs can work with stakeholders to encourage public entities to implement redress measures that will meaningfully strengthen budget credibility. This chapter also emphasizes the essential aspects of a strong audit report to make this happen. Annex 7.1 suggests ways to integrate budget credibility into the audit process while enhancing stakeholder engagement.

# Chapter 1: Budget credibility and public financial management

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**As countries increasingly focus on implementing policies in pursuit of the Sustainable Development Goals (SDGs), attention is often focused on the financing gap governments face in meeting their commitments. Not enough questions are being asked about the government’s capacity to effectively manage and spend the resources that they already have – or say they have.<sup>11</sup>**

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This chapter introduces the concept of budget credibility and provides an overview of the goals and processes of public financial management (PFM). After explaining how budget credibility is typically assessed, and reviewing recent research on the extent and determinants of credibility, this chapter also presents international standards and diagnostic tools relevant to budget credibility that auditors may find useful in their work.

## 1.1. What do we mean by “budget credibility”?

The standard definition of budget credibility refers to the government’s ability to meet its revenue and expenditure targets during the fiscal year. These targets should be explicit in the budget that is approved by the legislature and enacted into law.<sup>12</sup> When government spending deviates from the approved budget, this action is described as:

- **Underspending:** if actual spending is less than what was allocated in the budget, or

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<sup>11</sup>Paolo de Renzio, Jason Lakin, and Chloe Cho, 2019. Budget Credibility Across Countries: How Deviations are Affecting Spending on Social Priorities, IBP. at <https://internationalbudget.org/publications/budget-credibility-across-countries/>

<sup>12</sup>See the International Budget Partnership’s [Fact sheet on budget credibility](#)

- **Overspending:** if actual spending is greater than what was allocated in the budget.

A country's budget may be underspent or overspent overall – i.e., in aggregate – or within a specific area or sector of the budget (e.g., in agriculture, education, defense, etc.), or both. When shifting of spending among sectors occurs after the approval of the budget, the composition of the budget is changed, and in such a case, compositional budget credibility is affected. Thus, theoretically, a national budget could be credible in the aggregate, while its compositional spending is significantly off. (See Figure 1.5 at the end of this chapter for an example of deviations in sector spending.)

Measurements of the extent and prevalence of budget credibility in Section 1.3 and the international standards and assessment tools presented in Sections 1.4 and 1.5 are all built around this definition of budget credibility. In Chapter 2 and in other parts of this handbook, however, the discussion also looks at ways auditors can assess budget credibility more broadly to examine the many factors and risks that influence the attainment of credibility.

## 1.2. Public financial management (PFM) goals and processes

### What is PFM?

Public financial management (PFM) refers to the way governments manage public resources (both revenue and expenditure) to achieve the agreed-upon social and economic objectives of their country. It consists of processes defined by a broad set of rules and regulations that govern the management of public resources – i.e., revenue mobilization, the allocation of public funds to various activities, the actual expenditure on these items, and the accounting for spent funds.<sup>13</sup>

PFM systems are embedded in and influenced by the broader context of national institutions, bureaucratic systems and policy processes, which vary across countries. PFM comprises a variety of institutional arrangements. For example, while most countries have some form of external audit institution that checks the government's accounts, there are different models of Supreme Audit Institutions (SAIs) (judicial, collegiate/board, Westminster) with different mandates. Despite contextual differences, some processes in PFM systems are similar across countries, as described in the next section.

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<sup>13</sup>Rebecca Simson, Natasha Sharma, and Imran Aziz, 2011. "A guide to public financial management literature. For practitioners in developing countries", December, London, Overseas Development Institute.

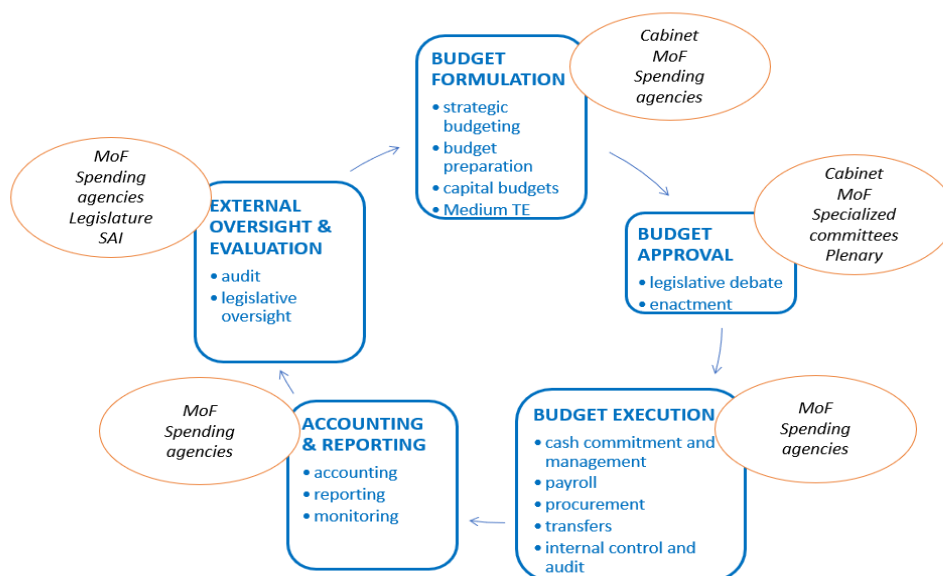
<sup>14</sup>Chapter 3 elaborates on the roles and responsibilities of the Ministry of Finance and the legislature.

## PFM processes and activities

PFM processes are commonly structured and described around the budget cycle. Each of

the stages of the budget cycle can be further subdivided into key processes and activities that involve different stakeholders.<sup>14</sup> (Figure 1.1.)

Figure 1.1. Overview of PFM processes and actors by stage of the budget cycle



Source: A. Guillán Montero, 2023.

## Budget formulation

A new budget cycle begins with the government planning for the use of resources for the coming year. Many countries start the formulation of the budget with a strategic budgeting phase, also referred to as the “pre-budget phase,” to ensure the budget is prepared with due regard to fiscal policies, strategic plans, and adequate

macroeconomic and fiscal projections.<sup>15</sup> This involves translating policy goals into financial targets, given expected economic and social conditions. Revenue forecasts and expenditure estimations are produced. Many countries attempt to produce multi-year estimates, and some use this process to generate program or performance budgets. (Box 1.1.)

<sup>15</sup>Matt Andrews, Marco Cangiano, Neil Cole, Paolo de Renzio, Philipp Krause, and Resnaud Seligmann, 2014. “This is PFM,” Center for International Development, Working Paper No. 285, July, Harvard University.

## Box 1.1. Program and performance budgeting

*Program budgeting* is a method of organizing and classifying the budget according to programs with shared objectives.

*Performance budgeting* introduces performance incentives through different approaches (e.g., considering performance objectives and indicators in the budgeting process). It is often introduced in combination with medium-term expenditure frameworks and usually draws on a program budget structure. (See also Box 6.6 on performance-based budgeting.)

Source: Simson, Sharma, and Aziz. 2011.

Budget preparation involves assembling and finalizing the budget proposal that will be submitted to the legislature, presenting revenue, expenditure, and financing plans for the entire government for the upcoming budget period. The budget proposal is usually produced on an annual basis and should contain, at least, the following elements: a macroeconomic framework and revenue forecast; a discussion of budget priorities, planned expenditure, and past outturns; a medium-term outlook; and details on budget financing, debt, and the government's financial position. Items in the budget proposal are classified according to the nature of financial flows.<sup>16</sup> Some countries use economic categories, others administrative units or specific functions and programs, and some actual performance.

Multiple entities participate in this process, but the Ministry of Finance plays a central role, producing projections and engaging with entities to assess their spending requests.

Each country's laws and regulations will specify how the budget documents should be prepared: by whom, by when (specified timelines), and with what content.<sup>17</sup> In accordance with international standards, budgets should be comprehensive, transparent, and realistic.

### Budget approval

Before the budget is approved, the budget proposal will be analyzed and debated in the legislature. Sometimes, the legislature will propose amendments. Amendment powers of the legislature vary across countries. The basis on which the budget is approved (e.g., by line item, program) is essential for accountability and reporting requirements and standards. The budget is ultimately enacted into law by the legislature, an action that subsequently authorizes the executive to raise revenue and spend resources.

<sup>16</sup> Simson, Sharma, and Aziz, 2011.

<sup>17</sup> The Fiscal Transparency Code: <https://www.imf.org/external/np/fad/trans/Code2019.pdf>



## Budget execution

Budget execution is the set of processes through which governments deliver on the proposals included in the budget.

**Expenditure control:** At this stage of the budget cycle, exerting tight and well-defined control over expenditure becomes the essential component of public financial management. Varying by country, the design of expenditure control can involve up to seven steps:<sup>18</sup>

1. authorization of expenditure;
2. apportionment of authorization for specific periods and spending units;
3. reservation of funds (less common);<sup>19</sup>
4. commitment of funds to all spending, including payroll and specific purchases;
5. verification (or certification) of deliveries;
6. payment order (authorization for specific payments); and
7. payment.<sup>20</sup>

Expenditure control frameworks differ greatly among countries – in terms of complexity, specific control measures, allocation of authority and responsibility, degree of centralization, and more – and the variation is largely influenced by administrative traditions.

A major challenge is how to manage the flow of resources to ensure that funds are available in time to meet payment obligations while preventing arrears accumulation, reducing the need for government borrowing, and maximizing returns on cash balances. Many governments use a single

treasury account where all government revenue is deposited before its allocation for expenditure purposes,<sup>21</sup> while others manage public funds over separate bank accounts.

Governments typically use significant resources to pay the personnel costs of the civil service and to purchase goods and services. Therefore, PFM systems include processes for the procurement of goods and services as well as processes for human resource management, i.e., the payment of wages and salaries, benefits, and pensions for civil servants.

### Managing changes to the approved budget

**mid-cycle:** The Ministry of Finance is responsible for monitoring and managing any in-year budget reallocations due to unforeseen circumstances or other factors. Substantial changes to the budget should require a budget supplement or another prescribed arrangement to obtain legislative approval.

*“The budget should be implemented as formulated and authorized with as little deviation as possible, but there should be room to adjust to changing circumstances (e.g., genuinely unexpected events) by modifying the budget as necessary during the year. Budget modifications during the year are done according to legally prescribed processes (e.g., virements, contingency reserves, and supplementary/revised budgets), transparently, and in a way that promotes governments’ chosen objectives.”<sup>22</sup>*

<sup>18</sup> Sailendra Pattanayak, 2016. Expenditure Control: Key Features, Stages, and Actors. IMF Technical note. p. 6-8. See <https://www.imf.org/external/pubs/ft/tnm/2016/tnm1602a.pdf>

<sup>19</sup> Some countries (e.g., Spain, Portugal, and France) include this stage to reserve funds for a specific known expense for which no legal commitment has been issued yet.

<sup>20</sup> Simson, Sharma, and Aziz, 2011.

<sup>21</sup> Andrews et al., 2014.

In countries where PFM rules allow executives greater leeway during budget implementation without legislative oversight, significant under

or over-spending is possible and can affect the delivery of goods and services. (Box 1.2)

### Box 1.2. Setting strict legal limits on adjustments to approved budgets

The Public Expenditure and Financial Accountability (PEFA) assessment (see Section 1.5) includes an indicator (#18.4) to determine whether there are “clear rules... for in-year budget adjustments by the executive... [and whether] the rules set strict limits on the extent and nature of amendments and are adhered to in all instances.”

SAls can play a critical role in monitoring and auditing whether the executive adheres to these rules during budget execution or not.

Source: PEFA Indicator 18.4, p 132: [https://www.pefa.org/sites/pefa/files/news/files/16\\_08\\_30-Fieldguide\\_0.pdf](https://www.pefa.org/sites/pefa/files/news/files/16_08_30-Fieldguide_0.pdf)

Internal control processes are designed to ensure compliance with established rules and procedures and the achievement of objectives. Internal audit provides information on areas of risk, where controls are lacking, and where failure to comply with management policies and rules may undermine the achievement of objectives.

### Accounting and reporting

This phase entails the internal recording, classifying, and summarizing of financial transactions to ensure compliance with budget rules and to demonstrate that public funds are used for their intended purposes.

While many countries still have cash-based accounting systems, where transactions are recorded only when cash is received or disbursed, others are transitioning to accrual-based accounting systems, which recognize transactions when they occur and thus record liabilities and assets.<sup>23</sup> Between these two, there are a variety of intermediate systems that incorporate elements of accrual accounting. The International Public Sector Financial Accountability Index tracks the distribution of countries using one accounting system or the other in their [Global Impact Map](#).

<sup>23</sup> See the <https://www.ifac.org/system/files/publications/files/IFAC-CIPFA-International-Public-Sector-Accountability-Index.pdf> p 4.

### Box 1.3. Transition to an accrual-based accounting system in Tonga

**Tonga** is transitioning from a cash-based accounting system to an accrual system. This is an important step towards improving the country's budget credibility as it provides a more complete picture of the country's financial status by incorporating fair valuations of government assets and liabilities. The 2020 Public Accounts audit recommended systems and processes to facilitate this transition.

Source: Claire Kelly 2021, "Synthesis of findings for the Pacific SAIs", consultancy report for the budget credibility project.

Financial reports aim to improve compliance and enable the assessment of government performance. Compiling these reports entails extracting and presenting data from the accounting system in ways that facilitate analysis. Governments produce a variety of reports throughout the fiscal year and after the end of the budget period. There are international standards both for the production and publication of annual fiscal reporting.<sup>24</sup>

The need to monitor the results of expenditure has led to the establishment of government monitoring and evaluation systems that produce reports on financial and non-financial performance. Non-financial performance can be measured at the level of outputs, outcomes, and impacts. There are different tools, methods, and approaches for monitoring non-financial performance. Governments must define sound indicators and systems to keep track of their progress on policy goals, share this information with their citizens, and use the information to refine, adjust or plan accordingly.

#### External oversight

Governments are required to submit their annual financial reports to independent bodies for external audit and accountability at the end of each budget cycle. SAIs play a critical role in providing oversight for the budget process. Depending on the type of SAI, they either report to the legislature or, if endowed with jurisdictional powers, may directly impose penalties or corrections. Information produced by SAIs can also be used by civil society and other stakeholders to promote accountability and remedial action.

#### PFM system objectives

Traditionally, PFM systems are expected to support the achievement of three main objectives (Box 1.4):<sup>25</sup>

- **Aggregate fiscal discipline:** when aggregate levels of revenue and public spending are

<sup>24</sup>The Open Budget Survey assesses the extent to which each country makes eight key budget documents available to the public: pre-budget statement; executive's budget proposal; enacted budget; citizens budget; in-year reports; mid-year review; year-end report; audit report. See <https://internationalbudget.org/open-budget-survey/>

<sup>25</sup>PEFA (Public Expenditure and Financial Accountability) Secretariat, n.d. "Introduction: What is PFM and why it is important?", Washington D.C., PEFA Secretariat; Andrew Lawson, 2015. "Public Financial Management", Professional Development Reading Pack, No. 6, GSDRC; Mark Miller, Tom Hart, and Sierd Hadley, 2021. "Public finance and service delivery. What's new, what's missing, what's next?" ODI Working Paper 607, London, Overseas Development Institute.

consistent with targets for the fiscal deficit and do not generate unsustainable levels of public borrowing.

- **Allocative efficiency:** where public resources are allocated to agreed strategic priorities and reallocated from lesser to higher priorities.
- **Operational efficiency:** when maximum value for money in the delivery of services is achieved.

## Box 1.4. Institutional arrangements to support traditional PFM objectives

### Aggregate fiscal discipline

- Overarching fiscal rules are set in place.
- Limits on total spending are established before individual spending bids are considered.
- Total spending must be consistent with these limits.
- Limits are set for the medium term and budget decisions are made within a medium-term expenditure framework.

### Allocative efficiency

- Spending limits are established for sectors or portfolios, and ministers are encouraged to reallocate within these limits.
- Bids to reallocate must be based either on evaluative findings of program effectiveness or on plans to evaluate policy initiatives.

### Operational efficiency

- Operating costs are cash-limited but managers have discretion in using these resources, including carrying over unused funds or to pre-spending a small portion of the next year's running costs.
- Budgeted outputs are specified in advance and actual outputs are compared to the targets.
- Costs are allocated (ideally on an accrual basis) to the activities responsible for them.

Source: Simson, Sharma, and Aziz, 2011, adapted from Schick 1998.

More recently, experts agree that additional objectives are also essential, notably:

- **Transparency and accountability** calls for the PFM system to follow due process, make information publicly accessible in a timely manner, and to apply checks and balances to ensure accountability;<sup>26</sup> and
- **Equity, sustainability, effectiveness, and inclusion** should be guiding principles throughout the system.<sup>27</sup>

Some authors have highlighted that these commonly agreed objectives are only partially influenced by the PFM system.<sup>28</sup> For example, fiscal discipline is influenced by prudent and credible revenue and spending patterns, but also by changes in decision-making, or rents from natural resources, among other factors. Therefore, they suggest focusing on the direct impacts of the PFM system to assess its functionality. From this perspective, well-functioning PFM systems would achieve four goals:

- Prudent decision-making and sustained fiscal health, as demonstrated by:
  - \* Spending decisions are affordable (deficit, debt levels, and debt payments).
  - \* Public debt management (information on what is owed, payments on time).
  - \* Deficits, debts, cash, and obligations are not threatening solvency or economic stability.

- Reliable and efficient resource flows and transactions leading to actual results and service delivery, including:
  - \* Cash is provided to spending agencies in a timely manner and in agreed amounts.
  - \* Salaries are paid in a timely manner.
  - \* Arrears are low or non-existent.
  - \* Goods and services are procured as planned, at appropriate quality and price.
  - \* Contracts are paid on time.
  - \* Financing is available to capital projects when agreed and in agreed amounts.
  - \* Corruption and non-performance losses are minimal.
- Institutionalized accountability, which records financial operations in a reliable and timely manner so that they can be subject to oversight:
  - \* All financial flows are recorded.
  - \* Financial reports are comprehensive, timely, and accessible, and allow comparison between actual spending and budget decisions.
  - \* Independent assurance that funds are collected, managed, and spent for their intended purposes, in compliance with laws and regulations,

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<sup>26</sup> Lawson, 2015.

<sup>27</sup> Paolo de Renzio and Jason Lakin, 2019. "Reframing public finance. Promoting justice, democracy, and human rights in government budgets", IBP. <https://internationalbudget.org/publications/reframing-public-finance-promoting-justice-democracy-human-rights-in-government-budgets/>

<sup>28</sup> Andrews et al., 2014.

- and with regard to value for money.
- \* Concerns raised by independent assurance are transparently discussed by citizens' representatives and receive timely follow-up and redress by the executive.
- Budget credibility, which is evidenced by:
  - \* Comprehensive and regular budgets that give a binding expression to government public finance priorities and plans.
  - \* Actual revenue policies and collection performance reflect proposals and forecasts.
  - \* Actual spending reflects budgeted promises both at aggregate and detailed allocations.

External audits may assess the achievement of all these objectives of the PFM system, including budget credibility, and/or examine whether the institutional arrangements in place contribute to the achievement of these outcomes. (Chapter 4.) Of note, the first bullet under budget credibility (directly above), is more relevant to a broader view of budget credibility which is discussed further in Chapter 2.

## PFM reforms

Countries introduce PFM reforms to improve the performance and functionality of PFM

systems, often with support from international organizations. These reforms tend to build on the results of assessment methodologies and tools (see Section 1.5) that evaluate PFM systems in terms of the degree to which they comply with international good practices, the quality of their processes, and/or their performance in certain areas. As a result, PFM reforms tend to coalesce around a common set of interventions. Table 1.1 summarizes some of the main areas of PFM reform introduced over the years.

Debate on PFM reform has focused on the choice of practices to be introduced and the sequence of reforms.<sup>29</sup> While some argue that governments in low- and middle-income countries need to focus on the basics of PFM systems before undertaking more advanced reforms,<sup>30</sup> striving to meet international standards even on "the basics" of PFM systems will help avoid problems in later stages.<sup>31</sup>

The success of PFM reforms will ultimately depend on the broader environment in which they are introduced. Not all PFM reforms are well-attuned to local problems, capacities, and institutional and political realities.<sup>32</sup> Different country contexts need different institutional solutions. More country-focused work and a better understanding of how systems operate in each country could support more effective PFM reforms. SAIs, through their audit work, play a critical role in providing information on bottlenecks and why they are arising at the country level.

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<sup>29</sup> Simson, Sharma, and Aziz, 2011; UNDESA, 2021. "CEPA Strategy Guidance Note on Fiscal and Budget Transparency", November, New York, United Nations.

<sup>30</sup> Miller, Hart, and Hadley, 2021.

<sup>31</sup> Sailendra Pattanayak, Racheeda Boukezia, Yasemin Hurcan, and Ramon Hurtado, 2022. How to Build Cash Management Capacity in Fragile States and Low-Income Developing Countries. IMF. <https://www.imf.org/en/Publications/Fiscal-Affairs-Department-How-To-Notes/Issues/2022/03/01/How-to-Build-Cash-Management-Capacity-in-Fragile-States-and-Low-Income-Developing-Countries-498003>

<sup>32</sup> For example, reforms that affect which resources go through the regular budget, in certain contexts, may contribute to budget credibility risks. To illustrate: a fiscal rule introduced in Brazil in 2000 may have created incentives for moving resources off-budget or outside the regular budget process to avoid a new spending ceiling. (Per a technical discussion on the draft handbook, June 2022, NYC.)

**Table 1.1. Select public financial management reforms**

Area of Reform	Description
Medium-term fiscal framework & medium-term expenditure frameworks	Multi-year strategic budgeting exercises that aim to create better linkages between policies and plans and revenue and expenditure forecasts.
Fiscal rules	Long-lasting constraints on fiscal policy, e.g., rules to limit spending, debt, and deficits.
Formalized budget preparation processes	Reforms focused on formalizing and structuring the budget preparation process (e.g., budget calendars, forecasting).
Budget classification systems	Coding and classifying budget items according to their economic, administrative, functional, or programmatic nature.
Program or performance-based budgeting	Changes in the budget classification system based on strategic objectives or anticipated results and changes to the processes of allocating resources, accounting for resource flows (to ensure a link between actual resource allocations and performance objectives), and the appropriation by legislatures.
Independent revenue collection agencies	Improving the transparency and efficiency of revenue policymaking and collections by creating independent revenue and customs bureaus and streamlining tax and customs policies and processes.
Treasury single accounts	Reforms to introduce single accounts that centralize financial stocks and flows in governments, ensuring that revenue is in one place and payments are also consolidated.
Integrated financial management information systems (IFMIS)	Automation of financial management processes, usually starting with accounting and reporting to streamline procedures and reduce opportunities for corruption. Usually require reform of existing processes and new human resource skills.
Public procurement	Reforms to promote transparent bidding processes and competitive procurement and to increase the efficiency and effectiveness of procurement.
Human resource management	Reforms to foster competitive hiring and merit-based civil service systems. Payroll reforms. Creating systems to record and track the number of people working in governments.

Area of Reform	Description
Internal control, audit, and monitoring	Introduction or strengthening of internal controls. Introduction of internal audit laws, units and processes. Monitoring mechanisms focused on performance and/or compliance.
Accounting and reporting	Reforms aimed at strengthening accounting and reporting activities, including standardizing charts of accounts and professionalizing the accounting function, as well as formalizing accounting and cash management procedures.
Legislative strengthening	Reforms to ensure time to assess budget proposals (e.g., budget calendar reforms), to enhance budget analysis capacity (e.g., setting budget offices), and to monitor budget implementation.
External audit and accountability reforms	Setting or strengthening the role of independent entities responsible for assurance and oversight. One recent trend is setting up Independent Fiscal Councils (IFCs) – some SAIs play this role.
Budget and spending transparency and participation	Enhance the availability of information on budget processes to make them more open to scrutiny by the public and so that adequate checks and balances can be established.

Source: Based on Andrews et al. 2014, p. 8-9.

## PFM and service delivery<sup>33</sup>

In recent years, increasing attention has been focused on how PFM systems can more effectively contribute to improving the delivery of public services. Research on the effects of PFM in specific sectors, and, particularly in the health sector, have led to calls for strengthening diagnostic tools (such as PEFA<sup>34</sup>) to highlight constraints that undermine service delivery.

Accordingly, more scrutiny is being placed on

factors that may limit PFM on service delivery. For one, when formulating the budget, how to better account for the complexities of allocation and ultimate downstream use of public revenues in the delivery of services. For example, in the health sector, this may mean trying to structure program budgets in different ways (e.g., by disease program).

On another front, the delegation of spending authority within the intergovernmental system can be critical for both PFM and service delivery. Questions surround (a) whether and how to

<sup>33</sup> This section is based on Simson, Sharma, and Aziz, 2011.

<sup>34</sup> See Sections 1.4 and 1.5.



decentralize control over resources at different stages of budget execution, and (b) how the ultimate impact is affected when a wider range of actors and processes, outside the Ministry of Finance and the legislature, are engaged more effectively. For some countries or sectors, this may mean getting subnational governments and other local actors more involved in the control of spending public resources along the service delivery chain.<sup>35</sup>

Again, recognizing the contextual nature of PFM systems and the political nature of PFM reforms is important. Also, how to consider the tradeoffs and tensions between different objectives of the PFM system – e.g., providing predictable, reliable budgets to line ministries and service delivery units while maintaining control over aggregate spending and inflation in an uncertain economy can be tricky. (Box 1.5)

### Box 1.5. Rising inflation adds challenges for auditors and budget credibility

Reversing trends of low or declining inflation over the last two decades, a significant and widespread acceleration in price increases in the last two years is affecting not only emerging or low-income countries, which are more vulnerable to exogenous shocks, but also more developed economies. In fact, according to forecasts by the International Monetary Fund (IMF), global inflation reached 8.8 percent in 2022, the highest since 1996, and is expected to still be at 6.6 percent in 2023<sup>36</sup>. Furthermore, of the 192 countries for which the IMF made an estimate for 2022, 36 countries would witness a double-digit price increase and none of them would experience deflation, in clear contrast to what happened, for example, in 2019, when only 16 countries had double-digit inflation and 16 other nations had deflation.

**Inflation can significantly enhance the risks to budget credibility.** On the one hand, inflation hinders and adds variability to the economic projections on which the budget estimates are based, particularly, but not exclusively, that of tax revenues, with the consequent variability of the effective availability of resources. In addition, during the execution of the budget, the sustained and widespread increase in prices affects the purchasing and hiring processes of public entities as well as the execution of contracts. Periodic reviews are required to adapt and adjust contracts to the increase in prices, a difficulty that becomes worse when the inflationary event is unexpected. Contract renegotiations would

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<sup>35</sup> NYU/ODI, 2021. "An inter-governmental perspective on managing public finances for service delivery", May, New York, NYU-Wagner.

demand greater allocation of funds, which in turn would necessarily require a budget reallocation, without an impact on total expenditures, but on the production of public goods or, failing that, an expansion of total spending to ensure the provision of services originally planned in the budget.

**Inflation also affects oversight activities.** Statistics on budget execution must be adjusted to make them comparable, which adds an additional source of uncertainty and error to the analysis. Additionally, the persistence of inflation requires moving from a model of valuation of financial statements based on “historical values” to another model called “homogeneous currency,”<sup>37</sup> applying the mechanism known as “adjustment for inflation” to make figures from different periods comparable. This must be considered by the financial auditor. Moreover, as mentioned above, high inflation results in changes in the value of the original contracts and, consequently, new economic recognition by the supplier. These modifications must be factored into the development of compliance audits and when considering the economic dimension of performance audits.

In short, auditors must incorporate the new inflationary dynamics into their audit work and consider its effects when conducting different types of audits.

Other factors that may affect service delivery include the relationship between PFM and other systems, such as human resource management or the model for regulating public sector performance, the different roles that sector ministries play, and/or the capacity of sector ministries.

In sum, improving public spending on service delivery requires considering both technical issues and the broader institutional and political context of a country. Various stakeholders have different and competing interests that influence resource allocation and use. Budgetary changes, PFM reforms, and approaches to service delivery

are influenced by decision-making structures and have an impact on different stakeholders and their interests. Therefore, an in-depth understanding of the dynamics of PFM systems and service delivery in a country is needed. Through external audits, SAIs can provide relevant information on both the performance of PFM systems and service delivery programs and entities.

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<sup>36</sup> IMF, 2022. World Economic Outlook Update: Gloomy and More Uncertain <https://www.imf.org/en/Publications/WEO/Issues/2022/07/26/world-economic-outlook-update-july-2022>  
<sup>37</sup> NIIF 29 – Financial information in hyperinflationary economies.

### 1.3. Measuring budget credibility, its prevalence, and related factors

Budget credibility, as it is typically defined, relates directly to budget execution.<sup>38</sup> Budgets are considered credible when governments collect and spend funds according to their legislatively approved budgets. But at what point does a deviation from the approved plan become a credibility issue?

**Measuring budget credibility:** Three dimensions of budget deviations can be examined: (1) expenditure deviations, (2) revenue deviations, and (3) deviations in spending composition.<sup>39</sup> The Public Expenditure and Financial Accountability methodology, widely known as “PEFA” has become the acknowledged standard for PFM

assessments.<sup>40</sup> PEFA establishes a 5 percent deviation of expenditure between the approved and executed budget (underspending or overruns) as a best practice not-to-exceed reference threshold for aggregate and compositional levels of spending (3 percent for contingency funds). The best practice for revenue variation is to be within 97-106 percent of the plan at an aggregate level and not to veer more than 5 percent off the plan’s target at a compositional level.<sup>41</sup>

Many PFM or budget laws set thresholds that constrain how much executives can shift from either the aggregate or budget line items or spend additional revenues within the fiscal year, without prior authorization from the legislature. Such laws contribute to maintaining budget credibility (Box 1.6).

#### Box 1.6. Tracking countries’ laws on the shifting or spending of funds without legislative approval

In establishing a country’s “oversight score”, the biennial Open Budget Survey (OBS) of the International Budget Partnership (IBP) also evaluates countries’ practices on the following questions:

- **OBS Q115.** Does the executive seek approval from the legislature prior to shifting funds between administrative units that receive explicit funding in the Enacted Budget, and is it legally required to do so?
- **OBS Q116.** Does the executive seek approval from the legislature prior to spending excess revenue (that is, amounts higher than originally anticipated) that may become available during the budget execution period, and is it legally required to do so?

<sup>38</sup> See Chapter 2 for a more expansive discussion on auditing not only the defined elements of budget credibility but also those factors which affect them.

<sup>39</sup> Paolo de Renzio and Chloe Cho, 2020. “Exploring the determinants of budget credibility” <https://internationalbudget.org/wp-content/uploads/determinants-of-budget-credibility-june-2020.pdf>

<sup>40</sup> <https://www.pefa.org/resources/pefa-2016-framework>

<sup>41</sup> See also Chapter 2, Box 2.1.

Colombia, Costa Rica, the Dominican Republic, Peru, Rwanda, Republic of Korea, Sri Lanka, Thailand, and Viet Nam are among the countries that scored well on this measure in 2021.

Source: See [https://internationalbudget.org/wp-content/uploads/2021-01-14-2021-OBS-Guide-and-Questionnaire\\_Final-ENGLISH.pdf](https://internationalbudget.org/wp-content/uploads/2021-01-14-2021-OBS-Guide-and-Questionnaire_Final-ENGLISH.pdf) for OBS methodology and <https://internationalbudget.org/open-budget-survey/country-results>

**Recent research:** A study conducted by IBP on 35 countries of different income levels gives an idea of the extent of budget deviations. On average, underspending of the annual national budget in aggregate reached nearly 10 percent over the group as a whole, i.e., well above the 5 percent deviation threshold set forth by the PEFA standards. Underspending was even higher in low-income countries, where it averaged approximately 14 percent in aggregate. When underspending affects key social or economic sectors, such as health or agriculture, it can have far-reaching consequences on people's lives.<sup>42</sup>

In other recent research by IMF staff, data for

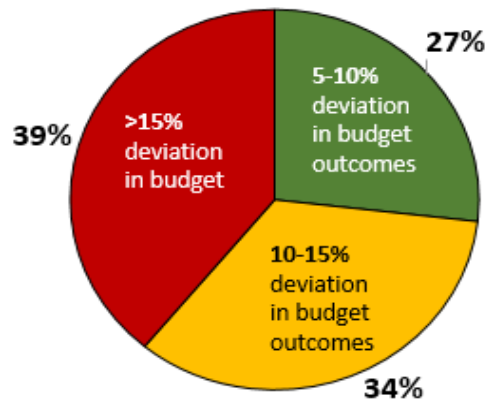
152 countries in the period 2005-2020 showed significant cross-country differences in terms of the deviation of aggregate expenditure from the approved budget. While 27 percent of countries in the dataset showed small deviations between 5-10 percent, 34 percent of countries experienced significant deviations (10 to 15 percent), and 39 percent had large budget deviations (greater than 15 percent). Some countries have made improvements in the credibility of their budgets over time, while others have regressed, and these results vary across income groups.<sup>43</sup>

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<sup>42</sup> de Renzio, Lakin, and Cho, 2019.

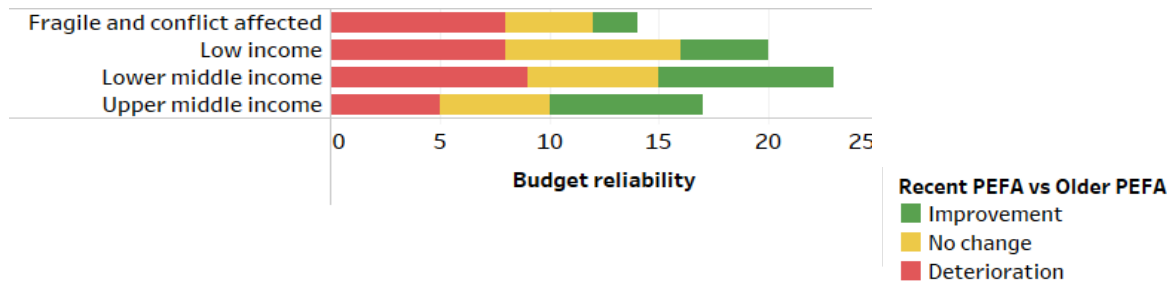
<sup>43</sup> Presentation by Fazeer Rahim, IMF, at the meeting on "Handbook on SAI's contribution to strengthening budget credibility through external audits" (New York, June 14-17, 2022).

**Figure 1.2. Aggregate expenditure: Extent of deviation from the approved budget**



Source: Fazeer Sheik Rahim, IMF (2022), based on data from PEFA for 152 countries from 2005-2020

**Figure 1.3. Changes in budget credibility over time, by country income category**



Source: Fazeer Sheik Rahim, IMF (2022), based on data from repeated PEFA assessments

**Factors affecting budget credibility:** Explaining the determinants of cross-country differences in terms of budget credibility is complex. Multiple factors explain budget credibility challenges and risks, including PFM processes and institutions (such as the role of the Ministry of Finance, preparation of fiscal forecasts, and internal and external oversight), the broader governance context (e.g., civil service independence, corruption risks), and exogenous factors and shocks (e.g., changes in commodity process,

economic downturn, COVID-19).<sup>44</sup> For example, due to the pandemic, most regions had significant budget deviations mainly in the direction of underspending (e.g., on average 12 percent in Oceania; 6 percent in Latin America and the Caribbean, with a few countries reaching 41 percent). Deviations of overspending were concentrated in Europe and North America (8 percent on average, but with some countries deviating up to 41 percent).<sup>45</sup> (See Box 1.7 on COVID responses.)

### Box 1.7. Accounting for COVID spending and its impact on budget credibility

The outbreak of the pandemic at the beginning of 2020 justified unforeseen and exceptionally important fiscal stimulus to mitigate its negative effects on health, activity, employment, and poverty.

According to the IMF's *Fiscal Monitor Database of Country Fiscal Measures in Response to the Covid-19 Pandemic*,<sup>46</sup> all countries provided to a greater or lesser extent, an unexpected fiscal stimulus to face and mitigate the effects of the pandemic. According to this survey, at a global level, fiscal aid totaled 15.9 percent of GDP in 2020, including 9.7 percent of GDP from additional expenses and loss of resources due to tax incentives. The rest of support measures totaled 6.2 percent of GDP, focused on improving the liquidity of companies (e.g., capital injections, purchase of assets, and guarantees, among others).

IMF information shows a positive correlation between the degree of relative development and exposure to the pandemic of each country and the magnitude of the fiscal measures. At the same time, there was high heterogeneity in the magnitude of the fiscal effort by each country. For example, while Mauritius aid accounted for 46.5 percent of GDP, Somalia's support reached only 0.2 percent of GDP.

Besides the magnitude of the fiscal effort, the processes of procurement, contracting, and providing direct assistance to companies and people in the face of the emergency took place under conditions of urgency, which significantly weakened accountability and oversight mechanisms, enhancing the risks of improper use of public resources.

<sup>44</sup> Ibid. (Presentation by Fazeer Rahim IMF).

<sup>45</sup> PEFA Secretariat, 2022. SDG Indicator 16.6.1 speaks how budgets are affected by COVID-19 pandemic. <https://www.pefa.org/news/sdg-indicator-1661-speaks-how-budgets-are-affected-covid-19-pandemic>

<sup>46</sup> IMF Fiscal Affairs Department, 2021. Fiscal Monitor Database of Country Fiscal Measures in Response to the COVID-19 Pandemic. <https://www.imf.org/en/Topics/imf-and-covid19/Fiscal-Policies-Database-in-Response-to-COVID-19>

The measures adopted had not been properly planned or contemplated in the originally approved budgets, forcing budget modifications and increases in spending. In many cases, these amendments to the budget were enacted without the intervention of the legislature and often under exception mechanisms. At the same time, the urgency also forced the use of exceptional and more discretionary contracting mechanisms, avoiding regular procurement processes that usually require a longer execution period and are supposed to be carried out with greater oversight and transparency. (See the International Budget Partnership's [Covid assessment](#).)

The allocation of extraordinary resources without adequate planning, in a very short period, mostly executed through more discretionary procurement mechanisms, together with a lack of transparency, amplified the risks of improper conduct in the use of taxpayer's money. These factors negatively affected the credibility of fiscal institutions as a whole and of the budget. In turn, budget credibility also suffered as the original budget objectives, both financial and the delivery of public goods and services, were significantly modified. Audit work by SAIs on the specific measures implemented during the pandemic is not only useful to identify deviations and/or improper conduct but also to improve government management in the throes of crisis contexts, thereby strengthening budget credibility.

The fiscal dynamics imposed by the pandemic revealed the need to strengthen governance, transparency, and accountability for the use of public resources. SAIs play a key role in achieving these objectives. Of note, the countries that received financing from the IMF during the pandemic have committed to implementing different measures to strengthen transparency and oversight such as i) publishing information on contracts; ii) publishing the end beneficiaries of the companies awarded the contracts; iii) reporting pandemic-related expenses; and iv) carrying out ex-post audits of those expenses.

Deviations between the approved and executed budget per se may not necessarily indicate failures in the performance of PFM systems. For example, some deviations may be justified due to an unexpected macroeconomic shift such as inflation or a pandemic, or because of increases in government efficiency in spending. Regardless, for the public to understand whether deviations are justified, the reasons for deviations should be documented and explained in budget implementation reports or performance reports. The assessment of credibility also depends on the reasonability and transparency of the

reasons that explain those deviations as well as the impact of the deviations themselves (e.g., on service delivery). Ultimately, those reasons and the impacts of budget deviations are also dependent on contextual factors.

SAIs can strengthen their work on the assessment of reasons for underlying deviations, which is often missing in audits (e.g., compliance). Of note, SAI Sweden finds that the reasons provided by their government to explain budget deviations have improved over the years, including as a result of the SAI's audits.<sup>47</sup>

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<sup>47</sup> Input from SAI Sweden at the UNDESA-IBP Technical Meeting on the development of this handbook, May 2021.

## Box 1.8: Are deviations from the budget explained?

The importance of governments explaining deviation from the approved plan is upheld in several international standards, for example:

- The highest score on the PEFA framework's indicator 16.4 is awarded to countries that explain "all changes to expenditure estimates" at the ministry level.
- IMF's Fiscal Transparency Handbook – e.g., Principle 1.4.3 (explanations for variances between different reports on budget implementation versus forecast) and Principle 2.4.3 (explanations related to either policy change, macroeconomic factors, or other factors as to why forecasts are changing over time).

IBP has highlighted the importance of explanations in in-year reports (IYR), mid-year reports (MYR), and year-end reports (YER) (see [Guide to Transparency in Government Budget Reports](#)), and identified the following criteria for government explanations:

1. Identify a causal link between a set of facts (A) and deviations from the budget (B) (minimum condition)
2. Explain the mechanism by which a set of facts (A) has caused deviations (B) and, where possible, the factors (C) that caused (A) in the first place
3. Provide sufficient detail to explain any variation in outcomes
4. Show how explanations are consistent with past experience or why conditions have changed
5. Explain the most important deviations

Source: Lakin, 2018. Assessing the Quality of Reasons in Government Budget Documents.

Given the multiplicity of drivers that lead to budget credibility, and the complex interrelation between them, some experts suggest considering not only the predictability and reliability in budget execution as an indicator of budget credibility but also other dimensions of PFM performance, including, among others:<sup>48</sup>

- Reliability and transparency of budgets
- Management of assets and liabilities

- Systematic assessment of fiscal trends as a basis for budget formulation
- Sound accounting and reporting systems

These different dimensions of PFM performance can be assessed by auditors as conditions that either affect and/or create risks for budget credibility. Chapters 3 to 6 illustrate how SAIs in different regions are auditing some of these dimensions.

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<sup>48</sup> Presentation by Srinivas Gurazada, PEFA Secretariat, at UNDESA-IBP Technical Meeting on the development of this handbook, May 2021.



Whether to focus more narrowly on the defined parameters of budget credibility or to assess the range of factors affecting budget credibility has implications in terms of audit methodology. Chapter 2 explores this further and looks at the concept of budget credibility and its operationalization for auditing.

## 1.4. Relevant international standards on PFM and budgeting

Several international standards related to PFM and budgeting have recognized the importance of the credibility of government budgets and sound governance principles, including transparency.

### Sustainable Development Goal 16

The importance of budget credibility for effective, accountable, and transparent institutions has been recognized in the 2030 Agenda through Sustainable Development Goal 16 on peace, justice, and strong institutions. Progress on target 16.6 is measured by two different global indicators, one of which – indicator 16.6.1 – is dedicated to budget credibility. The indicator measures credibility as “primary government expenditures as a proportion of the original approved budget (by sector, budget codes or similar),”<sup>49</sup> but only at the national aggregate level.

### Public Expenditure and Financial Accountability Initiative (PEFA)

The PEFA Initiative provides a framework for assessing and reporting on the strengths and constraints of public finance management systems using quantitative indicators to assess performance. Research shows a strong correlation between average performance across the PEFA pillars and budget credibility, with differences across pillars. Countries with better PFM institutions and processes tend to have better budget reliability. (See Section 1.5. for more on the assessment framework.) PEFA data is the source for UN member states’ reporting on SDG 16.6.1.

### Fiscal Transparency Code

The IMF’s Fiscal Transparency Code<sup>50</sup> is the internationally recognized standard for the disclosure of information about public finances. It comprises a set of principles built around four pillars: fiscal reporting; fiscal forecasting and budgeting; fiscal risk analysis and management; and resource revenue management. The Code includes three elements related to budget credibility: (1) independent evaluation – whether the government’s economic and fiscal forecasts and performance are subject to independent evaluation; (2) supplementary budgets – whether any material changes to the approved budget are authorized by the legislature; and (3) forecast reconciliation – whether budget documentation and updates explain any material changes to the

<sup>49</sup> United Nations A/RES/71/313 “Global indicator framework for the Sustainable Development Goals and targets of the 2030 Agenda for Sustainable Development”. Available at <https://unstats.un.org/sdgs/indicators/indicators-list/>; More information on the SDG global indicator framework is available at <https://unstats.un.org/sdgs/dataportal>

<sup>50</sup> The Fiscal Transparency Code 2019 can be found here: <https://www.imf.org/external/np/fad/trans/Code2019.pdf>

government's previous fiscal forecasts. The Fiscal Transparency Handbook (2018) provides detailed guidance on the implementation of the Code's

principles and practices, with many examples from countries around the globe.

### Box 1.9. SAIs use of international budget standards

In its performance audits of the budget process, SAI Indonesia has used the IMF Fiscal Transparency Code as a source of audit criteria, in addition to applicable laws and regulations, and relevant good practices. SAI Jamaica has applied the IMF Fiscal Transparency Code. The United States GAO (Government Accountability Office) uses OECD and IMF international practices and standards as references in its budget work.

### OECD Principles of Budgetary Governance

The OECD Principles of Budgetary Governance aim to provide practical guidance for designing, implementing, and improving budget systems to make a positive impact on citizens' lives. One of the principles highlights that budgets must be managed within clear, credible, and predictable limits for fiscal policy. The principles

also emphasize the importance of closely aligning budgets with the medium-term strategic priorities of the government. Another principle refers to the need to present a comprehensive, accurate, and reliable account of public finances. Comprehensiveness, transparency, and realism form an international standard against which the soundness of the budget is often assessed (Box 1.10). In OECD countries, these standards are achieved by designing annual, united, and universal budget systems.<sup>51</sup>

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<sup>51</sup> IMF, 1999. "Guidelines for public expenditure management, Section 3, budget preparation", available at <https://www.imf.org/external/pubs/ft/expend/guide3.htm>

## Box 1.10. International standards for a sound budget

### Comprehensiveness

- Is the coverage of government operations complete?
- Are estimates gross, or does netting take place?

### Transparency

- How useful is the budget classification? Are there separate economic and functional classifications that meet international standards?
- Is it easy to connect policies and expenditures through a program structure?

### Realism

- Is the budget based on a realistic macroeconomic framework?
- Are estimates based on reasonable revenue projections? How are these made, and by whom?
- Are the financing provisions realistic?
- Is there a realistic costing of policies and programs and expenditures (e.g., assumptions about inflation)?
- How are future cost implications taken into account?
- Is there a clear separation between present and new policies?
- How far are spending priorities determined and agreed upon under the budget process?

Source: IMF, 1999. Guidelines for Public Expenditure Management: <https://www.imf.org/external/pubs/ft/expend/guide3.htm>

## Global Initiative for Fiscal Transparency (GIFT)

GIFT is a global network that facilitates dialogue between governments, civil society organizations, international financial institutions, and other stakeholders on strengthening

fiscal transparency and participation. In 2011, GIFT reviewed the numerous relevant norms and standards circulating around the world for comprehensiveness and consistency to summarize the essence of each in an aggregate overall format. Their work informed the development of the [High-Level Principles on Fiscal Transparency, Participation, and Accountability](#)

in 2012 which was subsequently recognized that same year by the United Nations General Assembly.<sup>51</sup> GIFT continues to update and review the international standards,<sup>53</sup> against

which countries can assess their strengths and weaknesses and progress on their commitments related to budgetary governance, in general, and to budget credibility, in particular.

### Box 1.11. Excerpts from two of GIFT's ten High-Level Principles relating to budget credibility

Principle 3 on the quality of reporting on budget execution, calls for the presentation of fiscal information to be "...consistent across the different types of reports or include an explanation and reconciliation of differences."

Principle 8 on process, highlights that "no government revenue should be raised, or expenditure incurred or committed without the approval of the legislature through the budget or other legislation."

## 1.5 Diagnostic tools and assessments relevant for budget credibility

Building on international standards, in recent years, several different diagnostic and assessment frameworks, methods, and tools have been developed.<sup>54</sup> They tend to assess and compare national systems with different levels of practice within the standards. Used to inform PFM reform strategies, monitor reform progress, and assess risks, generally, these tools can be used in combination as they provide complementary assessments. They may be useful for auditors in their audit work on budget credibility. At the same

time, in-country analysis and information provided by SAIs further the understanding of how existing PFM systems and processes work.

### PEFA's Public Financial Management Performance Measurement Framework

The PEFA Initiative has also developed the PFM Performance Measurement Framework. This indicator-based tool provides an integrated assessment of PFM systems against seven performance pillars: (1) budget reliability, (2) transparency of public finances, (3) management of assets and liabilities, (4) policy-based fiscal

<sup>52</sup> United Nations A/RES/67/218 on "Promoting transparency, participation, and accountability in fiscal policies", 21 December 2012. Available at <https://financing.desa.un.org/document/ga-resolution-67218-promoting-transparency-participation-and-accountability-fiscal>

<sup>53</sup> In 2018, GIFT published an Expanded Version of the High-Level Principles on Fiscal Transparency, Participation, and Accountability and more recently the useful Summary of the Expanded High-Level Principles on Fiscal Transparency, Participation, and Accountability.

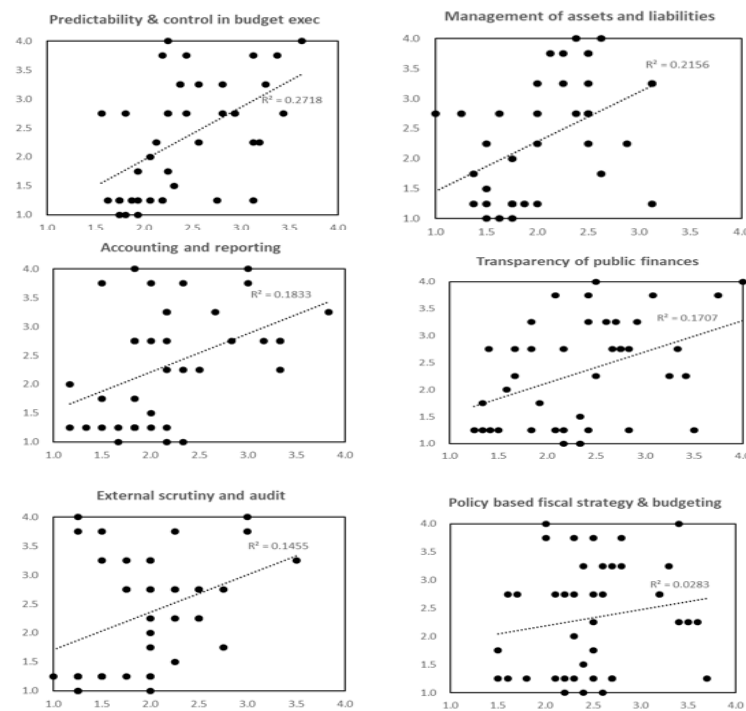
<sup>54</sup> UNDESA, 2021. "CEPA Strategy Guidance Note on Fiscal and Budget Transparency", November, New York, United Nations.

strategy and budgeting, (5) predictability and control of budget execution, (6) accounting and reporting, and (7) external scrutiny audit. (See Figure 1.4.) Within these seven broad domains, PEFA defines 31 specific indicators, disaggregated into 94 dimensions, that focus on key measurable aspects. It then assesses the likely impact of PFM performance levels on three desired budgetary outcomes: aggregate fiscal discipline, strategic allocation of resources, and efficient service delivery.

Since 2012, over 600 assessments have been conducted worldwide in 154 countries. PEFA

assessments have been used to conduct cross-country research on the performance of PFM systems,<sup>55</sup> as well as on the determinants of budget deviations.<sup>56</sup> The initial framework developed in 2011 was updated in 2016. PEFA has also been expanded with supplementary assessment tools on gender, climate, and guidance for sub-national governments with a particular focus on service delivery. More information on the assessment tool, cross-country reports, and country case studies is available at [PEFA framework](#).

**Figure 1.4. Predictability and expenditure control have the strongest correlation with budget credibility, among PEFA pillars**



Source: Fazeer Sheik Rahim IMF Presentation at review meeting (June 2022)

<sup>55</sup> Paolo de Renzio, 2009. "Taking Stock: What do PEFA Assessments tell us about PFM systems across countries?" Working Paper 302, Overseas Development Institute, May, London, UK.

<sup>56</sup> de Renzio and Cho, 2020.

## Open Budget Survey (IBP)

The Open Budget Survey (OBS) is an independent, comparative, and fact-based research instrument measuring three essential aspects of governance and accountability: transparency (i.e., the timely publication of the requisite documents for sound public financial management), opportunities for public participation in fiscal affairs, and the extent of oversight by the legislature and SAI. This biennial review is completed with in-country researchers and is currently evaluating 125 countries. (See also Box 1.6.)

## Fiscal transparency evaluations (IMF)

Fiscal transparency evaluations assess country practices against the standards of the IMF's Fiscal Transparency Code. The assessments provide information on the scale and sources of fiscal vulnerabilities, including measures of the coverage of fiscal reports, the quality of fiscal forecasts, and the size of unreported contingent liabilities. They also assess the strengths and weaknesses of country practices related to fiscal transparency through a set of summary "heatmaps," which facilitate benchmarking against comparator countries, the identification of reform needs, and the prioritization of recommendations.

These evaluations support the identification of fiscal transparency strengths, weaknesses, and challenges and place greater emphasis on fiscal transparency issues that are macro-critical and complement other public financial management standards and frameworks.

## OECD Budgetary Governance Reviews

The OECD Budgetary Governance Reviews look at good practices in budgeting and provide guidance on designing, preparing, approving, implementing, and reviewing budgets to ensure they are effective, efficient, and relevant and comply with the principles of budgetary governance. Reports are available at <https://www.oecd.org/gov/budgeting/>. The OECD International Database of Budget Practices and Procedures contains information on budget institutions from 97 countries, including 31 OECD member countries and 66 non-members from the Middle East, Africa, Eastern Europe, Asia, Latin America, and the Caribbean.

## BOOST

Budget credibility has also been recently analyzed using a dataset from the World Bank created in 2010. The BOOST dataset aims to facilitate access to budget data and promote their effective use for improved decision-making, transparency, and accountability. The dataset contains information on the approved budget, revised budget, and actual expenditure amounts broken down by government level, administrative unit; sub-national spending unit; economic classification; functional classification (sector and sub-sector); program classification; and financing source. BOOST data has also been used to support Public Expenditure Reviews, which evaluate the effectiveness of public finances.

## Box 1.12. An example of the type of data found in the BOOST database

In the case of **Uganda**, the BOOST database presents data on expenditures executed by the state and local governments. The data was provided by the Ministry of Finance and covers the period 2004-2016. It is organized following the country's budget classification system which includes an administrative, economic, functional, and geographic classification. The database includes data on the allocated budget, revised budget, and expenditures of central and local government agencies.

### Public Financial Management Reporting Framework (PFM-RM)

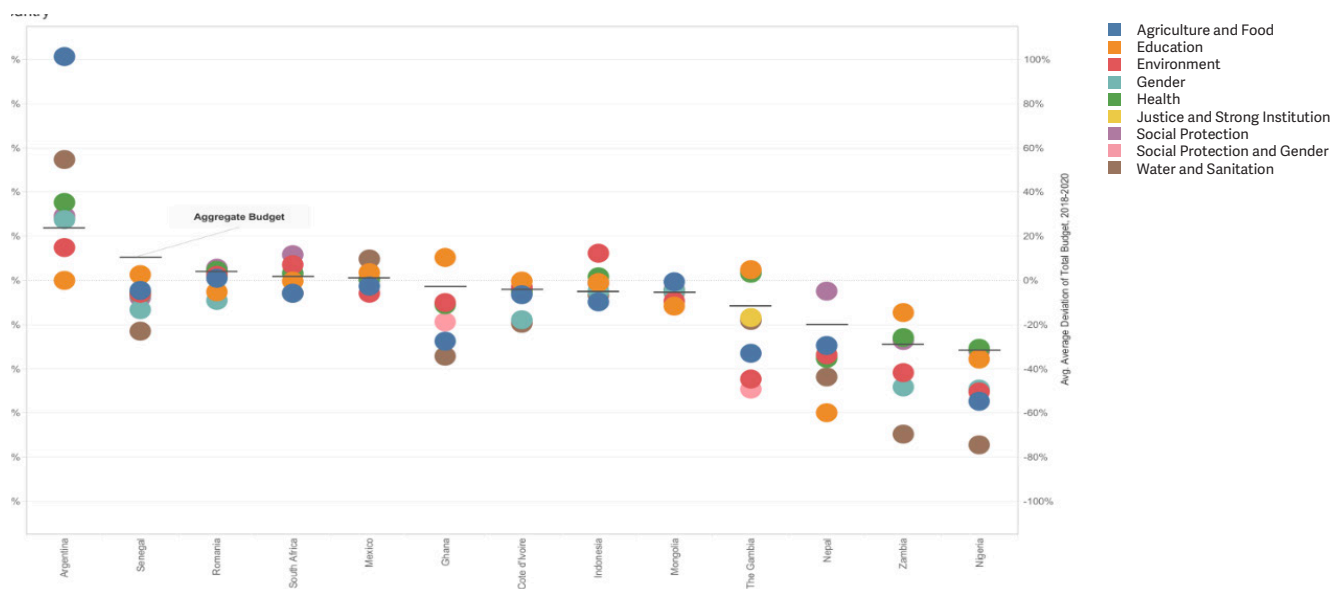
The Public Financial Management Reporting Framework (PFM-RM) developed by AFROSAI-E (the African Organization for English-Speaking Supreme Audit Institutions) and GIZ (the main German development agency, *Deutsche Gesellschaft für Internationale Zusammenarbeit GmbH*) is an assessment tool developed specifically for auditors. The PFM-RM is a diagnostic assessment tool to assess the performance of PFM processes (macroeconomic policy, fiscal policy and strategic budgeting; budget preparation; budget approval; financial management and service delivery; and accounting reporting and oversight) along the budget cycle. The assessments are entity-specific (and thus provide disaggregated information at the entity level) and allow auditors to assess each process in each entity (core PFM institutions as well as selected ministries, departments, and agencies), and compare results across them. Further information on this assessment tool and its application is presented in Chapter 4.

### Using other publicly available budget data

Other assessments rely on publicly available budget data at the national level. As indicated earlier, one limitation of the SDG indicator 16.6.1 on budget credibility, which relies on PEFA data, is that it is an aggregate indicator. Using publicly available budget data allows for disaggregated assessments at sector or program levels. This approach has been used in recent research conducted by IBP in 13 countries across seven sectors related to 10 SDGs for the period 2018 to 2020. The results show that governments often reduce the share of spending in social sectors related to SDGs during implementation, as compared to the aggregate budget.<sup>57</sup> Understanding how credible budgets are at the sectoral level is important for analyzing the implications of budget credibility for achieving the SDGs. See Figure 1.5.

<sup>57</sup> IBP, 2022. "Budget credibility and the Sustainable Development Goals" available at <https://express.adobe.com/page/kZhNwex9ayQ9C/>

**Figure 1.5. Average deviation between approved and actual spending from 2018 to 2020 (in seven sectors of 13 countries, by functional or administrative classification)**



Source: IBP and partner CSO original research based on publicly available budget data (Nov. 2022)

## External audits complement the use of diagnostic tools in assessing budget credibility

Auditors often use PEFA and other available assessment tools to get an overall picture of the PFM system in their countries. PEFA examines and measures budget credibility and budget deviations at the aggregate level. However, PEFA does not analyze the causes and institutional factors that explain the aggregate budget credibility score and/or changes (improvements or regressions) over time.

In contrast, audits can help illuminate the causes and institutional factors, both systemic and contingent, that explain budget deviations and changes in budget deviations over time. Audits can make recommendations to address those causes, enhance budget credibility, and improve the performance of PFM processes and systems. Therefore, assessment tools such as PEFA and external audits complement each other to conduct a better analysis of budget credibility and to improve the performance of the budget process and PFM systems.



## Chapter 2: Auditing budget credibility

Budget credibility is still an emerging concept in the field of auditing, and only in recent years has begun to be used by audit institutions as part of the audit process. This chapter looks at ways SAIs can determine whether and how to integrate budget credibility into their audit plans. In doing so, the chapter expands the concept of budget credibility for auditing purposes, introduces various approaches to auditing budget credibility, and provides an overview of relevant audit standards to guide an SAI's work on this subject.

### 2.1. Auditing credibility – taking a standard or broader perspective

Chapter 1 identified budget credibility as one of the goals of a sound budget process and PFM

system. Auditors are well-positioned to assess whether and how effectively governments are achieving this goal. But, audit work can also shine a light on the impact of the lack of budget credibility and on what poses risks to the credibility of government budgets. In essence, audits can assess budget credibility along the standard definition or they can take a broader view and look into the factors that affect the credibility of public funds.

As described in section 1.1, the standard definition of a credible budget is one that is executed according to the plan approved by the legislature at aggregate and detailed allocations. The focus is on short-term procedural rules and regulations and on budget deviations from the approved budget – on the reliability of the budget. (Box 2.1)

#### Box 2.1. The standard definition of budget credibility for auditing purposes

A **budget is credible when** (in at least two of the last three years):

- Actual *revenue* is collected according to the approved budget, within 97-106 percent of the plan, and variance in revenue composition is within 5 percent of the plan.
- Actual *expenditure at the aggregate level* does not deviate beyond 5 percent of the approved budget, and
- Actual *expenditure at the compositional or sectoral allocation level* does not deviate beyond 5 percent of the approved budget allocations; in the case of contingency funds, expenditure should not deviate beyond 3 percent.

Source: PEFA, 2016. Framework for assessing public financial management, 2nd edition. p. 14-18. [https://www.pefa.org/sites/pefa/files/resources/downloads/PEFA%202016\\_latest%20version\\_with%20links%20%28%29.pdf](https://www.pefa.org/sites/pefa/files/resources/downloads/PEFA%202016_latest%20version_with%20links%20%28%29.pdf)

A *broader view* of budget credibility not only focuses on the reliability of the budget but also on the *performance* of the budget. It reflects a shift from activity-based to output-based auditing, which assesses the performance of public spending. This understanding of budget credibility calls for using performance audit tools and /or integrated auditing, which incorporate different audit practices (e.g., financial, compliance, and performance; compliance and performance). In addition to budget deviations, auditors would consider:

- i. the premises on which the budget is formulated,
- ii. the fragmentation or integrality of the budget (i.e., the volume of resources and spending outside the budget),
- iii. compliance with PFM rules and processes, and
- iv. the performance of public spending for the delivery of public goods and services.

## Box 2.2. A broader view of budget credibility for auditing purposes

A **budget is credible when it:** (criteria are not exhaustive)

- Complies with public financial management rules and processes.
- Is effectively formulated and executed.
- Is formulated according to realistic and reliable macroeconomic projections and forecasts.
- Reflects government public finance and policy priorities and plans.
- Is comprehensive and integral.
- Supports fiscal sustainability and fiscal health.
- Ensures efficient processes and transactions for the effective delivery of services and the achievement of policy objectives.
- Is aligned to expected outcome and goals (i.e., benchmarking)

How broadly to consider the various aspects of budget credibility has implications in terms of audit methodology, particularly on the identification of the audit objective and the conditions to establish credibility. Two ways

of considering budget credibility for auditing purposes are presented in Table 2.1, one applies the standard definition and the other considers a more expansive understanding of the concept. These can be linked to different audit tools.

**Table 2.1. Auditing via the standard vs broader view of budget credibility**

Auditing by standard definition	Auditing with a broader view
<p><u>Focus:</u> budget predictability/reliability and execution (i.e., any deviations from the budget approved by the legislature).</p> <ul style="list-style-type: none"> <li>• Could consider reliability/execution for expenditures and revenues at both an aggregate and compositional level.</li> </ul> <p><u>Type of audit:</u> Financial audit (FA) and/or compliance audit (CA).</p> <p><u>Scope:</u> Single unit or aggregated (e.g., for all of the government through the audit of year-end accounts).</p>	<p><u>Focus:</u> determinants of budget credibility and performance and outcomes (impacts of deviations).</p> <ul style="list-style-type: none"> <li>• Could inquire into the determinants (e.g., PFM processes and institutions, governance) through a risk-based approach.</li> <li>• Could consider specific dimensions of budget performance related to credibility: e.g., transparency, information/reporting systems (including performance indicators).</li> </ul> <p><u>Type of audit:</u> Compliance audit (CA) and performance audit (PA), or mixed audits with PA elements.</p> <p><u>Scope:</u> Across government, single units, or aggregated /systems.</p>

The broader view of budget credibility can be operationalized through a risk-based approach, identifying how different factors can either create or mitigate risks in terms of unexpected or unjustified deviations (of either aggregate expenditure, revenue, or spending composition)

from approved budgets. SAIs can assess and weigh the risk of the different factors to prioritize and identify areas to be audited and then develop audit objectives and questions. On risks, see Annex 2.1 at the end of this chapter and Chapters 3 and 6.

**Table 2.2. Examples of audit approaches, objectives, and audit findings related to budget credibility**

<b>Audit approach</b>	<b>Audit objectives and audit methodology (in parentheses)* Examples:</b>	<b>Related audit findings linked to budget credibility Examples:</b>
Audits of the performance of the PFM system (Chapter 4)	Effectiveness of government's expenditure management system to support performance-based budgeting. (PA)	The lack of framework to measure the quality of government expenditure undermines the ability to assess how the budget contributes to the achievement of policy objectives (targets included in the medium-term national development plan).
Annual audits of year-end accounts or state budget execution (Chapter 5)	Assurance of financial statements and compliance of budget transactions with legal framework. (FA, CA)	Whole-of-government financial statements are not prepared in accordance with the applicable financial framework and the lack of compliance with existing public finance regulations creates credibility risks (e.g., indebtedness beyond the legal ceiling that undermines fiscal health).
	Whether reasonable projections for macroeconomic variables inform budget allocations. (CA, PA)	Poor or inaccurate macroeconomic forecasting creates credibility risks (e.g., deviations due to errors in revenue estimation).
Audits at budget program or entity level (Chapter 6)	Predictability – existence, completeness, and accuracy of documentation. (FA)	Incomplete, inaccurate documentation of expenditures may create overrun/underspending risks as entities do not know the volume of actual resources executed.
	Economy, efficiency, and effectiveness in an entity's preparation and execution of entities' budgets. (PA)	Inefficient planning /preparation of the entity's budget may create credibility risks as unrealistic spending targets make it difficult for entities to absorb funds and can lead to underspending.

\*PA=performance audit; FA=financial audit; CA=compliance audit.

## The challenge of linking budget execution and performance

Including performance aspects in addition to the financial and compliance evaluation of budget execution requires not only identifying budget deviations, but also analyzing their impact on the delivery of public services and goods. Making links between budget execution (particularly at the aggregate level) and performance at the

program or entity level is difficult. SAIs have varied experience and capacities in conducting value for money and operational audits. Multiple factors explain the performance of programs and entities. SAIs cannot possibly assess the performance of the entire universe of entities and programs annually. Still, SAIs are making an effort in this direction. For example, each year SAI Brazil selects a few programs for a performance assessment in the audit of the President's year-end accounts.

### Box 2.3. Challenges to linking budget execution to performance

Some SAIs, like **France** and **Brazil**, publish an annual report on the evaluation of public policies. This can provide an entry point to enhance the linkages between budget execution and performance. However, there are some challenges.

Brazil's Federal Court of Accounts (TCU) publishes an annual report\* of audits of public policies and programs (Relatório de Fiscalizações em Políticas e Programas de Governo, RePP) which evaluates approximately 10-15 programs every year. For example, in 2021, the analysis focused on social programs and programs of access to economic benefits in the context of COVID-19. Unfortunately, this evaluation does not usually influence the budget process, and it includes many programs that are outside the regular budget. Enhancing engagement with the legislature is critical to increasing the influence of this type of analysis on budget discussions. Another need involves strengthening the capacity of auditors on budget evaluation.

\*These reports are available at <https://sites.tcu.gov.br/relatorio-de-politicas/>

Nonetheless, while auditors may find it challenging to audit budget credibility with a focus on performance of service delivery, possible entry points for SAIs to move in this direction include:

- Audit performance at the entity level, using performance audit tools.
- Focus mainly on auditing and concluding on the "economy"<sup>58</sup> aspects of performance.
- Link budget formulation objectives and execution with the actual outcome.
- Audit critical elements related to performance such as government performance indicators.

<sup>58</sup> Economy, efficiency, and effectiveness are commonly described as the "3Es" in a performance audit

Some SAIs already do this regularly (e.g., Brazil's TCU, the UK's NAO).

- Link planning and budget execution and develop audit criteria that can be used to assess these linkages for different types of audits.
- Incorporate some automatized elements to audit effectiveness in the annual audit of budget execution.

## 2.2. Budget credibility across different contexts

Differences in the institutional and governance contexts and characteristics of PFM systems across countries may have a differentiated effect on the credibility of government budgets. For example, countries with high levels of debt and a constrained fiscal space may set fiscal targets that result in systematic underspending.<sup>59</sup> In some countries, the de-facto prevalence of the executive branch over the legislature in the approval and amendment of the budget may undermine credibility and affect citizens' trust in the budget process. And in other countries, amendments to the national budget by the legislature add to credibility challenges (see bullet "g" below and Chapter 6, Box 6.5).

Auditors should be knowledgeable of the wider country context and how these factors interplay with the SAI mandate and capacity. Relevant factors to consider include:

- External shocks and the macroeconomic and financial environment of the country.** What is the country's level of debt, financial obligations, and overall financial health? How dependent is the country on foreign aid or commodities? Additionally, national health crises, high energy prices, inflation, or other shocks will affect the credibility of budgets. (Boxes 1.5 and 1.7)
- The nature of the budget system and approach to budgeting, and any particularities (formal or informal) of the budget process.** Does the country rely on cash-based accounting or accrual-based accounting? Does the country rely on line-item budgeting or performance-based budgeting? Are there specific stages in the budget process unique to this country?
- The country's expenditure controls and fiscal rules.** These shape the country's PFM system and familiarity with them is essential for understanding how resources are designed to flow and who is responsible for various stages of the budget execution process.
- Ongoing or planned budget reform,** such as any movement toward performance-based budgeting, or changes in the budget legal framework.
- Technical factors that affect the performance of the PFM system** such as the existence of integrated information systems.
- Institutional characteristics related to the budget process** such as the existence or not of an Independent Fiscal Institution

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<sup>59</sup> Input from the General Comptroller of Costa Rica at the UNDESA-IBP Technical Meeting for the development of this handbook, (May 26-28, 2021).

(IFI) with the mandate to assess publicly and independently fiscal policies, plans, and performance against fiscal objectives (e.g., fiscal sustainability).<sup>60</sup> Some SAIs (e.g., SAI France, Finland, Lithuania) play this role in their respective countries.

- g. The role of parliament as well as the relationship between the SAI and parliament.**  
Does the parliament have the power to amend the budget? Is there a parliamentary budget office? What are the legislative capacities for effective budget oversight? For example, countries vary in the extent to which the

parliament can change the budget after it is submitted for legislative consideration. In many countries, the legislature can change the composition of the expenditure or revenue plans but not the global total.<sup>61</sup>

- h. Relevant characteristics of public administration and the center of government**  
such as the links between planning and budgeting, the soundness of monitoring and evaluation systems, the independence of the civil service, and the strength of internal control functions, among others.

**Table 2.3. Relevant factors of country variation that may affect budget credibility**

Wider country economic and governance context	PFM/Budget system	Institutional factors related to budgeting	Public administration and center of government
<ul style="list-style-type: none"> <li>• Macroeconomic constraints.</li> <li>• Fiscal space and health.</li> <li>• Level of public debt.</li> <li>• Level of foreign aid, if applicable.</li> <li>• Commodity exporters.</li> <li>• Countries in special situations (e.g., fragile states).</li> </ul>	<ul style="list-style-type: none"> <li>• Approach to budgeting and nature of the budget and accounting system (e.g., cash vs. accrual, line-item vs. program)</li> <li>• Planned or ongoing budget reforms (e.g., legal and regulatory framework, for improving performance).</li> </ul>	<ul style="list-style-type: none"> <li>• Distribution of budgeting powers between the executive and the legislature, and amendment powers of the legislature.</li> <li>• Legislative limits (e.g., on deficit).</li> <li>• Legislative capacity for budget oversight.</li> </ul>	<ul style="list-style-type: none"> <li>• Nature of planning processes (e.g., short, medium, long-term).</li> <li>• Linkages between budget and planning.</li> <li>• Soundness of monitoring and evaluation systems.</li> <li>• Internal control functions.</li> </ul>

<sup>60</sup> The institutional form, level of independence, and nature of the work conducted vary significantly across IFIs. For further information on IFIs, see IMF's dataset at <https://www.imf.org/en/Data/Fiscal/fiscal-council-dataset>

<sup>61</sup> IMF, (n.d.). Guidelines for public expenditure management, section 3: Budget Preparation." Available at <https://www.imf.org/external/pubs/ft/expend/guide3.htm>

Wider country economic and governance context	PFM/Budget system	Institutional factors related to budgeting	Public administration and center of government
<ul style="list-style-type: none"> <li>Fiscal transparency.</li> <li>Corruption risks.</li> </ul>	<ul style="list-style-type: none"> <li>Technical elements that affect the performance of the budget systems (e.g., integrated information system).</li> <li>Fragmentation of the budget.</li> <li>Off-budget accounts and extra-budgetary funds.</li> </ul>	<ul style="list-style-type: none"> <li>Existence of parliamentary budget office.</li> <li>Existence and competencies of Independent Fiscal Institution (IFI).</li> <li>Distribution of budget powers within the executive.</li> </ul>	<ul style="list-style-type: none"> <li>Independence of civil service.</li> <li>Linkages between internal and external oversight.</li> <li>Availability and quality of performance information.</li> </ul>

### Supreme Audit Institution

- Independence.
- Scope of powers and competencies in relation to SAI model (judicial/court, board/collegiate, Westminster).
- Special roles played by the SAI in some countries (e.g., IFI).
- SAI capacity (e.g., analytical) and resources.

## Additional contextual considerations

Several additional dimensions are relevant to operationalize the concept of budget credibility for auditing purposes and to determine whether budget credibility is significant in an SAI's national context. These include:

- The interplay between quantitative budget deviations and contextual factors.** While the 5 percent deviation threshold set by international standards provides a relevant

reference point, deviations below this threshold may represent a challenge for budget credibility in some contexts while higher deviations may not represent a problem in others.

- The role of various actors in the budget process and PFM.** Budget credibility risks and deviations can be influenced by different actors, not only the executive. For example, as noted earlier, in countries where the legislative branch has budget amendment powers, parliaments can be a driver of budget deviations. In decentralized or



federal countries, sub-national and/or local governments may contribute to deviations from the approved budgets (e.g., due to low implementation capacity). And, in some cases, delays in the release of funds by development partners may also play a part in budget credibility.

- **Informal budget processes and their impact on budget credibility, legitimacy, and accountability.** In certain contexts, informal processes may undermine formal budget institutions. For example, the executive may circumvent the budget approval and oversight roles of the legislature by relying on executive decrees to amend the budget. There are also credibility challenges related to extra-budgetary or out-of-budget funds (e.g., in the context of emergencies), to the fragmentation of budgets (e.g., different sources of revenue, donor funding with parallel systems), and to special funds (e.g., social security trust funds). Therefore, the definition of credibility would need to consider what is and what is not included in the budget per se.
- **Risks that emerge during budget execution.** Deviations from authorized spending may not surpass the 5 percent threshold, but become a significant problem during budget execution, for example through mandatory spending cuts or the approval of supplementary budgets. Some drivers of credibility risks may relate to the macroeconomic situation of a country (see Box 1.5 on inflation) and/or to political considerations.

- **Fiscal and budgetary outcomes.** The budget is an instrument for the achievement of national objectives and the effective delivery of policies. Therefore, budget credibility relates not only to the quantitative deviations from the authorized budget but from the intended results or policy goals to be achieved with the execution of budget resources, as well as their impact on the effective delivery of public services.

Each of these dimensions has implications for auditing. For example, by being outside the regular budget process, off-budget funds are by definition less transparent and tend to escape oversight. Therefore, SAIs face challenges with timely access to relevant information related to the execution of these funds. Oversight by SAIs and other stakeholders would benefit from improving the transparency of off-budget resources. Also, auditors could consider the full spectrum of funds and resources at different levels of government, as well as the role of different stakeholders that raise and execute resources with a public purpose. However, the mandate of an SAI may restrict its capacity to investigate some of these budget credibility risks. For example, budget credibility problems may be related to the weak implementation capacity of local governments, but an SAI's mandate is often limited to the national level and to transfers of national resources to subnational governments.

## 2.3. Selection of budget credibility as an audit topic

How an audit topic is chosen varies across SAIs in terms of who is responsible for topic selection, or whether the planning process in the SAI is annual or multi-year, among other factors. However, some common considerations will normally inform the SAI's choice of audit topics to be included in an annual or multi-annual audit plan: (a) its mandate, (b) the legal and regulatory framework, (c) the resources and capacities available, and (d) an analysis of the SAI's environment, including some form of risk analysis.<sup>62</sup>

An SAI may consider budget credibility as a possible theme in upcoming audits. An interest in strengthening budget credibility at the national level – for example, as part of ongoing budget reforms or as a result of a PFM assessment (e.g., PEFA) – can contribute to prioritizing budget credibility among the strategic objectives of an SAI. Or budget credibility can be used as a common thread by an SAI to link audits that address several dimensions of budget credibility and can be conducted in a certain period of time (multi-annual SAI audit planning).<sup>63</sup>

In any case, an initial step for an SAI to consider including budget credibility among its strategic priorities is to assess whether it is relevant and significant in the national context.

### Box 2.4. Questions for SAIs to consider when deciding whether or how to prioritize budget credibility

- Is the budget perceived as credible in the country?
- Is the PFM system performing according to international standards?
- What do aggregate indicators on the credibility of the budget indicate for the country (e.g., PEFA)?
- Has the government prioritized SDG 16.6.1 in its SDG implementation plans/national development plans?
- What might be the sources of budget deviations at the national level?
- Do government entities provide enough information on the rationale for budget deviations? Are budget deviations transparent?
- What are the impacts of budget deviations on the quality of service delivery?
- Are there indicators that budget deviations exist on the revenue/expenditure side and/or in spending composition?
- Are there indicators that budget deviations are relevant at entity or program levels?

<sup>62</sup> See Chapters 3 and 6 on risk analysis.

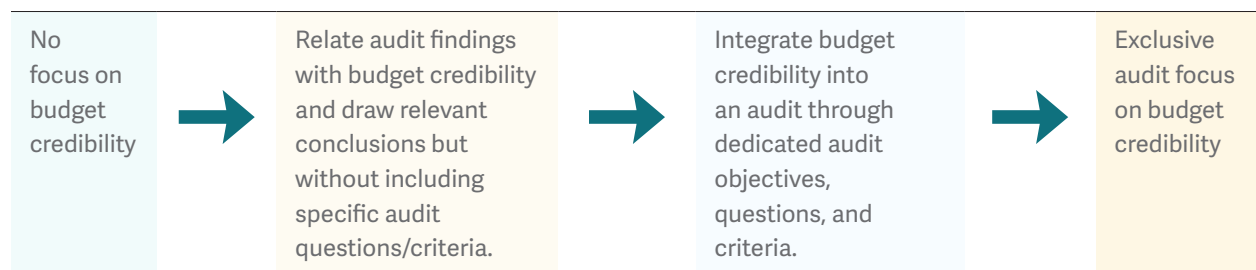
<sup>63</sup> See Chapter 4 for an example from Indonesia

Organizational considerations also inform an SAI's decision to focus on budget credibility as an audit topic, including:

- a. The mandate of the SAI on PFM/budget issues.
- b. The significance of budget credibility for the SAI and the mobilization of internal support for conducting this work.
- c. Existence of regional frameworks and technical guidance to inform and guide this type of work.
- d. Expertise and capacity of audit teams on PFM matters, including through mobilizing support from external experts.

- e. Access to timely information and data to analyze and use as supporting evidence.
- f. Availability of resources to examine the issue.

If an SAI explicitly signals an interest to include budget credibility in its audit plan, this strategic priority may be reflected in different ways. While some audits may focus exclusively on budget credibility, others may integrate a budget credibility angle as part of an audit on another related topic. Rather than exclusive, these approaches could be seen as incremental, or part of a continuum ranging from not focusing on budget credibility to exclusively focusing on budget credibility:



**Figure 2.1. Range of ways to approach budget credibility in an audit**

Source: A. Guillán Montero, 2023.

An exclusive and explicit focus on budget credibility in an SAI's audit plan will be more demanding in terms of resources and skillsets and might be better suited for an SAI with experience in budget auditing. In this case, audit work could focus more on the aggregate or whole-of-government level. Examples of possible audit objectives, questions, and criteria are presented in Annex 6.1.

Integrating a budget credibility perspective into other audits can be a less demanding option for an SAI with less experience in budget auditing (beyond providing assurance on the

financial statements of government entities), as SAIs currently audit many issues that relate to budget credibility. Thus, even if an SAI does not prioritize an exclusive focus on budget credibility, the credibility of government budgets can be a relevant consideration to be integrated when conducting other audits related to the budget and PFM system, and/or auditing particular entities or programs. Examples of possible audit questions to integrate budget credibility are provided in Chapters 5, 6, and Annex 6.1.

## Box 2.5. Ghana: Considering budget credibility in audits of the public accounts

**SAI Ghana** directly refers to budget credibility in some of its public accounts' audits. For example, in their audit of FY 2018, the SAI emphasized the need for the government to be accurate and consistent in meeting its revenue and expenditure estimates. The audit found that some entities with zero budget lines had been appropriated funds (e.g., for goods and services) from supplementary or contingency budgets that had not been included in the integrated financial management system, increasing the risk of incurring budget overruns.

Source: A. Guillán Montero, 2021.

Although the number of findings related to budget credibility may be more limited when integrating budget credibility as only one dimension into audit objectives, questions, and criteria, this will help auditors make more explicit links between audit findings and budget credibility. Auditors will have to explicitly relate the findings of the analyses to

credibility risks and problems and identify their causes. For example, one credibility problem is the deviation of collected revenues from their original forecasts and projections. Since some SAIs assess macroeconomic forecasts, they can consider the potential effects in terms of credibility and some of the possible causes. (See the example in Table 2.4.)

**Table 2.4. Relating an audit finding with budget credibility and identifying its causes**

Finding	Conclusions related to budget credibility	Causes
Poor or inaccurate macroeconomic forecasting creates credibility risks.	Unrealistic macroeconomic indicators can undermine the credibility of revenue forecasts and lead to multiple budget revisions due to resultant revenue/ expenditure mismatch.	<ul style="list-style-type: none"> <li data-bbox="1047 1455 1421 1654">• The inaccuracy of revenue projections may result from the poor quality of the revenue planning process due to capacity constraints, but also from political factors.</li> <li data-bbox="1047 1675 1421 1801">• Unexpected economic shocks may turn revenue estimations inaccurate (either over or underestimated).</li> </ul>

Another entry point for an SAI on this work may be via an entity or program that is suited to audits related to budget credibility. The audit could focus, for example, on the impact of budget deviations on beneficiaries or on any structures or internal processes that may underlie recurrent budget deviations in a specific program. Considerations for selecting relevant entities or programs could include:

- Those that involve the allocation/execution of large amounts of budget resources.
- Those with a track record of significant budget deviations (i.e., greater risk).
- Those where previous audits have identified weaknesses in internal controls, processes, or information systems, among others.
- Service delivery entities or programs that require certain conditions for eligibility (e.g., social programs) and /or delivery to beneficiaries.
- Common public services (e.g., related to health or education) where the availability of performance data may allow further inquiry into the impacts of budget deviations.

### Box 2.6. Examples of entities/programs that may be suited for audits that integrate budget credibility

**Brazil** - The Federal Student Loan Program failed to account in a timely manner for all expenditures, thereby unduly postponing bookkeeping and distorting the budget. The program also underestimated liabilities incurred by the government to private universities. The Federal Court of Accounts (TCU) issued an order for the executive branch to fully account for student loan expenditures in future budget legislation

**Indonesia** – The distribution of funds for some government assistance programs is not carried out in a timely manner, in the right amount, nor to the eligible beneficiaries. Deviations from the budget undermine the ability of the programs to meet the expected targets and accomplish their designated purpose. Unsound budgeting processes distort the planned budget for the programs and lead to deviations (underspending) during execution. One of the causes is the lack of reliable and valid data on the programs' beneficiaries.

**Portugal** – Recurrent deficiencies in the budgeting of basic and secondary education and health programs reveal structural problems in the budget forecasting process, which needs to be more realistic, and meanwhile represents a risk to budget credibility.

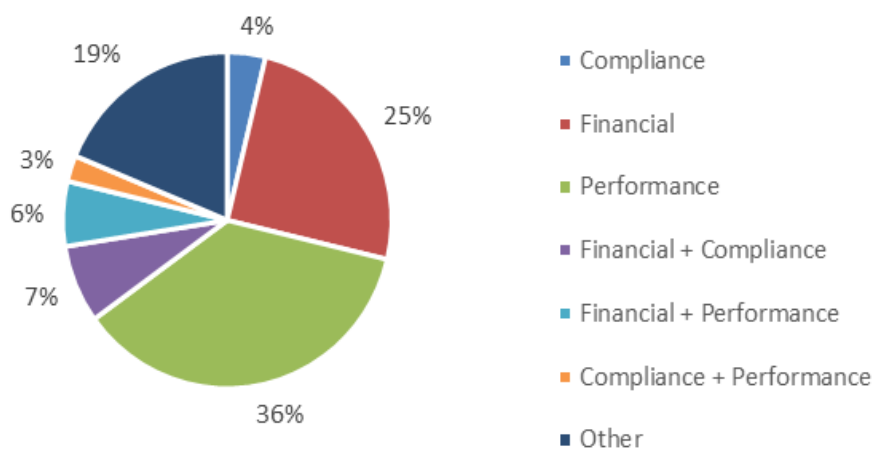
Source: UNDESA/IBP 2022 SAI survey; Input from SAI Brazil to the UNDESA-IBP Technical Meeting on the development of this handbook (May 26-28, 2021).

When selecting an entity or program for an audit related to budget credibility, auditors should consider the level of risks to budget credibility associated with the execution of the budget in that entity or program. If the level of risk is low, an examination with a focus on credibility may not add value. To the contrary, as the risks to budget credibility increase, an audit could help government officials address and strengthen budget credibility. For more on budget credibility risks, see Chapters 3 and 6.

## 2.4. Types of audits to examine budget credibility

Auditing budget credibility cuts across different types of audit practices. SAIs may examine issues related to budget credibility through financial, compliance, performance, and forensic audits, as well as through other activities (e.g., evaluations, inputs to the legislature). In a recent analysis of 80 audit reports from 20 SAIs that touched on budget credibility in some way, 20 of the reports were financial audits, three compliance audits, and 29 performance reports; 13 were a combination of two types of audits, and 15 were other types of SAI input. (Figure 2.2.)

Figure 2.2. SAIs can examine budget credibility through different types of audits



Note: This distribution is drawn from a sample of 80 audits analyzed in 2021.  
Source: A. Guillán Montero, 2021. "Upholding commitments. How supreme audit institutions can strengthen budget credibility through external audits," IBP.

Different types of audit practice may be more suited to examining specific aspects related to budget credibility. For example, as illustrated in Chapter 5, the scope of the audit of the year-end accounts varies across countries and auditors may use different audit methodologies and tools, ranging from financial to compliance audit, and even to performance audit.

Auditors may rely on different types of audits because of the nature of the issue examined and the objectives of the audit or due to their

mandate and professional experience. While some SAIs use all types of audits to examine budget issues (Indonesia, South Africa), some report only conducting financial (Kuwait), compliance (the Philippines), or performance audits (Latvia), and some report using two types of audits such as compliance and performance (the Netherlands) or financial and performance (South Sudan). Some SAIs also report using forensic audits (Algeria).<sup>64</sup>

## Box 2.7. Examining aspects of budget credibility through different types of audits

A financial audit confirms whether the financial statements and other financial information regarding the budget and the performance of the budget are complete and accurate in all material aspects. (Based on ISSAI 200.)\*

A compliance audit establishes whether the budget processes have complied with the legal and regulatory framework of the country and abides other relevant standards. (Based on ISSAI 400.)\*

A performance audit assesses whether government undertakings regarding the preparation and implementation of the budget have been carried out in an economical, efficient, and effective way. In addition, the audit will assess whether the objectives of the budget interventions have been achieved. (Based on ISSAI 300.)\*

\*See Section 2.5 for more on audit standards and principles.

Source: SAI Uganda 2022.

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<sup>64</sup> UNDESA/IBP SAI survey, 2022.

A comprehensive analysis of budget credibility at the aggregate level benefits from combining or integrating different types of audit information. However, combining different types of audit information must be well-defined in the scope of an audit, as different types of audits have different objects. Organizational barriers often make it difficult for auditors to work across audit

practices. For many SAIs, the various types of audit practice are generally conducted in silos and there is little or no synchronization of the audit periods covered or cross-referencing of audit findings. Despite these challenges, integrating audit practices can strengthen SAIs' budget work. (Box 2.8.)

## Box 2.8. The benefits of combining different audit practices and information

The Auditor General's Department of **Jamaica** has identified significant analytical benefits through meaningful recommendations when the auditing of an entity involved more than one audit type. In other cases, where analytical reviews (trend analyses) of the financial statements (FSA) were conducted as a precursor to a performance audit, the findings were more targeted, and the audit recommendations contributed to improvements in the entities' financial management. These positive results may contribute to the reduction of the entities' reliance on government budgetary support and increase fiscal space for the support of other important government programs.

Source: Input by Gail Lue Lim, UNDESA-IBP Technical Meeting on the development of this handbook (May 26-28, 2021).

## 2.5. Standards and general process to audit credibility

Audits of budget credibility follow the same standards and general processes as other audits. These standards and audit processes vary across audit practices - i.e., depending on whether an SAI conducts a financial, compliance, or performance audit, or an integrated audit which combines more than one type of audit (e.g., compliance and performance).

**Standards:** SAIs rely on relevant international auditing standards (ISSAI) established by the International Organization of Supreme Audit Institutions (INTOSAI) for each type of audit.<sup>65</sup> There are no specific standards or guidance on auditing budget credibility endorsed by INTOSAI. Auditors should apply the appropriate standards for the type of audit to be conducted. In addition, auditors should consider the existing standards and guidance related to specific topics such as auditing of information systems (GUID 5100); public debt audit (GUID 5250), or audit of the

<sup>65</sup> <https://www.issai.org/professional-pronouncements/?n=0-1000000000> There are handbooks to support SAIs in conducting each type of audit.



public debt information system (GUID 5259), among others. Relevant standards that cut across audit practices - such as ISSAI 100 and ISSAI 12 - also apply. Table 2.5 summarizes relevant INTOSAI standards and guidance that apply to auditing budget credibility.

SAIs also rely on their own internal guidelines, manuals, and standards for conducting different types of audits. According to the results of the survey conducted in 2022 for this handbook,

35 percent of respondents noted that their SAI follows internal standards and guidelines when conducting audits of the PFM system.<sup>66</sup> When using their own standards, SAIs must ensure that they are consistent with the relevant principles included in ISSAI 100, 200, 300, and 400. They can also rely on INTOSAI guidance on applying other relevant international standards (e.g., IPSAS for Public Sector Financial Statements, including IPSAS 24 and 42).

**Table 2.5. International audit standards and selected guidance relevant to auditing budget credibility**

Financial audit	Compliance audit	Performance audit
ISSAI 200-299 (FA principles) ISSAI 1000-1999 (now ISSAI 2000-2899) series of Financial Auditing Standards Guidance 2900 (to FA standards)	ISSAI 400-499 (CA principles) ISSAI 4000-4899 (CA standards) Guidance 4900 (authorities and criteria)	ISSAI 300-399 (PA principles) ISSAI 3000-3899 (PA standards) Guidance 3910 (central concepts PA), 3920 (PA process)
<b>Cross-cutting</b>		
ISSAI 12 (value and benefits); ISSAI 100 (fundamental principles of public sector auditing); ISSAI 140 (quality control) INTOSAI Gov 9100 (guidelines for internal control standards for the public sector)		

In addition, when conducting audits related to budget issues, SAIs also rely on international standards and good practices as sources of audit criteria. Some of these standards have been presented in Chapter 1. In the handbook survey, many SAIs reported using the [IMF Fiscal Transparency Handbook](#) and the [OECD Principles of Budgetary Governance](#), among others.<sup>67</sup>

Another relevant standard is the IMF Government Finance Statistics Manual (GFSM) (2014),<sup>68</sup> which provides a comprehensive conceptual and reporting framework for analyzing and evaluating fiscal policy, especially the performance of the general government sector and the broader public sector, and provides guidelines for presenting fiscal statistics.<sup>69</sup> For review engagements, with

<sup>66</sup> UNDESA/IBP SAI survey, 2022.

<sup>67</sup> Ibid. (UNDESA/IBP SAI survey, 2022.)

<sup>68</sup> <https://www.imf.org/external/Pubs/FT/GFS/Manual/2014/gfsfinal.pdf>

<sup>69</sup> Input by Gail Lue Lim to UNDESA-IBP Technical Meeting for the development of this handbook, (May 2021); UNDESA, 2021. CEPA Strategy Guidance Note.

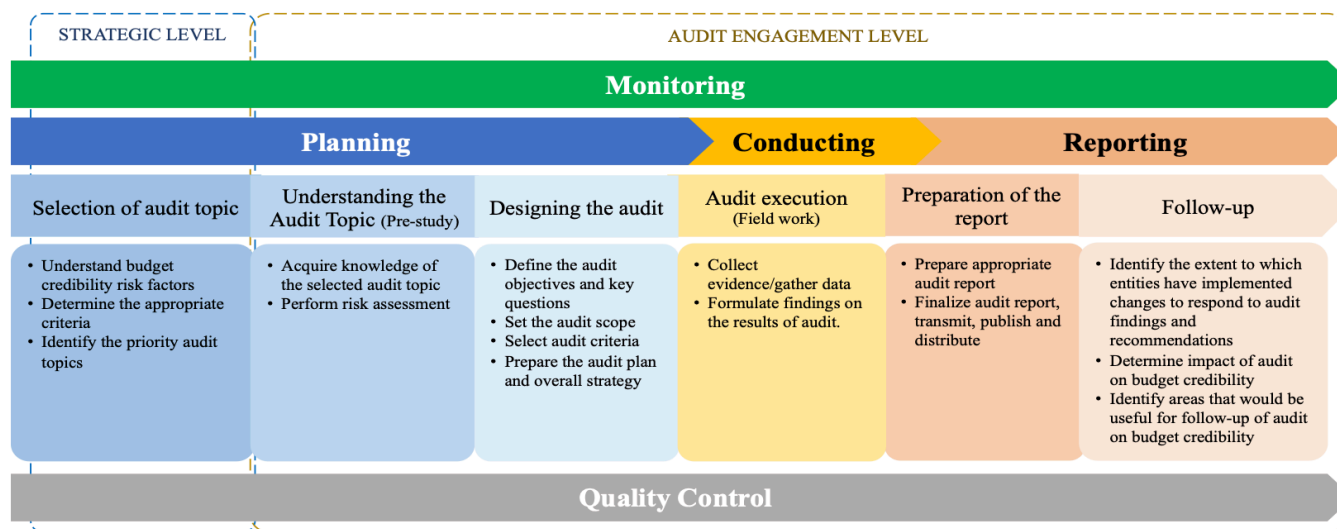
limited assurance, a relevant resource is the International Standard on Review Engagements (ISRE) 2400 (revised) (2013).

**General process:** Overall, the audit process can be structured in generic phases and elements across different audit practices, although the relevance of these phases may vary depending on the type of audit to be conducted. These generic phases of the audit process are illustrated in Figure 2.3.

When undertaking an audit related to budget credibility, auditors are confronted with different questions and requirements throughout these

phases. The questions are different depending on the frequency of the audits related to the budget. For example, audits of the year-end accounts or the execution of the state budget are conducted annually and therefore may require less investment in the planning phase, as the audit has a similar methodology from one year to another. Moreover, combining different types of audit practices also involves some choices and considerations related to the selection of the audit.

**Figure 2.3. Overview of the audit process**



Source: SAI Philippines 2022.

**Moving ahead:** To supplement the discussion in this chapter, Annex 2.1 presents examples of actual issues examined by SAIs in 20 countries and the potential risks they posed to budget credibility. Further, the next several chapters illustrate different options available for an SAI to enhance

its work on budget credibility. Each provides guidance and examples (e.g., audit objectives and questions) to help auditors understand what auditing budget credibility entails and addresses some of the questions and choices involved when undertaking this work

## Chapter 3: Budget credibility risks at the whole-of-government level

This chapter looks at budget credibility risks at the whole-of-government level. It provides examples of these risks at each stage of the budget process and illustrates how SAIs in several countries have assessed some of them. Building on the concept of budget credibility as discussed earlier, this chapter aims to raise awareness of the potential indicators of budget credibility risk and guides auditors on how to identify them when auditing government budgets.

### 3.1. Understanding budget credibility risks at the whole-of-government level

The credibility of government budgets is a key driver of effective service delivery and public confidence in government systems. At a technical level, a credible budget is one where deviations are insignificant at the end of the budget year.<sup>70</sup> From a governance perspective, a credible budget is one that has been subject to adequate oversight.

Budget credibility risks can occur at any stage of the budget process. At the whole-of-government level, they can be defined as credibility risks that relate to budget functions and processes (e.g.,

planning, monitoring) carried out by the main stakeholders responsible for the budget process at the national level and apply to the entire public administration at a consolidated level or the whole-of-government (as compared to specific entities or programs). The focus is on transversal (intersecting) processes rather than on specific institutions. For example, a recent assessment of nine countries using the AFROSAI-E assessment tool (see Chapter 4) identified transversal risk areas including the completeness of monitoring and supervision and policy automation of financial management and service delivery.<sup>71</sup> Budget credibility risks such as those to the whole-of-government can also result in credibility risks at the program and/or entity level, as discussed in Chapter 6.

In most jurisdictions, the main entities responsible for the budget process at the whole-of-government level are the Ministry of Finance and the legislature. Each plays a role at different stages of the budget process, as summarized in Table 3.1, although the exact distribution of their responsibilities varies among different countries depending on the governance model. Nonetheless, budgeting is a process that encompasses different entities and levels of government.<sup>72</sup> As highlighted in Chapter 1, other stakeholders also play important roles. For example, SAIs are critical

<sup>70</sup> John Whiteman, 2013. "Measuring the capacity and capability of Public Financial Management Systems," *International Public Management Review*, vol. 14, issue 2.

<sup>71</sup> AFROSAI-E, 2022. "Public financial management transversal risk report 2022", available at [https://afrosai-e.org.za/wp-content/uploads/2022/07/AFROSAI-E\\_Public-Financial-Management-Transversal-Risk-Report-2022.pdf](https://afrosai-e.org.za/wp-content/uploads/2022/07/AFROSAI-E_Public-Financial-Management-Transversal-Risk-Report-2022.pdf)

<sup>72</sup> OECD, 2014. "OECD principles of budgetary governance", Paris, OECD, available at <https://www.oecd.org/gov/budgeting/Draft-Principles-Budgetary-Governance.pdf>

to ensuring independent external oversight of the budget. Therefore, the budget process must be coordinated, consistent, and coherent across the public sector and across levels of government.<sup>73</sup>

**Table 3.1. Responsibilities of the Ministry of Finance and the Legislature in the budget process\***

Budget process stage	Tasks	Responsible stakeholder
Budget formulation	<ul style="list-style-type: none"> <li>Preparation of the annual budget in alignment with the country's long-term planning frameworks such as the National Development Plans and the Sustainable Development Goals (SDGs)</li> <li>Setting of revenue and expenditure targets at the national level</li> </ul>	Ministry of Finance
Budget approval	<ul style="list-style-type: none"> <li>Presentation of the draft budget to parliament or the legislature for review</li> </ul>	Ministry of Finance
	<ul style="list-style-type: none"> <li>Review and approval of the budget</li> <li>Enactment of the Appropriation bills</li> </ul>	Legislature
Budget execution	<ul style="list-style-type: none"> <li>Mobilizing revenue, as budgeted.</li> <li>Release of funds to implementing entities and programs according to the approved cash flow plan.</li> <li>Providing budget execution guidance to entities</li> </ul>	Ministry of Finance
Accounting and reporting	<ul style="list-style-type: none"> <li>Ensuring that there are functional budget monitoring systems within the government</li> </ul>	Ministry of Finance
	<ul style="list-style-type: none"> <li>Ensuring that entities account for resources provided</li> <li>Ensuring that information regarding the performance of the budget is available, easily accessible, and reliable</li> </ul>	Legislature
External oversight and evaluation	Discussing and taking action on issues raised in the audit reports regarding the execution of the budgets by entities.	Legislature

\*Distribution of responsibilities can vary depending on the country's governance model.  
Source: Chapter authors.

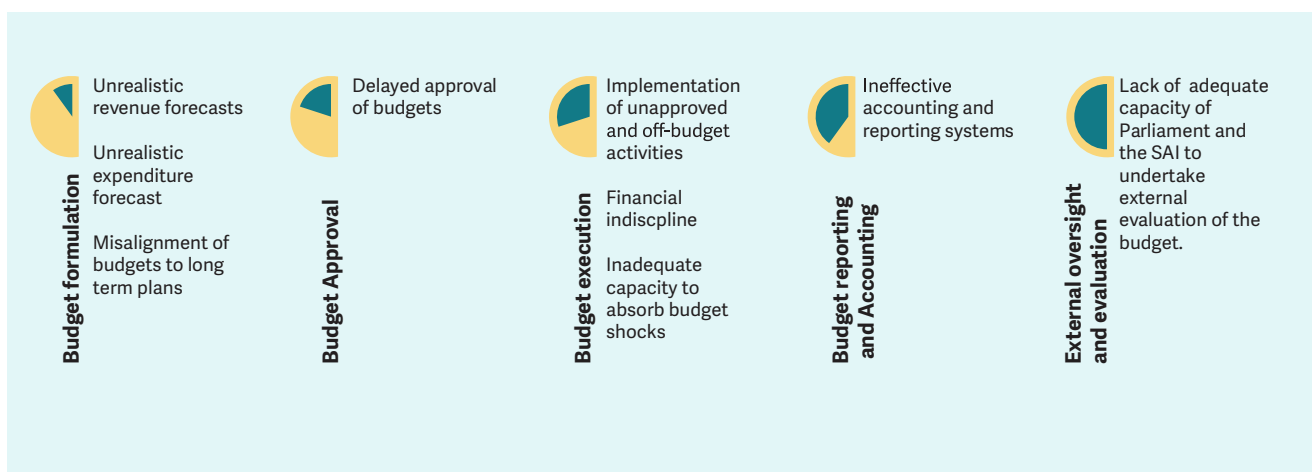
<sup>73</sup> Ibid

### 3.2. Common budget credibility risks at the whole-of-government level

Budget credibility risks related to whole-of-government functions are found at each of the

stages of the budget process. The most common ones are summarized in Figure 3.1.

Figure 3.1. Common budget credibility risks at the whole-of-government level



Source: Chapter authors

#### Risks for budget credibility at the budget formulation stage

Among the most common budget credibility risks that affect the budget formulation stage concern forecasting and alignment with long-term national plans.

#### Unrealistic revenue and expenditure projections/forecasts

The accuracy of revenue and expenditure forecasts will affect the credibility of the budget. More credible revenue forecasts are associated with fewer expenditure deviations.<sup>74</sup> Estimates of revenue and expenditure must be realistic and reflect the existing economic circumstances at the national level. The executive must also be able to mobilize/raise the projected revenue and spend it as planned. Unreliable forecasts are likely to result in major discrepancies between planned revenue

<sup>74</sup> de Renzio and Cho, 2020.

versus the actual revenue collected at the end of the year, both for individual revenue sources (e.g., tax, grants) and aggregate total revenue. In turn, this tends to lead to significant variation between

planned and actual expenditure, both at the aggregate and at the program, entity, and activity levels.

### Box 3.1. Unreliable revenue and expenditure forecasts result in the misallocation of resources

**SAI Jamaica** found that the Ministry of Finance's reliance on the projections approved by the Cabinet when the Special Early Retirement Program was first conceived, instead of undertaking the necessary research to identify credible up-to-date estimates, resulted in overfunding of the budget. This required a reduction of J\$2.5 billion (approx. US\$19 million) in the First Supplementary Budget. Poor budgeting, due to the lack of credible estimates, can result in a lack of funding for other relevant programs, a worrisome outcome in a context of limited fiscal space.

Source: "The importance of budget credibility to SAI Jamaica and related issues", Gail Lue Lim, Chief Economist and Deputy Auditor General, Auditor General's Department of Jamaica, 2021.

Unreliable estimates of revenue and expenditure affect the allocation of resources including service delivery (and outcomes achieved), with some programs or entities not receiving enough budget resources while others are over-funded. (Box 3.1.) When macroeconomic constraints are not properly factored in and/or underlying economic assumptions of costs are weak, the budget is too often forecasted on the basis of the previous year's budget, i.e., via a "bottom-up" approach determined by spending requests, which often leads to overspending.<sup>75</sup>

Governments tend to abandon revenue targets and other fiscal rules during external shocks (e.g., pandemics, natural disasters, and other

emergencies) and in times of poor economic performance and recession due to the adverse impacts on revenue realization and pressures to expand spending. These actions further affect revenue and expenditure targets, and the credibility of the budget.<sup>76</sup>

In sum, audits should examine the ability of the executive to make reliable revenue and expenditure forecasts and ensure that this revenue is mobilized. The inability to produce reliable forecasts may result from systemic causes or other factors (including political pressure), and may necessitate reforms to the entire forecasting system. (Box 3.2.)

<sup>74</sup> de Renzio and Cho, 2020.

<sup>75</sup> IMF, 1999. <https://www.imf.org/external/pubs/ft/expend/guide3.htm>

<sup>76</sup> Pratap Ranjan Jena and Satadru Sikdar, 2019. "Budget credibility in India-Assessment through the PEFA framework," No 284, NIPFP Working paper series, available at [https://www.nipfp.org.in/media/medialibrary/2019/12/WP\\_284\\_2019.pdf](https://www.nipfp.org.in/media/medialibrary/2019/12/WP_284_2019.pdf)

## Box 3.2. Deciphering systemic causes of unreliable revenue and expenditure forecasts

In 2013, **SAI Uganda** found limitations in their government's forecasting, including the lack of formal rules and a well-structured process to guide the revenue forecasting process; coverage gaps in revenue forecasts; low transparency in revenue forecasting; little or no systematic process for reviewing and learning from past revenue forecasts or assumptions; and the use of very basic forecasting models. The SAI specifically highlighted that these factors have negative consequences for the credibility of revenue forecasts.

Source: VFM audit report on revenue forecasting by MoFPED- OAG Uganda- 2013.

### Misalignment of budgets to long-term planning frameworks and the SDGs

Making progress on the implementation of the Sustainable Development Goals (SDGs) requires effective national policies and credible budgets that reflect public finance and policy priorities. National Development Plans play a critical role in SDG implementation, as they reflect the long-term aspirations of the government and its citizens for a period of five, ten, or more years.<sup>77</sup> These plans highlight interventions, pathways, and timelines for the achievement of the targets set by the executive.

Annual budgets are the tool through which governments implement these long- and medium-term strategic plans, and accordingly, they are expected to be aligned to the national development frameworks. Different mechanisms can help link budgets to cross-cutting policy

objectives. For example, the tagging of spending for SDGs, gender, climate, or children in financial information systems<sup>78</sup> can help track and assess the allocation of resources towards the achievement of the SDGs and other cross-cutting priorities.

Assessing the extent of alignment of annual budgets to national development plans is an important way for audits to identify opportunities for corrective actions. SAI audit reports have highlighted that a weak alignment of the budget to long-term national development frameworks undermines the achievement of long-term national priorities. Similarly, failure to integrate the SDGs into the budget cycle may impair progress on the achievement of the SDG targets. (Box 3.3.)

<sup>77</sup>Tarek Katramiz and Mahesti Okitarashi, 2021. "Accelerating 2030 Agenda integration: Aligning National Development Plans with the Sustainable Development Goals," Policy brief no. 25, United Nations University.

<sup>78</sup>Jennifer Asman, Claire Schouten, Sally Torbert, and Nik Mandalia, 2022. IMF blog: "How to Maintain Progress on Implementing the SDGs" at <https://blog-pfm.imf.org/en/pfm-blog/2022/10/how-to-maintain-progress-on-implementing-the-sdgs>. Also, see UNDESA, 2019. Sustainable Development Goal 16: Focus on public institutions, World Public Sector Report 2019, Chapter 3, Division for Public Institutions and Digital Government, NY, available at: <https://publicadministration.un.org/en/Research/World-Public-Sector-Reports>

### Box 3.3. Misalignment of budgeting to long-term planning frameworks can inhibit progress on SDGs

An audit looking at the alignment of **Malawi's** national budget against its commitment to implement the SDGs concluded the country would face challenges in achieving its SDG targets because of significant financing gaps in the annual budget to support their implementation.

Source: UNDP, 2018. "[SDGs audit on the national budget alignment in Malawi](#)," November.

#### Risks for budget credibility at the budget approval stage

Risks for budget credibility may also arise around the submission of the draft budget and its approval by the legislature. A major risk relates to the timing of the submission and approval of the budget.

#### Delays in budget approval by the legislature

Many countries have set regulatory frameworks to structure the way budgets are prepared by the executive, including timelines for the submission of the draft budget to the legislature for deliberation, scrutiny, and approval. The IMF Code of Fiscal Transparency, the OECD budget guidelines, and the PEFA framework

### Box 3.4. Delayed approval of the budget creates risks for budget credibility

The 2020 financial audit report on budget execution of **Bosnia and Herzegovina's** institutions highlighted that, despite the existence of deadlines for passing and adopting the budget laws to facilitate implementation of the budget, the 2020 Budget/Appropriations Act was only passed in July 2020. Financing of institutions and servicing of international obligations was carried out for most of the year based on temporary decisions of the Bosnia and Herzegovina Council of Ministers. From a governance perspective, this case highlights a major budget credibility risk, i.e., having the budget implemented based on temporary decisions by the Council of Ministers without oversight by the legislature.

Source: Response from SAI BiH to survey conducted in 2022 in preparation for the handbook



provide good guidance on this aspect (see Chapter 1). Most regulatory frameworks establish that the budget should be submitted to the legislature at least three to four months before the beginning of the next fiscal year.

Despite timelines established by law, budgets are still submitted late to the legislature (e.g., in many countries draft budgets are submitted to the legislature only one or two months before the beginning of the fiscal year).<sup>79</sup> This significantly reduces the time legislators have to scrutinize and analyze the budget and its fiscal objectives before approval, which increases the risk of budget deviations during budget execution. Moreover, delayed approval of the budget prevents government entities from initiating procurement processes based on the approved budget, especially in cases where cash warrants have to be provided to public entities. Inadequate procurement planning may also affect credible cash planning practices, which in turn affect the implementation of projects that would improve the living conditions of citizens.<sup>80</sup> Poor cash planning may create risks for debt management or lead to significant end-of-year spending. Late approval of the budget may also exacerbate other existing problems such as unsound revenue forecasting, further undermining budget credibility.<sup>81</sup> (Box 3.4.)

Delays in the approval of the budget are an indicator of potential budget credibility risk to be considered by auditors. Audits should pursue any explanations put forth, illuminate the effects of such delays, and make recommendations to prevent these delays in the future.

## Risks for budget credibility at the budget execution stage

Auditors may come across information and evidence suggesting credibility risks at the budget execution stage, too.

### Implementation of unapproved and off-budget activities

One of the credibility risks during budget execution is the allocation of budget resources for the implementation of activities that have neither been scrutinized nor approved by parliament. This can be limited to a few specific programs as discussed in Chapter 6, but could also be widespread across programs and subprograms throughout the budget. In this case, it is no longer a risk at the program level but becomes a risk at the whole-of-government level. Since unapproved activities were never allocated resources by the legislature, this puts pressure on other areas and increases the risk of diversion of resources and underperformance of some programs in relation to others.

In some cases, the executive implements activities using funds that were never disclosed to parliament for appropriation or “off-budget financing”. Failure to disclose funds to the legislature implies that the budget that is finally approved is understated by the amount of off-budget financing. Sometimes these funds are significant in terms of volume and implemented with limited transparency and oversight.<sup>82</sup>

<sup>79</sup> CABRI, AFROSAI, and ATAF, 2010. “A status report on good financial governance in Africa,” Pretoria, Collaborative Africa Budget Reform Initiative, available at [https://www.afdb.org/fileadmin/uploads/afdb/Documents/Generic-Documents/Annual\\_Meetings/2013\\_AM\\_Interpreters\\_Working\\_Documents/27%20Mai%20CABRI%20Status%20Report%20on%20GFG%20Web%20Version%20English\\_01.pdf](https://www.afdb.org/fileadmin/uploads/afdb/Documents/Generic-Documents/Annual_Meetings/2013_AM_Interpreters_Working_Documents/27%20Mai%20CABRI%20Status%20Report%20on%20GFG%20Web%20Version%20English_01.pdf)

<sup>80</sup> Ianna Jato Gideon, 2015. “Budget Implementation and Governance in Nigeria” Academic Discourse: An international journal, available at <https://www.globalacademicgroup.com/journals/academic%20discourse/BUDGET%20IMPLEMENTATION%20AND%20GOVERNANCE%20IN%20NIGERIA.pdf>

<sup>81</sup> Camille Karamaga, 2012. “Timing is everything: Why delays in budget approval are undermining fiscal policy in Africa ... and what can be done about it,” September, IMF PFM Blog, <https://blog-pfm.imf.org/en/pfmblog/2012/09/timing-is-everything-why-delays-in-budget-approval-are-undermining-fiscal-policy>

Large amounts of “off-budget” financing outside the appropriation structures of the regular budget affect policy choices and outcomes and involve a risk in terms of budget credibility. The lack of accountability for off-budget spending may lead to overall overspending and poor provision of goods and services, create opportunities for corruption and maladministration, and prioritize non-strategic spending. Also, off-budget financing undermines external oversight by the SAI and other stakeholders and therefore, affects the assessment of budget credibility risks that were based only on resources that were regularly appropriated by parliament.

### Financial indiscipline within the executive and legislature

The credibility of the budget also relates to the financial discipline of stakeholders, particularly the executive and the legislature. Budget credibility risks may arise as a result of the relative balance of

powers between the executive and the legislature in the budget process. This balance is shaped by the political economy of executive-legislative relations throughout the budget process and the institutional arrangements that influence those interactions.<sup>82</sup> Parliaments have budgetary powers which are not always used effectively and responsibly. In some cases, these powers may be used to avail resources for achieving political agendas at the expense of sound budget execution and effective service delivery. See Box 3.5.

Other stakeholders, especially within the executive, may use budgetary powers for granting tax waivers for political reasons, for the unsustainable accumulation of debt, or for the implementation of projects without confirming their economic viability at the expense of service delivery. See Box 3.6

### Box 3.5. Legislative amendments can affect budget credibility

In 2018, in **Brazil**, an audit of individual parliamentary amendments to the budget bill by the Federal Court of Accounts (TCU) revealed that a total of R\$ 8.15 billion was authorized through parliamentary amendments between 2014 and 2017. Out of this, only R\$5.4 billion (66 percent) was committed and R\$ 4.5 billion was finally spent. Lack of technical capacity to implement projects at the subnational level was, among other factors, one of the causes of underspending. The audit further noted that the execution of those expenditures was prioritized in 2017 and 2018, most likely due to electoral considerations.

Source: A. Guillán Montero, 2021.

<sup>82</sup> Linda J. Bilmes, 2018. “The Fiscal Opacity Cycle: How America Hid the Costs of the Wars in Iraq and Afghanistan.” *Toward A Just Society: Joseph Stiglitz and Twenty-First Century Economics*. Ed. Martin Guzman. Columbia University Press, 457-478.

<sup>83</sup> Carlos Santiso, 2005. “Budget institutions and fiscal responsibility. Parliaments and the political economy of the budget process in Latin America,” Washington D.C., World Bank Institute, available at <https://documents1.worldbank.org/curated/en/963711468265796384/pdf/358630WB10BudgIsponsibilityIPUBLIC1.pdf>

### Box 3.6. Political pressure can affect budget execution and credibility

In **Nigeria**, the budget contained unrealistic capital spending projections for several years (2009-2016), because multiple projects were included in the budget for political reasons, even though the executive had a very low capacity to implement any of them. More than a third of these projects were never started or completed. In such circumstances, critical projects had to compete for budget resources with non-priority projects.

Source: Atiku and Lakin, 2019. "The Contours of Budget Credibility in Nigeria", <https://internationalbudget.org/publications/the-contours-of-budget-credibility-in-nigeria/>

External audits can shed light on the credibility risks related to legislative amendments or the use of executive budgetary powers for political considerations.

#### Inadequate capacity to absorb budget shocks due to emergencies or long-term risks

External shocks, emergencies such as COVID-19, and, increasingly, longer-term external risks such as climate change, put pressure on the executive to increase spending in certain areas and shift resources within the budget in order to mobilize the resources required to respond to these emergencies or longer-term risks. The likelihood of budget deviations significantly increases if budgets cannot sufficiently absorb the pressure. In

these cases, when the executive has no clear plan to respond, the only way out is to cut resources originally allocated to areas to raise resources for contingency and supplementary budgets which will affect the performance of the undercut programs. (Box 3.7.)

A study by IBP which examined expenditure deviations related to 10 SDGs in 13 countries for the period 2018-20 showed that budget shifts as a result of Covid-19 did not worsen budget credibility with respect to the SDGs, but overspending in the health and social protection sectors was facilitated by resources pulled from other key sectors. As a result, underspending in education, water and sanitation, and gender was significant, on average to 18 percent, 15 percent, and 13 percent respectively.<sup>84</sup> (See Figure 1.5 in Chapter 1.)

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<sup>84</sup> IBP, 2022. "Budget Credibility and the Sustainable Development Goals"

### Box 3.7. Budget credibility in the context of COVID-19

Confronted with the onset of the pandemic, in FY 2019/20, **Kenya's** health budget was overspent compared to previous years. Health programs' spending exceeded the original approved health budget by 11 percent. This was largely on account of additional resources to the Health Policy, Standards, and Regulations program (which included the COVID-19 Emergency Response), which overspent its budget by 63 percent.

While the National Safety Net Programme's budget was increased by 63 percent to expand the reach of the government's social protection programs in FY 2019/20, only 82 percent of that budget was absorbed. This represented significant underspending just when the economic impact of COVID-19 was at its peak with a strict lockdown in the country.

Transparency and accountability challenges persist in how the government raised and spent the COVID-19 allocations. Disaggregated information on pandemic-related budget allocations was limited. For instance, detailed information on how funds from the Kenya COVID-19 Emergency Response Fund were allocated and expended was not available, particularly with regard to voluntary contributions, grants, and donations to the fund. Spending information at the national level, as provided in the Controller of Budget Reports and Sector Working Group Reports, was also not comprehensive regarding spending at the very granular budget lines and the resulting impact.

Source: FaithAnn Kinyanjui, Abraham Ochieng, Abraham Rugo, John Kinuthia, 2021. [https://internationalbudget.org/covid/wp-content/uploads/2021/08/Kenya-Brief-Managing-COVID-Funds\\_Paper.pdf](https://internationalbudget.org/covid/wp-content/uploads/2021/08/Kenya-Brief-Managing-COVID-Funds_Paper.pdf)

Auditors need to examine how the executive mobilizes and executes resources to respond to emergencies or other economic shocks given that they present opportunities for significant risks to budget credibility. Countries that have a low capacity to accommodate shocks are more likely to have major diversions of resources from social programs than countries where the budget has some flexibility to accommodate such unexpected occurrences. This will drive

deviations and underperformance in the programs which have been undercut. Poor implementation capacity may explain at least some of the significant underspending of critical resources during emergencies. Auditors should also examine the transparency and accountability provisions governing the mobilization and execution of resources in response to emergencies. (See Box 3.8.)

## Risks for budget credibility in budget reporting and accounting systems

Strong and comprehensive accounting and reporting systems contribute to strengthening budget credibility since they ensure the availability of budget information and enable effective oversight over public spending and the correct use of resources. Strong accounting and reporting systems also significantly reduce the risk of diversion of resources from approved budgets. Moreover, the integration of non-financial and performance information holds stewards of public resources accountable for results.

## Ineffective reporting and accounting systems

Weak reporting systems are characterized by insufficient and/or inappropriate performance indicators, poor quality data, and information (notably limited transparency on contingent liabilities and the debt management framework, ad-hoc and unsystematic monitoring of activities, and weak linkages between financial and performance indicators, which exacerbate credibility issues).<sup>85</sup> Disaggregated information on budget allocations and spending is often limited. Despite overall improvements in budget transparency over the years, significant challenges remain that create risks for budget credibility. (Box 3.8.)

### Box 3.8. Lack of budget transparency contributes to budget credibility risks

Despite overall improvements in budget transparency (Open Budget Survey scores have increased over 20 percent among countries surveyed between 2008 and 2021), most countries are still far from being sufficiently transparent to allow for meaningful engagement and scrutiny of public spending. Nearly one in three budget documents that should be published worldwide are missing from the public domain. Three out of five countries surveyed do not publish mid-year reports, which are important channels to communicate changes in spending during budget execution. Many governments failed to provide information about debt.

Serious gaps remain in the checks and balances of executive's management of public funds. In three out of five surveyed countries, executives can shift funds between agencies without first gaining legislative approval and in two thirds can reduce budgeted funds without prior approval. In these countries, executives can act unchecked and disregard public and legislative input as expressed in approved budgets.

Source: IBP 2022, Open Budget Survey 2021.

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<sup>85</sup> A. Guillán Montero, 2021.

### Box 3.9. Budget credibility and the quality of performance indicators and information

A report by the Auditor-General of **New Zealand** (2008) identified weak linkages between medium-term outcomes and organizational strategies and annual output information, as well as the lack of well specified and relevant performance measures and standards for both medium-term and annual forecast information as one of the areas that affect budget performance.

The **Republic of Korea's** SAI conducted a review of the performance reports of 52 central government agencies in 2015. The SAI found overlapped settings in the performance index, and errors in reporting the achievement of performance indicators. In 2016, an analysis of 563 of 740 program indicators (76 percent) showed that 38 cases in performance planning and 24 in performance reporting had been wrongfully evaluated.

Source: A. Guillán Montero, 2021.

Audits need to examine the effectiveness of the accounting and reporting systems to produce accurate, complete, and reliable reports and information. Linking budget execution to improved service delivery requires effective

accountability systems that include non-financial and performance indicators and information. Performance reviews indicate that weak accountability systems contribute to budget credibility issues. (See Boxes 3.9 and 3.10)

### Box 3.10. Calls for legislative tightening of reporting requirements to enhance budget credibility

In a November 2022 letter to Parliament, citing the need for better visibility on how budget decisions relate to the long-term outcomes that government is pursuing, the Auditor General of **New Zealand** requested the body to clarify and tighten the reporting requirements on government spending, generally, but also on what is being achieved by that spending. Too often the reports are “tenuous, lack transparency and are focused on the short term.”<sup>86</sup>

For more from SAI NZ's efforts to strengthen performance reporting, see:  
[Performance reporting — Office of the Auditor-General New Zealand \(oag.parliament.nz\)](#) and  
[Part 3: The Controller function — Office of the Auditor-General New Zealand \(oag.parliament.nz\)](#)

<sup>86</sup> See [Letter to the Officers of Parliament Committee about accountability concerns — Office of the Auditor-General New Zealand \(oag.parliament.nz\)](#)

## Risks for budget credibility at the external oversight and evaluation stage

The government has a duty to account for the use of public resources and results achieved. Risks for budget credibility can also stem from the processes and stakeholders meant to ensure independent oversight and evaluation of the budget – mainly the legislature and external audit agencies.

## Capacity of parliament and SAIs to provide evaluation and oversight of budget execution

Effective external oversight and evaluation helps to mitigate risks to budget credibility. Accountability in the budget process depends on (1) the legislature having the means to question and authorize budget proposals and to track the integrity and effectiveness of their implementation and the corresponding outcomes and (2) external audit agencies that can provide an ex-post assessment of the degree to which the executive reports on resources raised and spent, whether such operations were carried out in compliance with existing laws and regulations, and if the spending achieved its policy objectives.

Budget reforms in recent years have sought to strengthen budget accountability by strengthening the role of parliament, enhancing

the capacity of independent oversight institutions, and opening more opportunities for citizens to engage in the budget process. However, challenges to budget accountability remain in relation to formal constraints (e.g., mandates of accountability institutions), limited capacity and resources, and the wider governance context in which both parliaments and SAIs operate.<sup>87</sup> For example, just over half of the SAIs that responded to the recent UNDESA/IBP survey (2022) cited challenges such as scarcity of resources and lack of expertise to conduct audits related to budget credibility.

In many countries, budget evaluation and oversight by the legislature is not adequate. Parliaments have the power to approve budgets before implementation, but more frequently their budget hearings are not open to all interested participants. Rather, in three out of four countries surveyed by the most recent Open Budget Survey (OBS),<sup>88</sup> legislatures invited only specific individuals to testify or provide input prior to budget approval.

The low level of public engagement in budget processes in most jurisdictions contributes to the challenges. Where it does occur, public engagement and debate around budgeting processes (through organized civil society, citizen platforms, and the media) creates pressure on the executive to align the budget to the aspirations and demands of citizens (as seen from several examples in Chapter 7). Yet few legislatures hold hearings on budget outcomes. For example, legislatures in only 19 out of the 120 countries surveyed in the most recent OBS engage with the

<sup>87</sup> UNDESA, 2019. Sustainable Development Goal 16. Focus on public institutions.

<sup>88</sup> IBP, 2022. Open Budget Survey 2021, available at <https://internationalbudget.org/open-budget-survey/>

<sup>89</sup> Ibid.



public on the review of the Audit Report.<sup>89</sup>

The capacity of SAIs to undertake budget credibility reviews and evaluations is critical in promoting budget credibility. During the planning phase of the audits on the budget, SAIs should assess if they have the required capability to undertake budget reviews. In some cases, SAIs may have to use consultants as they build internal capacity. Measures to enhance the skills of auditors, including on assessments of budget credibility, are critical to strengthening the SAI role and mitigating risks related to weak external oversight. High-quality audit reports present an important opportunity to strengthen budget credibility and have a powerful positive impact on citizens' lives, but only if their recommendations are well-formulated, communicated, and spur the

appropriate remedial action by all the relevant stakeholders. (See Chapter 7.)

### 3.3. Indicators of credibility risks across the budget process

During the planning and execution of the audit, auditors should pay attention to common red flags that indicate budget credibility may be compromised. Many examples of such indicators are presented in Table 3.2. (and Annex 2.1). When auditors observe these indicators in the course of their work, they should review the evidence to assess and document the significance of the risks to budget credibility.

**Table 3.2. Examples of common indicators of budget credibility risks**

Budget Stage	Budget Credibility Risks	Common Indicators
Budget formulation	<p>Unrealistic revenue and expenditure forecasts.</p> <p>Misalignment of annual plans to long-term planning frameworks and SDGs.</p>	<p>Poor revenue planning processes.</p> <p>Lack of adequate technical competencies in the departments responsible for preparing the forecasts.</p> <p>History of under-collection of revenues by executive-without justification.</p> <p>History of requests for supplementary funding by the executive during budget implementation.</p> <p>History of requests for approval of new debt by the executive during budget implementation.</p> <p>Differing investment priorities within annual budgets and long-term planning frameworks.</p> <p>History of budget cuts for programs and entities.</p>



<b>Budget Stage</b>	<b>Budget Credibility Risks</b>	<b>Common Indicators</b>
Budget approval	Delayed approval of the budget.	<p>Frequent requests for and granting of emergency authorizations for government spending.</p> <p>Short periods for legislative scrutiny of budget proposals before approval.</p>
Budget execution	Un-approved/off-budget financing.	<p>Actual expenditure is often significantly more than appropriated expenditure.</p> <p>Regular seeking of retrospective approvals for expenditure already incurred by the executive.</p> <p>Significant number of approved projects are unfunded.</p> <p>Unabsorbed funds on several programs and sub-programs.</p> <p>High risk/prevalence of corruption and inefficiencies within expenditure systems</p>
Budget reporting	Ineffective reporting and accounting systems.	<p>Significant variations between formal performance indicators and targets and actual deliveries to citizens.</p> <p>Unreliable performance indicators.</p> <p>Incomplete and/or untimely performance data and reports.</p>
Budget oversight and evaluation	Capacity of and incentives for parliament and SAI to provide evaluation and oversight of budget execution.	<p>Resolutions of parliament are not public.</p> <p>Limited public debate on the budget.</p> <p>Focus of assessments is on the accuracy of financial information rather than assessing impact of government investments in communities</p>

### 3.4. Wrapping up

The budget, as a tool for the delivery of services and the fulfillment of government's policy objectives, can only be effective if deliberate efforts are made to uphold its credibility. Throughout the budget process, there are risks to budget credibility that need to be audited

from a whole-of-government perspective. SAls need to strengthen their arsenal of skills and competencies to be able to identify and address the risks to budget credibility when undertaking their audits. Annex 3.1 offers some guiding questions to support auditors in probing budget credibility risks in each stage of the budget process.

## Chapter 4: Auditing the performance of the public financial management system

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**A sound PFM system is essential to ensuring an effective state that delivers goods and services to its citizens, reduces poverty, supports economic growth, taxes fairly and efficiently, and spends responsibly.<sup>90</sup> Improving the effectiveness of the PFM system can generate widespread and long-lasting benefits, and may in turn help to reinforce wider societal shifts towards more inclusive and effective institutions.<sup>91</sup> ...[which] generate trust, promote innovative energies, and allow societies to flourish.<sup>92</sup>**

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External audits on the performance of the public financial management (PFM) system can shed light on whether and how the institutional arrangements in place are contributing to budget credibility. Building on the experience of the SAIs of Indonesia and Zambia, in particular, as well as SAIs from several other countries, this chapter discusses different approaches to auditing the PFM system through performance audit techniques and by combining auditing with other reporting tools. The chapter discusses the challenges and impact of these audits and identifies opportunities to enhance the PFM system further.

### 4.1. Focusing on the performance of the PFM system

SAIs play an important role in the public financial management (PFM) system. Auditing and reporting on how governments mobilize revenues, allocate public funds, undertake public spending, and account for spent funds, are critical PFM processes.<sup>93</sup> To ensure proper oversight of the stewardship and use of public resources, SAIs should be independent, effective, and credible in the execution of their mandates.<sup>94</sup> Moreover, SAIs should have unrestricted rights of access to all

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<sup>90</sup> OECD, 2011. "Supporting Capacity Development in PFM - A Practitioner's Guide," 4th High-Level Forum on Aid Effectiveness.

<sup>91</sup> Lawson, 2015. cited in Albert Kasoma, 2018. Analysis of the Public Finance Management Act of 2018. Policy Monitoring and Research Centre. Lusaka, Zambia

<sup>92</sup> Daron Acemoglu and James Robinson, 2012. *Why Nations Fail: The Origins of Power, Prosperity, and Poverty*, NY: Crown; and Dani Rodrik, ed., 2003. *In Search of Prosperity: Analytic Narratives on Economic Growth*, cited in Lawson, 2015.

<sup>93</sup> Lawson, 2015.

<sup>94</sup> INTOSAI, 2019. INTOSAI P-12, The Value and Benefits of Supreme Audit Institutions – making a difference to the lives of citizens; INTOSAI P-1, The Lima Declaration; and INTOSAI P-10, The Mexico Declaration on SAI Independence

necessary information for the proper discharge of their statutory responsibilities.<sup>95</sup>

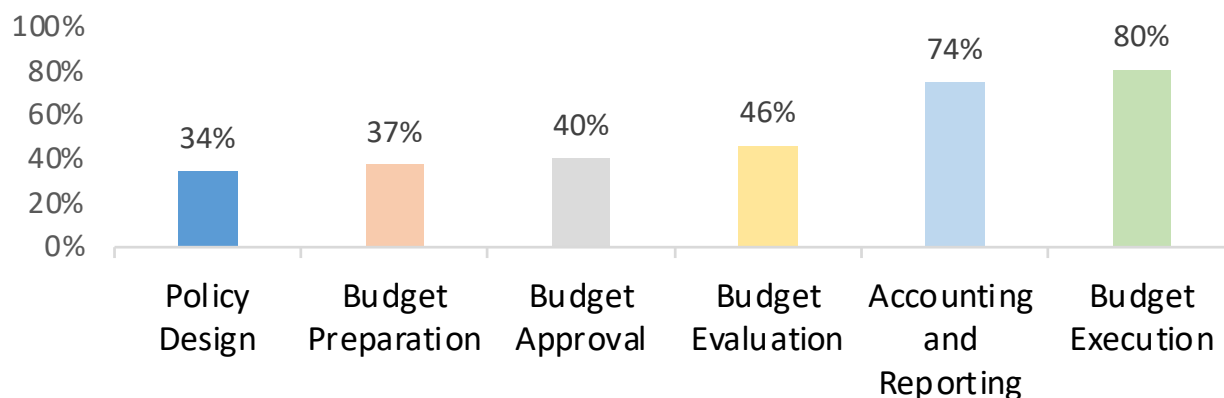
### Introducing the approach

External audits can assess budget credibility in different ways, including through scrutiny of the performance of the PFM system more broadly. For example, SAIs can evaluate how reliable and transparent budgets are, how assets and liabilities are managed, whether the budget is based on an assessment of fiscal trends or just ad hoc information, whether there is predictability in budget execution, the reasons for any

underspending or overspending, and whether accounting and reporting are effectively informing and supporting the other pillars of the PFM system, among other aspects.

Many SAIs already have experience auditing the performance of the PFM system, as indicated by two-thirds of the respondents to the UNDESA/IBP SAI survey in 2022.<sup>96</sup> Among these surveyed countries, SAIs are auditing specific PFM processes of the budget cycle including budget execution, accounting and reporting, budget approval and budget evaluation, and to a lesser extent budget preparation and policy design (strategic budgeting). (Figure 4.1.)

**Figure 4.1. Sample distribution\* of audit work on the performance of the PFM System, by budget stage**



\*Percentage of survey respondents (N 25) that conduct audits on aspect(s) of the PFM system

Source: Chapter authors, from UNDESA/IBP 2022 SAI survey data

<sup>95</sup> INTOSAI, 2019. INTOSAI P-12.  
<sup>96</sup> UNDESA/IBP SAI survey, 2022. p. 16.

As to methodology, an SAI can use a performance audit to assess the performance of the PFM system,<sup>97</sup> or, depending on its mandate, may conduct combined audits incorporating financial, compliance, and/or performance aspects. In such cases, the standards relevant to each type of audit should be complied with. Thus, an SAI may consider a combination of financial and performance audits or compliance and performance audits in assessing the performance of the PFM system.<sup>98</sup>

In addition to audit tools, auditors may also rely on available diagnostic and reporting frameworks to produce information that complements their assessment of the performance of PFM systems. SAI experiences with these different approaches will be presented in the following sections.

## Taking account of the particularities of national PFM systems

How PFM operates in practice differs across countries.<sup>99</sup> Some countries may experience institutional capacity constraints that undermine the system's performance. For example, some experience delays in the approval of the budget, or budget execution is driven by short-term needs rather than longer-term priorities and national objectives.

Auditors should be knowledgeable of both the common processes that structure the PFM system and the particular characteristics and features of the system in their own national context, including the normative framework, processes, activities, and main stakeholders. As an example, SAI Indonesia recounts its specific PFM process through the budget cycle with various stakeholders in Box 4.1.

### Box 4.1. An overview of the budget cycle and relevant stakeholders in Indonesia

The budget cycle at the central level of government in Indonesia is primarily regulated by the State Finance Laws (Law No. 17/2003, Law No. 1/2014, and Law No. 15/2004). The main budget/PFM processes and stakeholders are described below:

**Budget formulation:** The government prepares its fiscal policies, basic macroeconomics assumptions, the annual working plans, and allocates the budget for each work plan. All these materials are included in the draft of the state budget act to be discussed and approved by the legislature.

<sup>97</sup> Performance audits examine whether a government is using public resources in an effective, efficient, and economical manner. These audits identify the reasons for any underperformance, what is working well within audited entities, and/or measure how performance has improved due to changes in policy or operations. A performance audit may focus on a single program, policy, entity, or fund, or may focus on outcomes or systems. See INTOSAI-IDI, 2021 ISSAI Performance Audit Implementation Handbook; INTOSAI 2019, INTOSAI-P 1, The Lima Declaration, Section 4.

<sup>98</sup> ISSAI 300 Performance Audit Principles and ISSAI 400 Compliance Audit Principles.

<sup>99</sup> Chapter 1 presents the common processes, activities, and stakeholders of PFM systems while Chapter 2 highlights the contextual nature of PFM and the variety of institutional arrangements in different countries.

**Budget approval:** The proposal of the state budget act is discussed with the legislature. Based on the discussion, the legislature will specify the Proposal to be the State Budget Act. The bill on the state budget submitted by the President must be voted on by the legislature within two months before the end of the fiscal year (end of October). However, if the budget is not approved by the legislature, the Constitution provides for the reenactment of the state budget of the previous year.

**Budget execution:** The President issues a Presidential Regulation concerning the details of the Annual Budget (APBN). Starting January 1 of the new fiscal year, government agencies/ministries may carry out revenues and expenditures related to their mandate in accordance with the budget implementation document. The President, as head of government, holds the overall responsibility for state financial management. The finance minister as the fiscal manager is responsible for the overall administration of public finances, including the consolidation of the central government financial report which ensures accountability for the execution of the annual state budget. Expenditure controls are executed by the responsible financial officers at different levels of government and include mechanisms such as segregation of duties, authorization of approvals, and restrictions on access to resources and information.

The supervision of the implementation of the State Budget Act is carried out internally by the Inspectorate General within each government agency/ministry and the Financial and Development Supervisory Agency. The inspector general supervises the activities of ministries and agencies funded through the APBN. The Financial and Development Supervisory Agency supervises cross-sectoral activities, state treasury activities performed at the request of the Minister of Finance as the general treasurer and other activities per the President's request.

**Budget evaluation:** As a form of accountability for the implementation of the annual state budget, the government will submit the Central Government Financial Report to the Supreme Audit Institution (BPK RI) to be audited. Law No. 15 of 2004 on the Audit of State Financial Management and Responsibility provides the BPK RI with independence in audit planning, execution, and reporting of audit findings. The audit of financial statements considers compliance with the Government Accounting Standard, adequacy of disclosure, compliance with legislation, and effectiveness of internal controls. The SAI also conducts performance audits and special-purpose audits. No later than six months after the end of the fiscal year, the President will submit to the legislature a draft law on accountability for the implementation of the annual state budget along with the central government's financial reports that have been audited by the SAI.

## Assessing performance against the objectives of the PFM System

Auditors need to be aware of and identify the ultimate objectives of PFM systems against which performance can be assessed and measured. Chapter 1 presented the objectives that PFM systems are expected to support: aggregate fiscal discipline, allocative efficiency, operational efficiency, transparency and accountability,<sup>100</sup> equity and inclusion, as well as four other goals including budget credibility; prudent decision-making, and sustained fiscal health; reliable and efficient resource flows and transactions; and institutionalized accountability.

Ideally, the performance of the PFM system is assessed by measuring performance against these objectives. For example, the achievement of aggregate fiscal discipline can be measured through the PEFA assessment (see Chapter 1) which quantifies how closely revenue collection and spending adhere to the approved budget, and transparency and accountability can be assessed by the Open Budget Survey (OBS), which provides a reasonable proxy for transparency, oversight, and opportunities for public engagement in fiscal affairs.

However, measuring strategic allocation and operational efficiency requires in-depth studies. Some OECD countries and middle-income countries (e.g., South Africa) undertake these regularly through program evaluations or value for money audits. For example, as procurement

processes involve considerable expenditure and are a key component of the PFM system, regular auditing would ensure that value for money is achieved – or reported on, where it has not been.

In practice, however, the assessment of PFM systems usually focuses on the examination of the institutions, rules, and procedures that are most likely to ensure the achievement of the objectives of the PFM system.<sup>101</sup> Therefore, external audits may assess the achievement of these objectives of the PFM system, including budget credibility, and/or examine how the institutional arrangements in place contribute to their success. That is, auditors can directly examine how the PFM institutional arrangements work to ensure budget credibility (based on the processes defined in Chapter 1) and the causes of underperformance. Alternatively, they can focus on other important elements of the PFM system, such as transparency or fiscal discipline, and relate the audit findings with risks for budget credibility.

## SAIs' use of PFM assessment and reporting frameworks

In addition to audit tools, SAIs may also rely on existing PFM reporting frameworks to evaluate the performance of the PFM system in terms of budget credibility. These frameworks can be used by themselves, as sources of audit criteria, and /or in combination with audit methodologies and tools.

<sup>100</sup> Marco Cangiano, 2017. "What is Public Financial Management?" at [https://www.rgs.mef.gov.it/Documenti/VERSIONE-I/Comunicazione/Workshop-e-convegna/Seminario\\_2017-02-6\\_8/01\\_-\\_What\\_is\\_PFM\\_-\\_Cangiano.pdf](https://www.rgs.mef.gov.it/Documenti/VERSIONE-I/Comunicazione/Workshop-e-convegna/Seminario_2017-02-6_8/01_-_What_is_PFM_-_Cangiano.pdf); Lawson 2015

<sup>101</sup> Allen Schick, 1998. "Why Most Developing Countries Should Not Try New Zealand's Reforms", *The World Bank Research Observer*, Volume 13, Issue 1, February 1998, Pages 123–131, <https://doi.org/10.1093/wbro/13.1.123> cited in Lawson, 2015.

## International PFM assessment frameworks

Various ways to assess and compare national PFM systems against international standards were presented in Chapter 1. SAIs can use these

analytical tools, indicators, and frameworks in their audit work on budget credibility<sup>102</sup> and can combine them with in-country analysis and information from audits to further understand how existing PFM processes in place are working. (See Box 4.2.)

### Box 4.2. SAI Peru applies the PEFA framework to assess budget credibility

The General Comptroller of **Peru** has used the PEFA framework to evaluate the credibility of public spending in Peru for the period 2019-2021. SAI Peru found that significant deviations from the originally approved budget (54 percent on average over these years) inhibit proper scheduling of the contracting and execution processes, causing the accrual level to be a significantly lower proportion of the modified budget, particularly in the case of investments, and diverting funds away from intended priorities.

Source: Nelson Shack and Rogers Rivera, 2022. Evaluación de la credibilidad presupuestal del gasto público en el Perú. Documento de Política en Control Gubernamental. Contraloría General de la República. Lima, Perú.

Available at <https://www.gob.pe/institucion/contraloria/informes-publicaciones/2781606-evaluacion-de-la-credibilidad-presupuestal-del-gasto-publico-en-el-peru>

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<sup>102</sup> Auditors should be mindful that some assessment frameworks only evaluate budget credibility at the aggregate level.



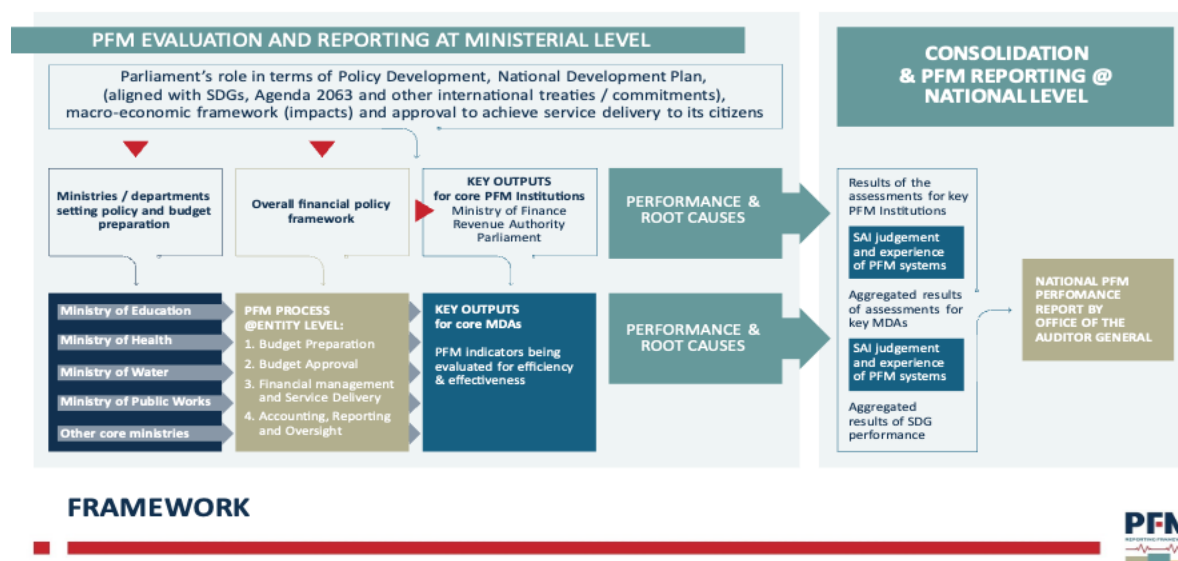
## SAI regional guidelines and reporting frameworks

AFROSAI-E and GIZ have developed the [PFM Reporting Framework](#) enabling auditors to assess the performance of PFM processes along the entire budget cycle.<sup>103</sup> This Excel-based tool covers all stages of the budget cycle starting with macroeconomic policy, fiscal policy, and strategic budgeting; budget preparation; budget approval; financial management and service delivery; and accounting, reporting, and oversight. The tool focuses on the core PFM institutions: the ministry of finance, the revenue authority, and parliament. In addition, the SAI selects line ministries (MDAs) to include, based on their country’s Sustainable Development Goal (SDG) priorities and their budgetary relevance.

verify the readiness of the national PFM system in supporting the SDGs. The tool includes audit procedures focusing on the resilience and disaster preparedness of the PFM system and combines audit procedures from financial, compliance, and performance audits. By recognizing the need to situate audit findings within the wider PFM system and highlighting the interlinkages of root causes for underperformance across audited entities, the PFM Reporting Framework aims to contribute to the drafting of meaningful audit recommendations. Unique methodological features of the tool are the application of root cause analysis (see also Chapter 7, Box 7.1) and the dashboard summary of results. These features result in positive spillover effects into other areas of audit and can be integrated into the annual statutory audit.

The PFM Reporting Framework allows auditors to

Figure 4.2. Overview of the AFROSAI-E PFM Reporting Framework



Source: GIZ/AFROSAI-E.

<sup>103</sup> Available at: <https://pfmreporting-tool.com/resources/#get-the-tool>

Since its inception in 2018, this framework has been applied in 15 countries in Africa, Europe, and Latin America. Several SAIs have moved to conduct the assessment a second time and aim for an annual application. Some SAIs, such as the Office of the Auditor General of Kenya, have integrated the PFM Reporting Framework into their standard audit software. Figure 4.2 summarizes the framework.

## 4.2. Auditing the performance of the PFM System

This section highlights some specific steps and provides examples of how they relate to budget credibility.

### Type of audit

As noted earlier, some SAIs rely on performance audit techniques to audit the performance of the PFM system or some of its processes, while others use other audit methodologies or a combination of various audit techniques. Some SAIs assess the performance of the PFM system for the purpose of forming an audit opinion on the government's financial statements or conduct performance audits that focus on specific aspects of the PFM system. For example, SAI New Zealand noted that "the Auditor General does not assess the performance of the public finance management system itself other than for the purpose of forming an audit opinion on the financial statements of the Government of New Zealand, or in the case of some performance audits where aspects of the PFM system are considered." Other SAIs, such as SAI Indonesia, have systematically conducted various performance audits to assess the performance of several PFM processes and systems in recent years.

### Relevant audit standards

As noted in other chapters of this handbook, to ensure high-quality assessments, SAIs should observe the relevant International Standards for Supreme Audit Institutions (ISSAIs) when conducting compliance, financial, or performance audits of the budget and reporting on the performance of the PFM system and its processes. Chapter 2 presents the international audit standards as they relate to budget credibility.

When auditing the performance of the PFM system, SAIs need to apply audit standards in accordance with the type of audit and objectives that have been set. To make it easier to determine audit criteria, it is recommended that an SAI refer to existing best practices. Each SAI will also have its own standards for performance auditing that should be used in evaluating the performance of the PFM system.

Numerous handbooks are available to assist auditors in conducting each type of audit, for example, the [Financial Audit ISSAI Implementation Handbook](#); the [Performance Audit ISSAI Implementation Handbook](#); and the [Compliance Audit ISSAI Implementation Handbook](#).

### Selecting the area and topic to be audited

When conducting an audit on the performance of the PFM system, it is prudent to have a specific strategy for selecting the key area(s) to be audited, identifying the audit topic, and developing the audit criteria.

## Key steps for selecting an audit topic

- Understand the interests and priorities of the ministry, legislature, government, and other stakeholders such as civil society organizations and/or the public.
- Use selection criteria to ensure audit topics are significant, auditable, and consistent with the SAI's mandate.
- Scan the audit environment by conducting risk, financial, and policy analyses.
- Prioritize audit topics and determine the SAI's highest priorities.

Audit topics related to budget credibility can be derived from two main sources: (1) from general issues identified by scanning the audit environment, including previous audits; government views, budget papers, etc.; agencies' annual reports and evaluations; media and external reports; previous audit fieldwork; analysis of performance indicators; discussion with agencies/entity; and review of legislative and government priorities; and (2) from requests or suggestions from relevant stakeholders, e.g., from

the legislature; government/executives; internal stakeholders; non-governmental organizations; and others.

If the country's PFM system has been assessed using PEFA indicators or another international assessment framework, the SAI can consider the results to identify areas that need improvement and can be the subject of an audit. Feedback from citizens might also be considered in selecting audit topics. (Box 4.3.)

### Box 4.3. Feedback from citizens can also inform the choice of audit topic

In 2013, the **Australia** National Audit Office (ANAO) decided to open all in-progress performance audits to input from members of the public through a web-based platform. Through the ANAO website contact page and social media platforms (Twitter, LinkedIn), members of the public are able to provide comments at any time and on any matter, for example, to raise concerns with an area of administration or to request that consideration be given to a potential audit topic.

Source: <https://intosajournal.org/journal-entry/civil-society-participation-in-audit-the-australian-national-audit-offices-approach-to-citizen-engagement-in-performance-audits/>

In selecting areas to be audited, SAI Indonesia frequently uses a quantitative method called RIAS (risk, impact, auditability, and significance) where each of these four factors are scored, and the area(s) with the highest cumulative scores are proposed as key area(s) for the detailed audit (see Annex 4.1):

- **Risk:** how much risk is management subject to when trying to accomplish the objectives.
- **Impact:** how beneficial is corrective action responding to the audit likely to be.
- **Auditability:** how feasible is the audit considering available audit staff and location.
- **Significance:** how significant is the program/ activity to the organization's goals.

When auditing the performance of the PFM

system, SAI Indonesia refers to previous audits to select audit topics. For example, based on a previous performance audit on budget preparation, the SAI found the planning and budgeting process lacked synchronization between the two separate ministries who handle the process. This finding led to the selection of synchronization of national development planning and budgeting as an audit topic.

## Designing the audit

Designing the audit involves formulating clear and relevant audit objectives, key questions, and identifying audit criteria that will be supported by the documentation of the audit plans and strategy

### Key steps in audit design

- Conduct a pre-study to better understand the audit topic.
- Determine the audit approach.
- Develop the objective(s) to establish the reason for the audit.
- Formulate audit questions to guide the specific areas of the audit.
- Identify suitable audit criteria to measure the audited entity's performance against what is expected.
- Develop the methodology to guide the collection and analysis of information.
- Document the design, such as with a matrix, and develop a project schedule.

## Audit objectives

Formulating the audit objectives is a key step when auditing the performance of the PFM system and is related to the SAI decision regarding the type of audit and audit approach to be followed. In a financial audit the objectives are more general in nature, usually verifying the government’s financial statements and rendering an opinion thereon. In contrast, performance and compliance audits usually have specific objectives and questions. Performance auditing seeks to provide new information, analysis, or insights and, where appropriate, recommendations for improvement according to the principles of economy, efficiency, and effectiveness. As the example of **SAI Zambia** illustrates later in this chapter, an assessment

of the performance of the PFM system can supplement the audit of the financial statements.

**Incorporating budget credibility:** Auditors are encouraged to formulate specific audit objectives and questions that focus on budget credibility as an objective of the PFM system or that relate the performance of the PFM system to budget credibility. As indicated in other chapters, for audits that do not focus exclusively on budget credibility, the audit objective should be flexible enough to allow auditors to relate the potential audit findings with budget credibility in the audit conclusions and recommendations. Some examples of audit objectives to audit the performance of the PFM system or some of its processes are presented in Table 4.1 and Box 4.4.

**Table 4.1. Examples of objectives for an audit of the performance of the PFM system**

SAI/Country	Audit objective	PFM/budget process	Audit objective’s connection to budget credibility
SAI Bosnia and Herzegovina	To assess the extent to which budget planning contributed to increasing the efficiency and effectiveness of budget expenditures.	Budget planning	<ul style="list-style-type: none"> <li>Reliability and transparency of budgets.</li> </ul>
SAI Bosnia and Herzegovina	To assess the effectiveness and efficiency of budget planning and execution.	Budget execution	<ul style="list-style-type: none"> <li>Reliability and transparency of budgets.</li> </ul>
SAI Egypt	To assess whether public funds are used in an economical, effective and efficient way in alignment with the national plan to achieve the Sustainable Development Goals (SDGs).	Budget execution	<ul style="list-style-type: none"> <li>Management of assets and liabilities.</li> <li>Verifying the reasons for under and/or overspending (indicators of budget credibility).</li> </ul>

SAI/Country	Audit objective	PFM/budget process	Audit objective's connection to budget credibility
SAI Latvia	To assess whether the budget planning process was effective.	Budget planning	<ul style="list-style-type: none"> <li>Systematic assessment of fiscal trends as a basis for budget formulation.</li> </ul>
SAI Myanmar	To determine whether the original purpose or objective of the PFM system is achieved, and the budget execution is effective, efficient, and economical.	Budget execution	<ul style="list-style-type: none"> <li>Verifying the reasons for under and/or overspending (indicators of budget credibility).</li> </ul>

#### Box 4.4. Examples of audit objectives to assess the performance of PFM processes

**SAI Indonesia** has conducted several audits on the performance of specific PFM processes. These audits use performance and compliance methods. The following are examples of the audit objectives formulated for these audits.

- i. To assess the effectiveness of the preparation and provision of the state budget to support the implementation of the Government-Wide Work Plan.
- ii. To assess the effectiveness and quality of central government expenditure management in the framework of performance-based budgeting.
- iii. To assess the effectiveness of planning and budgeting activities as tools for accountability, management, and policy of COVID-19-related programs.
- iv. To assess whether the synchronization of planning and budgeting for national development in 2021 was conducted in accordance with laws and regulations, including (a) the process of synchronizing national development planning and budgeting, especially regarding government priority projects and major projects; (b) whether national development planning has been supported by a reliable integrated information system.

## Audit questions and criteria

The *audit question* is a description of the audit objectives that have been previously set. To its auditors, SAI Indonesia recommends arranging audit questions into at least three levels of questions such that sub-questions at the lowest level are answered by performing certain audit procedures. The audit sub-questions at the lowest level will also refer to the specific criteria that will be used and become the basis for gathering audit evidence.

*Criteria* in performance audits are often derived from audit questions. Criteria can be qualitative or quantitative with a focus on “*what should be*” based on laws/regulations/standards; “*what is expected*” according to good principles, scientific

knowledge, best practices, or “*what could be, given better conditions.*” After developing audit questions and audit criteria, the auditor then identifies the audit evidence and the procedures necessary to collect this audit evidence. SAIs can use Focus Group Discussions and benchmarking methods in designing the audit criteria and audit questions. (See Box 4.5.)

All the above information, ranging from audit objectives, audit questions, audit criteria, audit evidence, sources of audit evidence, and audit procedures are contained in an audit design matrix (ADM). This matrix must be able to show a logical relationship between the columns. An example of an ADM form used by SAI Indonesia can be seen in Annex 4.2.

### Box 4.5. Developing audit criteria to assess the effectiveness and quality of expenditure management

In 2018, **SAI Indonesia** conducted a performance audit to assess the effectiveness and quality of the central government’s expenditure management within the framework of performance-based budgeting.

Audit objectives focused on expenditure budget planning; expenditure budget execution; and expenditure budget monitoring and evaluation. The auditors set about developing the audit criteria by first identifying better management practices to improve the management of central government expenditure including (1) alignment of planning and budgeting processes to ensure the achievement of national targets; (2) a clear definition of quality spending by considering effective and efficient spending within fiscal limitations and national priority activities, as well as productive spending; (3) effectiveness of performance-based budgeting in accordance with the follow the money program policy; (4) effectiveness of budget implementation (right amount, right time and on target); and (4) effectiveness of the monitoring and evaluation activities that encourage quality spending.

The criteria were developed using various sources including regulations, relevant best practices, as well as preliminary audit results. The auditors held Focus Group Discussions with PROSPERA (Australia-Indonesia Partnership for Economic Development), SAI Indonesia SDG Auditors, and SAI Indonesia Secretariat. The main audit criteria were agreed upon with the Ministry of National Development Planning and the Ministry of Finance.

Ultimately, the *audit criteria* were formulated as follows:

- Activities and expenditures of ministries/agencies are planned and budgeted in a measurable and appropriate manner.
- The implementation of the expenditure budget is effective; and
- Expenditure monitoring and evaluation activities are integrated and effective.

## Conducting the audit

Auditors are required to conduct their audit work professionally and according to established

standards. An SAI can support its auditors with audit tools and skills/capacity development. In general, audit tools and skills needed for PFM audits are similar to other audits.

## Key steps in conducting the audit

- Understand the importance of collecting sufficient and appropriate evidence.
- Gather information and data by employing the approved methodology.
- Analyze the collected information and data using qualitative and quantitative methods.



During the audit, auditors may utilize audit techniques such as Focus Group Discussions (FGD) and Benchmarking to support their argument in areas that are not clearly stipulated in rules/regulations. Auditors can also hire experts to assist them with specialized skills such as statistical computation and analysis. For example, the Office of the Controller and Auditor General of New Zealand (NZ OAG) commonly uses independent external expertise to provide assurance to parliament and citizens that budget preparation is responding to the risks and challenges that arise in a period of increased public spending (e.g., such as during the national response to the pandemic and the implementation of the government's broader reform agenda).

Tools including guidelines/handbooks and computer software are also essential in the audit process. Audit guidelines/handbooks will guide auditors in designing, planning, executing, and reporting the audit to ensure that the audit process meets the requirements set by the standards.

Auditing the PFM system involves processing enormous amounts of data. Integrating big data analysis as part of the audit process requires sufficient hardware. Possession of high-end laptops/PCs accelerates data processing. For field analysis, auditors can consider using drones to reach remote areas to prove whether the government has built infrastructure (e.g., bridges, roads, irrigations) or buildings as stated in the budget execution/evaluation reports.

For computer software in general, computer-based audit tools such as ACL, SQL, office software, and statistics software, are used in the audit process. In addition, Geographical Information System (GIS) software and GPS would also be useful if the auditors need to assess some aspects in a certain area. For example, using geospatial data and analysis to track the scale of stable light in an area for certain longer periods as a proxy for the scale of economic activities.

*Big data analytics (BDA)* is essential in assessing government-wide data. It can be used to analyze data at the whole-of-government level as part of audits on the performance of the PFM system. For example, through BDA, auditors can analyze government budget behavior and discern the trends of each government account over time, both at the whole-of-government level and ministries/agencies level. BDA has been used to analyze and compare the databases of the planning and budgeting systems to determine whether these processes are synchronized. This enables auditors to recognize anomalies in the budget cycle such as whether budget performance indicators (output/outcome) stated in the budget documents are aligned with the indicators stated in the planning documents. BDA has also been used to identify anomalies in the procurement process.

## Box 4.6. Using big data analytics in auditing PFM performance

**SAI Indonesia** has used big data analytics for analyzing and comparing:

- The planning and budgeting systems.
- The data on social grant recipients in the payment system with the master database of recipients.
- Recipient databases from different programs and ministries to determine eligibility of government social grant programs.
- Government budget behavior over time.

SAIs can help develop auditors' competency in auditing the performance of the PFM system through training on topics including system thinking, root cause analysis (RCA), problem-solving, effective communication, IT literacy, and big data analysis, among others.<sup>104</sup> Seminars and Focus Group Discussions (FGD) can also help develop auditors' capacities. During the audit, auditors can also use FGD to identify and address relevant issues regarding budget credibility, collect additional data and information, and confirm identified issues. If needed, auditors can hire experts to assist them in several aspects during the audit (e.g., on statistical analysis).

## Developing audit findings, conclusions and recommendations, and reporting

Where PFM processes show deficiencies or underperformance, auditors analyze the evidence, develop audit findings, and produce recommendations that can highlight areas that affect budget credibility. SAIs should communicate the audit findings to the auditee to receive comments and further clarification on the findings. The expectation is that the main problems identified in the findings will be solved once the audited entity implements the appropriate audit recommendations.

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<sup>104</sup> System thinking is a holistic approach to analysis that focuses on the way a system's constituent parts interrelate and how systems work over time and within the context of larger systems. Root cause analysis (RCA) is the process of discovering the root causes of problems to identify appropriate solutions. See Box 71.

## Key steps in developing audit findings, formulating recommendations, and reporting

- Identify the audit findings.
- Balance positive and negative findings.
- Draft conclusions and recommendations, if applicable.
- Structure the report to effectively communicate the audit results.
- Draft the report in accordance with SAI guidance.
- Obtain the audit entity's comments on the draft report.
- After receiving SAI management approval, finalize and publish the report.
- Communicate the audit results to the relevant parties.

In auditing the performance of the PFM system as it relates to budget credibility, auditors follow their adopted audit standards and practices for the documentation and analysis of audit findings. Communication is essential for developing audit findings; auditors need to maintain effective

and proper communication with the relevant stakeholders within the SAI and the audited entities. Box 4.7 provides a look at SAI Indonesia's audit findings on expenditure management, a key aspect of PFM.

### Box 4.7. SAI Indonesia: Audit findings on expenditure management using the performance-based budgeting framework

#### Expenditure budget – planning

- *The government did not have an explicit policy to define and set indicators of quality expenditure:* The quality of government spending is important to manage state finances in a way that supports economic growth and ensures fiscal sustainability. However, the Indonesian government did not have specific arrangements to define and measure quality expenditure nor a roadmap for ensuring the quality of spending in order to support the achievement of the targets included in the medium-term national development plan in a sustainable and comprehensive manner.

- *Lack of a mechanism to disaggregate the performance indicators of performance-based budgeting:* The government did not have a technical guide to establish the hierarchy and accuracy of the target indicators according to the logical relationship between them. There were problems of alignment between targets and activities and sub-activities, and the performance targets had not been fully used as the basis for selecting programs/activities. In addition, the development target indicators included in the 2015-2019 Medium-Term National Development Plan were not disaggregated at the level of activity output indicators. Some indicators were unclear, not relevant or could not be measured.
- *Sharing data processes between the planning and the budgeting information systems were less than optimum.*

#### **Expenditure budget – execution**

- Some budgets were not executed in a timely manner. The cash withdrawal plan was not optimally used as a performance indicator in evaluating budget implementation due to accuracy problems. The absorption of state spending accumulated at the end of the year. Some outputs of the execution of the expenditure budget were not as planned.

#### **Expenditure budget – monitoring and evaluation**

- The existence of three monitoring and evaluation information systems for execution and budgeting undermined the consistency of data between the budget ceiling and budget realization. Some national priority targets of 2017 were not reported.

Recommendations to correct the deficiencies and other findings identified during the audit are developed, as needed. Auditors should communicate their recommendations as early as possible and should discuss and obtain the audited entity's comments on the audit findings and recommendations before publishing the report and submitting it to the government and the parliament. Many SAIs (including SAI Indonesia) require the audited entity to prepare an action plan detailing the actions to be undertaken to implement the audit recommendations, as well as the proposed timeline. Chapter 7 elaborates on this practice and the follow-up to audit recommendations.

Conclusions allow auditors to make a concise and persuasive argument that action is needed to address a deficiency. When drafting conclusions, the audit team should critically consider how they relate to the audit findings, evidence, audit criteria, and the audit objective.

### **Following up on audit results**

As indicated in other chapters, audits that examine the performance of the PFM system or some of its processes and activities should observe the reporting requirements established by

the SAI, following international practice. Chapter 7 provides examples and practical information on how SAIs may address budget credibility and improve the performance of the PFM system through well-crafted audit recommendations, effective monitoring and follow-up, and engagement with stakeholders.

### 4.3. Combining assessment tools and auditing to evaluate PFM: Zambia's experience

Some SAIs have reviewed the performance of their PFM system by combining available assessment frameworks with audit methodology. For example, SAI Zambia has combined the PFM Reporting Framework developed by AFROSAI-E with the process of annual financial audits to assess the performance of the main entities of the PFM system. This section presents detailed information and practical steps to using this approach based on the experience of SAI Zambia.

#### Zambia: Approach and methodology

SAI Zambia has used several methodologies and procedures to conduct the assessment in combination with audit techniques. First, to facilitate compliance with the requirements of

INTOSAI-P-12, the SAI used the PFM Reporting Framework tool (discussed earlier in this chapter), an assessment tool with 112 questions.<sup>105</sup> Second, the audits were conducted using the financial audit methodology. The audit findings were analyzed using the "5 Why model" to understand the root causes/deficiencies that led to the audit findings. The findings and key observations were linked to one or more of five institutional capacity areas: (i) policy and legal framework; (ii) organizational structure and human resources; (iii) information systems; (iv) governance and oversight, and (v) communication and stakeholder management.

Third, the performance assessments of the PFM processes and entities were done using the PFM Reporting Framework dashboards. The processes were scored from zero (no process implemented) to a maximum of four (performance functioning ultimately as designed). A performance score below two indicated a risk area. Fourth, interviews were conducted with key personnel and the management of the institutions involved to gather an understanding of the key PFM processes.

Finally, a review of documents helped the auditors obtain sufficient and appropriate audit evidence. A list of the useful documents reviewed is presented in Box 4.8.

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<sup>105</sup> The PFM tool can be accessed from the website <https://pfmreporting-tool.com/resources/#get-the-tool>.

## Box 4.8. Documents reviewed to assess PFM performance in Zambia

- Constitution of Zambia (Amendment), Act No. 2. of 2016.
- Appropriation Act of 2019.
- 2020 Annual Economic Report.
- National Planning and Budgeting Act.
- Public Finance Management Act No 1 of 2018.
- Service Commission Act.
- Voluntary National Review on the Sustainable Development Goals (SDGs).
- Seventh National Development Plan (NDP).
- Medium-term Expenditure Framework and Green Paper.
- Budget Process in Zambia.
- Central Government Accounting Policies.
- Guidance on Risk Management Framework.
- Budget Outturn Report.
- Output Based Budget.
- Budget Speech.
- Public Financial Management Handbook for Members of Parliament and Staff.
- Debt Statistical Bulletin.
- Debt Sustainability Analysis.
- Central Bank of Zambia Annual Report on National Payments Systems in Zambia.

The criteria applied to select entities for auditing included (i) those that received large budgetary allocations in relation to the overall national budget; (ii) those that had institutional capacity to contribute to the achievement of the SDGs as outlined in the country's National Development Plan (NDP).

### **Zambia: Findings, recommendations, and expected benefits in terms of budget credibility**

***Significant findings.*** A combination of using various sources of information and audit methodologies helped the Zambian auditors identify the following:

- The SDGs were incorporated into government policy documents, including the planning documents of the NDP, and responsibilities were distributed among various institutions through cluster advisory groups. The country prepares a five-year NDP which reflects the government agenda (and is aligned to the electoral/political process).
  - Although institutional strategic plans are aligned to the NDP, most of these plans are not regularly updated due to delays in the preparation of the NDP and the high turnover of key personnel.
  - While the Ministry of Finance consults various stakeholders who are required to submit their budget proposals regarding expenditure and tax and non-tax revenues, participation in the consultation process by some stakeholders was limited.
  - Most of the budgeting documents, such as strategic plans, were not costed. Ultimately, the budgets prepared by the institutions were usually cut and the final allocations in the approved budgets by the legislature were less than requested, largely due to the budget ceilings set by the Ministry of Finance.
  - The SAI found weaknesses in several areas related to budget execution including procurement, payroll management, internal controls and audit, cash management, and insufficient monitoring of SDG implementation and service delivery.
  - Other significant findings included the lack of alignment between the debt management policy and the medium-term fiscal strategy; weak mechanisms for tracking and accounting for resources disbursed to the institutions (due to the lack of integration of the Financial Management Information Systems); and the inaccuracy of revenue, grants, and expenditure projections, which were below the actual outturns.
- Recommendations.** To address these findings, the SAI recommended the following actions:
- Implement stakeholder awareness programs on the importance of participating in the budget process to ensure that public concerns are addressed during the formulation of the budget.
  - Ensure various core PFM institutions update their strategic plans in line with the current NDP in a timely manner.
  - Ensure the Revenue Authority makes realistic revenue projections that reflect the tax base and takes steps to enhance taxpayer awareness of the importance of paying their tax obligations.
  - Establish a system to manage the expansion of debt by the Executive such that the approval of any new debt must be approved by the legislature.
  - The Ministry of Finance's debt management system should be interlinked with the Central Bank to ensure debt settlement is supported by available resources.
  - During budget approval, the Ministry of Finance should ensure that the budget ceilings set for ministries, departments, and other spending agencies (MDAs) are sufficient for them to carry out their mandates and to accomplish the objectives included in the Strategic Plan and NDP.
  - Budget documents should be costed with proper/realistic estimates to enable adequate

funding that allows institutions to fulfill their obligations and mandates under the NDP.

- Financial Management Information Systems (FMIS) should be integrated and rolled out from head offices to the lowest-level spending units to ensure timely preparation of financial and other reports, sharing of information, and accountability.
- The payroll system should be robust and integrated. Information should match the actual workforce and be regularly reviewed.
- Enhance public procurement regulations.
- The Audit Committees should adequately carry out their oversight functions on the financial reporting processes, reviewing the institutions' internal control environments.
- Improve the use of Commitment Controls to effectively establish a system of expenditure control and prevent entities from incurring unauthorized commitments.
- The ministries should put in place adequate monitoring mechanisms, including staff training, to identify shortcomings in service delivery and take corrective actions as needed.

**Benefits to budget credibility.** The implementation of these recommendations would strengthen PFM and enhance budget credibility by increasing accountability over the utilization of public resources and the likelihood that funds are used, as intended, for the benefit of the designated beneficiaries. Improved access to information

and stakeholder engagement programs would contribute to a more inclusive budgetary process and the informed participation of citizens in the budget process. The improved flow and sharing of information between different financial systems, internal controls, and oversight institutions would also help in preventing fraud.

Budget documents that are costed with proper/realistic estimates, based on up-to-date strategic plans, would enable MDAs to negotiate more appropriate budget ceilings (i.e., based on the cost of meeting their sector objectives and relative contribution to GDP) during the budget hearings and negotiations of the budgeting process. This could transform the budget hearing/negotiation process away from being a purely formal exercise. Rather, MDAs could present realistic budgets, reflecting their actual resource needs to meet their respective sector objectives outlined in the NDP. The Ministry of Finance and the Parliament should be aware of this information and provide appropriate feedback to the MDAs to inform their future budgeting.

Increased awareness and adherence by taxpayers on the need to pay their tax obligations would result in both the expansion of the tax base and more revenue to support the Ministry of Finance in its budget preparation process.

Linking the debt management systems of the Ministry of Finance and the Central Bank would make it easier to establish a clear and comprehensive country debt position, and enable the Ministry of Finance to make informed and coordinated decisions on debt contracting and management.



The rolling out of the Integrated Financial Management Information System (IFMIS) to all government institutions would facilitate the dissemination of financial information to enable efficient production of financial statements and support the monitoring of budget execution. It would also help the timely and comprehensive capture of financial transactions by units under MDAs that are not connected to the IFMIS for reporting purposes. Making the IFMIS more flexible and relaxing certain procedures to facilitate quick disbursement in case of emergencies, while adequately accounting for those resources, would increase disaster preparedness and the timely response to emergencies at both national and institutional levels.

#### 4.4. Additional SAIs share significant audit findings, recommendations, and impacts

In the 2022 UNDESA/IBP SAI survey, several SAIs highlighted examples of significant impacts of their audit work on the performance of the PFM system. This section presents some of them, organized by PFM process.

### Policy design – Findings, recommendations, and audit impacts

A common finding at the policy design stage is that the models and assumptions used as the basis for policy-making are not up-to-date.

**SAI Netherlands** recommended the government improve legal provisions and control, and that the parliament actively verify draft budget estimates. As a result, the parliament has successfully pressed the government to adopt the same accountability regime that applies to the regular budget laws to several newly installed funds that contribute to major fiscal expansion. Similar but more technical issues have also been found by SAI Latvia and SAI Indonesia.

In an audit on the effectiveness of budget planning, **SAI Latvia** revealed that no assessment was conducted on the level of debt that Latvia could afford. Also, there was no economically sound assessment of the optimal level of debt that Latvia could incur in the long-term considering pessimistic demographic growth estimates. Identified impacts of this audit included the setting of a clearer and more equal procedure for reviewing the base expenditure of institutions; the term “budget investment” was more clearly defined and the budget remarks provided more complete information on the planned public investment projects by sector; and the budget explanations disclosed information on the impact of the most significant tax reliefs (rebates) on the state budget for the ensuing years.

On the revenue side, **SAI Indonesia** found that the government had not fully considered all possible impacts from policies in the taxation

sector when preparing the tax revenue budget. In addition, in the non-taxation sector, the revenue target from the sale of oil and gas was not based on the lifting targets agreed upon by the authorities and the contractors. The SAI recommended the finance minister establish a mechanism for preparing revenue targets that considers the impact of each tax policy or tax policy plan and that the government determine the mechanism for calculating the oil and gas non-tax revenue budget in the annual budget in line with the reliable oil and gas lifting target. Based on these recommendations, the government has considered tax policies while budgeting for tax revenue.

**SAI Portugal** discovered that vast reforms of public financial management, with very ambitious schedules, were undertaken with insufficient strategy and coordination, a lack of human and material resources, and insufficient skills and training in public administration. The audit recommended the government define the leadership and coordination of the reforms and update the implementation strategy by setting priorities and phased processes. As a result of the audit, leadership and coordination were enhanced and professional training was planned for the implementation of the new accrual accounting system. Half of the public entities completed their transition to the new accrual accounting system and reported their 2020 accounts under that

regime. The public financial management reforms were included in the Portuguese Recovery and Resilience Plan, ensuring the allocation of required financial support in the following years.

## Budget preparation: Findings, recommendations, and audit impacts

A timely and transparent budget preparation process can be an indicator of a sound and well-performing PFM system.

**SAI Bosnia & Herzegovina** found the budget preparation process was not timely nor sufficiently transparent and clear responsibilities for defining goals, programs, and related budget funds were not always established. Up-to-date and complete information on the budget was not always available to all interested parties. The SAI recommended the government ensure the timely completion of budget preparation; consider how to establish a politically-driven budget review process; and increase the use of performance information in the budget preparation process – with an ultimate goal of making the latter the primary criterion for budget decision-making.

### Box 4.9. SAI Indonesia – Budget preparation: Findings, recommendations and impacts of PFM audits

#### Findings:

- The setting of indicative ceilings had not considered the performance of ministries in previous years.
- The government had no specific and explicit policy to set definitions or indicators of quality expenditure; and
- Management of performance-based budgeting had no performance indicator cascading mechanism.

#### Recommendations:

- To the government: improve the mechanism preparing the indicative ceilings and consider the performance of ministries in previous years when allocating the budgets.
- To the finance minister: determine the definition and indicators of quality expenditure.
- To the national development planning minister: establish guidelines on performance indicator cascading mechanism.

#### Impacts:

- The government has developed a framework to define and set indicators of quality spending.
- The budget execution performance indicator as well as performance evaluation have improved.

### Budget execution: Findings, recommendations, and audit impacts

The issues raised by the SAIs at the execution stage usually revolve around the inaccuracy of receipts and expenditures compared to the approved budget.

**SAI Myanmar** observed that revenues were not

fully collected and expenses were not effectively utilized as per the budget proposal in most of the line ministries and agencies. SAI Myanmar recommended that these institutions collect the relevant revenues fully and utilize the expenditures effectively and efficiently as per the budget proposal.

Issues with unutilized budget provisions resulting from non-implementation or the delay in the implementation of significant projects were found

by **SAI Mauritius**. The audit advised management to put in place an adequate mechanism for the prompt implementation of projects.

**SAI Japan** noted a large amount of carry-over and unused budget. The audit recommended that ministries and agencies analyze the causes to accelerate the implementation of measures related to COVID-19; make an effort to execute the projects in a timely and appropriate manner; and provide the public with information on the budget implementation status of the projects. Based on these recommendations, the government provided more information on the status of budget execution regarding COVID-19 measures and initiatives ahead of the Tokyo Olympic and Paralympic Games.

**SAI Cuba** discovered that the automated systems for budget control at all budget levels were

not interconnected with other systems of the state financial administration, and there were weaknesses in the implementation of internal control systems in budget units. To solve these issues, SAI Cuba recommended prioritizing actions to hasten the move to the computerization strategy of the state financial administration systems to enable real-time monitoring of budget execution, with the use of CAATs<sup>106</sup> incorporating BIG-DATA and data analytics. These recommendations would facilitate improvements in the treasury system; the implementation of the government accounting system and approval of measures to strengthen the general accounting of and financial discipline of entities; and strengthen tax control and the implementation of measures to combat tax evasion.

### Box 4.10. SAI Philippines – Budget execution: Findings, recommendations, and impacts of PFM audits

#### Findings:

- **Underspending:** Fund releases under the Department of Budget and Management (DBM)-administered Financial Assistance (FA) to Local Government Units (LGUs) and Assistance to Cities (AC) were only 46.3 percent and 5.7 percent, respectively, of the total appropriations for Fiscal Year (FY) 2018; thus, resulting in missed opportunities to provide the services intended for the public under the said funds.
- **Delays** of 2 to 132 working days were noted in the processing of Special Allotment Release Order (SAROs) under the Local Government Support Fund (LGSF) for FY 2018, thereby hindering the timely implementation of priority projects and programs financed by the fund.

<sup>106</sup> CAATs are computer-assisted audit tools.

### Recommendations:

- *For FAs to LGUs:* assign the DBM Regional Offices the tasks of providing technical assistance to LGUs, conducting an initial review of LGUs' requests and of the completeness of their documentary requirements, and forwarding the compliant requests to the Central Officer (CO) for evaluation.
- *For ACs:* consider providing technical assistance to those LGUs that do not have the financial capacity to hire consultants to conceptualize the design of complex projects. Also, increase the number of seminars and workshops to be conducted to inform the city officials concerned of the documentary requirements to be complied with.
- *For management:* require the Local Government and Regional Coordination Bureau (LGRCB) to ensure that all requests/endorsements from LGUs/Department of Interior and Local Government are processed and approved within 15 working days as committed in their Office Performance Commitment and Review (OPCR).

### Impacts:

- The DBM has improved its management of LGSF in CY 2019 and the years thereafter. On the other hand, the Bureau of the Treasury (BTr) was able to properly monitor their budget vis-à-vis actual expenditures and improve reporting in the Statement of Budget and Actual Amounts, through compliance with the audit recommendations.
- The government has developed a framework on definitions and indicators of quality spending.
- The government has improved the budget execution performance indicator as well as performance evaluation.

## Accounting and reporting: Findings, recommendations, and audit impacts

Information and reporting mechanisms are critical to assessing the performance of the PFM system. Accounting and reporting mechanisms ensure some standardization of what items need to be reported on, to whom, and how. However, SAIs have identified some critical issues in this area.

**SAI Azerbaijan** observed incorrect reporting of individual components of public finance, non-compliance of accounting and reporting

with legal provisions and best practices, and lack of knowledge on budget documentation. The SAI advised the government to consider the provisions of legal acts, introduce new fiscal institutions, widen the application of best practices, and prepare a Budget Code. This guidance led to the implementation of new fiscal institutions, improvements in the MTEF and budget regulations, and improvement of budget documentation.

**SAI Bosnia-Herzegovina** noticed that the availability of information on the achievement of program goals was limited. Reports and information on the effectiveness of programs

and institutions were rare, and often unavailable to the public and to those responsible for the preparation and adoption of the budget. For most of the program budget objectives, information on their implementation was not included in the existing reports. The SAI recommended the government ensure all interested parties have immediate access to all available information on the implementation of defined program goals of institutions and that the government improve the information system and establish financial reporting according to the program classification.

**SAI Egypt** pointed out that with the issuance of the Unified Public Finance Law no. (6) for the year 2022, it was necessary to make some accounting amendments that the audited entity was informed about. This resulted in the proper utilization of

public funds; promoted the performance of the PFM system to achieve the SDGs; and facilitated auditing the extent of the commitment to implementing the State Financial Policy.

**SAI Netherlands** found that the government is not systematically registering its assets and that the reporting of government performance is fragmented and lacks a common architecture. Therefore, it recommended adopting government-wide accrual standards to improve asset registration and management, and to select a limited number of key national indicators to be monitored independently. As a result of these recommendations, the government announced it would integrate a set of independently monitored key national indicators in its budget process.

### **Box 4.11. SAI Yemen – Accounting & reporting: Findings, recommendations and impacts of PFM audits**

#### **Findings**

- Final accounts data did not include the results of actual implementation of the budget of the economic institution.
- Failure of most enterprises/units of the economic sector to complete their financial statements on time, resulting in a discrepancy between the financial statements issued by the respective economic units/enterprises and the final account statements issued by the Ministry of Finance.
- The final calculations of the budgets of the units of the economic sector did not realistically reflect the actual withdrawal of external financing in those units, where the resources achieved from external loans according to the final accounts data amounted to about one billion Yemeni riyals, while the actual withdrawal from the reports of loans and assistance issued by the Ministries of Finance and of Planning and International Cooperation was over eight times that amount.

### **Recommendations**

- Require the economic units to complete their financial statements on time as set by the Financial Law and its relevant regulations/bylaws.
- The Ministry of Finance must not accept any final account for any economic unit unless its financial data are obtained from the approved financial statements of that entity and for the same period.
- The Ministry of Finance should require the sector specializing in loans and external assistance to coordinate with the Ministry of Planning and International Cooperation to reconcile financial information of loan centers with the economic units benefiting from this external financing, and monitor the estimates of allocations in annual budgets and the actual use of them in the final accounts in order to avoid the discrepancies and disparities that appear annually.

### **Impacts**

- Most economic units complete their accounts and submit them to the agency and the Ministry of Finance on the legally set dates.
- Completion of the financial statements of most economic units on time.
- Coordination between the foreign relations sector of the Ministry of Finance and the respective sectors in the Ministry of Planning and International Cooperation to determine the actual withdrawal of loans and foreign assistance, which leads to showing f all the amounts withdrawn in the final accounts of the economic units

## Budget evaluation: Findings, recommendations, and audit impacts

Adequate management and evaluation tools are needed to conduct an effective budget evaluation in the last part of the PFM cycle, before starting the next.

**SAI Bosnia-Herzegovina** reported that independent monitoring has not been organized for most of the program objectives of their institutions, and evaluation reports were rare. Ministries and Council of Ministers (CoM) bodies did not have oversight in place for all areas under their responsibility. Available assessment reports in some areas are not tailored to the needs of those responsible for preparing the budgets. The limited availability of information on the realization of program budget objectives limits the potential impact of results on future budget allocations. Without information on the program objectives and their implementation, it is difficult to prepare and adopt a budget that encourages the efficiency and effectiveness of budget expenditures. SAI Bosnia Herzegovina recommended the Parliament and the CoM consider how to develop a politically-driven budget review process.

**SAI Philippines** observed that the Department of Budget and Management (DBM) did not have a complete monitoring and evaluation system over the release of funds under the Local Government Support Fund (LGSF), particularly on the financial assistance (FA) to local government units (LGUs) and assisted city (AC) components. Therefore,

no overall assessment was made to determine whether the primary objectives of the programs were achieved. SAI Philippines recommended the Director of the Local Government and Regional Coordination Bureau (LGRCB) establish a complete monitoring and evaluation system by (a) preparing a consolidated report on the status of project implementation and fund utilization from FYs 2016 to 2018 and for the years thereafter pending the development of the Unified Reporting System (URS); (b) drafting and issuance of policy guidance for monitoring and evaluation of projects; and (c) carrying out of an evaluation of the completed projects at the regional level to validate the status provided in the reports submitted by LGUs. Moreover, SAI Philippines recommended imposing appropriate sanctions to LGUs that do not comply with the reporting requirements and with prescribed project timelines, as reflected in their Program of Works.<sup>107</sup>

## 4.5. Challenges in auditing the performance of the PFM system

SAIs experience some common challenges, both internal and external, when auditing the performance of the PFM system.

### Internal SAI challenges

#### 1. Lack of expertise on PFM issues.

Auditing the performance of the PFM system is

<sup>107</sup> This case is related to the one presented in Box 4.10 on the Local Government Support Fund, but here the focus is directly on the monitoring and evaluation system of the Fund. In Table 6.2 (under Timing of Spending), a related issue is also presented as an example of a risk factor.



different from auditing the financial statements, which is the work that auditors are most familiar with. One challenge is to map the key areas and processes to be examined and select/develop suitable criteria. Inadequate human resources and insufficient skills (e.g., ability to mine big data) may limit the audit scope.

SAIs can address these shortcomings by facilitating knowledge sharing, providing comprehensive training programs, and organizing workshops for auditors. In addition, SAIs could design the audits incrementally. For example, to audit how the government manages debt financing, auditors need to understand several aspects starting from budget formulation, budget execution, and cash management. Therefore, the audit could be designed incrementally, starting with auditing budget formulation in year  $x$ , then budget execution in year  $x+1$  and  $x+2$ , cash management in year  $x+3$ , and debt management in year  $x+4$ .

## **2. Limited resources.**

SAIs may have allocated most of their resources to mandatory and/or priority audits. In addition, SAIs may not have sufficient support for acquiring computer hardware and software or for the IT infrastructure needed to work with the large databases where most of the data used for the PFM system are stored.

## **3. Siloed organizational structure and working methods.**

Conducting a performance audit of the PFM System requires coordination of several units within the SAI since the PFM system involves many government agencies across all levels. Different SAI units are responsible for auditing the central government, local government agencies,

and state-owned and local government-owned enterprises. Therefore, it is crucial to coordinate all audit activities to produce comprehensive audit reports about the PFM system. If the audit agencies only focus on their respective duties and functions, it will be difficult to get a comprehensive picture of the PFM system. Hence, SAIs need to adopt a “whole-of-SAI” approach and break the “silos” within the organization.

SAI Indonesia addressed this challenge by conducting an audit with a National Thematic Audit Approach. This approach involved several units in SAI Indonesia to conduct audits on specific themes related to the SDGs. For example, five different audit units worked together to produce a comprehensive audit report on the quality of education that engaged several government agencies (e.g., Ministry of Education, Local Government Education Agencies, National Statistics Agency, Ministry of Social Affairs, National Planning Agency, and Ministry of Financial Affairs).

During the pandemic, in an effort to break the silos and deliver coordinated sound recommendations, SAI Indonesia initiated Audit Universe, an audit strategy involving all the audit units in the organization to ensure accountability and transparency of government efforts in combating Covid-19 across all government bodies vertically and horizontally.

## **4. Lack of customized assessment frameworks.**

Not all SAI regional organizations or INTOSAI groups have issued customized PFM assessment frameworks that may help SAIs to conduct their assessments. Therefore, SAIs may need to design and develop their own approaches, drawing on existing frameworks.

## External process challenges

### **1. Multiple (potentially conflicting) objectives of the PFM system** (e.g., expansive budgeting policy versus fiscal rules) **can make it difficult for auditors to determine audit objectives.**

As to audit objectives, SAIs need to find, assess, select, and determine the most important issues or problems in their national PFM systems.

### **2. Inadequate internal controls.**

The government may not have implemented adequate internal controls over financial reporting and management activities. In these cases, the integrity, reliability, and even the quantity of data and documents processed by the government will be limited and the SAI may need to conduct extra work in certain areas. Auditors can assess this problem as part of their auditability analysis to determine whether the audit can be carried out or not. Auditors can also consider conducting an audit to improve internal control.

### **3. Complexity of the system and audited entities plus a lack of synergies and collaboration among key stakeholders of the PFM system.**

PFM is complex. First, multiple budget cycles usually take place simultaneously. The external audit and accountability process for a previous year's spending takes place while resource management processes are active for the current year. At the same time, the strategic budgeting process has already begun for the following year. Secondly, each process involves a wide range of government bodies, entities, and agencies, each with their own characteristics, priorities, and interests. Spending entities want to see

their budget allocation increase, for instance, but finance ministries are tasked with keeping overall spending under control. These tensions make the PFM process a competitive and contentious one. International organizations contribute to this mix in many countries, advising governments on reform initiatives and sometimes financing a substantial share of public spending.

For example, in Indonesia, the planning and budgeting functions are carried out by two different ministries (the Ministry of National Development Planning and the Ministry of Finance). This separation of duties discloses several issues of synergy and synchronization between the planning and budgeting process. Some planned programs may not have a budget allocation, some budgeted programs are not included in the planning documents, and different information systems are used for each process which ushers in redundancy and challenges for monitoring and evaluation.

In addition, each government agency may have its own data collected and processed for its programs. However, the data of one government agency may lack integrity and interoperability with the data of other government agencies. The lack of data interoperability among government agencies would be the main drawback of implementing a social support program since different data are used for different programs resulting in inclusion and exclusion errors. Therefore, an SAI needs to collect and analyze data from many different government agencies.

### **4. Limited access to information.**

An SAI may face challenges regarding data availability, especially for confidential documents related to budget approval by parliament and approved macroeconomic assumptions. Auditors

may have to go through several steps (that take up audit time) to access the data.

SAIs need to evaluate the necessity of confidential information for the audit conclusion and to ensure enough time to obtain such information if it is deemed significant for the audit.

## 4.6. Recommendations for SAIs

- 1. Understand the SAI mandate** – Auditors should familiarize themselves with their SAI mandate so as to identify entry points for auditing the performance of the PFM system.
- 2. Use and develop big data analytics to support audits of the PFM system** – SAIs need to enhance their IT hardware and software capacity as well as the auditor's IT skills to collect and analyze data from various government sources.
- 3. Cooperate with other SAIs on capacity development** – SAIs may jointly improve their organizational capacity and professional competence in some areas, such as on fiscal and macroeconomic policy, budget credibility measurement using the Public Expenditure and Financial Accountability (PEFA) framework, the IMF Fiscal Transparency Code, Fiscal Transparency Evaluation, economic and financial analytical data, and forecasting for future trends such as computational assumption analysis on economic growth, inflation, and long-term fiscal sustainability.
- 4. Select the area of PFM in greatest need of an audit** – Identify areas that most need improvement and for which the audit could have an impact. If several areas are identified, the SAI may consider conducting a series of audits.
- 5. Ensure the effectiveness of follow-up to audit recommendations** – Follow-up on the audit recommendations by the government needs to be monitored. SAIs should have an effective follow-up mechanism. Further discussion on this issue is presented in Chapter 7.

## Chapter 5: Auditing the state budget on a regular basis

Many Supreme Audit Institutions (SAIs) audit their national government's year-end accounts by conducting a retrospective analysis of budget execution at the end of the fiscal year. Audits of the year-end accounts, as well as other audits of the budget carried out recurrently during the fiscal year, are critical to fostering budget credibility. They help reinforce the expectation that public-sector entities and public servants will perform their functions effectively, efficiently, ethically, and in accordance with applicable laws and regulations. Although the legal mandate of an SAI and the particular country context influence this audit work, there is an increasing global convergence on combining performance, compliance, and financial audit tools when conducting these audits. This chapter examines regular audits on the execution of the state budget or year-end accounts, highlights their value, and provides guidance on how to conduct these audits and link them with budget credibility.

### 5.1. Understanding the approach

Auditing the state of public finances has been a key role of SAIs since the establishment of structured oversight entities in Western Europe. This is reflected in the preamble to the

Lima Declaration (1977), which highlights that "the orderly and efficient use of public funds constitutes one of the essential prerequisites for the proper handling of public finances and the effectiveness of the decisions of the responsible authorities."<sup>108</sup>

The transactions associated with maintaining the financial operations of the modern nation-state – namely, those pertaining to the collection of government revenue and the disbursement of public funds – take place on a regular basis. Therefore, it is to be expected that auditors in charge of verifying the regularity of these transactions also conduct audits of the state budget on a regular or recurring basis.

Accordingly, recurring audits of the state budget, including audits of the year-end accounts, refer to audit work that is conducted by SAIs on a regular basis – whether it is every year, or over different time intervals (e.g., every six or three months). Recurring audits of the budget typically have a wide scope and take a consolidated, whole-of-government approach. This does not exclude the possibility that recurring audits encounter and address audit findings and recommendations at the program or entity level. (Box 5.1.)

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<sup>108</sup> INTOSAI P-1, The Lima Declaration <https://www.issai.org/pronouncements/intosai-p-1-the-lima-declaration/>

## Box 5.1. Defining characteristics of regular audits of the state budget or year-end accounts

**Conducted on a recurrent basis:** These audits are carried out every year, every six months, three months, etc., depending on the SAI mandate and country context. Yearly audits (which encompass the entire fiscal year) have different characteristics from mid-year audits.

**Varied audit methodologies and reporting formats:** These audits may be reported and published in different forms, including the audit of the government's accounts; audit of the year-end financial statements; audit of the expenditures and revenues of the state; and audit of budget execution, among others. These audits may draw on prior audits conducted during the targeted time frame. They may prioritize financial, compliance, or performance auditing, or a combination thereof.

**Comprehensive:** These audits have a wide scope and take a comprehensive approach. By contrast, other SAI reports – e.g., the SAI's yearly institutional report; the collection of SAI audit results; the yearly audit of an individual government department/program – do not constitute a recurring assessment of the budget because they do not provide a comprehensive analysis.

## Benefits of recurring audits of the budget

Sound public financial management is positively correlated with budget credibility.<sup>109</sup> An evaluation based on the Public Expenditure and Financial Accountability (PEFA) methodology<sup>110</sup> can be a reliable indicator for measuring and monitoring the intertemporal evolution of budget credibility (See Chapter 1). A sound PFM system makes it possible for a country to advance on fiscal discipline at the aggregate level, strategic allocation of resources, and the effective provision of services.

Recurring audits of the budget, through year-end reports and other audits conducted during the fiscal year, provide an important diagnosis of constraints in the PFM system. The audit findings relate specifically to the procedures of budget apportionment, as well as to broader issues in the system. Besides contributing directly to budget credibility through their findings and recommendations, SAIs can also use the findings from recurring audits to plan additional work to further assess and address budget credibility. For example, in the year-end audit of consolidated statements for 2017, the Auditor General of Canada found the federal payment management system had significant inconsistencies. This

<sup>109</sup> Jens Kromann Kristensen, Martin Bowen, Cathal Long, Shakira Mustapha, and Urška Zrinski, eds., 2019. PEFA, Public Financial Management, and Good Governance, Washington DC, World Bank. Available on <https://www.pefa.org/sites/pefa/files/resources/downloads/9781464814662.pdf>

<sup>110</sup> PEFA Secretariat, 2019. Framework for Assessing Public Financial Management. Available on [https://www.pefa.org/sites/pefa/files/resources/downloads/PEFA%202016\\_latest%20version\\_with%20links%20%282%29.pdf](https://www.pefa.org/sites/pefa/files/resources/downloads/PEFA%202016_latest%20version_with%20links%20%282%29.pdf)

resulted in a specific follow-up audit in 2020, which reported that subsequent work was necessary to fully implement the Auditor General's recommendations.<sup>111</sup>

A key advantage of recurring audits of the budget is that they allow stakeholders (including the general public, the legislative branch, public servants, the media, local and foreign investors,

scholars, entrepreneurs, the international donor community, and multilateral organizations) to gain a clear understanding of the evolution of public finances over time. Moreover, recurring audits enable a timely response to evolving trends in the government's accounts, thereby generating incentives for responsible budget management. (Box 5.2.)

## Box 5.2. Benefits of recurring audits of the budget

These audits contribute to budget credibility by:

- Providing a coherent, comprehensive analysis of the nation's budget.
- Tracking and identifying inconsistencies across the budget cycle in a timely manner.
- Providing useful information to legislators, citizens, and other stakeholders.
- Enhancing spontaneous adherence to fiscal rules and regulations.
- Demonstrating the institutional value of the SAI and its professional work to verify and make recommendations regarding the nation's finances.

Beyond promoting transparency and raising awareness about budget deviations and other credibility risks found during audit work, an SAI may directly contribute to improving budget credibility and the country's public finance framework by issuing and following up on audit recommendations from these audits.<sup>112</sup> These audit recommendations are normally addressed to the executive branch. For this reason, conducting recurring audits of the budget generally enhances

the status and value of an SAI as the guardian of national financial stability and sound PFM.

## Frequency of recurring audits of the budget

Most SAIs carry out at least a yearly audit, based primarily on but not limited to the government's year-end accounts. In addition, governments

<sup>111</sup> Office of the Auditor General of Canada, 2020. Follow-up Audit on the Implementation of the Office of the Auditor General of Canada Recommendations on Payroll Management. Available on <https://www.publicsafety.gc.ca/cnt/rsrcs/pblctns/2020-foag-pm/index-en.aspx>

<sup>112</sup> See Chapter 7 on the follow-up to audit recommendations.

increasingly publish mid-year reports, to furnish up-to-date information on the budget's execution during the fiscal year. Both the year-end and mid-year reports should be published by governments, in line with the Best Practices for Budget Transparency issues by the OECD.<sup>113</sup>

The frequency of the mid-year reports varies, and multiple budget transparency reports may be filed within a fiscal year. Mid-year budget transparency reports may also be subject to the SAI's oversight. The frequency of mid-year recurring audits depends on the frequency of the government's partial budget reports. In mid-year audits, SAIs can check for the consistency of effective revenue collection and spending, compared with the projections set in the budget. For instance, the SAI may point out that excessive spending early in the year will make it unlikely for fiscal targets to be met. During budget execution, the SAI may also detect failures to comply with the law within

a time frame that enables course corrections and makes SAI recommendations more effective.

In year-end recurring audits, on the other hand, SAIs benefit from a broader outlook of the year's budget execution practices. SAIs may emit an opinion on the government's annual financial statements. Government auditors may also carry out compliance work, often in combination with financial analysis, verifying whether budget execution followed pertinent fiscal rules and regulations. For example, in the year-end report of the fiscal year 2019, the SAI of Sierra Leone found that senior government officials had incurred public spending "without policy or legal justification."<sup>114</sup> Recurring audits of the budget provide an important venue to raise awareness of detected failures in government compliance with laws and regulations, supporting the implementation of corrective measures.

### Box 5.3. Periodicity of SAIs' recurring audits of the budget

SAIs conduct recurring audits of the budget at various times of the fiscal year and with different periodicity (every three months; every four months; every six months, depending on circumstances). Some examples are provided below:

- Only when auditing the year-end accounts: Algeria, Australia, Bahrain, Bulgaria, Cuba, Cyprus, Eritrea, France, Ireland, Kuwait, Latvia, Madagascar, Mauritius, Myanmar, the Netherlands, Portugal, Puerto Rico, Romania, South Sudan, Viet Nam.
- When auditing the year-end accounts and in other audits during the fiscal year (recurring mid-year audits): Argentina, Bosnia and Herzegovina, Dominican Republic, Egypt, Greece, Guatemala, Indonesia, the Philippines, South Africa, United States, Yemen.
- Only mid-year audits: Croatia, Paraguay.

Source: Survey of SAIs conducted in 2022 in preparation for this handbook (N=38 respondents).

<sup>113</sup> OECD, 2002. *Best Practices for Budget Transparency*, p. 10.

<sup>114</sup> See: <https://www.audit-service.gov.sl/wp-content/uploads/2020/12/Annual-Report-on-the-Account-of-Sierra-Leone-2019.pdf>



## 5.2. Implications of the SAI mandate for auditing the state budget or year-end accounts

External audit institutions are typically classified in three models based on their mandates: judicial or Napoleonic model (Court of Accounts), Westminster or parliamentary model (Auditor-General), and Board of Audit or collegiate model. The legal mandate and institutional model of an SAI is a critical consideration when defining the cycle of recurring audits of the budget.

The institutional model of an SAI has implications for whether and how to conduct recurring audits of the budget. SAIs that adhere to the Court of Accounts model often specialize in compliance auditing, focusing on the detection of deviations between administrative acts and the provisions that govern such acts in laws and regulations. Given their status as administrative or jurisdictional decision-making bodies, Courts of Accounts may issue rulings that impose penalties, such as pecuniary fines, to government personnel. SAIs of the Auditor-General and Board of Audit models traditionally conduct financial audits of the state's balances and may also carry out performance (also known as value for money) audits to provide the parliament with relevant information for decision-making.

An audit of the consolidated year-end and/or mid-year accounts by a Court of Accounts may form the basis for an SAI ruling or could inform the ruling by another entity. Such a ruling may

attribute responsibilities and result in penalties to high-level personnel, including government ministers. Therefore, given the complexity of the budget process, which is beyond any single entity's domain, SAIs with jurisdictional powers may take additional precautions. These precautions include conducting a careful analysis of cause-effect relationships, considering concurring actors, understanding the legal framework, and scrutinizing all relevant actions in the time frame related to the potential infraction. Another important precaution is to provide all actors involved the opportunity to present a defense, which should be considered in the SAI's ruling.

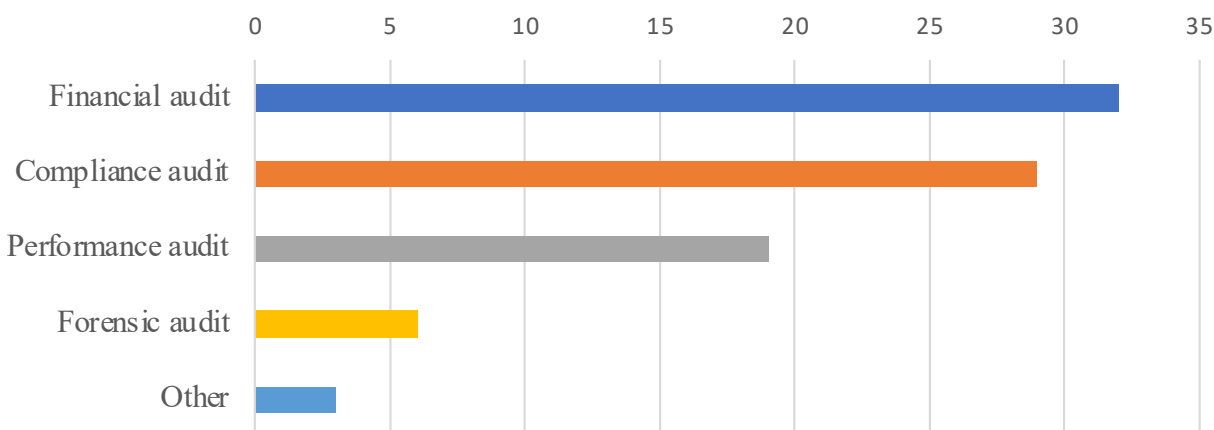
In recent years, there has been a convergence in the nature of the audit work undertaken by SAIs pertaining to different institutional models.<sup>115</sup> SAIs that follow the Courts of Accounts model are directing more efforts to financial and value for money auditing, while Auditor-General SAIs increasingly conduct compliance work. Evident in the survey supporting this study, these trends are also reflected in the enhanced quality and comprehensiveness of budget oversight from the recurring audits of the budget. Out of 35 respondents, 89 percent of SAIs reported they conduct financial audits of the consolidated year-end accounts, 80 percent compliance audits, and 52 percent performance audits. Fifteen SAIs (43 percent) undertake all three types of audit work.

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<sup>115</sup> World Bank, 2020. *Enhancing Government Effectiveness and Transparency: The Fight Against Corruption*, p. 306. Available at [https://documents.worldbank.org/en/publication/documents-reports/documentdetail/235541600116631094/enhancing-government-effectiveness-and-transparency-the-fight-against-corruption?cid=gov\\_tt\\_gov\\_en\\_ext](https://documents.worldbank.org/en/publication/documents-reports/documentdetail/235541600116631094/enhancing-government-effectiveness-and-transparency-the-fight-against-corruption?cid=gov_tt_gov_en_ext)



**Figure 5.1. Type of audit work conducted by SAIs in the year-end audits of the budget**



Note: By number of respondents (out of 35 total). Respondents could select multiple options.  
Source: Chapter authors from data provided by the 2022 UNDESA/IBP SAI survey.

An SAI’s mandate also affects the nature of audit procedures that auditors follow as part of the recurring audits of the budget. It may prevent auditors from undertaking certain types of audits and exclude some government departments or entities from the SAI’s supervision. For instance, the Australian SAI’s Audit Manual indicates that audit teams shall not investigate instances of potential fraud or other wrongdoing, except in exceptional circumstances as decided by the Auditor-General.<sup>116</sup>

An SAI’s mandate will also determine its ability to conduct prospective audits, i.e., to examine preparatory documents before an administrative procedure is concluded. In the context of recurring audits of the budget, this could refer to issuing an audit opinion of the budget’s macroeconomic

assumptions, pre-project estimates, and other draft budget documents, before the budget proposal is approved by the legislature.

Some auditors and SAIs reject prospective control, arguing that recommendations made at the budget preparation stage would constrain an SAI, and undermine its ability to freely exercise professional judgment over the final budget law. However, based on the experience of some SAIs with prospective auditing, such as SAI Brazil, this type of oversight is valuable as it allows the early detection and correction of inconsistencies in the budget process. Auditors would not necessarily be bound by conclusions reached at the prospective stage if the motives that lead to apparently conflicting conclusions are properly explained.

<sup>116</sup> Available at <https://www.anao.gov.au/work/audit-manual>

### 5.3. Combining audit procedures in recurring audits of the budget

The type of audit work performed to examine the year-end accounts is affected by an SAI's mandate and the nature and scope of the government's year-end report.

As noted in Section 5.2, SAIs are increasingly open to conducting audit work that a priori would not be typical of their institutional model. It is advisable that all SAIs conducting recurring audits perform a financial audit of the national accounting balances, thereby expressing an opinion on the appropriateness of the reports. A financial audit provides extremely valuable insights regarding the soundness of a country's public financial management, and SAIs are in a unique position to do this work since government auditors are not subject to the same pressures and incentives that may hamper private accounting firms. Even those SAIs that adhere to the Courts of Accounts model

are gradually adopting financial audits. A review of SAIs in Francophone countries found that the Courts of Accounts of Belgium and France have recently adopted yearly financial audits of accruals-based national financial statements.<sup>117</sup>

Whenever permitted by their mandate, SAIs should also use compliance and performance audit techniques in their recurring audits of the budget. Through recurring audits that include compliance work, SAIs under the Auditor-General and Board of Audit models could enhance their advice to legislators by recommending legislative changes to close loopholes that allow for improper conduct in government. Similarly, value for money audits would allow Court of Accounts SAIs to yield findings that would not have been possible in a compliance audit and to issue recommendations that can improve the provision of public services.

#### Box 5.4. SAI Morocco: Mandated to conduct a yearly comprehensive audit

The Court of Accounts of the Kingdom of **Morocco** is legally mandated to carry out a comprehensive audit of the government budget at the end of the fiscal year. In its year-end report, the Court of Accounts employs a broad set of audit procedures, with a focus on compliance and performance audit work, as well as a financial audit of the government's consolidated financial report.

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<sup>117</sup> Rémi Frenzt, 2022 (unpublished), Supreme Audit Institutions and Budget Credibility in Francophone Countries. p. 14-15.

Recurring audits of the budget that include financial auditing plus the oversight of the government's operations using both compliance and performance audit procedures require a broad audit scope, an ample timeframe, and sufficient resources. Year-end recurring audits with a whole-of-government approach encompassing all public revenue and spending provide the best setting for achieving this goal. Mid-year recurring audits tend to be more limited in duration and scope, and therefore they should focus primarily on financial

and/or compliance auditing of key documents and financial statements.

The nature and scope of the year-end and mid-year reports also influence an SAI's work on recurring audits of the budget. The government's year-end report yields a more in-depth, whole-of-government approach to the government's budgetary and financial management policies since it covers a longer time frame. While the specific contents of the year-end accounts reports can vary considerably across

### Box 5.5. Type of audit work carried out by surveyed SAIs in annual audits of the budget

- **Financial audit:** Australia, Cyprus, Kuwait, Latvia, New Zealand, Viet Nam.
- **Financial and compliance audit:** Argentina, Azerbaijan, Bosnia and Herzegovina, Croatia, Eritrea, Greece, Guatemala, Guinea-Bissau, the Philippines, Romania.
- **Financial, compliance, and performance audit:** Algeria, Bahrain, Cuba, Dominican Republic, Egypt, France, Indonesia, Ireland, Japan, Mauritius, Myanmar, the Netherlands, Paraguay, Portugal, Yemen.\*
- **Other:** Bulgaria (*compliance audit*), Madagascar (*performance and compliance audit*), South Africa (*audit of pre-determined objectives*), South Sudan (*performance, compliance and forensic audit*), United States (*performance audit*).

\*Some SAIs in this group also reported conducting forensic audits.

Source: UNDESA/IBP SAI survey, 2022 (38 respondents).

countries, according to the applicable legal and constitutional mandate, generally, they report on the status of the nation's financial statements, and in light of this fact, SAIs should perform financial audit work.

In addition, the country's normative framework may require the year-end accounts to cover other topics. In these accounts, the government may detail the status of the public financial management system in a particular year.

For example, they may include a justification of the measures taken at different stages of the budget process and allow a close-up assessment. First, at the stage of budget preparation, whether reasonable projections for macroeconomic variables were informing decision-making on budget allocations. Second, whether the budget was formulated in accordance with the country's fiscal rules. At the budget execution stage, whether disbursements during the fiscal year followed fiscal rules and good practices and how budget deviations, additional or unforeseen spending, and other noteworthy issues were handled. Finally, in this context, the last stage of budget revision involves reporting the final aggregate statements on revenue collection

and outlays allocation, comprising the entire budget during the fiscal year. Budget revision in the year-end accounts may also entail a projection of the consolidated budget into the future, in terms of its impact on fiscal solvency, on projected macroeconomic scenarios, as well as considerations of contingent liabilities and outstanding risks.

These supplementary considerations may demand a different approach by an SAI. In addition to the audit of financial statements, auditors may also use compliance auditing tools to check for the legality and the propriety of reported procedures.

### Box 5.6. Argentina's audit of the annual financial statements

The government of **Argentina** publishes an annual report disclosing the nation's financial statements in addition to other yearly reports on budget execution, the national debt, and other public finance information. The General Audit of the Nation (AGN) runs a year-end audit of the whole-of-government accounts (cuenta de inversión).

In auditing the Consolidated Financial Statements (CFS), AGN considers the budgetary, accounting, and physical aspects of the State's action. As a result, the report may include outcomes from specific annual audits on:

- Public debt service.
- National Social Security Administration.
- Federal administration of public revenues.

The CFS must be accompanied by various legal documents related to:

- Budget execution status.
- Statements that show the movements and situation of Central Administration's Treasury.
- The updated state of the internal, external, direct, and indirect public debt.
- The Central Administration's accounting-financial statements.
- A report that presents the consolidated financial management of the public sector during the year

and shows the corresponding operating, economic, and financial results.

- A report on the degree of compliance with the objectives and “physical goals” originally planned.
- The behavior of costs and efficiency indicators of public production.
- National Public Sector’s (NPS) financial management.

In this audit, the SAI employs financial and compliance audit techniques to provide Congress with an audit opinion on the regularity of budget execution and financial reporting.

Finally, although less common, the year-end accounts may also report on the results and the impact of public policies implemented during the fiscal year. In this case, the SAI will also use a performance audit toolset. Auditors would file their findings as to the efficiency, efficacy, and economy of government programs. This approach is employed by the SAI of Brazil, whose year-end report contains a section on public policy outcomes; by the SAI of the European Union which prepares a separate year-end report on the performance of the EU budget; and by the SAI of Sweden which includes a compilation of key findings from performance audits published during the year, plus additional follow-up and analysis of outstanding challenges. Naturally, having limited time to conduct such audit work within a broader recurring report is often the case, and audit teams should factor that in accordingly.

Depending on a country’s practices and regulations, general information on the public financial management system may be published in various documents, such as in ancillary reports to the budget law. In the United States, for example, some ancillary documents are published in the yearly “Analytical Perspectives” volume and in the Appendix to the Federal Budget, while in New Zealand there is a requirement that the government issue a Budget Policy Statement, a Budget Economic and Fiscal Update, and additional reports on the Fiscal Strategy and on Child Poverty. Even if the relevant information is not part of the government’s yearly accounts, it still falls under the purview of external auditors, and the SAI may take it into consideration in its recurring audits of the budget. (See Box 5.7.)

### Box 5.7. Potential sources of information about the PFM system

- Government databases.
- Preparatory and ancillary reports to the budget proposal and deliberations, prepared by the executive and legislative branches of government.
- Other official reports on budgetary execution and fiscal policy (such as reports on public debt, fiscal management, administrative pay, and state-owned enterprises).
- Previous reports from internal and external auditors, including audit reports from the SAI.
- Evaluations and reports from private-sector and international researchers.
- News media reports.

In addition to the audits of year-end accounts, recurring audits of the budget during the fiscal year could play an important role in a country's budget oversight. Besides what it records on the year-end accounts, the government may issue other official documents on budget execution during the fiscal year.

According to the 1977 Lima Declaration,<sup>118</sup> the 2007 Mexico Declaration of SAI Independence,<sup>119</sup> and United Nations Resolution A/66/209,<sup>120</sup> governments should make information of public interest available upon request by external auditors. If the government does not disclose mid-year reports on budget execution, SAIs must request and gather the necessary data from official sources. In the survey conducted in 2022

to support the development of this handbook, 95 percent of respondents indicated that, by law, the SAI has unrestricted access to records, documents, and other relevant information.

Mid-year reports offer an opportunity for SAIs to track and analyze the evolution of public revenue and disbursements, with a smaller time gap between decision-making and auditing. Exercising oversight of the budget during the fiscal year allows the SAI to formulate timely conclusions and recommendations. Auditor opinions may be instrumental in correcting course and avoiding imbalances that might otherwise go unchecked for longer periods of time and hinder administrative controls.

**Table 5.1. Recurring audits and SAI tasks across the budget cycle**

Budget formulation	<p>The SAI may collect pre-budget reports and other data that support the initial formulation of the budget, typically put together by the executive branch. The evidence collected at this stage reveals the intent of policymakers when the budget was formulated. It may underscore whether budget projections were made in good faith and regulations and good practices followed.</p> <p>Depending on its mandate, the SAI may be able to publish an early audit report at the budget formulation stage. The information from this stage will be useful for the SAI to reach conclusions associated with the budget proposal.</p>
Budget approval	<p>The approval of the budget proposal generally corresponds to the legislative branch. The SAI may be called upon to assist legislators in this task by conducting a budget-related audit. Given the cyclical nature of the budget, this work may translate into a recurring mid-year audit of the budget by the SAI.</p>

<sup>118</sup> The Lima Declaration <https://www.issai.org/pronouncements/intosai-p-1-the-lima-declaration/>

<sup>119</sup> [https://www.intosai.org/fileadmin/downloads/documents/open\\_access/INT\\_P.1\\_u\\_P.10/INTOSAI\\_P.10\\_en\\_2019.pdf](https://www.intosai.org/fileadmin/downloads/documents/open_access/INT_P.1_u_P.10/INTOSAI_P.10_en_2019.pdf)

<sup>120</sup> [https://www.intosai.org/fileadmin/downloads/documents/open\\_access/intosai\\_and\\_united\\_nations/66\\_209\\_2011/EN\\_un\\_resol\\_66\\_209.pdf](https://www.intosai.org/fileadmin/downloads/documents/open_access/intosai_and_united_nations/66_209_2011/EN_un_resol_66_209.pdf)

Budget execution	<p>During the fiscal year, budget execution involves the discharge of government functions in line with budget appropriations approved by the legislative branch as well as other pertinent regulations.</p> <p>Information related to budget execution is crucial for SAIs in their audits of the budget. SAIs may conduct one or several mid-year audits of the budget at this stage to track budget execution.</p>
Budget evaluation and oversight	<p>At the end of the fiscal year, the government is generally required to publish consolidated information related to budget execution, financial statements, and public policy outcomes.</p> <p>At this stage, the SAI can conduct a year-end, comprehensive audit of the budget, covering budget execution and public financial management for the entire year. Audit teams will benefit from more data availability and have more time and resources to conduct the audit. A greater array of audit techniques may be used. The year-end audit usually draws more attention from stakeholders on the SAI's work.</p>

## 5.4. Relevant audit standards

Recurring audits share commonalities with other audits. Therefore, the foundations outlined in auditing standards such as the International Standards of Supreme Audit Institutions (ISSAIs) provide the starting point for conducting recurring audits of the budget. The stages of the audit process (planning, execution, reporting, and follow-up) also apply, with some peculiarities, as described in the other sections of this chapter. In accordance with the scope and specific objectives of each audit, the auditor must select and apply the most appropriate auditing standards recommended by the International Organization of Supreme Audit Institutions (INTOSAI), expressed in the different ISSAIs, or the combination of different standards when the audit includes more than one objective. Attention should also be paid to existing standards related to auditing a specific topic, such as information systems (ISSAI 5100); public debt audit (ISSAI 5250); and audit of the public debt information system (ISSAI 5259), among others. (See Chapter 1, section 1.4.)

Depending on the audit objectives, other manuals, standards or guidance can also be useful. For non-financial information, the auditor can use the International Standard on Assurance Engagements (ISAE) 3000 (revised) and the Assurance Engagements Other than Audits or Reviews of Historical Information, issued by the International Auditing and Assurance Standard Board (IAASB).

In the case of audits of public financial statements, the IMF's Fiscal Transparency Handbook (2018) and their Government Finance Statistics Manual (GFSM) (2014) are useful. The GFSM provides a comprehensive conceptual and reporting framework suitable for analyzing and evaluating fiscal policy, especially the performance of the general government sector and the broader public sector, providing guidelines for presenting fiscal statistics within an analytical framework. The Fiscal Transparency Handbook (2018) covers Pillars I to III of the Fiscal Transparency Code and provides detailed guidance on the implementation of the Code's principles and practices, with examples from different countries. For review engagements, with limited assurance, a relevant resource is the International Standard on Review Engagements (ISRE) 2400 (revised) (2013).

## 5.5. Conducting recurring audits to assess and address budget credibility

Recurring audits of the budget may be carried out as year-end or mid-year audits. The distinction between these two types of audits should be considered for each phase of the audit cycle. With this in mind, this section provides guidance for conducting recurring audits (year-end and mid-year) to assess budget credibility.

Recurring audits of the budget should be aligned with an SAI's audit strategy. Recurring audits can focus on many possible areas, depending on the legal mandate of the SAI, which stipulates the work to be done in each fiscal year, and on the SAI's own suggestions of specific work to include in its audit plan. Therefore, to increase budget credibility and monitor it over time, an SAI could promote an integrated assessment of the PFM system to identify potential weaknesses and credibility risks. Based on their diagnosis, an SAI could include yearly recurring work or ad-hoc one-time audits to monitor relevant items in its audit plan. (See Chapter 3 on budget credibility risks.)

### Year-end audits versus other recurring audits of the budget

Recurring audits track and verify budget execution over a certain period, checking for the regular application of financial and compliance audit criteria. SAIs may also employ performance audit techniques to provide an overview of the results of the implementation of programs and public policy.

Because the budget cycle is typically structured around a fiscal year, recurring audits of budget execution tend to occur annually. This has some advantages. Over the course of a year, auditors have more time to collect evidence to document how that year's budget was developed; whether budgetary execution was regular and proper (see ISSAI 4000/24); if financial records were kept in accordance with existing regulations; and the extent to which non-compliance was material or justifiable, among other relevant criteria. Audit teams have more time to collect data, allocate resources, and develop their report. Some audit institutions may opt for a longer period, conducting recurring budget audits every two or three years, although this is less common. For example, SAI Morocco issues a yearly report on budget execution, but also a two-year general report analyzing other macroeconomic issues that would generally be part of an SAI's comprehensive year-end report.

SAIs may also establish an audit cycle that includes conducting multiple audits of budget execution during a single year. These mid-year audits allow SAIs to quickly react to inconsistencies in budget execution and suggest ways to address them. If audits of budget execution are conducted every two, three, or four months, auditors do not have to wait for a full year to publish an audit report that can flag budget credibility risks and sway budget execution favorably, ultimately contributing to better resource allocation and enhancing budget credibility. Frequently checking budget execution through mid-year audits also tends to improve spontaneous compliance by public officials.

Mid-year audits differ from broader, full-year audits. Because they refer to a shorter timeframe and are carried out with less time and fewer resources, audit teams must focus mid-year



audits on certain items to be verified, typically related to major fiscal rules and critical risk areas. Performance audit procedures are generally not suitable for mid-year audits.

Conducting several smaller, mid-year audits is compatible with a broader, yearly audit of the budget. In fact, mid-year audits may yield relevant findings that inform the broader year-end audit. This makes the year-end report more robust, as auditors will have looked into budgetary execution earlier in the year, and have more time to discover and investigate inconsistencies. This also contributes to greater effectiveness of audit work, as management may be better prepared to implement recommendations derived from mid-year reports that were already published. For example, SAI Germany conducts a mid-year audit related to each government ministry in addition to the year-end audit of the budget. The mid-year audits evaluate budget execution during the year, looking into parameters such as budget deviations and changes in staff, together with information from the last few years, to assist legislators in their discussions around the new budget proposal.

The SAI of Brazil has developed a recurring audit cycle that combines some mid-year audits with a broader year-end audit of the budget. In mid-year audits, the SAI makes projections to verify whether major fiscal rules would be observed throughout the entire fiscal year. The SAI also makes recommendations for course corrections.

## Audit planning

Planning for recurring audits of the budget must consider the breadth of the subject matter. Recurring audits should present a comprehensive, whole-of-government analysis of budget execution, even though conclusions may require

auditing relevant individual topics. Therefore, it is not expected that the procedures and results of a recurring audit are as detailed as those of a stand-alone audit. For example, in the case of policy outcomes, performance audit tools are used, but a complete performance audit of budget execution is not feasible in most contexts.

**SAI resources and skills:** Recurring audits pose a challenge in terms of resources. An SAI must have sufficient personnel to continuously process and examine large sets of data related to fiscal rules, public revenue, and spending. Budget auditing also demands a unique set of abilities, at the confluence of various disciplines including law, accounting, and economics. Due to the recurring nature of budget processes and the constant need to audit them, it is advisable that an SAI has a specialized team dedicated to conducting recurring audits at the end of and throughout the fiscal year. Sufficient and specialized human resources are critical. Auditors must have enough time to analyze year-end and mid-year budget reports, financial statements, and other documents.

SAIs with a broader mandate should assemble a diverse team to conduct recurring audits, involving experienced staff who are able to conduct audit work requiring accountancy, economic, and legal knowledge. Some background in law is particularly relevant for audit teams in SAIs with jurisdictional powers, since recurring audits may have legal repercussions.

Ideally, recurring audits of the budget should fall under the responsibility of a dedicated department within the SAI. Budget auditing demands a unique set of abilities to repeatedly carry out audit techniques in year-end and mid-year audits. Having specialized staff to run recurring audits of the budget is preferable to ad hoc engagements by auditors that generally perform other duties in the

audit institution and would increase productivity and help ensure that the proper routines are followed.

The narrower focus of other recurring audits of the budget carried out during the fiscal year allows

for some flexibility in terms of human resources. A smaller permanent team could conduct these recurring audits, with additional staff for the broader year-end audit.

### Box 5.8. Critical factors for consideration in *planning* a recurrent audit of the budget

**Scope:** Auditors should define the scope of their work on budget execution according to their legal mandate. For example, does it include the reviewing of pre-budget projections, public debt sustainability, and public policy outcomes. The SAI's mandate also influences its ability to make audit recommendations. Since the scope of recurring audits of the budget can scale up quickly, audit teams should carefully plan the audit, considering the available resources and the expected results.

**Resources, information and methodology:** Year-end audits require more resources and information given their longer timeframe. They also provide opportunities for different audit activities, combining financial, compliance, and performance audit procedures.

**Level and depth of analysis:** Recurring audits are not as detailed on all aspects of budget execution as individual audit engagements. For instance, the level of reporting on the evaluation of policy outcomes in a recurring audit of the budget is not as in-depth as in a stand-alone performance audit

**Audit object:** When planning recurring audits of the budget, SAIs must discern which objects will be selected for analysis to provide a comprehensive overview of budget execution. Typically, this will entail a careful selection of budget execution topics based on materiality, relevance, and risk. Overarching fiscal rules, general legal requirements for budget appropriations and disbursement, major national policy targets, and consolidated debt outcomes, are some of the major budget-related audit objects in the purview of a recurring audit of the budget.

Another relevant consideration for the selection of the objects of analysis is whether the recurring audit is a year-end or mid-year audit. (Box 5.8) Since year-end audits cover budget execution during the entire year, they examine more audit objects, rely on a wider set of audit procedures and have broader conclusions. Other recurring audits conducted over shorter periods during the fiscal year have a more limited and focused approach.

The auditors should present a general, preliminary overview of the audit object to the audited

entity to ensure mutual understanding of the object and its organizational environment. The auditors should consider existing legislation and the specific rules applicable, the entity's organogram, and the working flow of processes, operations, projects, programs, activities, as well as its routines and manuals, and the strategic and operational plans. It might also be useful to read the results, findings, and recommendations of previous audits. In addition, auditors should conduct a risk assessment as described in Chapter 3.

**Control environment:** As a rule, auditors must consider the control environment when planning new audits. In operating environments with weak internal controls and low compliance, auditors are expected to carry out more extensive tests and procedures to minimize audit risks. Therefore, in countries with indicators of a fragile control environment (e.g., high levels of corruption, investigations of crimes committed by public officials), recurring year-end audits of budget execution should use a broader set of audit procedures, involving at least financial and compliance auditing: the procedures do not differ significantly from those used in government auditing generally, such as confirmation, inspection, and recalculation.

Further, all terms of the audit should be defined during the planning phase, including the specific roles and responsibilities of both the auditor and the management of the audited entity.

SAIs should also ensure that they will have timely access to the relevant information to conduct recurring audits – i.e., access to government

documents, especially the year-end and mid-year budget reports and financial statements, and large datasets related to budget planning, execution, and policy results at the whole-of-government level.

**Audit objectives:** Audit planning requires identifying audit objectives. In general, the main audit objective in recurring audits of the budget is to express an opinion on the adequacy of the country's financial and budgetary statements. Secondary audit objectives include the examination of the adequacy of financial statements, the soundness of fiscal policy, the solvency of the state through sustainable public indebtedness, the adherence to laws and regulations in budget management, and the effective delivery of public policies.

By relating the audit objectives of the recurring audit to budget credibility, the audit work will contribute towards the enforcement of budget credibility in the PFM system. To get an idea of how audit objectives for the year-end accounts can be directly related to budget credibility, see Table 5.2.

**Table 5.2. Year-end accounts: Relating audit objectives to budget credibility, an example from SAI Philippines<sup>121</sup>**

Audit objective	Implication for budget credibility
To obtain reasonable assurance on whether the account balances in the financial statements are fairly presented and are free from material misstatements (statement of comparison of budget and actual amounts).	This work leads to strengthening credibility in the country's PFM system by providing independent support and credence to national accounting data.
To determine whether claims against government funds are authorized, valid, and supported with complete documentation.	This supports the credibility of budget execution by overseeing compliance with legal requirements for the allocation and disbursement of funds.
To determine that Accounts Payable balances as presented in the financial statements are valid obligations and supported with sufficient evidence.	The analysis of the regularity of obligations promotes the credibility of pending credits held against the State.
To determine whether recorded revenues and receipts are incurred during the period to which it relates.	This objective reinforces the credibility of budget execution consistent with the principle of budget annuality.
To determine whether budgetary information is properly disclosed in the Notes to Financial Statements as required in IPSAS 24.	The verification of the budget's reporting structure in accordance with international standards provides credibility as to proper budget transparency and regularity.

**Audit scope:** Subsequently, the auditors must define the audit scope, which is related to the subject matter, and the criteria which will be used to assess and report on the subject matter. The scope of the audit should be defined in a way that allows it to respond to the audit objectives. Defining the scope of the audit involves: (i) articulating audit questions; (ii) establishing the depth of the audit procedures that will be conducted during the execution phase; (iii) describing the nature and the extent of these procedures; (iv) delineating the auditable universe,

and (v) defining the audit samples to be obtained.

**Audit questions:** Audit questions will be informed by the SAI's mandate and the nature and circumstances of the budget process in the country, as discerned in the auditor's overview of the object of the audit. Audit questions are formulated to yield relevant conclusions on the audit objectives. In the case of recurring audits, audit questions should consider the nature of work and whether it pertains to mid-year or year-end accounts.

<sup>121</sup> UNDESA/IBP SAI survey, 2022.

**Planning matrix:** A planning matrix can be a useful tool to help the audit team during the planning phase. In recurring audits, audit planning benefits from the cyclical nature of audit work, and the team may iterate and improve the planning tools established in previous assignments. Once a planning matrix is developed, it can serve as the initial basis for audit planning in subsequent budget cycles.

For each audit question, the matrix asks:

- What information is required to answer the audit question.
- What criteria can be utilized as a benchmark to assess the information
- What are the sources of information.
- Which procedures will be conducted to obtain the data.
- Which procedures will be conducted related to data analyses.

- What limitations are potential constraints to the analyses.
- What conclusions can be drawn from the analyses.

The planning matrix highlights the relevance of access-to-information systems used by the government in budget-related work, which will provide the bulk of the information in a recurring audit of the budget. Annex 5.1 provides an example of this tool.

## Audit Execution

When conducting the audit, auditors should perform the audit procedures described in the planning matrix to obtain sufficient and appropriate audit evidence. ISSAI 100 defines audit evidence as any piece of information used by the auditor to determine whether the subject matter complies with the applicable audit criteria

### Box 5.9. Critical factors for consideration in the *execution* of a recurrent audit of the budget

**Specialized team:** Due to the complexity of the audit object and the cyclical nature of both the government's budget and recurring audits, it is recommended that a specialized team is tasked with these audits on a permanent basis in the SAI, rather than an ad-hoc collaboration between auditors.

**Skillset:** Conducting recurring audits of the budget requires a specific set of skills and knowledge related to the PFM system, the budget process, and policy implementation. It is important to provide appropriate training to strengthen auditors' skills in these areas.

**Understanding of previous audit work:** In recurring audits, there is a strong incremental element to auditing reports. Examinations and conclusions are often based on findings from previous audits, whether recurring or regular audit engagements. Over time, auditors will be able to better identify proper audit objects and challenges.

**Access to information:** The extent to which the audit team will be able to obtain information, including pre-budget reports and economic projections, and to carry out financial, compliance, and/or performance audit procedures, will depend on the SAI's legal framework as well as on the audit's scope defined at the planning stage.

**Audit findings:** Any fact that does not comply with the audit criteria is an audit *finding*. An audit finding is the result of the comparison between the situation found and the applicable criteria and should be attested by audit evidence. The finding has four main attributes: the situation found (or condition), the applicable criteria, the cause, and the consequence.

An audit finding can be classified as an *impropriety* or as an *irregularity*, according to the nature of the finding. An impropriety comprises flaws of formal nature, which do not result in material or financial damage to the public purse. Findings of improprieties related to budget credibility may refer, for instance, to an incomplete disclosure of budget data to the public, in violation of national law or international good practices on transparency. An irregularity refers to the incurrence of illegitimate, antieconomic or illegal management, violations of legislation, and damage to public funds. For example, such findings may relate to public resources spent in areas not authorized by the budget, or to the government's inability to account for funds spent in terms of corresponding deliverables.

The audit evidence that corroborates the audit findings should be sufficient and complete to allow third parties that have not engaged in the audit process to reach the same conclusions as those reached by the audit team.

**Documentation:** Recurring audits of the budget require that SAIs collect documentation with relevant data and information on government revenues and expenditures. These include the national budget law itself, plus other official documents published during the budget cycle.

During the budget preparation phase, in addition to the budget proposal, the government may also publish a pre-budget statement (PBS) containing relevant macroeconomic information that will guide the approval of budget legislation. If the SAI has the legal mandate, it can review the information contained in the PBS or similar preparatory documents, such as macroeconomic forecasts of growth in gross domestic product and inflation; revenue and expense growth forecasts; the alignment of the budget proposal with national plans; the strategy for achieving fiscal objectives, the dimensioning of fiscal result targets, as well as the existence of fiscal risks that could affect the achievement of objectives; the long-term sustainability and credibility of public debt; verification of fiscal rules, such as the allocation of minimum and/or maximum mandatory expenses, maximum expenditure on personnel, and other country-specific situations.

Recurring audits aimed solely at assessing budget preparation are uncommon. However, every year the SAIs of Brazil and Germany execute recurring audits of the draft budget proposal and analyze its contents to inform discussions and deliberations in their legislature.

**Sources of information:** During the fiscal year, evidence for all budgetary transactions should be available to the SAI. Partial budget execution reports are an important source of information for mid-year recurring audits. Typically, this involves storing information in massive electronic databases. This can pose a challenge to auditors, due to limited technological capabilities in government agencies and/or in the SAI, multiple sources of information, time delays in data availability, and denial of access to some

datasets. The SAI should consider the need for technological proficiency from the audit planning stage and use its general powers to gather such data. If the SAI does not have access to timely, complete information, this may constrain the audit's scope and should be mentioned in the audit report. The government may also prepare comprehensive mid-year budget execution statements on a regular basis, showing the state of effective revenue collection and incurred obligations and outlays.

At the end of the fiscal year, the government may render accounts to the public in a specific report. The year-end report may contain financial statements and ancillary notes, plus other data related to the country's fiscal situation and the performance of government programs, and forecasts for the next fiscal year. In short, these year-end government reports are key and useful sources of information. For instance, the Comptroller and Auditor General of India (C&AG) conducts a recurring, year-end financial audit of the national government as well as a year-end compliance audit over various issues detected in the government's annual accounts (e.g., violation of laws and statutes, poor project management, lapses in internal controls). Similarly, the SAI of Georgia carries out recurring financial and compliance audits of the government's yearly state budget execution report.

In their year-end recurring audits, SAIs can also audit the performance of public policy results observed during the fiscal year. This entails looking at the effectiveness of government programs in areas such as education or healthcare. These

areas may be selected by criteria such as relevance, size of the budget, and previous risk assessment. For example, the SAI of Brazil runs specific performance audit verifications in its year-end report, examining the consistency and appropriateness of performance indicators, and evaluating observed policy results in the fiscal year, compared with government targets and external benchmarks.

SAIs may also compile the main findings of performance audits conducted during the fiscal year for inclusion in the year-end audit. The SAI of Sweden includes performance audit findings in its year-end report based on their relevance and risk considerations. In its 2021 year-end report of the budget, the SAI underscored a performance audit conducted earlier in the same year, in which it found that government subsidies for highway infrastructure in remote areas had had a limited impact on regional development.<sup>122</sup> The SAI of Japan provides an outline of key performance audit findings, based on audits executed during the year, in addition to financial and compliance audit work.<sup>123</sup>

The inclusion of performance-related work in recurring audits of the budget contributes to assessing budget credibility. Public-sector performance is a major factor in budget credibility, as a public finance management system that fails to effectively deliver goods and services cannot be regarded as credible.<sup>124</sup>

Both mid-year and year-end recurring audits (particularly the latter) may contain recommendations for the correction of improprieties found by the SAI, in addition to

<sup>122</sup> Riksrevisionen, 2021. Annual Report of the Auditor General 2021, p. 9. Available at [https://www.riksrevisionen.se/download/18.608c1dd117d5c1cd2ffb329d/1638355391810/Annual\\_Report\\_2021.pdf](https://www.riksrevisionen.se/download/18.608c1dd117d5c1cd2ffb329d/1638355391810/Annual_Report_2021.pdf)

<sup>123</sup> <<https://www.jbaudit.go.jp/english/effort/procedure5.html>>

<sup>124</sup> OECD, 2014. Principles of Budgetary Governance.

<sup>125</sup> See Chapter 7 for more on reporting and follow-up of audit recommendations.



follow-up on recommendations made in previous recurring audit reports. In recurring audits, SAIs may also replicate findings from audits conducted during the year – this highlights that these findings are considered relevant, and merit being featured in the recurring audit of the general budget.

## Reporting and follow-up<sup>125</sup>

Reporting consists of preparing a formal and technical document where the auditor communicates all relevant information to stakeholders, which may include audit objectives, audit questions, scope, the methodology employed, findings, and results.

A good audit report should use clear and straightforward language, be easy to understand, free from vagueness or ambiguity, and be complete. It should be objective and fair, present information supported by sufficient and appropriate audit evidence, and put findings into perspective and context. The form and content of a report may vary according to the nature of the audit, the intended users, the applicable standards, and the legal requirements.

SAIs have a role in the monitoring actions taken by the responsible party in response to the matters raised in an audit report. As a good practice, the SAI could request the audited entity prepare an action plan, where the responsible entity manager describes the actions that will be implemented to address the findings and recommendations. For each finding, this document should contain the

actions to be implemented; the entity personnel responsible for the action; and the implementation schedule. The action plan may also include additional elements such as the objectives, the indicators, and the benefits derived from the implementation of each recommendation.

## 5.6. Regular audits of the budget – two SAI experiences

Brazil and the Republic of Korea audit the year-end accounts of the state budget through annual as well as other regular audits conducted throughout the fiscal year.

### Brazil

The constitutional mandate of the Federal Court of Accounts of Brazil (TCU) includes the execution of year-end audits of the comprehensive annual national budget reports. The Court enjoys a broad mandate to perform financial, compliance, performance, and asset auditing. These functions are discharged by the Court in its year-end recurring audits. The TCU's audit report and opinion are submitted to Congress for a final decision on the President's accounts.

Traditionally, the TCU's recurring audit reports focused on compliance auditing of the budget transactions during the fiscal year. Some budget operations were selected to undergo analysis,

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<sup>125</sup> See Chapter 7 for more on reporting and follow-up of audit recommendations.



considering public finance regulations. Auditors also checked whether general fiscal rules were enforced.

In a 2012 peer review, the OECD recommended TCU be more concise, take a more critical stance on the analysis of information provided by the government, improve its financial auditing capabilities, and better communicate its audit opinion. Over time, the development of information technology solutions has also expedited the audit process, although compliance auditing still represents the core of the year-end and mid-year audit reports. There is a specialized unit at TCU to conduct recurring audits of the budget.

The TCU's recurring year-end report presents an outline of the country's macroeconomic situation and likely scenarios; the policy framework expressed by the government in the budget proposal, and the considerations made by Congress upon budget approval as compared against market consensus expectations. Additionally, in the year-end report, auditors verify whether the government abided by key fiscal rules, such as the Constitutional expenditure ceiling and the "golden rule" of indebtedness.

The Court's year-end report also contains a section on public policy outcomes. The Court surveys a rotating sample of performance indicators and analyzes the reported results of government policies in comparison with expected performance, as well as the appropriateness of the indicators themselves. Finally, the TCU also performs a financial audit of the national balance sheet. Regarding fiscal years 2018, 2019, and 2020, the TCU was unable to express an opinion on the national financial statements.

In its year-end report, the TCU may build or expand upon the conclusions of other audits conducted

by the Court. For example, this may include findings identified when the TCU discharges its annual rulings on the adequacy of individual public managers' tenure of office. The results of recurring mid-year audits may also be incorporated into the consolidated year-end report.

Furthermore, annually the TCU evaluates the draft proposals for the budget appropriation act ("lei orçamentária") and budget guidelines law ("diretrizes orçamentárias") submitted by the government to Congress. When examining draft legislation, the TCU may issue recommendations to support congressional discussions and highlight risks to the attainment of fiscal rules, expected targets, and the upkeep of public policies.

The Court also conducts mid-year audits of the budget based on the bi-monthly government reports on budget execution. In these audits, the TCU tracks whether the government has followed regular budgetary procedures for appropriation disbursement and whether fiscal targets are likely to be met.

In all audits, the TCU may issue recommendations to the government. These recommendations are followed up on by the Court, which can reinstate or modify recommendations. The repeated refusal to comply with the Court's recommendations may result in an adverse opinion from the SAI. This was the case concerning the year-end reports for fiscal years 2014 and 2015.

## Republic of Korea

The Board of Audit and Inspection (BAI) of the Republic of Korea conducts recurring audits with examinations of the settlement of accounts and audit activities, relative to each fiscal year, pursuant to the National Finance Act.<sup>126</sup> For

example, in its audit of fiscal year 2016, the BAI identified 99 discrepancies in reported financial statements of national assets and liabilities, related to underrepresentation and overrepresentation of figures.<sup>127</sup>

The BAI's yearly audit includes an overview of the state of public finance and macroeconomic variables. The BAI describes the trajectory of government revenue and spending, the consolidated and operational budget balance, national debt, and special government funds.

In its year-end recurring audit, the BAI also examines government performance and compliance with legal statutes. The Board of Audit does not limit itself to an analysis of indicators as reported by the government but also examines the appropriateness of performance planning and the reliability of performance reporting. Therefore, it may conclude that performance indicators are wrongly reported, due to inconsistencies and unreliability. In terms of policy performance, for example, the BAI reported 62 discrepancies in 2016.

In terms of compliance auditing, in its yearly report, the BAI compiles the results of audits carried out during the fiscal year. It may

recommend that government officials be reprimanded, that individuals compensate the State for unaccounted outlays, and that government agencies rectify wrongful legislation and administrative regulations. The BAI also makes recommendations for corrective measures.

## 5.7. Key challenges

The execution of recurring audits of the budget involves several challenges. A major one is the broad scope of a general audit of the budget. Recurring audits, particularly in the case of the year-end audit of government accounts, typically have an ample scope, encompassing a large share, or even the totality, of the state's budget. Hence, auditors must deal with a variety of subject matters, numerous sources of information, various government managers, and other stakeholders. To tackle this challenge, the SAI must carefully define the scope of this work, seek to apportion the necessary resources, and empower auditors with the tools and skills necessary to obtain relevant information to support a robust audit opinion.

### Key challenges to undertaking recurrent audits of the budget

- Addressing the breadth of the state's budget operations, in accordance with the SAI's mandate.
- Establishing a specialized audit team to conduct recurring audits, preferably on a permanent basis.
- Working with different types of audit techniques, related to financial, compliance, and/or performance auditing.
- Ensuring timeliness of audits and reporting of the results to other state institutions and the general public.

<sup>126</sup> National Finance Act 2006 of Korea, Article 60.

<sup>127</sup> Board of Audit and Inspection of Korea, Examination of the Final Accounts of 2016.

Another significant challenge stems from the need to consider all sources of government revenue and expenditures, given that relevant income and obligations may be yielded outside of the budget framework. SAIs should be diligent in their inquiry regarding extra-budgetary transactions that have an impact on the state's fiscal standing and budget credibility.

The institutional process of these audits may also present some challenges. For example, when the year-end audit conducted by the SAI is a preliminary opinion subject to approval by the legislature, there may be significant delays or even the omission by the legislature in discussing and approving the SAI's report on budget execution. Another challenge here concerns the fulfillment of the statutory time limits by the SAI to finalize its audit report. These challenges apply to other types of audits as well and can generally undermine budget oversight. However, they have a particular impact on recurrent audits of the budget as these are expected to be conducted within a specific time frame, aligned with the budget cycle/fiscal

year. Any delay undermines the potential of these audits to provide a regular diagnostic of the PFM system and the ability to address any potential problems in a timely manner.

Yet another important challenge surrounds the communication of recurrent audits of the budget with stakeholders. In general, effective communication is a key issue that SAIs strive to address – see, for instance, INTOSAI's efforts in creating a Communications Task Force, and the overview provided in EUROSAI paper "Roadmap for Reaching Supreme Audit Institution Communication Goals."<sup>128</sup>

However, communication with stakeholders is particularly consequential in the case of recurring audits of the budget. Such audits are among the most impactful activities performed by an SAI. The outcomes of recurring audits convey significant information to the legislature and the judiciary, the general public, civil society organizations, academia, investors, news media, as well as policy managers and internal auditors in government entities. Effective communication

### Box 5.10. US Government Accountability Office's communication strategy

The SAI of the **United States** relies on a multi-pronged communication approach through several media resources, producing key highlights for each audit, communicating information to Congress through a dedicated website, and engaging with the general public through the GAO blog. All these various resources are used to communicate findings of the audit of the consolidated financial statements in addition to other recurring fiscal oversight work, such as the yearly report on debt sustainability.

<sup>128</sup> EUROSAI, 2017. A Roadmap for Reaching Supreme Audit Institution Communication Goals  
<https://www.eurosai.org/handle/404?exporturi=/export/sites/eurosai/content/documents/strategic-plan/goal-team-1/Roadmap-for-Reaching-SAI-Communication-Goals.pdf>

with such a wide array of social actors is critical. On the one hand, SAIs should be aware of the potential repercussions of a recurring audit in the country's public sphere and in decision-making at all levels. On the other hand, recurring audits are able to increase the SAI's institutional profile due to their broad appeal, and are a powerful tool to communicate the value and benefits of auditing in the public sector.

## 5.8. Wrapping up and recommendations

Recurring audits of the budget can have a positive impact on increasing budget credibility, as they contribute to greater rationality and predictability in budget allocation and execution. Because they are conducted regularly, they generate positive expectations for both the public and the audited agencies and may become a "flagship" product of the SAI, leading to a greater public understanding of the value and benefits promoted by the audit institution.

The SAI's institutional model notwithstanding, it is suggested that year-end recurring audits of the budget involve financial auditing of the national financial statements, as well as some compliance and performance audit techniques to establish the degree of regularity and effectiveness of the government's acts and policies. In year-end recurring audits, risk-based selection may lead SAIs to scrutinize critical threats to fiscal rules and policy decisions that have the greatest impact on the lives of citizens.

Given the recurring nature of these audits and the analysis involving large amounts of complex information, SAIs could consider the following recommendations:

- a. Budget credibility should take center stage during SAI work on recurring audits of the budget. Beginning with adequate preparation to ensure sufficient human and technological resources, proper audit planning, audit execution of financial, compliance, and/or performance audit procedures, and the follow-up on recommendations and communication of results, recurring audits should not lose focus of budget credibility, amidst the abundance of information collected by the team.
- b. The planning of recurring audits must be included in the SAI's strategic plan to ensure the necessary material and human resources.
- c. Establishment of a technical unit dedicated to these audits, as well as to the definition of internal bylaws or specific auditing standards to guide this type of work, is important. The creation of a specific technical unit would contribute to the specialization and training of the audit team, with positive impacts on the predictability of audit procedures.
- d. Indicate and communicate clearly which standards will be used as a reference in the recurring audits of the budget, so that the executive branch can better understand and benefit from the audits.
- e. Establish clear and precise audit objectives to enhance critical analysis and identify

opportunities for improvement and corrections (instead of simply reproducing the information submitted by the executive).

- f. Conduct the audit work within a reasonable time frame to ensure the relevance of the audit findings and the impact of the recommendations.
- g. Audit recommendations, in cases when SAI mandates allow for them, must be articulated in a clear and direct way, indicating how their compliance can contribute to budget credibility.
- h. Develop a communication strategy to increase the positive impact of recurring audits of the

budget. The strategy should target the main stakeholders (e.g., the executive branch, parliament, the media, and civil society) to convey the general and specific objectives and value of recurring audits and their results.

- i. In line with the communication plan, produce customized documents for the different stakeholders to inform them of the main audit findings, recommendations, and how any indicated remedial action will impact the credibility of the budget. Consider the use of non-technical language, depending on the target audience.

## Chapter 6: Assessing budget credibility risks at the program/entity level

In examining budget credibility risks at the program and entity level, this chapter guides auditors to identify and analyze how such risks emerge, how they are managed by the responsible officials, and how they can be mitigated through audit recommendations. The chapter emphasizes the planning phase of the audit because the focus on budget credibility risks should be clear from the beginning of the audit and throughout the entire audit process. A summary reference guide on selecting criteria for a budget credibility audit and an auditor's self-checklist are appended to this chapter (Annex 6.1 and 6.2).

### 6.1 Focus on budget credibility risks at program/entity level

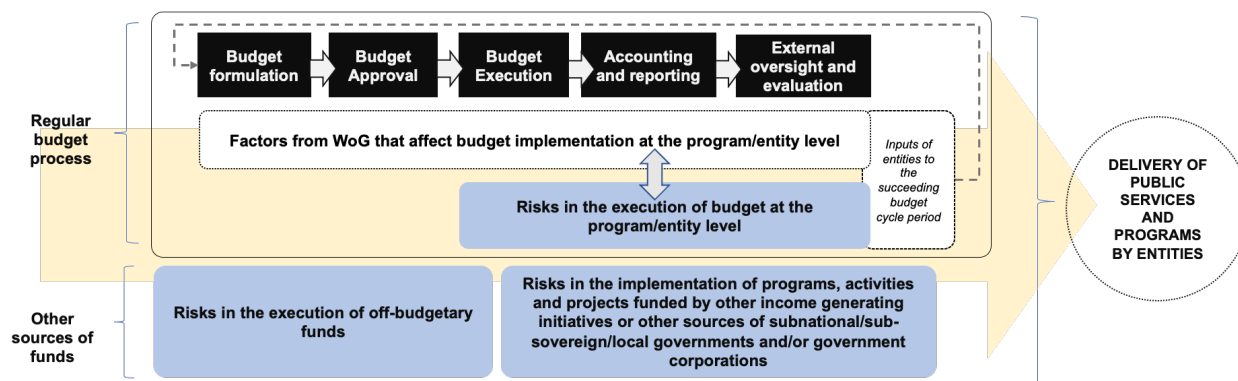
SAls regularly conduct audits of budget execution at the program/entity level as part of their audit

plans.<sup>129</sup> Auditors are encouraged to review their current audit practices, mandate, and country governance context and consider performing assessments of credibility risks at the program/entity level. In addition to the usual activities surrounding budget execution at the program/entity level, auditors are also encouraged to look into off-budgetary financing and other practices where funding comes from outside the regular budget process (e.g., income generation of local governments and government corporations, intergovernmental fiscal transfers/national tax allocation to subnational/local governments). The areas covered in this chapter are illustrated in Figure .6.1.

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<sup>129</sup> Audits of the government's budgets and year-end accounts, which are carried out on a regular, cyclical time schedule, are the principal focus of Chapter 5.

Figure 6.1. Scope of topics covered in chapter 6



Source: Chapter authors. SAI Philippines

Budget execution and implementation at the program/entity level may be affected by risks at the whole-of-government level.<sup>130</sup> For some issues evaluated at the program/entity level, SAIs are uncovering root causes that emanate from risks at the whole-of-government level. (For example, see Box 6.1.) feedback, via the mandatory reporting from programs and entities on their budget implementation, informs

Thus, risks at both levels (whole-of-government and program/entity) are interrelated and may

not be mutually exclusive from one another. For example, feedback from programs and entities (e.g., via mandatory reports on their budget implementation) informs budget preparation for the next fiscal year at the whole-of-government level. Similarly, as noted by SAIs in their audits, issues related to the generation and management of performance information from the program/entity level may also contribute to the preparation and forecasting of the budget for the whole-of-government.

### Box 6.1. Risk factors from the whole-of-government level can affect program implementation

In their annual opinion on the General State of Accounts, **SAI Portugal** includes recommendations to the parliament or to the government to overcome shortcomings of budgetary management, treasury, national debt, and state assets, as well as the organization and operation of services. These deficiencies are closely linked to budget credibility risks and some of them arise from the functioning of the budget programs. In fact, one recent example of a relevant audit finding at the program level is the non-compliance with budget limits of the Basic and Secondary Education and Health programs of the Portuguese government. The SAI found that this has been a recurring situation and reveals “structural problems in the budget forecasting process, whose approach needs to be more realistic, and represents a risk to budget credibility as a whole.”

Source: SAI Portugal

<sup>130</sup> Thus, this chapter is closely related to Chapter 3 on the assessment of credibility risks for the whole-of-government.

## Execution of the budget and use of funds at the program or entity level

Understanding how funds are disbursed to and used at the program or entity level will help the auditor pinpoint potential risks for budget credibility.

### Budget execution

Budget execution refers to the process through which financial resources are made available to an entity, which is mandated to direct, plan on,

and control the use of those resources in order to achieve the purpose and goals identified in the approved budgets. This process has several parameters, such as adhering to legal and administrative requirements as well as compliance with program descriptions based on relevant laws, rules, and regulations. In many budget systems around the world, budget execution is when the entities prepare their financial plan and individually execute their annual plan and targets based on the approved budget from the whole-of-government level.

The common budget execution activities followed by governments regarding program/entity level expenditure are summarized in Table 6.1.

**Table 6.1: How the budget is released to, spent, and reported on by a program/entity**

Activity	Stakeholders	Description
Budget programming/determination – i.e., preparing the final summary plan of how monies will be distributed amongst the ministries	Ministry of Finance or Budget  Inter-agencies/committee  National cabinet in charge of budget development and coordination	Budget determination/programming at the entity/program level usually takes place once the overall economic targets, expenditure levels, revenue projection, and financing plan have been determined by the Ministry of Finance or Budget, the inter-agencies/committee, or the national cabinet in charge of budget development and coordination. (See Box 6.2 for examples.)  The MoF, Department/Ministry of the Budget or other equivalent government institution prepares the budget program based on the appropriations approved by the legislative body and the entities' plans, financial and physical targets, and schedules for the year. <sup>131</sup> This process kicks off the budget execution phase in the final months of the year prior to the subject fiscal year.  In cases where the legislative body has not approved the budget before the subject fiscal year starts, the government may be allowed to spend on the basis of “ <i>vote on account</i> ” <sup>132</sup> where it can obtain an advance on the money needed for the next financial year <sup>133</sup> that should be enough to last for a few months until the new financial year starts. <sup>134</sup>

<sup>131</sup> In most countries, the MoF is responsible for formulating and implementing the core financial functions of the government which, among others, include budget formulation, macroeconomic forecasting, long-term fiscal projections, and tax policy. See [The Evolving Functions and Organization of Finance Ministries](#), by Richard Allen, Yasemin Hurcan, Peter Murphy, Maximilien Queyranne, and Sami Yläoutinen; IMF Working Paper WP/15/232; November 2015. In other countries, the budget formulation, and implementation functions are the responsibility of a separate ministry or department of budget: [Guidelines for Public Expenditure Management—Section 3—Budget Preparation \(imf.org\)](#).

<sup>132</sup> Guidelines for Public Expenditure Management—Section 4—Budget Execution <https://www.imf.org/external/pubs/ft/extend/guide4.htm>

<sup>133</sup> Votes on account - MPs' Guide to Procedure - UK Parliament.

<sup>134</sup> “Vote on account” is practiced in the United Kingdom and India.

<sup>135</sup> IMF, 2016. Expenditure Control: Key Features, Stages, and Actors



Activity	Stakeholders	Description
Allotment release / obligation authorization	Program/entity Ministry of Finance Line ministries, agencies, main spending units	<p>Upon submission of the entities' budget execution documents outlining their financial plans and performance targets for the year, the allocation of appropriations or release of funds through cash limits, funds transfers, etc. will take place.</p> <p>The MoF releases the designated appropriations to the line ministries (either quarterly or monthly). In turn, line ministries allot their apportioned appropriations to their subordinate spending units<sup>135</sup> and authorize the agencies to enter into obligations against their respective budgets.</p>
Obligation of expenses for the purchase of goods and services and other processes	Program/entity	<p>Thereafter, spending entities enter into the commitment stage or obligation that the government will pay for, as the programs, activities, and projects of the entities are implemented. Spending entities incur obligations when they enter into contracts with the suppliers of goods and services; these are subject to rules and regulations (particularly during the procurement process) of their respective governments. Spending entities undertake procurement and other processes before they "obligate" funds.</p>
Disbursement/ payment of obligation	Line ministries, other spending agencies, or Ministry of Finance	<p>Depending on the country's PFM process, authorization for payments on entities' commitments will be made by officials of line ministries, other spending agencies, or even the MoF.<sup>136</sup></p>
Accountability reporting	Program/entity	<p>The management of the entity reviews the performance of the programs/projects and submits required accountability reports to appropriate oversight and/or monitoring authorities. (See Box 6.3) accountability reports to appropriate oversight and/or monitoring authorities. (See Box 6.3)</p>

<sup>136</sup> Ibid

## Box 6.2. Examples of budget programming

The draft state budget laws of **Morocco, Romania, and the Philippines** are accompanied by a report on the macroeconomic situation for the budget year, on which the draft budget is prepared, including the projection for the next few years. From that, budget ceilings for each program or entity are determined and disseminated through the issuance of budget circulars and calendars by the Ministry of Finance or equivalent institutions.

In **Australia**, entity budgets are published in the “Portfolio Budget Statement” in the month of May every year to inform parliament of the proposed allocation of resources to government outcomes by entities within the relevant portfolio.

Sources: UNDESA/IBP 2022 SAI survey and chapter authors; <https://www.finance.gov.au/government/federal-budget/budget-process>

Spending entities pay funds from the government’s treasury to settle obligations they incurred for the delivery of goods and services to citizens. (To expedite the payment process, the budget department in some countries, including the

Philippines, have introduced a checkless and cashless disbursement mechanism whereby entities/agencies settle the payment of goods and services they procured through bank-to-bank transactions in lieu of checks and cash advances.)

## Box 6.3. An example of regulations on the financial management of an entity’s budget

In **South Africa**, Treasury Regulation 2.1.3 provides for the accounting officer (of an entity/department) to execute duties related to the department’s effective financial management, including the exercise of sound budgetary control practices, the operation of internal controls, and the timely production of financial reports. The same regulation also makes the chief financial officer of an entity/department responsible for submitting final documents to their Public Finance/Budget Office.

## Off-budgetary financing and expenditures

The three principles of universality, unity, and specificity for the fulfillment of budget functions guide governments to prepare budgets such that the expenditures financed by taxes/levies and all revenues collected (universality) are indicated in the budget document; all planned expenditures and revenues to be collected are presented to guide authorities to decide on the approval of the budget (unity); and expenditures and revenues are specified separately in required detail (specificity).<sup>137</sup>

Despite efforts to come up with a budget that fulfills these standards, budget institutions often encounter difficulties when consolidating other forms of expenditures that threaten the functioning and credibility of the budget. These are referred to as off-budgetary expenditures,

“items below the line” and “back-door” expenditures. Off-budget funds are entity monies authorized by law and deposited in the governmental depository banks used for expenditures that are not part of the budget or mentioned in the budget document.<sup>138</sup> With this common set-up of off-budgetary funds, the expenditures or budget information tend to hide the actual extent of government spending, borrowings, debt, and interest burden.<sup>139</sup> (See Chapter 3.)

Auditors may use the same guidance and references in this chapter when assessing credibility risks in the utilization of funds from off-budgetary financing, considering the impact of these operations on public debt and contingent liabilities (namely those arising from guarantees).

### Box 6.4. SAI India: Flagging off-budgetary financing and the need for its transparency

In January 2021, in a presentation to the Indian Finance Commission, the Comptroller and Auditor General pointed out that the central government’s deficit figures might be considerably higher than those reported in their government’s budget. **SAI India** suggested a policy framework for off-budget financing that should include transparency on the amount, rationale, and purpose of funding.

Source: [The Economic Times \(indiatimes.com\) |Time for clear picture - What is off Budget financing and why everyone wants to know about it this time.](https://www.economicstimes.indiatimes.com/news/economy/finance/what-is-off-budget-financing-and-why-everyone-wants-to-know-about-it-this-time/what-is-it/slideshow/80478104.cms)

<sup>137</sup> OECD, 2004. OECD Journal on Budgeting, Volume 4 Issue 1, OECD Publishing, Paris, [https://www.oecd-ilibrary.org/governance/oecd-journal-on-budgeting/volume-4/issue-1\\_budget-v4-1-en](https://www.oecd-ilibrary.org/governance/oecd-journal-on-budgeting/volume-4/issue-1_budget-v4-1-en)

<sup>138</sup> <https://www.dbm.gov.ph/wp-content/uploads/BESF/BESF2019/GLOSSARY.pdf>

<sup>139</sup> The Economic Times (indiatimes.com), 2021. What is off Budget financing and why everyone wants to know about it this time - What is it? <https://economicstimes.indiatimes.com/news/economy/finance/what-is-off-budget-financing-and-why-everyone-wants-to-know-about-it-this-time/what-is-it/slideshow/80478104.cms>

## Funding sources and utilization of subnational/sub-sovereign/local government units and/or government corporations/state-owned enterprises (SOEs)

In many countries, increasing decentralization of governance means that enhanced responsibilities and roles are allocated to local governments. For example, some countries allocate as much as half of their national budgets to lower levels of government.<sup>140</sup> Decentralizing sectoral programs such as health, education, and social welfare, is seen as a more effective way to ensure that intended beneficiaries receive benefits as planned in these programs. (See Chapter 1) Discerning the extent that this is the case should be considered among the audit priorities of SAIs in strengthening budget credibility both at the level of program implementation or entity's spending and the whole-of-government.

Auditors responsible for auditing lower levels of government (subnational/ local) and other types of government entities (e.g., government corporations) are also encouraged to use this guidance to assess the credibility risks of those entities. Many SAIs, however, have only a limited mandate – if any – to audit the subnational level of government and government corporations. Thus, in these countries with limited oversight at the lower levels of government, the use of funds by entities might escape a sufficient level of scrutiny and accountability.

In most jurisdictions, shareholders of government

corporations or SOEs have the primary responsibility for appointing and/or approving the external auditor with only some governments relying on SAIs to audit government corporations/ SOEs to evaluate the use of public assets and finances and observance of legal regulations.<sup>141</sup>

Nonetheless, auditors who have the authority to investigate the spending of these institutions hold an important role in advancing budget credibility. The discussions and guidance provided in this chapter speak about the universality of looking into credibility risks whatever the funding sources, budget/fund implementation process, and level of government (entities, institutions, or ministries) providing services and delivering programs to stakeholders.

## Additional factors that affect budget implementation at the program/entity level

Among the other factors that influence budget execution at the program/entity level are the translation of strategic priorities of the central government to individual entities; the adequacy and clarity of budget regulations and laws; and the feasibility of programs that are approved through legislative/congressional amendments. Varying across countries, these factors often reflect the relative powers and interests of the executive and the legislature in the planning, prioritization, and approval of programs as well as political considerations influencing the relations between both branches of government. When auditing entities and/or programs, auditors should consider

<sup>140</sup> Arturo Herrera Gutierrez, 2015. "What are we talking about when we talk about "subnational" governments?" World Bank blog. <https://blogs.worldbank.org/governance/what-are-we-talking-about-when-we-talk-about-subnational-governments>

<sup>141</sup> OECD, 2022. Monitoring the Performance of State-Owned Enterprises: Good Practice Guide for Annual Aggregate Reporting. <https://www.oecd.org/corporate/ca/Monitoring-performance-state-owned-enterprises-good-practice-guide-annual-aggregate-reporting-2022.pdf>

the budgetary legal framework and the relative power and capacity of the executive and the legislature to better understand various factors

influencing the risks to budget credibility in their country.

### Box 6.5. Examples of executive and legislative influence in budget preparation and program planning

**Nigeria:** Recent research by the International Budget Partnership (IBP) pointed to the legislature as one of the main drivers of budget credibility challenges in Nigeria. The legislature has considerable power to amend the budget and uses it to alter the budget each year. In recent years, data showed that the legislative branch contributed to underspending by introducing additional projects that could not be implemented.

**Philippines:** In 2011, the Executive introduced the Disbursement Acceleration Program (DAP) as a reform program aimed at expediting public spending and boosting economic growth by enabling the government to implement streamlined processes in budget execution. The DAP was not a fund, but a mechanism “to support high-impact and priority programs and projects using savings and unprogrammed funds.” Given the public and institutional concerns about the legitimacy and constitutionality of the program, audits of programs and projects funded by the DAP were conducted and the high court held hearings on the matter. In July 2014, the high court declared three schemes under the DAP unconstitutional.

**Brazil:** While some constitutional changes have enhanced the objectivity, transparency, and inclusiveness of budget amendments (particularly with a view to redistribution of resources to the poorest regions), the budget amendment process has also become more complex and burdensome in terms of the allocation of resources. The budget proposed by the Executive may be amended by the legislature in four different ways: through amendments by individual congressmen, state delegations, congressional committees, and rapporteurs. Political actors often leverage weaknesses in the process to forward their political and personal interests, which in turn affects the technical feasibility and successful implementation of programs and projects.

**Costa Rica:** The Parliament incorporates an entire chapter in the Budget Law on budget execution that establishes rules of budget under-execution and conditions for the execution of certain expenses, which affects the fulfillment of the annual goals and the efficiency and flexibility of the expense.

Sources: Nigeria: S. Atiku and J. Lakin, 2019. That’s incredible! The contours of budget credibility in Nigeria, Washington DC, IBP, <https://internationalbudget.org/wp-content/uploads/the-contours-of-budget-credibility-in-nigeria-ibp-2019.pdf>; Philippines: The Disbursement Acceleration Program | Official Gazette of the Republic of the Philippines; COA checking Palace’s spending booster program (rappler.com); Brazil and Costa Rica: Contribution of SAI Brazil and SAI Costa Rica for the development of this chapter.

## Common credibility risk factors at budget execution and program implementation

The traditional budget execution system focuses on compliance, which can be achieved when there are detailed input controls to lessen or avoid budget overruns and budget deviations.<sup>142</sup> Budget deviations (overspending and underspending of the budget) may happen because of non-compliance by entities with the spending limits defined by the budget itself or with the applicable rules and regulations.

The key risks to budget execution refer to whether deficit targets are likely to be met, and whether any budget adjustments determined at the budget preparation stage are being implemented as planned. On the expenditure side of the budget, risks refer to whether the actual budget spending is likely to be within the set budget, whether there are incidental implemented changes in spending priorities in specific areas or programs as planned, and whether any problems, such as the buildup

of payment obligations or overstatement of revenues, happen during budget execution.<sup>143</sup>

Any analysis or assessment of budget execution and controls should also cover issues related to budget preparation, and consider both the risks of repetitive disruptive budgeting, the requirements for cash controls, and compliance controls.<sup>144</sup> These credibility risks may occur despite having budget execution systems in place that ensure that the resources used to implement policies are incorporated into the planned budget.

For auditors, the usual starting point for analyzing budget credibility risks is familiarizing themselves with the risk factors of the environment of the audited program/entity. A recent analysis of 80 audit reports from 20 countries indicated that common budget execution problems are usually related to management capacities and procedures, documentation of expenditures, estimation of costs/spending, the timing of spending, and generation, capture, and management of performance information.<sup>145</sup>

### Box 6.6. A note on performance-based budgeting

The lack of alignment between expenses and the government's strategic objectives poses a risk to credibility. To tackle this issue, where feasible, some countries are moving towards performance-based budgeting, which aligns expenses with the government's strategic objectives and priorities and is an important tool for improving performance guidance, including program evaluation and spending review. The performance budget, in addition to aligning expenses with the government's strategy, objectives, and priorities, constitutes an important tool to improve performance guidance, including program evaluation and spending review. (See [OECD Best Practices for Performance Budgeting](#) and Chapter 3.)

<sup>142</sup> Asian Development Bank, 1999. Managing Government Expenditures, <https://www.adb.org/publications/managing-government-expenditure>

<sup>143</sup> IMF (n.d.). Guidelines for Public Expenditure Management—Section 4—Budget Execution <https://www.imf.org/external/pubs/ft/expend/guide4.htm>

<sup>144</sup> Asian Development Bank, 1999.

<sup>145</sup> A. Guillán Montero, 2021.

Additional types of execution problems that may create risks to budget credibility include weak documentation of expenditures, unjustified expenditures and their use for unplanned purposes, non-compliance to laws, rules, and regulations, and internal control deficiencies. (See Chapter 2.)

Key credibility risk factors commonly assessed by auditors on the execution of the budget at the program/entity level are described in Table 6.2 alongside a few relevant findings from SAIs.

**Table 6.2. Common budget credibility risk factors at the program/entity level (and sample observations)**

Common risk factors	Sample observations from SAIs on risk factors
<p><b>Management capacity and procedures</b></p> <ul style="list-style-type: none"> <li>Inconsistencies across information systems and legal frameworks.</li> <li>Weak administrative procedures leading to overrun or underspending with impacts on service delivery.<sup>146</sup></li> </ul>	<ul style="list-style-type: none"> <li>Lack of regulations, facilities, and mechanisms to implement social programs contribute to deviations during execution which lead to underspending (<i>Indonesia</i>).</li> <li>For programs and projects with cross-sectoral beneficiaries that are implemented by multiple institutions, coordination of implementing agencies is critical to minimize the lapses in planning programs and attaining determined outputs (<i>Philippines</i>).</li> </ul>
<p><b>Documentation of expenditures</b></p> <ul style="list-style-type: none"> <li>Lack of integration, consolidation, and cross-referencing of all activities regarding actions taken on spending.</li> <li>Weak integration of the documentation into the government's financial systems.</li> <li>Lack of documentation (i.e., lack of reports, records, supporting evidence, etc.)</li> </ul>	<ul style="list-style-type: none"> <li>Officials responsible for the implementation of a budget mixed up the classifications of budget information, which caused their budget statement to not be actual or real (<i>Egypt</i>).</li> <li>Budget execution is not supported fully by reliable and valid data on the beneficiaries of government programs (<i>Indonesia</i>).</li> </ul>

<sup>146</sup> Ibid. (A. Guillán Montero, 2021.)

Common risk factors	Sample observations from SAIs on risk factors
<p><b>Cost estimation and spending</b></p> <p>Poor cost estimation:</p> <ul style="list-style-type: none"> <li>Means budgets are inaccurate, which can impede capacity to spend</li> <li>Makes it impossible to check against spending to manage and prevent overruns.</li> </ul>	<ul style="list-style-type: none"> <li>Finance ministry attempted to control overall expenditures by underbudgeting in education and health programs and through centralized appropriations requiring approval from the Ministry of Finance to be relocated and used. This has resulted in a larger volume of reallocations, increasing red tape, not paying expenditures in due time, and the recurring problem of arrears (<i>Portugal</i>).</li> </ul>
<p><b>Timing of spending</b></p> <ul style="list-style-type: none"> <li>The lapse of time between authorization and actual spending may facilitate unauthorized spending that causes deviation from the approved budget.</li> </ul>	<ul style="list-style-type: none"> <li>There have been significant delays, of up to 132 working days, in processing the specific authorizations<sup>147</sup> that are issued to spending entities to incur obligations in their local government support fund, which assists the municipalities in delivering basic services to their constituents. These delays hinder the timely implementation of priority projects and programs financed by such funds, which could have benefitted people from the localities (<i>Philippines</i>).</li> </ul>
<p><b>Generation, capturing, and management of performance information</b></p> <ul style="list-style-type: none"> <li>Weak systems for capturing or gathering performance information affect the sufficiency and appropriateness of performance indicators and targets for government programs and projects.</li> </ul>	<ul style="list-style-type: none"> <li>Distribution of funds to some social programs was not carried out in a timely manner, in the right amount, or to the intended beneficiaries. As a result, there have been deviations from the planned budget, which could undermine the program's effectiveness in meeting the targets and objectives. These issues have been caused by the lack of reliable and valid data on beneficiaries as well as an information system that is not fully optimized to support government planning and program execution (<i>Indonesia</i>).</li> </ul>

Sources: The common risk factors on budget execution and implementation are based on the report from A. Guillán Montero 2021. The SAI examples were selected from the responses to the UNDESA/IBP survey of INTOSAI members conducted in 2022.

<sup>147</sup> In the Philippines, the special authorization is called Special Allotment Release Order (SARO).



Several of these risks may be detected simultaneously when examining budget execution of programs or by entities and may appear in combination with whole-of-government risks. The risks may overlap due to budget and program management areas that cut across the execution of the budget and implementation of programs.

## 6.2. Assessing budget credibility risks at the program/entity level

This section provides guidance on how budget credibility risks can be factored into audit work at the program/entity level – audit planning, performing the audit procedures/risk responses, evaluating the evidence, and forming conclusions and recommendations – and in consideration of the SAI's mandate, capacities, and resources. In assessing budget credibility risks at the program/entity level, auditors may follow the typical audit process being implemented by most SAIs and apply the relevant auditing standards, as previously presented in Chapter 2.

### Planning

Planning for an audit that looks at budget credibility risks at the program/entity level is necessary at both the strategic and the audit engagement phases. These planning activities can result in the identification of critical audit areas and programs (audit topic/s) which are likely to affect budget credibility.

### Strategic planning

As part of the strategic planning process, an SAI can provide clear audit instructions to its auditors on how to determine, formulate, and implement audit plans and procedures that factor in credibility risks from the beginning of the audit year. The strategic audit plan or similar top-level plan of an SAI should become the guiding document at the institutional level leading towards this direction.

Through the strategic audit approach in planning, SAIs can look at how well entities have articulated their goals and objectives that contribute to sustainable development at the national level.<sup>148</sup> Further, SAIs can examine whether entities have developed strategies for achieving objectives and whether evidence is used on results and strategic planning, allocation of public resources, monitoring, evaluation, and reporting.<sup>149</sup> One way of doing this is by detailing the number of target audits of programs and entities, as well as training needs and resources, that are required in the SAI's strategic plan, which will be supported, monitored, and implemented by the annual operational plans of the SAI. With this vertical articulation of the priorities to audit, the auditors who assess budget credibility at the program/entity level will be properly engaged on the selected audit topic/s.

SAIs may have different approaches to identifying the universe of critical areas for audit. As an example, the practice of SAI Bulgaria is presented in Box 6.7.

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<sup>148</sup> INTOSAI Russia (n.d). "Strategic audit," <https://intosairussia.org/news-media/news/best-practice-cases-of-strategic-approach-to-public-auditing.html>

<sup>149</sup> Ibid.

### Box 6.7. Determining research areas for a compliance audit of the budget at the entity level in Bulgaria.

Auditors identify three groups of activities based on their relation to the budget process:

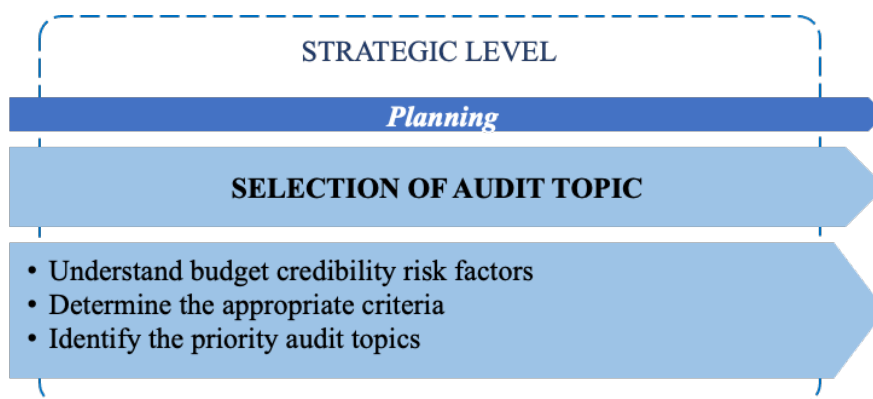
- Areas related to the implementation of the revenue part of the budget which includes processes/ sub-processes of planning, revenue administration, and implementation of the revenue part of the entity (budget procedure, implementation of tax and non-tax revenues, income from the funds of the European Union, others).
- Areas related to the implementation of the expenditure part of the budget, which relates to assuming obligations and making expenses (personnel expenses, maintenance costs, capital expenditures, public procurement expenditures, professional, training and retraining expenses, etc.).
- Areas related to the acquisition, management, and disposition of property which includes planning, lending of property, providing accommodation, purchase, and donations in favor of the state, among others.

These areas are analyzed according to two main criteria:

- Depending on the functions (powers) of the entity.
- Relations of the specific activity to the budget process (income from the activity and protection of the entity's property).

Source: SAI Bulgaria's contribution to the UNDESA/IBP SAI survey 2022.

Figure 6.2.1 Activities under Selection of Audit Topic



## Selection of the audit topic

Determining the prevalence of credibility risks in critical programs and areas should be the first step in assessing these risks in program/entity-level audits. SAIs may use a risk factor matrix (see Table 6.3) to identify high-risk areas as potential audit topics for credibility risk assessments and a decision criteria matrix (see Box 6.7) to select which of these topics which will be subjected to an audit. The following discussion presents the essential steps in selecting the audit topic (i.e., understanding budget credibility factors/applying risk factors to audit planning, determining the appropriate criteria, and identifying priority audit topics) and are supported with the presentation of sample tools to facilitate these actions. SAIs have different practices in performing these steps depending on their contexts, internal procedures, audit approaches, audit tools, etc.

### (i) Understand budget credibility risk factors

Knowledge of credibility risk factors (as presented in this chapter) and other relevant factors of the country/SAI context is important and valuable. Auditors must also understand which current sectoral programs and government activities are deemed critical or of high importance.

Useful criteria and questions that auditors could consider in selecting budget credibility as an audit topic are provided in Chapter 2. These include, among others, an assessment of the relevance and significance of budget credibility in the national context. A sample process for evaluating critical areas for an audit at the program/entity level is illustrated in Table 6.3.

**Table 6.3. Illustrative risk factor matrix**

Critical areas for audit	Risks factors*						Total
	i	ii	iii	iv	v	vi	
Sectoral programs and responsible entities**							
Social services (e.g., health, education, social protection programs, etc.)	✓	✓	✓	-	✓	-	4
Economic services (e.g., infrastructure, agrarian reform, agriculture, communication, etc.)	✓	✓	✓	✓	✓	-	5
General public services (e.g., general administration, public order, safety, etc.)	✓	✓	✓	-	✓	-	4
Debt burden (e.g., debt service, interest payments, etc.)	✓	✓	✓	-	✓	-	4

Critical areas for audit	Risks factors*						Total
	i	ii	iii	iv	v	vi	
Defense (e.g., domestic security)	✓	✓	✓	✓	✓	-	5
Government-wide							
Procurement	✓	✓	✓	✓	✓	-	5
Payroll (salaries and wages, personnel services)	-	✓	✓	-	✓	-	3
Others	-	-	-	-	-	-	-

\***Risk factors:** (i) Management capacity and procedures; (ii) Documentation of expenditures; (iii) Timing of spending; (iv) Cost estimation and spending; (v) Generation, capturing, and management of performance information; (vi) Other as identified according to country/SAI context.

\*\*Specific programs and responsible entities can be considered in the actual assessment

In the risk factor matrix, SAIs may modify the extent of classifications as to the sectoral programs and include specific programs depending on their relevance to budget credibility. For instance, pursuant to the Philippines' Magna Carta of Women, auditors may consider gender and development (GAD) risk factors, particularly on the allocation and utilization of GAD funds per entity. For documentation, the auditors should include comments and justification of the rating per critical area.

The idea of this exercise is to help auditors understand and clarify among themselves the occurrence of credibility issues and risk factors in important audit areas of government programs and activities. The critical audit area/s which garner the highest number of risk factors will be considered high-risk and can help prioritize audit work.

### (ii) Determine the appropriate criteria

Once the high-risk programs or activities have been identified, SAIs will identify the audit topic

using various criteria. SAIs will refer to their internal policies for the criteria and, depending on their flexibility, may develop their own selection criteria and procedures to choose audit topics. Aside from national laws, rules, and regulations that may require an audit of particular government programs or activities, the SAI/ auditors are expected to consider materiality (all its appropriate aspects), significance, risks, audibility, and impact, among other selection criteria. Especially in the case of programs, the auditor can also consider the commitments to standards, measures, and results adopted by auditee management, including specific targets.

In addition to reviewing priority programs for budget credibility risk, as per Table 6.3, SAIs should consider budget credibility within each of the criteria they choose to prioritize. Criteria to identify the audit topics, their respective descriptions, and their relevance to budget credibility are presented in Annex 6.1. Derived from the INTOSAI Performance Audit Standards

<sup>150</sup> INTOSAI-HDI, 2021. Performance Audit ISSAI Implementation Handbook. <https://www.idi.no/work-streams/professional-sais/work-stream-library/performance-audit-issai-implementation-handbook>.

Guideline on Selecting Performance Audit Topics,<sup>150</sup> Annex 6.1 is intended as a helpful resource to guide SAIs through this process.

identify the audit topic. One way for an SAI to determine and document their strategic audit priorities for a particular period is through a Decision Criteria Matrix, using a template and steps as illustrated in Box 6.8.

**(iii) Identify the priority audit topics**

After setting the criteria, SAIs may evaluate the high-risk programs/activities against them to

**Box 6.8. Decision criteria matrix for determining audit topics for budget credibility**

The weight for each criterion may be decided upon by the SAI or auditors, depending on the SAI context. Each program/activity will be scored against the criteria and a weighted score will be calculated accordingly. When all the programs/activities are analyzed and scored, the SAI should rank them based on their aggregated weighted score. The program/activity with the highest rank shall be considered a priority for auditing

**Audit topic selection matrix template**

Criteria	Weight*	Topic 1		Topic 2		Topic 3		Topic 4	
		Score	Weighted score	Score	Weighted score	Score	Weighted score	Score	Weighted score
Materiality	xx								
Possible Impact	xx								
Improvement	xx								
Legislative or public interest	xx								
Risks to SAIs	xx								
Relevance	xx								
Timeliness	xx								
Auditability	xx								
Other major worksplanned or in progress	xx								
Request for audit	xx								
Aggregate weighted score	100								
Rank									

\*The SAI has the flexibility to assign points for the selected criteria depending on their context

In identifying priority audit topics at the strategic level, SAIs will consider the resources and internal capacities needed as well as the purpose and impact of their deliverables. This also guides SAIs in deciding the more practical approach to auditing credibility, whether to perform the audits with (1) an exclusive focus on the budget credibility of a program/entity; or (2) to integrate budget credibility-aligned audit objectives/questions into other general audit areas/themes; or (3) to relate findings to budget credibility. (See Chapter 2.)

### Audit engagement

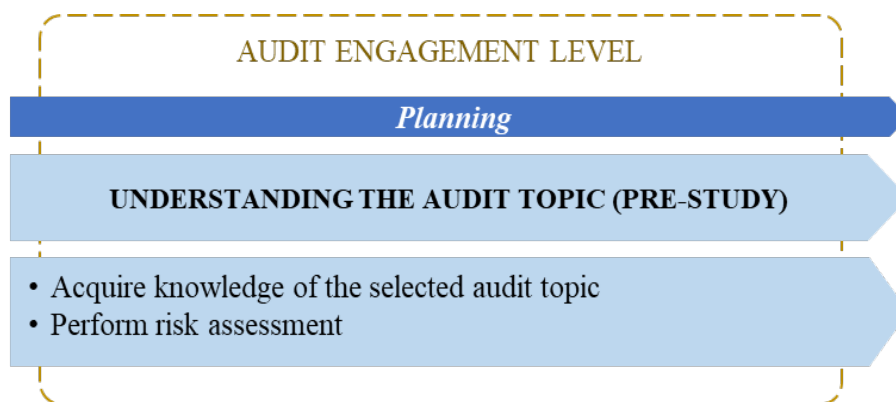
The strategic considerations become important entry points for the audit planning process. Once

the audit topic has been selected and defined, the planning at the individual audit level begins. The planning process at the individual audit level depends on acquiring solid knowledge of the work of programs or entities to be audited and understanding of the audit topic.

### Understanding the audit topic / Pre-study

The pre-study includes two activities to ensure that the auditor has a sufficient understanding of the program or entity to be audited: (i) acquire knowledge of the selected audit topic, and (ii) perform risks assessment

**Figure 6.2.2: Activities under Understanding the Audit Topic (Pre-Study)**



Based on these two activities, the auditor should be able to assess whether the audit is realistic, attainable, and likely to be useful.

#### (i) Acquire knowledge of the audit topic

Auditors usually inquire about the audit results of a program or entity from prior years. In some SAIs, e.g., the Philippines, which follow a residency audit approach,<sup>151</sup> auditors gain a broad practical knowledge of their assigned entities'

operations. They gather information to understand the entities' organization and operations, main programs and activities, results of previous audits, etc.

Auditors may refer to the sources of information summarized in Table 6.4 to further understand budget execution at the program/entity level in relation to the sample of credibility risk factors.

<sup>151</sup> Residency audit approach means that audit teams hold office in their assigned agencies.

**Table 6.4. Common sources of information on programs/entities per budget credibility risk factor\***

Risk Factors	Sources of Information
Management capacity and procedures	<ul style="list-style-type: none"> <li>• Program/project/activities details and implementing guidelines/regulations</li> <li>• Work plan and State budget/general appropriations act</li> <li>• timelines of programs</li> <li>• Profile of the audited program’s implementers (e.g., capacities, the mandate on the individuals or offices who carry out the work)</li> <li>• Information system available to managers</li> <li>• Organic laws or delegations setting out organizational roles and responsibilities</li> </ul>
Documentation of expenditures	<ul style="list-style-type: none"> <li>• Official documents authorizing government agencies to incur obligations</li> <li>• Procurement plans</li> <li>• Use of integrated FMIS, existence of paper records, receipts, and other related documents</li> </ul>
Timing of spending	<ul style="list-style-type: none"> <li>• Official receipt/cash notice allocation/disbursement documents</li> <li>• Performance and accountability reports of implementing agencies</li> <li>• Financial information systems</li> </ul>
Cost estimation and spending	<ul style="list-style-type: none"> <li>• Budget parameters</li> <li>• Budget proposals of program/agencies</li> <li>• Performance and accountability reports of implementing agencies</li> <li>• Budget execution reports</li> </ul>
Generation, capturing, and management of performance information	<ul style="list-style-type: none"> <li>• Government rules and guidelines on performance and accountability reporting</li> <li>• Performance and accountability reports of implementing agencies</li> </ul>

\* The auditor may obtain information from other sources based on the environment, as deemed relevant

**(ii) Perform risk assessment**

At the audit engagement level, auditors identify budget credibility risks that may hamper the achievement of the program or entities’ objectives. This data, as well as all the information gathered from the selection of the audit topic up to the pre-study activities, will be consolidated in the risk assessment process. (Common risk factors during

budget execution were explained earlier in this chapter.) Auditors are expected to identify specific risks and define them, as illustrated in Table 6.3.

Identifying the root causes of budget credibility risks enables auditors to gain a deeper understanding of them and to explore a set of more focused audit responses. This helps auditors to make more insightful recommendations to

the entities regarding the risks and controls to prevent them. Auditors can use various tools for the identification and analysis of root causes to supplement their initial analysis of the potential causes of risks (e.g., 5Whys, Ishikawa diagram, and problem tree analysis).<sup>152</sup> See also Box 7.1 in Chapter 7.

The identification of specific government accounts and activities allows auditors to assess whether some control procedures have been performed by the entity in relation to their requirements for internal control of budget execution.

Also, an important element of risk assessment is the identification of responses to address each of the risks identified. Generally, auditing is one way to respond to risks. Integrating the theme of budget credibility in an audit, auditors should ensure that risk responses effectively address the risks, as the choice of audit procedures will depend on the risk assessment or problem analysis. Risk assessment also guides auditors in the formulation of audit objectives, scope, and audit questions particularly on the theme of

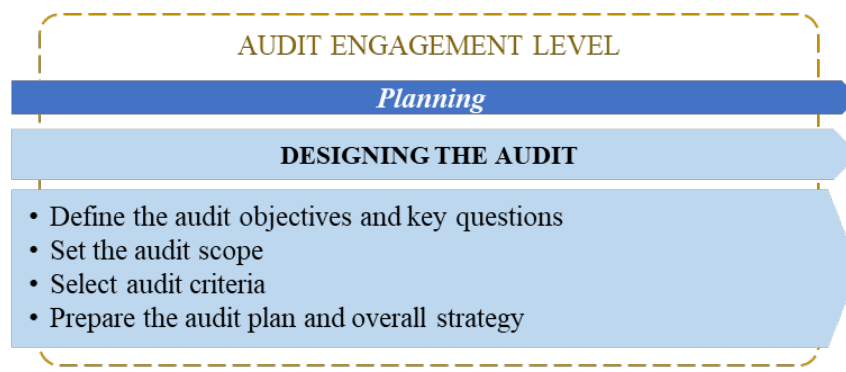
budget credibility.

Possible risks and illustrative examples, as well as audit objectives and specific audit questions related to each risk factor are presented in Table 6.5.

### Designing the audit

A well-designed audit that examines budget credibility risks relies on thoughtfully selected objectives, questions, and criteria which should be informed by the planning and pre-study activities and clearly documented. Credibility risks can be the exclusive focus of a standalone audit or integrated into a larger/regular audit scope. Designing the audit involves formulating clear and relevant audit objectives, key questions, and the identification of audit criteria, among other elements that would be supported by the documentation of the audit plans and strategy.

**Figure 6.2.3 Activities under Designing the Audit**



<sup>152</sup> The Canadian Audit and Accountability Foundation prescribes the use of root cause analysis tools for performance audits in their discussion paper on “Better Integrating Root Cause Analysis into Public Sector Auditing.” <https://www.caaf-fcar.ca/images/pdfs/research-publications/RootCauseAnalysisEN.pdf>



**(i) Defining the audit objectives and key questions**

Defining the audit objectives and the scope of the audit is closely related to the SAI's decision on audit approach. Auditors are encouraged to formulate specific audit objectives and questions that relate to budget credibility for all audits, not only for those that focus on budget credibility risks or integrate this angle. If an audit does not include specific budget credibility-related objectives or questions, auditors should ensure that the audit objectives are flexible enough to relate the prospective findings with budget credibility, as needed, during drafting of conclusions. (See examples in Table 6.5.)

To integrate the concept of budget credibility, auditors start from the identified risks and determine the appropriate objectives and/or questions. Auditors may break down the audit objectives into specific audit questions to ensure the audit objectives sufficiently cover the identified risks (Table 6.5). The formulation of specific audit questions guides auditors in the data collection process and with the analysis of the information in the next stages of the audit process. Early in the process, the auditor can determine whether the selected audit questions are likely to result in constructive recommendations.

**Table 6.5. Examples of audit questions to assess budget credibility risks at the program level**

Risk factor	Specific Risk	Risk statement	Audit objective*	Specific audit questions	Budget credibility – integration into the audit
Management capacity and procedures	Inconsistencies across information systems.	Deficient internal control systems of the entity do not provide accurate targets nor/or identification of program beneficiaries, which may result in budget overrun or underspending.	(CA) To ascertain whether the program beneficiaries were selected in accordance with the prescribed qualifications/criteria.	1. Are there established criteria for the identification of beneficiaries?  2. Is the selection/targeting process based on the established criteria?	Broad view of budget credibility: assessment of internal control systems, as enforcing/protecting the credibility of the audited program.
			PA) To determine the extent to which the program achieved its goals and objectives.  To determine whether program funds were utilized for the intended purpose (distributed to intended beneficiaries)	1. Was the total budget for the program spent in accordance with the program objectives? What are the causes of deviations, if any?  2. Are there any control mechanisms in place to ensure that  a. Targeted program beneficiaries are accurately and completely captured in the system?  b. Only qualified beneficiaries are recipients of the program?	Could be exclusive audit focus or integrated into another audit.

Risk factor	Specific Risk	Risk statement	Audit objective*	Specific audit questions	Budget credibility – integration into the audit
Documentation of expenditures	Poor cost estimation and spending	The expenditures incurred by the entity may not be related to the purpose of the program.	(FA) To determine whether the recorded program expenditures are supported with the appropriate documentation.	<p>Are recorded program expenditures:</p> <ol style="list-style-type: none"> <li>1. Supported with valid documentation (occurrence)?</li> <li>2. At the appropriate/correct amounts (accuracy)?</li> <li>3. In the proper accounting period (cut-off)?</li> <li>4. Under the appropriate account (classification)?</li> </ol>	<p>In line with the standard definition of budget credibility: audit is focused on the reliability of program expenditures.</p> <p>Could be integrated into another audit or relate the audit findings with budget credibility. (Chapter 2)</p>
Timing of spending	Unauthorized spending	Program expenditures may be incurred beyond the authorized period / budget period which: (a) facilitate unauthorized spending by the entity, or (b) affect efficient service delivery.	[CA/FA/PA] To determine whether the budget allotted for the program is spent/used within the budget period.	<ol style="list-style-type: none"> <li>1. Are the reported expenditures incurred within the reporting period/budget period? Are there expenditures incurred beyond the budget period?</li> <li>2. What are the factors/reasons that contributed to the untimely spending?</li> <li>3. How has the delayed utilization of program funds affected service delivery/program objectives?</li> </ol>	<p>Could be either standard (timing of spending) or broad view of budget credibility (factors affecting the timely spending).</p> <p>Could be exclusive audit focus or integrated into another audit</p>

\*CA=compliance audit; FA=financial audit; PA=performance audit

**(ii) Set the audit scope**

Defining the audit scope sets the boundaries of the audit. As discussed earlier, the SAI should decide on the approach or strategy, either to conduct an audit with an exclusive focus on budget credibility at the entity/program level or to integrate an assessment of credibility risks within an audit at the program/entity level. In either case, auditors should be able to narrow down the audit scope to focus on significant credibility risks that relate to the audit objectives.

To decide the scope of the audit, auditors consider the time period of the program or entity's operations to be covered and the geographical location (locale of the entity) to be covered in the audit.

**(iii) Select audit criteria<sup>154</sup>**

In auditing programs and entities, auditors first look at and evaluate domestic laws, rules, and regulations to identify the appropriate audit criteria to support their audit procedures. These criteria are the most relevant since they provide sets of guidelines and important information on the public sector governance framework and the specific characteristics of budget management in the country's context. The auditor can also consider the standards, measures, and performance commitments adopted by the program management or entity, including specific targets.

Auditors may also identify relevant audit criteria to assess credibility risks of budget execution at the program/entity level in international standards and good practices.<sup>155</sup>

**(iv) Prepare the audit plan and overall strategy**

Auditors should refer to their internal guidelines on preparing the audit plan, the audit program, the audit design matrix, etc., according to the type of audit to be conducted. However, in preparing these audit documents, auditors should make sure the focus on budget credibility or the integration of a budget credibility perspective is clearly reflected in those plans and documents (e.g., providing budget credibility-focused audit objectives or questions in the audit programs). These audit plans provide auditors with guidance as they move into conducting the audit, but can also be adjusted and refined as needed considering the emerging outcomes throughout the audit process.

## Conducting the audit

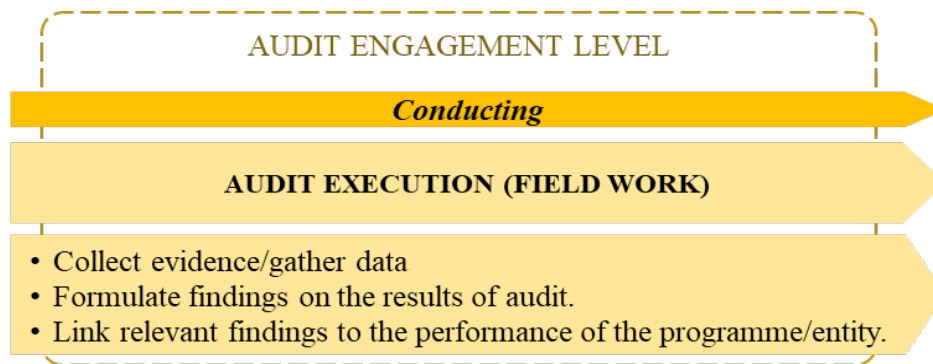
Conducting the audit refers to the activities needed to execute all the audit elements that have been planned by the auditors. In this phase, the auditors should obtain sufficient and appropriate audit evidence to establish the audit findings, draw relevant conclusions in response to the audit objectives and questions, and issue recommendations. These activities involve consultation/communication with the audited entity and effective data collection and gathering of evidence. It is critical that auditors analyze and evaluate the data and evidence taking into account budget credibility as reflected in the audit objectives and questions. When conducting the audit, auditors should follow the audit plan (which should be adjusted if necessary) and carry out the audit in accordance with the audit standards adopted by the SAI.

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<sup>154</sup> Note that the "selection criteria" presented in Box 6.7 refer to the steps at the strategic level in deciding what to audit from the numerous programs, projects, and activities while "audit criteria" are the benchmarks used to evaluate the subject matter (audited programs), ISSAI 100/27.

<sup>155</sup> Many of these best practices and standards are discussed in Chapter 1.

Figure 6.2.4 Activities under Audit Execution



### Audit execution (fieldwork)

#### (i) Collect evidence

Collect sufficient and appropriate evidence. Well-crafted audit objectives and audit procedures allow auditors to efficiently collect information and data that becomes evidence to support the analysis of budget credibility. Auditors should be alert to potential problems or weaknesses in the information and data they gather, as this can affect the reliability, validity, sufficiency, and relevance of the evidence. Exercising sound professional judgment is particularly necessary to assess whether the quantity and quality of evidence will allow for adequate conclusions or whether alternative sources of evidence need to be considered.

#### (ii) Formulate findings on the results of the audit.

Audit findings are the result of the comparison between the audit criteria (“what should be”) and the condition (“what is”), the identification of the cause of any deviation from the criteria (“why is there a deviation from the criteria”), the effect of such a deviation (what are the consequences”), and an assessment of the available evidence.<sup>156</sup> In auditing budget credibility risks of a program or entity, auditors follow their adopted audit standards and practices for the documentation and analysis of audit findings. A sample illustration of an actual audit finding is offered in Table 6.6. (Chapter 7 addresses audit findings as well.)

<sup>156</sup> INTOSAI-IDI, 2021. Performance Audit ISSAI Implementation Handbook.

**Table 6.6. Example of an audit finding at the program level related to budget credibility**

Risk factors	Specific risks	Audit objective [PA=performance audit; CA=compliance audit; FA=financial audit]	Actual SAI findings associated with the risk factors and specific risks
Management capacity and procedure	Inconsistencies across information systems	PA] To determine the extent to which the program has achieved its goals and objectives.  [PA] To determine whether program funds were utilized for the intended purpose (distributed to intended beneficiaries).	“The distribution of some government assistance programs is not fully carried out in a timely manner, in the right amount, [nor]to the intended recipients. Deviations from the intended plan as stated in the budget documents [will] undermine the effectiveness of the assistance programs.”
Timing of spending	Unauthorized spending and delayed spending	[CA/FA/PA] To determine whether the budget allotted for the program has been spent/used within the budget period.	

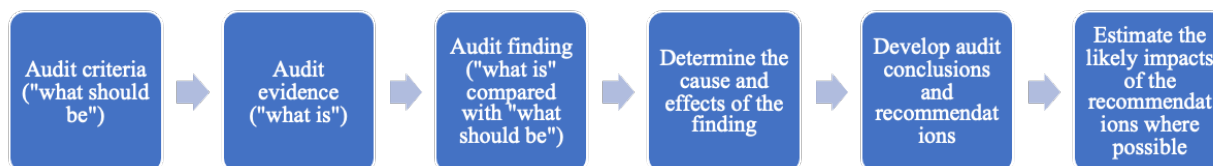
**(iii) Link relevant findings to the performance of the audited entity.**

When conducting audits related to budget credibility, auditors are encouraged to link their findings of budget deviations to the performance of the program/entity being audited. The auditor’s process of analyzing evidence, developing findings, and producing recommendations is a critical tool for addressing the areas where

programs/entities demonstrate poor practice and, thus, where budget credibility is weak. The ASOSAI Performance Auditing Guidelines suggest a tailored process for linking evidence, findings, and recommendations.<sup>157</sup> Auditors may adopt this process for audits on budget credibility to inform budget users, entities, and responsible parties about potential opportunities for improvement. (See Figure 6.3.)

<sup>157</sup> ASOSAI, 2000. ASOSAI Performance Auditing Guidelines. <https://www.eurosai.org/en/databases/products/ASOSAI-Performance-Auditing-Guidelines/>

**Figure 6.3 Generic process for linking evidence, findings, and recommendations**



Source: Adopted from the ASOSAI Performance Audit manual.

## Reporting and follow-up

Audits that examine budget credibility risks at the program/entity level should observe the reporting requirements established by the respective SAI, based on their legal framework and institutional arrangements. The aim of issuing audit reports, audit recommendations, and follow-up on recommendations is to provide entities and budget users the opportunity to improve budget and program management. Chapter 7 provides examples and practical information.

### 6.3. Challenges and lessons learned

Audits of the budget at the program/entity level have always covered risks and important elements of budget execution, but few SAIs have linked budget credibility and related concepts to actual audit findings, conclusions, and recommendations. The study and discussions in the development of this handbook anticipated

significant challenges but also lessons that would inform auditors on how to take this work forward.

#### Key challenges in assessing budget credibility risks at the program/entity level

**a) Mandate and independence of the SAI.** SAIs with a limited mandate and independence may find it challenging to include budget credibility audits in their work, as doing so normally would require constitutional amendments or support from stakeholders to examine the budget credibility of certain programs and entities. The challenges on mandate and independence have an overarching effect on other organizational aspects of an SAI, such as justifying resources and capacities for new theme-specific audits, setting audit focus/scope, and access to data, among others.

**b) Resources and capacities of the SAI.** SAIs that are not familiar with the concept of budget credibility may find it challenging to maximize their current human resources and institutional

knowledge of the subject matter, as well as to develop the audit strategies and tools to conduct the audits. The skills of auditors also affect the extent and quality of the audit they perform on the implementation of budget laws and regulations across the SAI. SAIs should consider capacity building on audits of budget credibility and emphasize the importance of relying on policies and regulations as audit criteria to minimize varied interpretations.

**c) Determination of the audit focus (exclusive or integrated budget credibility audits).** SAIs usually face the challenge of having too many programs and entities to audit in their portfolio. This may make it even more difficult for auditors to determine whether to focus an audit exclusively on budget credibility or to integrate a budget credibility perspective into another audit. This challenge could be addressed with clear audit instructions from the appropriate audit authority and/or by raising awareness of the value of incorporating budget credibility into audits with senior management of the SAI.

**d) Access to and quality of information and data.** Auditing at the program/entity level requires specific, timely, and reliable information and data. The challenge of having access to an entity's information and data relates to the mandate and independence of an SAI and the transparency policies and framework of the respective country. SAIs that plan to conduct budget credibility audits at the program/entity level should ensure that they have access to information and data in a format that can be easily collected and analyzed. Furthermore, since the quality of information and data from the entities cannot always be assured, auditors should perform methodologically sound audit procedures and corroboration activities to arrive at high-quality and reliable audit findings and recommendations.

**e) Changing political priorities.** As audit priorities emanate from the SAI's strategic audit plans, which are based on annual national priorities and long-term plans, a changing political landscape in countries may also represent a challenge. Conducting budget credibility audits may not be a priority area under a specific administration. In these circumstances, an SAI could advocate enhancing budget credibility as a good practice of budget execution among public entities.

## Lessons learned from SAI experience

**a) Importance of budget credibility-related findings.** Audit findings related to budget credibility at the entity level are easily appreciated by the parliament, the media, and the general public because they are all stakeholders of the programs that entities implement. For instance, in the Philippines, Parliament highlights the importance of the SAI's role in ensuring budgets are utilized in an efficient and effective manner and properly accounted for.

**b) Advocating the institutionalization of audits of budget credibility at the program/entity level within the SAI.** Institutional-level support from top management contributes to the quality of audits, including on budget credibility. Many SAIs follow a vertical approach in their audit planning process. This means that setting audit priorities for a particular year is usually based on the SAI's top management advice and instructions. Prioritizing the inclusion of budget credibility risk assessments at the top would facilitate incorporating budget credibility as an area to be examined in audit work.

**c) Readiness of information technology (IT) infrastructure of SAIs and digitization of governments.** The pandemic pushed SAIs to strengthen their IT infrastructure to address the demands of their oversight work. The readiness of SAI's IT resources will allow auditors to collect evidence (digitized) from the entities they audit, and to process and analyze them in a remote work set-up. SAIs should perform constant data back-ups and ensure flexibility to enable auditors to do their work despite changing work arrangements.

**d) Effective communication and engagement of stakeholders.** In this type of audit, auditors benefit from constant communication with the audited entities. Understanding the stakeholders and their roles, as well as their expectations and responsibilities would make it easier to conduct the program/entity level audits of the budget as planned. In SAIs with a robust practice of engaging stakeholders, particularly civil society organizations (CSOs), auditors may also consider involving these groups in the relevant audit activities of the audit process. The inputs and contributions from CSOs may be helpful in gathering relevant documents and information, particularly on audits that focus on program

implementation, as many CSOs work directly in the communities and perform monitoring of government programs. For example, in Argentina, after their audit showed public funds allocated to controlling the debilitating illness, Chagas, were insufficient and not spent as planned, the SAI successfully joined forces with the CSO, Asociación Civil por la Igualdad y la Justicia (ACIJ), to raise awareness of the issue. (See more on this collaboration and many others in Chapter 7.)

**e) Maximize SAI resources.** For one, as introduced in this handbook, an assessment of budget credibility risks at the program/entity level may be integrated into an audit whose main objective might be different. Regardless, auditors should maximize and customize the available audit tools to ensure they can support their assessment of budget credibility. Audits of specific sector programs may require technical expertise that may be outside the collective capacity of the team. SAIs should encourage the strengthening of technical capacities within the organization (e.g., data analytics of bigger datasets, technical reviews of contracts by civil engineers, etc.) to support auditors in their work on budget credibility.



## Chapter 7: Strengthening budget credibility through audit reports and follow-up

For audit work to advance budget credibility, SAIs need to produce quality audit findings; solid and actionable recommendations; and have a system in place to monitor the response by government entities. To that end, this chapter (1) provides guidance on ways to improve the formulation of findings and recommendations; (2) reflects on how audit follow-up can monitor and spur the implementation of recommendations more effectively; and (3) highlights the importance of SAIs working with key stakeholders to enhance audit impact and improve citizens' lives.

As noted throughout this handbook, the auditor is well placed to report on cases where budgets lack credibility – that is, where the government has not raised or spent its resources according to the approved plan. Given SAIs' traditional mandate for oversight of budget execution, even if external audits do not present audit findings in terms of budget credibility explicitly, the information they provide can be used to assess and address the lack of it. On the other hand, as discussed in Chapter 3, because of SAIs' important role in the public financial management ecosystem, if audit work and follow-up are ineffective, the risk of inefficient budget execution increases and, ultimately, worsens budget credibility.

In the audit process, *follow-up* refers to the examination of corrective measures adopted by the audited entity to respond to the audit findings, as well as the implementation of the recommendations. (See Figure 1.1 in Chapter 1.) Follow-up is important for all types of audits (financial, compliance, and performance) and increases the value of an audit by strengthening its impact.<sup>158</sup>

Still, audit impact is not something that SAIs can achieve on their own. For an SAI to be able to perform effectively and meaningfully, it needs to stay relevant to its stakeholders. Therefore, it is crucial for SAIs to identify and engage with key stakeholders during and after the audit process, from planning through follow-up on audit recommendations.<sup>159</sup>

### 7.1. Towards a quality audit report: Formulating findings and recommendations

Centering audit work around the idea of budget credibility is meant to focus audit objectives more squarely on bettering public financial management

<sup>158</sup> See ISSAI 100, ISSAI 200 and ISSAI 300.

<sup>159</sup> INTOSAI-IDI, 2021. Audit of Transparency, Accountability, and Inclusiveness of the use of emergency funding for COVID-19 (TAI Audits). A practical guide for Supreme Audit Institutions. <https://idi.no/elibrary/professional-sais/tai-audit/1212-tai-practical-guide/file>

(PFM) and service delivery. Regardless of the SAI mandate or type of audit conducted, the execution stage of the audit process involves obtaining appropriate and sufficient evidence to answer the audit objectives and questions. In turn, these audit findings will be the inputs for formulating the audit recommendations (if applicable).<sup>160</sup>

Accordingly, the audit report should explain why (*causes*) and how (*effects*) the problems identified (*findings*) affect the performance of the auditee, and how addressing those causes through specific corrective actions (*recommendations*) can help improve governance and/or service

delivery. This requires not only focusing on the audit findings but, where applicable, also on the recommendations formulated to correct the deficient situations.<sup>161</sup>

Pinpointing the causes and effects of an audit finding is essential for an audit to ultimately generate impact. Findings can often be symptoms or manifestations of deeper, systemic issues. Delving into the underlying or “root cause” of a deficiency finding allows the auditor to develop more appropriate recommendations to correct it. (Box 7.1.)<sup>162</sup>

### Box. 7.1. Root cause analysis

Root cause analysis is not a single methodology, but rather a body of qualitative and quantitative tools and techniques to understand why something happened or how a situation developed. It allows audit offices to develop recommendations to correct the underlying causes of reported findings and deficiencies.<sup>163</sup>

For example, key questions to probe include:

- Why do the deficiencies occur?
- Why are the entities not in compliance?
- Why are risks not being managed or intended results not being realized?
- Why are strategies not developed?
- Why is the information needed to support decisions not available?

The basic elements of findings and recommendations to be addressed in an audit report include:

- the observation – including the details of the irregularity or deviation,<sup>164</sup>
- its fundamental cause,

- the justification, if any, by the auditee for the irregularity or deviation
- corrective measures that should be taken and by whom
- the likely effect<sup>165</sup> of the implementation of the recommendation

<sup>160</sup> Some SAIs, according to their mandate, cannot formulate audit recommendations.

<sup>161</sup> INTOSAI P-12, 2019. The Value and Benefits of Supreme Audit Institutions - making a difference to the lives of citizens [https://www.intosai.org/fileadmin/downloads/documents/open\\_access/INT\\_P\\_11\\_to\\_P\\_99/INTOSAI\\_P\\_12/INTOSAI\\_P\\_12\\_en\\_2019.pdf](https://www.intosai.org/fileadmin/downloads/documents/open_access/INT_P_11_to_P_99/INTOSAI_P_12/INTOSAI_P_12_en_2019.pdf)

<sup>162</sup> CAAF, 2020. Better integrating root cause analysis into Public Sector Performance Auditing

<sup>163</sup> Ibid.

**Table 7.1. Examples of audit findings related to budget credibility.**

SAI	Budget credibility finding	Recommendation(s)	Impact
Indonesia	A large amount of carry-over and unused budget monies	Identify the affected program/project/ activities and provide a catch-up plan to resolve any adverse effects of unutilized funds. Provide sufficient information to the public on the large carry-over and unused amounts.	More projects are realized. Improvement in the budget execution performance indicator as well as the performance evaluation.
Zambia	Debt management policy is not aligned with the medium-term fiscal strategy	There should be a system to manage the contraction of debt by the Executive such as approval of new debts by the Legislature. The MoF debt management system should be interlinked with the Central Bank to ensure debt settlement is supported by the available resources in the Central Bank.	The linking of the debt management systems between the Ministry of Finance and the Central Bank will make it easier to establish a clear and comprehensive country debt position and help the MoF to make informed coordinated decisions on debt contracting and management.

## Communicating findings and recommendations effectively

Recent surveys reveal that too many stakeholders – including audited entities – do not find audit reports understandable or accessible. Writing up findings and audit recommendations in a simple and straightforward manner is essential – but also not easy.

SAI manuals should encourage the writing of findings in plain language so that all stakeholders

can easily understand the main results of the audit work. Many auditors (including 79 percent of the 38 respondents to our SAI survey) rely on their SAI audit manual for guidelines on formulating recommendations, tips on writing style, the number of recommendations considered appropriate in an audit report, and other aspects of producing their audit report.<sup>165</sup> Some SAIs that have established stronger alliances with civil society enlist citizens to advise them on the readability of their report. (See Box 7.2.)

<sup>164</sup> Lakin and Herrera, 2019.

## Box 7.2. Civil society can help to simplify audit reports for wider audiences

As part of an innovation drive, **the Philippines'** Commission on Audit (COA) set up the Citizen Participatory Audit (CPA) where citizens and the COA exchange aspirations, objectives, and more. Among other things, the COA and citizens partner in simplifying and communicating audit reports, designing data gathering instruments, formulating policy, developing courseware and learning material and facilitating training.

Source: <https://cpa.coa.gov.ph/> and INTOSAI Capacity Building Committee, 2021. "SAI, and Civil Society Engagement – Good Practices," p. 5 available on [https://www.intosaicommunity.net/document/knowledgecenter/CSO\\_SAI\\_good\\_practices\\_V2.pdf](https://www.intosaicommunity.net/document/knowledgecenter/CSO_SAI_good_practices_V2.pdf)

SAIs are more effective if their work is known, read, and understood outside the organization. Following the general principles of the SMART<sup>166</sup> model – drafting specific, measurable, attainable, relevant, and time-bound guidance – is the

best way to deliver accessible findings and recommendations to the auditees and to external actors, including the executive, the legislature, civil society, and the media.

## Box 7.3. Guidelines for writing up SMART findings and recommendations relating to budget credibility

Ensure findings and recommendations are simple to read, clear, logical, and:

**SPECIFIC:** Focus on a specific finding in a specific context and point to the specific stakeholder(s) positioned to address the issue.

**MEASURABLE:** Describe the extent of the deviation from the approved plan and detail the parameters of the recommendation to redress it.

**ATTAINABLE:** Are the recommendations realistic? Present recommendations in order of the most important issue and progress to the least important and move from the corrective steps that are easiest to achieve to the most difficult ones, or to the sequence of steps needed for implementation. Convey to the Executive that implementation will enhance the administration's overall viability – and gain public trust.

<sup>165</sup> UNDESA/IBP SAI survey, 2022.

<sup>166</sup> Barbara Adams and Ann Winstead, 2008. Write SMART: Internal auditors can use a specific communication technique to create value-added audit reports, Institute of Internal Auditors, USA.

**RELEVANT:** Be aware of the benefits of the audit results to the user. This does not mean compromising findings that adhere to acceptable practices or standards, but it does mean stating findings in such a way that urgency in the tone of the writing elicits a constructive response to report results.

**TIME-BOUND:** Address benchmarks and deadlines for achieving measurable results. Organize the recommendations and corrective actions in a matrix that provides a timeline for completion; this will not only give attention to them but will give direction on how the results should be interpreted and used. Designate timeframes clearly so the user will know whether all areas of concern have been completely addressed within the specified period. Further, a timely report enables prompt and effective action.

## Preparing the audit report

When completing the audit, the auditor will need to determine which recommendations to move forward, in what order, and when. Keeping the audit objectives top of mind, classifying recommendations according to certain criteria is a useful way to guide the auditee and will help focus the legislature and civil society on the aspects of the audit that the SAI considers most pressing – e.g., those items that will lead to more credible PFM and improved service delivery. Surprisingly, at this point only 34 percent of respondents to the handbook survey indicate they use any specific criteria to classify their audit recommendation.<sup>167</sup>

**Weigh priorities:** Different criteria can be used to classify and prioritize audit recommendations, including, for example:

- risk (high, medium, low)
- significance associated with the universe of stakeholders affected (greater importance to those recommendations that have a greater impact on a larger universe of stakeholders),
- temporality (recommendations that can be implemented in the short, medium, or long term),
- the systemic or particular nature of the recommendations (if they can be implemented exclusively by the audited entity or require joint management with other entities).

### Box 7.4. The concept of materiality is important when prioritizing audit findings and recommendations.

- Findings are considered material if, individually or in the aggregate, they could reasonably be expected to influence relevant decisions taken, based on the auditor's report.
- Will the relative importance of the matter, in the context in which it's being considered, influence the decisions of users of the report, such as the legislature or executive?
- In addition to monetary value, materiality includes issues of social and political significance, compliance, transparency, governance, and accountability.

<sup>167</sup> UNDESA/IBP SAI survey, 2022.

- The auditor's consideration of materiality is a matter of professional judgment and is affected by the auditor's perception of the common information needs of the intended users.

Source: GUID 3910. Central Concepts for Performance Auditing, INTOSAI, 2019 <https://www.issai.org/wp-content/uploads/2019/08/GUID-3910-Central-Concepts-for-Performance-Auditing.pdf>

### Box 7.5. Increasingly, SAIs and civil society are coming together to apprise each other of their priorities.

In **Peru**, public hearings held by the national audit agency, CGR, have made it possible to map significant problems that affect its citizens. During the period, 2018-2019, over 11,000 citizens spoke out in 128 public hearings on irregularities in the use of public goods and resources. Since 2019, new workshops have educated citizen participants on the mandate of the CGR and improved the quality of citizen input.

**Kenya** has a Citizen Engagement Framework to identify the CSOs and stakeholders for its Citizen Accountability Audit which in turn informs the SAI's Annual Audit Plan and can even lead to stand-alone audits.

In **Ghana**, the Audit Service launched the CITIZENEYE app in 2019, the first mobile application in Africa that allows citizens to report public service delivery issues to the Auditor General.

Sources: Marcos Mendiburu, 2020. La participación ciudadana en las entidades fiscalizadoras superiores en América Latina: ¿avance o impasse?, p. 33 <https://accountabilityresearch.org/wp-content/uploads/2020/08/2020-Mendiburu-PANORAMA-mayo2020.pdf> INTOSAI Capacity Building Committee, 2021. SAI, and Civil Society Engagement – Good Practices, p. 3, [https://intosaibc.wpengine.com/wp-content/uploads/2021/06/20210629-Engagement-with-Civil-Society\\_A-Framework-for-SAIs\\_CBC\\_28-June-2021\\_fnl.pdf](https://intosaibc.wpengine.com/wp-content/uploads/2021/06/20210629-Engagement-with-Civil-Society_A-Framework-for-SAIs_CBC_28-June-2021_fnl.pdf)

**Confer with the auditee:** Ideally, the auditor will meet with the audited entities to discuss audit results before releasing their report to the

executive (and the public). (See Box 7.6 for an example.)

## Box 7.6. Conferring with the auditee for best outcomes – an example

Prior to completing their audit report, **the Philippines'** Commission on Audit (COA) conducts an exit conference for dialogue and collaboration with their auditee. This is done to give both the auditee and auditor the opportunity to clarify areas of findings, to eliminate miscommunication, and to ensure the recommendations are (a) specific, measurable, achievable, relevant, and time-bound; (b) address the root cause(s) of the problem or deficiency; and (c) provide clear citation of measures to resolve identified deficiencies.

Further, the auditees are urged to prepare an "Implementation Plan" in consultation with the auditor to ensure they understand and agree to the workability of the audit recommendations.

**Establish deadlines:** Most of our survey respondents (67 percent) highlighted the need to establish deadlines for the audited entity to implement the recommendations. Some SAIs reported having deadlines set in advance. For example, for financial audits, the deadline is usually the following fiscal year. Others define it on a case-by-case basis according to the nature (materiality, urgency, and significance) of the recommendation and/or the type of audit. Some SAIs discuss and agree on the implementation period with the auditee; this dialogue contributes to the objective of achieving impact and adding value. Finally, even in those cases in which the SAI does not establish a deadline, they do require the auditee to provide a clear plan identifying the steps they will take to ensure implementation of the audit recommendations.

## 7.2. Following up on audit recommendations

While issuing robust recommendations during the audit process is very important, monitoring to follow-up on the remedial actions taken to restore credibility is crucial. The extent to which the recommendations are implemented by government entities is a key indicator of the impact of an audit. Yet, this remains the weakest link in the work cycle of SAIs. According to the latest INTOSAI Global Stocktaking Report (2020), SAIs self-report that only half of their recommendations are mostly or fully implemented.<sup>168</sup>

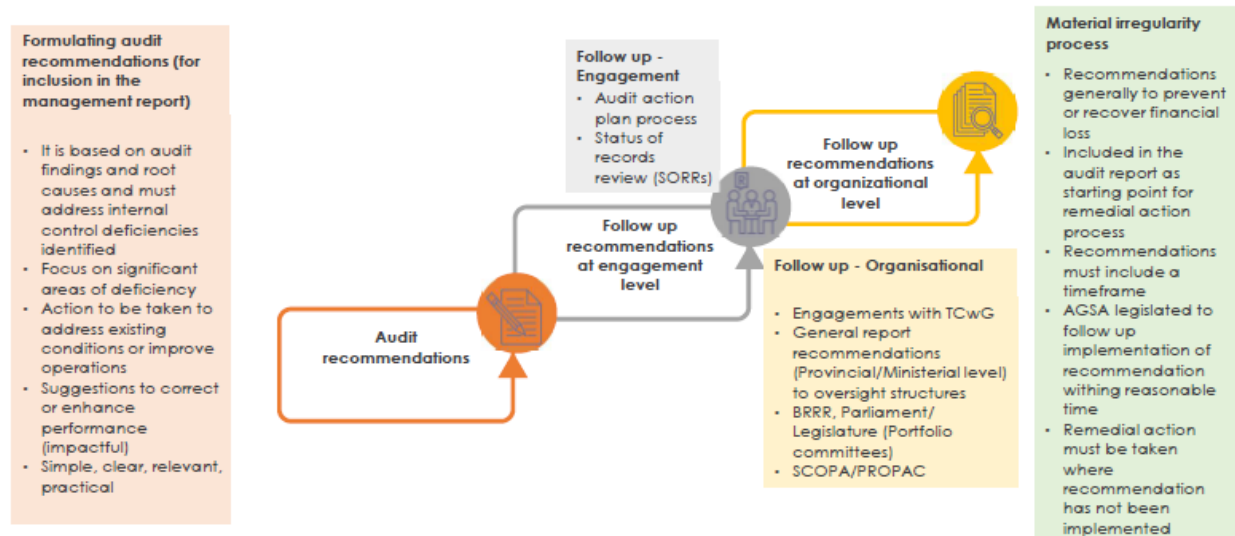
SAIs need to systematically keep track of how their findings are being used and their

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<sup>168</sup> INTOSAI Development Initiative (IDI), 2020. Global SAI Stocktaking report, Oslo, IDI at <https://www.idi.no/elibrary/global-sai-stocktaking-reports-and-research/global-sai-stocktaking-report-2020/1476-idi-global-sai-stocktaking-report-2020-v0104/file>

recommendations implemented. A follow-up process not only facilitates the effective implementation of corrective action but also provides valuable feedback to both the audited

entity and other stakeholders (e.g., civil society). (See Figure 7.1 for an example from SAI South Africa.)



**Figure 7.1. Monitoring and follow-up to audit recommendations in South Africa**

Source: Auditor General of South Africa

**Process:** Many SAIs (including 92 percent of the respondents to the 2022 UNDESA/IBP SAI survey) report they have some sort of procedure(s) in place to follow up on audit recommendations. These systems could be leveraged to follow up on recommendations related to budget credibility. Already 76 percent of survey respondents follow up on recommendations concerning some aspect of the annual execution of the state budget.<sup>169</sup>

For audits that are carried out regularly, the monitoring processes can become inputs for risk

assessment and decision-making in planning future audits (ISSAI 400).<sup>170</sup> For example, the SAI of South Sudan uses the recommendations of one audit as the starting point for the next. The audit recommendations not implemented by the audited entity are transferred to the results of the next audit.

**Frequency:** In terms of the timing of the follow-up on audit recommendations, some SAIs have established a regular frequency (quarterly, semi-annual, or annual monitoring), while others

<sup>169</sup> UNDESA/IBP SAI survey, 2022, p. 43.

<sup>170</sup> INTOSAI, 2019. ISSAI 400. Compliance Audit Principles, <https://www.issai.org/wp-content/uploads/2019/08/ISSAI-400.pdf>



monitor the implementation of recommendations according to the nature of the audited matter and/or the type of audit (financial, compliance, or performance). Rather than pursuing a specific interval for follow-up, Japan's SAI monitors the implementation of its audit recommendations on an ongoing, continuous basis until the auditors consider that the corrective measures have been correctly implemented.

**Reporting:** The follow-up actions to audit recommendations can be reported on individually or in a consolidated report, which includes the analysis of different topics and/or different audits. It may, in turn, form part of the audit report or be presented as a separate document (as was the case for 57 percent of our survey respondents). A separate document on follow-up is preferred for performance audits. Further, an insufficient or unsatisfactory performance by an audited entity may require an additional report from the SAI.<sup>171</sup> The assessment of this responsibility is generally based on whether the SAI or the legislature publishes a report to the public that monitors the actions of the executive to address the audit recommendations. In either case, it is important that the SAI and the legislature publish all monitoring reports in accessible formats.

**Action plans:** Some SAIs, per their mandate, have the legal authority to require the government, ministry, and audited entities to prepare a plan of action to implement the recommendations of the audit reports. In general, an action plan should always describe (1) the actions to be implemented, (2) the stakeholder who is responsible for carrying them out, (3) the resources to be committed, and (4) the deadline for compliance.

Encouraging auditees to draw up an action plan is more likely to lead to the successful implementation of corrective measures. At a minimum, as described in the example in Box 7.6, an action plan provides a useful means for the auditee and the auditor to communicate with each other and to ensure the auditee correctly understands the recommendations.

**Incentives:** SAIs grapple with how to create incentives for audited entities to follow up on their recommendations. The Philippine government offers a performance-based bonus to agencies that achieve or exceed their performance targets;<sup>172</sup> compliance with the audit recommendations is only one criterion but the SAI is the validating agency providing the government the information on this aspect. By contrast, in the countries where the SAI is of the jurisdictional model, an entity may face fines or other sanctions for noncompliance (e.g., in Brazil). Other SAIs have learned that the timely accessible publication of audit findings and recommendations results in more public and legislative pressure on the audited entities to address their shortcomings.

**Communication:** Again, it is important that SAIs communicate their work in a way that makes it easy for legislators (and for all other stakeholders) to act on the audit findings. In most cases, SAIs present the results of their audits to Parliament and request the lawmakers' feedback. SAIs can also seek feedback from the public on the outcomes of their audits through surveys, the monitoring of media coverage of audits, and the enabling of all stakeholders to share their comments via the SAI's website.

<sup>171</sup> INTOSAI, 2019. ISSAI 100. Fundamental Principles of Public-Sector Auditing. <https://www.issai.org/wp-content/uploads/2019/08/ISSAI-100-Fundamental-Principles-of-Public-Sector-Auditing.pdf>

<sup>172</sup> Jose Ramon Albert, Ronald Mendoza, Janet Cuenca, Gina Opiniano, Jennifer Decena-Monje, Michael Pastor, and Mika Muñoz, 2019. Process Evaluation of the Performance-Based Bonus (PBB) Scheme, Philippine Institute for Development Studies. <https://pidswebs.pids.gov.ph/CDN/PUBLICATIONS/pidsdps1915.pdf>

### Box 7.7. On communications and engaging with civil society – an example from Sierra Leone

In **Sierra Leone**, the Audit Service and civil society collaborate to simplify and communicate audit findings, jointly visit auditees with parliamentarians, and follow up on audit recommendations in critical areas, including water, sanitation and hygiene in schools.

“[W]e set up a communications unit to deal directly with civil society organizations through town hall meetings, radio programs, and a variety of other venues. Our goal is to train them on how the audit process works and how to use our reports to monitor the public services important to them,” explains Adama Renner, (former) deputy auditor general for the Audit Service. “Without public engagement with our audit findings, they are just reports packed up and stuck on a shelf.”

Source: <https://internationalbudget.org/stories/sierra-leone-civil-society-teams-with-auditor-to-assure-children-study-in-safe-healthy-schools/>

Ensuring the results of the audits are available to the public is key. Countries with publicly available audit reports are more likely to follow up on audit recommendations, and subsequently, more likely to steer towards a better performance on credibility. Moreover, it is good practice to prepare

and publish periodic reports for the state and the public on the progress and impact of audit recommendations, including information on financial and other benefits resulting from the SAIs' audit activity.<sup>173</sup>

### Box 7.8. Civil society using audit reports to affect change – an example from Sri Lanka

In **Sri Lanka**, the civil society organization, Verité Research, relies on audit reports to better understand the government's spending and uses the evidence to hold the government to account. Underspensing of the national budget has been prevalent and across critical sectors including health, education, social welfare, and agriculture. During the period 2011-2017, the government's tendency to spend significantly less than what it allocated was particularly pronounced in agriculture, (except in 2015, an election

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<sup>173</sup> IBP, 2021. Open Budget Survey 2021.

year when many sectors were overspent). Absolute deviations ranged from 10 to 40 percent and compromised services that a significant proportion of Sri Lankans depend on.

The CSO continues to review audit reports and make use of the audit findings in their advocacy, including when writing briefs and press releases or in meetings with officials. Most notable is their “budget promises” dashboard which directly highlights lapses in budget credibility.

Sources: IBP, 2019. Explaining Budget Deviation: A Budget Credibility Snapshot – Sri Lanka at <https://internationalbudget.org/wp-content/uploads/sri-lanka-budget-credibility-snapshot-ibp-2019.pdf>; Verité Research’s “Budget Promises” website: <https://www.veriteresearch.org/tag/budget-promises/>

**Measuring impact:** When possible, the best way to measure the impact of audit recommendations is both quantitatively and qualitatively. A purely quantitative approach generally details the number or percentage of recommendations implemented but does not give more weight to more important recommendations and vice versa, and thus may overstate (or understate)

the overall audit impact. On the other hand, a purely qualitative description of impact would be more useful if it included more granular and quantitative data.<sup>174</sup> In all cases, for more efficient monitoring, SAIs should create a database to track the implementation – and impact – of their recommendations.

## Box 7.9. Examples of positive impacts from SAIs auditing the performance of the PFM system

**SAI Latvia** reported the audits resulted in clearer and more equal procedures for reviewing the base expenditures of institutions.

**SAI Egypt** noted the audits had resulted in the proper utilization of public funds and enhanced the performance of the PFM system to achieve the Sustainable Development Goals (SDGs).

**SAI Ireland** highlighted the audits had an impact on the modernization of central government accounting and assisted in bringing fiscal documentation in line with international standards.

Source: UNDESA/IBP, 2022. Assessing the credibility of government budgets through external audits: Results of a survey to INTOSAI members at [https://internationalbudget.org/wp-content/uploads/Report-survey-results-budget-credibility\\_updated\\_9May2023.pdf](https://internationalbudget.org/wp-content/uploads/Report-survey-results-budget-credibility_updated_9May2023.pdf), p. 20

<sup>174</sup> EUROSAI, 2021. Follow-up of the implementation of audit recommendations. Best practices guide, issued by the project group <https://www.eurosai.org/handle/404?exporturi=/export/sites/eurosai/content/documents/2021-02-03-Final-report-for-EUROSAI.pdf>

**Electronic monitoring:** Only 29 percent of the respondents in our SAI survey indicated they use an electronic system to monitor the implementation of audit recommendations. Some SAIs use ICT-based systems also for internal monitoring and/or to provide information publicly. As mentioned earlier, the transparent disclosure

of the audit report in a timely manner can provide further impetus for entities to implement the audit recommendations as their status will now be publicly available. Three examples – from Georgia, Indonesia, and the U.S. (in Box 7.10) – suggest electronic systems can significantly improve follow-up on implementation.

### Box 7.10. Three SAIs on how they are using electronic monitoring for follow-up

**SAI Georgia** deploys an electronic system that integrates its audit reports, the audit results, the corresponding recommendations, and the action plans for the implementation of the recommendations. SAIs, auditees, and Parliament have access to the system. As a result of its use, the implementation rate of audit recommendations increased from 43 percent in 2015 – 2017 to 60 percent in 2018 – 2019. Although this system is not available to civil society, the data collected is presented in reports to Parliament.

Source: IBP-IDI, 2020 All hands on deck: Harnessing accountability through external public audits, <https://www.idi.no/elibrary/reports/1096-all-hands-on-deck-harnessing-accountability-through-external-public-audits/file>

**SAI Indonesia** formally requires the auditee to take appropriate action to follow up on the audit recommendations and reports on the consequences of lack of appropriate actions in subsequent audit reports. Every semester, the SAI also reports to the parliament and the president on the progress of the implementation of recommendations. Not fulfilling the obligation to follow up on the audit recommendations is considered a criminal action.

The SAI has developed two electronic systems for monitoring the implementation of audit recommendations, including those related to budget credibility:

- a. The SIPTL (follow up monitoring information system) is used by the auditee to provide information and supporting documentation on the follow-up actions they have undertaken. It is also used by auditors to analyze the information and documents provided and to determine the progress and status of the audit recommendations.
- b. The SMP (audit management system) is used internally by auditors to monitor and report on the progress of implementation of audit recommendations.

**US GAO** has established an action tracker, an online public control dashboard that is used to monitor the progress or regression of federal agencies based on the recommendations made by the oversight body. It is an interactive tracker in which users can filter by state area and track the actions carried out by the audited entities. Within each observation, the tool shows the year of its identification and its status based on the last update.

Every year, GAO identifies opportunities to reduce fragmentation, overlap, and duplication across the government as well as reduce costs and increase revenue for the federal government. In its 2022 annual report, the actions they wanted Congress and federal agencies to take to address their findings were listed. For further information, check [www.gao.gov](http://www.gao.gov).

### 7.3. Engaging stakeholders for maximum impact

Communication with stakeholders is an essential aspect of SAI work, both towards furthering the understanding of the SAI's findings and recommendations and fostering collaboration on action to heighten the impact of the audit.<sup>175</sup> Beyond the audited entities, SAI stakeholders also include:

- The legislature
- The executive
- Civil society
- The public
- The judiciary
- The media
- Development partners, academics, and professional bodies

Establishing and maintaining good working relationships with these stakeholders will generally improve the likelihood of a successful audit impact and, most importantly, progress toward the SDGs. We elaborate here on the first few.

**The legislature** is one of the most important external stakeholders for an SAI, both in general and in terms of furthering credibility, as it has the power to hold the executive accountable for the use of public funds. The ability of the legislature to engage and make use of SAI products is critical to an SAI's effectiveness.

Legislative scrutiny and follow-up on audit recommendations vary across countries. In some cases, the legislative body takes an active role to promote redress measures, including by requesting improvement plans (e.g., **the Netherlands**) or by using the percentage of implemented audit recommendations as one of the bases for the review and approval of the proposed budget (e.g., the Philippines). In other cases, the SAI and the legislative body liaise with other accountability institutions with enforcement powers (e.g., South Sudan). In New Zealand, the SAI performs an informal advisory role to the parliament in the legislative review of the performance of public entities.<sup>176</sup> And yet in other countries, parliaments/legislatures cannot or do not act sufficiently (or at all) on the SAI's

<sup>175</sup> INTOSAI, 2016. Supreme Audit Institutions Performance Measurement Framework. <https://www.idi.no/elibrary/well-governed-sais/sai-pmf/426-sai-pmf-2016-english/file>

<sup>176</sup> UNDESA/IBP SAI survey, 2022, p. 41.

<sup>177</sup> INTOSAI-IDJ, 2020. Global SAI. Stocktaking report 2020.

recommendations due to political discord or stalemate, or because of other characteristics of or inefficiencies with their processes.

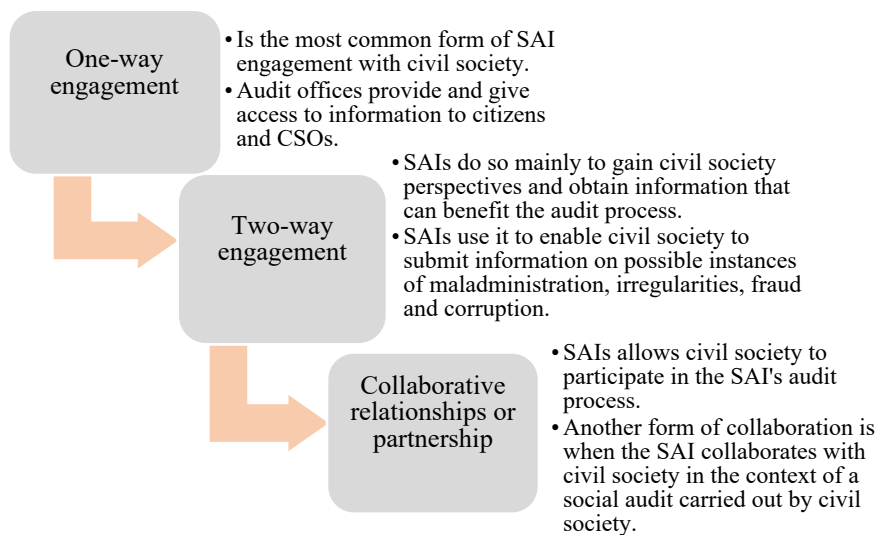
**Executive response**, or rather lack of it, is the most frequently reported impediment to the implementation of audit recommendations, according to a recent INTOSAI global survey.<sup>177</sup> In many cases, this is due to a weak relationship with the executive or stems from the SAI not approaching the Executive for feedback on the status of audit recommendations or for evidence of implementation. However, in other countries (e.g., Brazil) sending a recommendation to the Executive, and asking them to submit a proposal to their legislature, is an effective way to get the legislature’s attention on an issue.

**Civil society** is an increasingly important and largely underutilized stakeholder for an SAI. While formerly mostly excluded from deliberations on public financial management, in recent decades,

many governments have begun to recognize that civil society can and should be included in budget discussions and can be a source of great support during the audit process.

Public participation in the follow-up to audit recommendations is often critical as civil society can exert pressure on the executive and the legislative body for the implementation of audit recommendations.<sup>178</sup> (See Boxes 7.11 – 7.14 for examples.) Nonetheless, the handbook survey results confirm what has already been identified in OBS 2021: opportunities for public collaboration with the work of SAIs are still most common during the planning phase of an audit. The involvement of CSOs decreases as the phases of the audit process advance – with only 10 percent of the respondents indicating that it takes place in the follow-up to recommendations.

**Figure 7.2. Progressively richer forms of SAI engagement with civil society**



Source: Own elaboration based on documents of INTOSAI-CBC<sup>179</sup> (2021) and CAAF<sup>180</sup> (2020).

<sup>177</sup> INTOSAI-IDI, 2020. Global SAI. Stocktaking report 2020.

<sup>178</sup> OCDE, 2001. Participación ciudadana. Manual de la OCDE sobre información, consulta y participación en la elaboración de políticas públicas. [https://www.socioeco.org/bdf\\_fiche-outil-88\\_en.html](https://www.socioeco.org/bdf_fiche-outil-88_en.html); Vivek Ramkumar and Warren Krafczik, 2005. The Role of Civil Society Organizations in Auditing and Public Finance Management, IBP. <https://internationalbudget.org/wp-content/uploads/The-Role-of-Civil-Society-Organizations-in-Auditing-and-Public-Finance-Management1.pdf>

<sup>179</sup> INTOSAI-CBC, 2021. Engagement with civil society. A framework for SAIs. [https://www.intosaicbc.org/wp-content/uploads/2021/06/20210629-Engagement-with-Civil-Society\\_A-Framework-for-SAIs\\_CBC\\_28-June-2021\\_fnl.pdf](https://www.intosaicbc.org/wp-content/uploads/2021/06/20210629-Engagement-with-Civil-Society_A-Framework-for-SAIs_CBC_28-June-2021_fnl.pdf)

<sup>180</sup> CAAF, 2020.

When asked about the participation of CSOs in audits related to budgetary aspects, 61 percent of the respondents in the recent handbook survey indicated that it does not occur. When it does, civil society participation mostly occurs in performance audits (37 percent of respondents)

but remains very limited in financial audits (only 8 percent of the respondents). Nonetheless, in some countries, close SAI-CSO collaboration in the audit process, and particularly on follow-up, has made impressive gains in improving budget credibility. (See examples in Boxes 7.11 – 7.14).

### **Box 7.11. SAI – CSO collaboration in Argentina improved health sector outcomes**

In 2012 and again in 2018, the Auditor General of the Nation (AGN) conducted performance audits on the government's program to prevent and control Chagas (a parasite-driven infection that affects 1.5 million people, mostly of modest means). In 2018, the AGN found that allocated funds were both insufficient and not spent as planned. Moreover, staff was limited and there was little coordination with the provinces. The AGN called for the implementation of the Chagas Prevention and Control Law and sufficient state investment to address Chagas.

In June 2019, the civil society organization, Asociación Civil por la Igualdad y la Justicia (ACIJ), met with the AGN to discuss the 2018 report. ACIJ recommended more substantial input from civil society to help raise awareness about Chagas. The meeting encouraged the AGN to continue monitoring the program's finances. As part of their strategy, the SAI sent its report to the Mixed Review and Children's Commission while ACIJ cultivated individual members on the Commission to encourage them to review spending on Chagas, developed alliances with medical professionals and affected families, and engaged with relevant ministries.

As a result, in August 2020, the Ministry of Health began an ongoing process to regulate the Chagas Prevention and Control Law. In October 2020, the annual budget proposal included the highest planned funding related to Chagas in 10 years. The government also initiated the opening of 18 regional offices for Chagas control. In addition, the government collaborated with ACIJ in a trans-disciplinary working group for communication and education about Chagas. ACIJ and its allies developed sensitization materials for distribution through national TV channels and continue to monitor spending and results to prevent, diagnose, and treat Chagas. The Ministry of Health and the Ministry of Education are now legally responsible for producing Chagas education materials to distribute from preschool to university level.

As a consequence of ACIJ and allies' work, during 2022, the President of Argentina enacted a new regulation to facilitate the implementation of the Law and the Ministry of Health created the National Chagas Program. All of these important developments were recommendations of the AGN's 2018 report.

Sources: Chagas. A current problem, an outstanding debt. State responsibility in neglected endemic diseases. <https://acij.org.ar/chagas-una-problemativa-vigente-una-deuda-pendiente-la-responsabilidad-estatal-en-las-enfermedades-endemicas-desatendidas/> and <https://proyecto-chagas.acij.org.ar/>

## Box 7.12. SAI Ghana works with civil society to enhance audit impact

In Ghana, the Audit Service has long adhered to the value of working with stakeholders, including civil society, to enhance audit impact.

A couple of examples:

1. In 2017, civil society went to court and won a verdict allowing the SAI to recover approximately \$12 million of misappropriated funds.
2. More recently, the civil society organization, SEND GHANA, and the Audit Service have collaborated on tackling gross financial irregularities and mismanagement in the country's flagship "School Feeding Program" (SFP), a critical service affecting 3.3 million pupils. SEND Ghana amplified the audit report's findings and recommendations by broadcasting them across radio, newspapers, and social media and conducted complementary research on the SFP catering contracts to assess compliance with procurement standards. Moreover, they convened various stakeholders at the national, regional, and district levels, including the Ghana School Feeding Program Secretariat, the Ministry of Food and Agriculture, representatives of the Ghana Education Service, district assembly officials, caterers, school management committees, school health education program coordinators, and more.

The responsible stakeholders agreed to implement measures to address the major challenges in the SFP, including the procurement and allocation processes, timely payment of caterers, and the provision of higher quality food to pupils. In early December 2021, the Minister of Gender, Children, and Social Protection reassured that the remaining arrears owed to SFP caterers would be settled soon and an information management system would be established to ensure effective and efficient service delivery to all beneficiary schools as well as the caterers.

Civil society-led consultations – with more than 400 representatives from traditional authorities, women and adolescent girls, people with disabilities, and opinion leaders on their social sector priorities – led to the inclusion of the School Feeding Program as a priority (budget credibility) issue in the citizen manifestos presented to political parties ahead of the national elections.

Ghana's civil society continues to defend the independence of the Audit Service, to engage with them to identify audit topics and to advocate for the timely publication and uptake of audit reports.

Sources: <https://internationalbudget.org/sai-cso-collaboration/>; <https://newsghana.com.gh/lets-de-politicise-recruitment-of-gsfp-caterers/>; <https://allafrica.com/stories/202112170205.html>; <https://thebftonline.com/2021/12/16/school-feeding-grant-still-gh%C2%A21-per-plate/>



### **Box 7.13. SAI Colombia and CSOs work together through a practice of articulated audits**

In Colombia, the articulated audit (AA) is a practice of participatory fiscal control through which CSOs with deep knowledge about an audited entity support the auditing process of the General Comptroller of the Republic of Colombia (CGR). In essence, the social control action carried out by CSOs articulates with the fiscal control processes run by the CGR.

The CGR and the CSOs bring their priorities to the table and jointly establish monitoring mechanisms. The articulation between the CSOs and the CGR is carried out through at least a couple of meetings. The first is held during the planning stage of the AA, where the CSO provides inputs and makes contributions that are validated by the audit group. The other meeting is held at the end of the process where the final audit report is presented and shared. Informative meetings could also be scheduled during the execution period of the audit at the request of citizens. If required, the CSO may also contribute to the process of collecting information related to the object of the AA.

The CSO provides the citizen's perspective on the work of the audited entity so that the auditors can include it in their financial, compliance or performance analyses.

Source: Marcos Mendiburu, 2020. La participación ciudadana en las entidades fiscalizadoras superiores en América Latina: ¿avance o impasse?, p. 43-44 <https://www.rendiciondecuentas.org.mx/wp-content/uploads/2020/05/PANORAMA-mayo2020.pdf>

### **Box 7.14. SAI Nepal formalizes a process to work with CSOs**

In Nepal, the Office of the Auditor General began organizing roundtable discussions with CSOs in 2013 and formalized the process by developing a CSO Engagement Guideline and aligning it to the SAI's five-year strategic plan. The SAI has identified several areas where CSOs can make meaningful inputs. The audit planning phase is one of the key areas. It provides an opportunity to solicit inputs from CSOs on important areas for performance audits and risk areas related to the financial audits. The SAI also uses the opportunity of their relationship with CSOs to collect feedback and evidence on budget credibility, i.e., the use of resources, the impact of programs, and service delivery.

Source: INTOSAI Capacity Building Committee, 2021. SAI and Civil Society Engagement – Good Practices, p. 4 [https://www.intosaicbc.org/wp-content/uploads/2021/06/20210629-Engagement-with-Civil-Society\\_A-Framework-for-SAIs\\_CBC\\_28-June-2021\\_fnl.pdf](https://www.intosaicbc.org/wp-content/uploads/2021/06/20210629-Engagement-with-Civil-Society_A-Framework-for-SAIs_CBC_28-June-2021_fnl.pdf)

Increasingly fruitful collaboration emerging between SAIs and civil society in various earlier phases of the budget process (examples of which are sprinkled throughout this handbook) hold promise for stronger constructive interaction during the follow-up and monitoring stages of the auditing process, too.

## 7.4. Summing up

Successful follow-up is integral to ensuring audit recommendations are implemented and will improve budget credibility. This depends on many factors, including:

- **Quality recommendations:** are they well-determined, clear, specific, and attainable?
- **Productive collaboration between the SAI and the auditee** – the more exchange between the two, the more likely implementation will be successful. Meeting with the auditee before the release of the audit report, ensuring the auditee writes up an action plan so that both the SAI and the auditee can keep track of

achievements, and/or setting deadlines for implementation are essential to propelling progress forward.

- **Engagement with the legislature, the executive, civil society, and other stakeholders** for support on monitoring and incentivizing action is key. Achieving maximum impact requires teaming up with others. Annex 7.1 presents a sample list of the kinds of actions that the SAI can take, most of them with other stakeholders, not only in the monitoring stage but also in earlier stages of the audit process, to put the focus on and ultimately to strengthen budget credibility.

Good audit work will be reflected in the improvement of governance and service delivery. The quality and conscientious communication of findings and recommendations, productive follow-up with auditees, and thoughtful engagement with relevant stakeholders will make it happen.

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# Annexes

## ANNEX 2.1. Selected credibility-related issues and risks examined by SAIs<sup>1</sup>

Budget area	Issue examined by SAI	Potential effect in terms of budget credibility
Governance framework	Budget policy and debt management	Strategic use of budget deficits can undermine budget credibility.
	Mandatory spending cuts—e.g., to achieve deficit targets	Timing, amount, and distribution of in-year mandatory cuts may cause systematic underspending in certain sectors and affect the predictability of budget flows.  Limited transparency of spending cuts and their impacts undermines credibility assessments.
Planning and preparation	Economic modeling (macro forecast)	Poor revenue forecasting creates credibility risks.
	Revenue estimation	Errors in revenue estimation create risks of overruns.
	Planning processes—e.g., setting spending ceilings, priorities, etc.	Unrealistic spending targets make it difficult for entities to absorb funds and lead to underspending.
Approval	Legislative amendments—when applicable	Underspending of funds authorized by the legislature through amendments due to, e.g., electoral considerations while disregarding technical and capacity aspects.
	Circumventing approval	Excessive aggregation or otherwise inappropriate categorization of spending facilitates circumventing legislative approval, creating credibility risks related to in-year reallocations or overruns.
Execution and implementation	Management capacity and procedures	Inconsistencies across information systems create risks of overruns or underspending.  Inconsistent legal frameworks and weak administrative procedures create risks of overruns or underspending with impacts on service delivery.
	Documentation of expenditures	Lack of integration of all spending (e.g., supplementary) in integrated financial systems creates overrun risks.
	Estimation of costs/spending	Bad cost estimation makes it impossible to check against spending to manage and prevent overruns with potential impact on service delivery.
	Timing of spending	Differences in timing between authorization and actual spending facilitates unauthorized spending that may deviate from the approved budget.
	Generation, capture and management of performance information	Weak systems to capture performance information—including lack of, insufficient or inappropriate performance indicators and targets—affect the ability to assess impact of executed budget and to identify negative effects of non-credible budgets.

Budget area	Issue examined by SAI	Potential effect in terms of budget credibility
Control and oversight	Rule compliance	Unlawful spending, due for example to poor and untimely cost estimation, creates credibility risks.
	Internal controls	Weak internal controls or capacity constraints for internal oversight create credibility risks, given the potential lack of detection and sanction.
	Reporting, including to Parliament and SAI	Excessive aggregation of spending makes it difficult for the legislature to assess budget availability and detect credibility problems. Poor information and reporting problems make it difficult for oversight actors to assess whether spending has proceeded according to plan and whether results correspond to execution.

[1] Based on a sample from 80 audit reports from 20 countries. See Guillán Montero, 2021.

### ANNEX 3.1. Questions to ask about potential budget credibility risks at the whole-of-government level

Stage of the budget cycle	Potential budget credibility risks	Guiding questions
Budget formulation	Un-realistic revenue and expenditure forecasts	<ul style="list-style-type: none"> <li>• What is the quality of revenue planning as a whole?</li> <li>• Is there a system through which revenue estimates are forecast?</li> <li>• Are there adequate procedures and guidelines for the forecasting process?</li> <li>• Are the forecasts comprehensive? Do they identify and assess all the potential sources of revenue?</li> <li>• Are the assumptions used in generating the forecasts realistic, based on realistic macroeconomic indicators?</li> <li>• Are the models used in generating the forecasts reliable?</li> <li>• Are the models aligned to current legislation and government policy?</li> <li>• Are there contingency plans in case of unforeseen occurrences that may disrupt revenue performance?</li> <li>• Does the team producing the forecasts have adequate skills and know-how?</li> <li>• Is there a relationship between the expenditure forecasts and revenue forecasts?</li> <li>• Are the expenditure forecasts reliable and reasonable?</li> <li>• Are the deficit financing provisions realistic?</li> <li>• Are the cost of government policies and programs, and therefore expenditures, realistically calculated (e.g., assumptions about inflation, exchange rates...)?</li> </ul>
	Misalignment of budgets to long-term planning frameworks and SDGs	<ul style="list-style-type: none"> <li>• Are the priorities within the national budget aligned with the national planning frameworks?</li> <li>• Is there a system in place to ensure that the annual budget is aligned with national planning frameworks?</li> <li>• In cases where non-alignment was noted, what has been the impact/effect of such an occurrence?</li> <li>• What are the causes of any non-alignment, who is responsible and how can these be addressed?</li> <li>• What has been the trend in terms of alignment in previous years? Is this systemic or a one-off occurrence?</li> </ul>
Budget approval	Delayed approval of the budget by the legislature	<ul style="list-style-type: none"> <li>• Are the requirements of the law clearly known and understood?</li> <li>• Did the executive comply with the timelines for budget approval?</li> <li>• If cases of non-compliance are identified, what is the cause?</li> <li>• How does non-compliance affect revenue and expenditure performance?</li> </ul>

Stage of the budget cycle	Potential budget credibility risks	Guiding questions
Budget execution	Implementation of unapproved and off-budget activities	<ul style="list-style-type: none"> <li>• Is there a system in place to ensure that the executive does not include unapproved activities within the budget?</li> <li>• What were the non-approved activities included and who was responsible?</li> <li>• What was the cause of circumventing approvals for the unapproved activities?</li> <li>• What was the effect of these non-approved activities on revenue and expenditure performance?</li> <li>• In cases where the budgets have been revised, were the revisions approved by the legislature or other necessary authorities, as required?</li> <li>• Is the practice of circumventing approvals entrenched or are the cases noted one-offs?</li> </ul>
	Financial indiscipline within the executive and legislature	<ul style="list-style-type: none"> <li>• Is there a clear system to minimize political interference in the activities of the technocrats?</li> <li>• Have there been past occurrences of interference and what was the effect of this interference?</li> <li>• Are the roles and responsibilities of each of the players well-defined and not in conflict?</li> <li>• Where interference was noted, what was the cause and who was responsible?</li> </ul>
	Limited capacity to absorb budget shocks due to emergencies	<ul style="list-style-type: none"> <li>• Are there provisions within the budget laws for emergencies?</li> <li>• Is the budget, as prepared by the executive, reflective of current economic trends?</li> <li>• Is the budget flexible enough to absorb shocks?</li> </ul>
Budget reporting and accounting	Ineffective reporting and accounting systems	<ul style="list-style-type: none"> <li>• Do government performance and statistical systems produce performance information that is accurate and reliable?</li> <li>• Do the reports produced from the monitoring and reporting systems facilitate performance analysis including understanding and identifying performance deviations, and understanding trends?</li> <li>• Are performance data and reports easily accessible to users and stakeholders?</li> <li>• Does the system link the performance information to the delivery of services?</li> <li>• Does the system of monitoring and reporting budget implementation track performance for assessment of long-term outcomes?</li> <li>• Is the team responsible for budget monitoring and reporting adequately skilled and equipped?</li> </ul>



Stage of the budget cycle	Potential budget credibility risks	Guiding questions
External oversight and evaluation	The capacity of, and incentives for, the SAI and the legislature to provide external evaluation	<ul style="list-style-type: none"> <li>• Does the SAI have an adequate mandate to undertake reviews of the budget?</li> <li>• Does the SAI have adequate expertise to undertake reviews of budget credibility?</li> <li>• Are legislative discussions and resolutions regarding the budget open or relayed to the public?</li> <li>• Does the SAI have a functioning system for monitoring and following up on audit recommendations?</li> <li>• Does the legislature approve the audits of budget execution on a timely basis?</li> <li>• Does the SAI engage regularly with parliament on budget oversight and evaluation?</li> </ul>

#### ANNEX 4.1. Applying the RIAS method to examine the performance of expenditure management – an example from SAI Indonesia

A RIAS form is used for the following audit:

**Audit Objective:** To assess the effectiveness of expenditure management by the central government in the framework of performance-based budgeting

**Audited Entities:** (1) Ministry of Finance; (2) Ministry of National Development Planning; (3) Ministry of Health

**Audit Scope:** The budget year 2018 and the first semester of 2019

No.	Potential Key Areas To Be Audited	Selecting Factor (Score) <sup>6)</sup>				Total Score	Order of Priority of Key Area	Decision (Chosen/ Unchosen) <sup>5)</sup>
		Risk <sup>1)</sup>	Impact of Audit <sup>2)</sup>	Auditability <sup>3)</sup>	Significance <sup>4)</sup>			
1	Design of Performance-Based Budgeting	2,13 <sup>1)</sup>	2,50 <sup>2)</sup>	2,75 <sup>3)</sup>	2,00 <sup>4)</sup>	8,38	4	Unchosen
2	Planning and Budgeting	2,50 <sup>1)</sup>	2,33 <sup>2)</sup>	2,75 <sup>3)</sup>	2,33 <sup>4)</sup>	8,91	2	Chosen
3	Budget Execution	2,50 <sup>1)</sup>	2,83 <sup>2)</sup>	2,75 <sup>3)</sup>	2,33 <sup>4)</sup>	9,41	1	Chosen
4	Monitoring and Evaluation	2,25 <sup>1)</sup>	2,67 <sup>2)</sup>	2,75 <sup>3)</sup>	2,00 <sup>4)</sup>	8,67	3	Chosen

- Risk** is related to how much risks are faced by management in achieving the objectives set out in the economy, efficient, and effective framework. (See Annex 4.1.1)
- Impact** is related to how much benefit and improvement could be gained by the entities if they implemented the audit recommendations on each key area. (See Annex 4.1.2)
- Auditability** is related to the feasibility of an area to be audited by considering factors such as the number of auditors and audit location. (See Annex 4.1.3)
- Significance** is related to how significantly a program/activity will contribute to the organization's goal. (Annex 4.1.4)
- Subject to auditor professional judgment. The audit team may choose one or more potential key areas to be audited. The decision takes into account the available audit resources.
- Scoring Scale:** – High: 3; Medium: 2; Low: 1

Note: In the tables on the following pages, the blank spaces in this example are normally meant to be filled out. Also, the factors included in each table are subject to the auditor's professional judgment.

### ANNEX 4.1.1 – RISK

No	Potential key areas to be audited	RISK FACTORS																Average Score
		A		B		C		D		E		F		G		H		
		Score	Desc.	Score	Desc.	Score	Desc.	Score	Desc.	Score	Desc.	Score	Desc.	Score	Desc.	Score	Desc.	
1	Design of Performance-Based Budgeting	2	By design, budgeting is prepared based on the performance of the previous 2 years	3		3		2		3		2		1		1		2,13
2	Planning and Budgeting	2		3	The performance targets listed in the Work Plan were not achieved significantly	2		3		3		3		2		2		2,50
3	Budget Execution	3		3		3	No changes were made to address the overspending of personnel spending	2		2		3		2		2		2,50
4	Monitoring and Evaluation	2		1		2		2		3	Multiple government agencies involved	3		2		3		2,25

#### RISK FACTORS

- A. Significant under/over budget spending
- B. Not achieving the goals that have been set
- C. Management does not react to weaknesses found
- D. Sudden program expansion
- E. Relationships of responsibilities that are overlapping, unclear or confusing
- F. Activities that are complex in an environment full of uncertainty
- G. Lack of security of electronic data and/or information systems
- H. Indication of Non-compliance Audit Finding

## ANNEX 4.1.2: IMPACT OF AUDIT

No	Potential key areas to be audited	IMPACT OF AUDIT FACTORS												Average Score
		A		B		C		D		E		F		
		Score	Desc.	Score	Desc.	Score	Desc.	Score	Desc.	Score	Desc.	Score	Desc.	
1	Design of Performance-Based Budgeting	3	Improvement in implementation and measurement of achievement	3		3		2		2		2		2,50
2	Planning and Budgeting	3		3	Improvement in standardization of performance indicators, related to the determination of outputs and outcomes	3		2		2		1		2,33
3	Budget Execution	3		3		3	Improve the transparency and accountability of budget execution performance outcomes	3		3		2		2,83
4	Monitoring and Evaluation	3		3		3		3	Encourage the government to use the performance information reported to develop more efficient planning by taking into account past performance achievements	3		1		2,67

### IMPACT OF AUDIT FACTORS

- A. Effectiveness
- B. Improved planning, control, and management
- C. Increased accountability
- D. Efficiency
- E. Economic
- F. Service Quality Improvement

### ANNEX 4.1.3: AUDITABILITY

No.	Potential key areas to be audited	AUDITABILITY FACTORS							Average Score
		A				B	C	D	
		A.1	A.2	A.3	TOTAL				
1	Design of Performance-Based Budgeting	2	2	2	2	1	2	2	1,75
2	Planning and Budgeting	2	2	2	2	1	2	2	1,75
3	Budget Execution	2	2	2	2	1	2	2	1,75
4	Monitoring and Evaluation	2	2	2	2	1	2	2	1,75

### AUDITABILITY FACTORS

- A. Personnel
  - A.1. Auditor skills/expertise
  - A.2. Auditor's experience of the area to be audited
  - A.3. Number of auditors
- B. Time available to conduct the audit
- C. Significant changes to the entity
- D. Audit Location

#### ANNEX 4.1.4: SIGNIFICANCE

No.	Potential key areas to be audited	SIGNIFICANCE FACTOR						Average Score
		Materiality		Critical Limit of Success		Visibility		
		Score	Description	Score	Description	Score	Description	
1	Design of Performance-Based Budgeting	1		2		3	Weaknesses in the design will significantly affect the achievement of the expected outcomes for the public	2,00
2	Planning and Budgeting	1		3	If problems are resolved, will have a significant impact on the overall performance-based budgeting process	3		2,33
3	Budget Execution	2	The budget and realization of the sampled area are material	2		3		2,33
4	Monitoring and Evaluation	1		2		3	Disorderly reporting of monitoring and evaluation results and invalid data will make it difficult to see how far a program or activity has achieved the expected results	2,00

#### SIGNIFICANCE FACTOR

**Financial materiality** is based on the valuation of the assets controlled and the amount of revenue and expenses managed by the audited entity. The higher the level the financial materiality of an activity/program/field, the higher likely to be a key area to be selected as audit scope. Materiality in financial audits and performance audits may vary and the same object can be viewed differently. Therefore, an object/area could be considered as material from the performance audit point of view, but immaterial from the financial audit perspective, and vice versa.

**Critical Limit of Success:** The critical aspect of success limits shows the importance of an area in determining the success of an entity. If improvements significantly impact the entity's operations, the significance will be high. For a job that is routine and improves the performance of an object, but does not have a broad impact on the performance of the entity, the level of significance is relatively low.

**Visibility:** The visibility or clarity of an area is closely related to the external impact of an activity/program/field. This relates to the social, economic, and environmental aspects of the activities/programs/fields and the importance of these activities to government or community programs. For example, performance audit in the area of land service management at a land office.

## ANNEX 4.2. Draft audit design matrix (ADM) to assess the performance of expenditure management – an example from Indonesia

**Audit Objective:** To assess the effectiveness of expenditure management by the central government in the framework of performance-based budgeting

**Audited Entities:** Ministry of Finance (MoF), Ministry of National Development Planning (MoNDP), Ministry of Health (MoH)

**Overall Audit Question (Level 1):** Has the management of central government expenditure been effective – within a performance-based budgeting framework?

- **Audit Question (Level 2):** 1.1. Are activities and expenditures of Government Ministries planned and budgeted in a measurable manner and as needed?
  - **Audit Question (Level 3):** 1.1.1 Is the budgeting of expenditure consistent with the planning of activities?

Audit Criteria	Criteria References	Audit Evidence	The Sources of the Audit Evidence	Audit Evidence Acquisition Method	Audit Procedure	Audit Risk / Limitation / Constraint	Mitigation of Audit Risk / Limitation / Constraint	Potential Audit Finding	Potential Audit Conclusion (level 3)	Potential Audit Conclusion (level 2)	Potential Audit Conclusion (level 1)	Potential Audit Recommendation	Expected Added Value/ Benefits
Type and volume of activity output stipulated in the planning document/ Work Plan is in accordance with what is stated in the budget document	1 Act no 25 (2004) Chapter 2; 2 Government Regulation No. 17, (2017) Chapter 23 3 Research Study of ...	1 Work Plan 2 Budget document (Country-specific).	1 MoNDP 2 MoF 3 Government Agency (sample).	1 Inspection 2 Analyzing the procedure 3 Query/ Interview.	1 Inspect the Work Plan and Budget Document to know whether the type and volume of activity output specified in the Work Plan are the same as those outlined in the Budget document.  2 If there are differences and the budget is approved by the parliament, ensure that the MoNDP approves the intended change and has accommodated it in the changes to Work Plan  3 If the budget hasn't been approved by the parliament, make sure the budget document is given a special note/mark;	1 Documents are restricted  2 Poor Documentation.	1 Prepare documents requests well in advance (spare enough time)  2 Prepare a high-level official meeting if needed	There is a discrepancy between the type and volume of activity output stipulated in the planning document and that set forth in the budget document.	The budgeting of expenditure is not consistent with the planning of activities	Activities and expenditures of Government Ministries have not been budgeted as needed	The management of central government quality expenditure in the budgeting activities has not been effective	Build and develop an information system to enhance the synchronization and alignment of planning and budgeting processes.	Improvement in the alignment of planning and budgeting processes to ensure the achievement of National Priority targets that has been planned by the government.

Audit Criteria	Criteria References	Audit Evidence	The Sources of the Audit Evidence	Audit Evidence Acquisition Method	Audit Procedure	Audit Risk / Limitation / Constraint	Mitigation of Audit Risk / Limitation / Constraint	Potential Audit Finding	Potential Audit Conclusion (level 3)	Potential Audit Conclusion (level 2)	Potential Audit Conclusion (level 1)	Potential Audit Recommendation	Expected Added Value/ Benefits
					<p>4 Ensure that there is approval for the differences in budget documents from the MoF.</p> <p>5 Analyze the impact of the differences on the achievement of the planned targets.</p>								
<p>Other criteria could include, for example:</p> <p>1.1.2: Type and volume of activity output of new initiatives/ policies as outlined in the budget document are referenced in the National Work Plan;</p> <p>1.1.3: Classification and naming of programs and targets of program/activity/output in the Budget Document are consistent with the Work Plan;</p> <p>1.1.4: All changes to the formulation of programs and/or activities arising from the reorganization have been accommodated in changes to the Work Plan and Budget Document</p>													

### Notes:

- Overall Audit Question (level 1) is designed to answer the audit objective.
- Based on the overall audit questions (level 1), the Auditor breaks down the question into several sub-questions (level 2). There can be more than one level 2 question to support and answer the level 1 question. Normally, the level 2 questions are in line with the key area to be audited.
- Based on the level 2 audit questions, the auditor breaks down the question into several sub-sub questions (level 3). There can be more than one level 3 question for each level 2 question.
- In designing the hierarchy of audit questions, auditors must ensure that sub-audit questions at the lowest level will be answered by carrying out certain audit procedures. Sub-audit questions at the lowest level will also refer to specific criteria which will be used, and at the same time become the basis for collecting audit evidence. Audit criteria are designed based on the audit question at the lowest level (level 3). The audit criteria should consider several characteristics which are relevant, understandable, complete, reliable, objectives, and auditable.



### ANNEX 5.1. Draft planning matrix for a comprehensive year-end audit

**ENTITY:** The National Government, the Ministry of Finance, and line ministries

**OBJECTIVE:** To express an opinion on the adequacy of the country's financial and budgetary statements; to examine the soundness of fiscal policy and the adequacy of financial statements

AUDIT QUESTION	AUDIT CRITERIA	REQUIRED INFORMATION	SOURCES OF INFORMATION	PROCEDURE RELATING TO ANALYSIS OF DATA	LIMITATIONS <sup>2</sup>	WHAT CONCLUSIONS CAN BE DRAWN FROM THE ANALYSES
Are imbalances in the government's financial statements fairly presented and free from material misstatements?	IPSAS (International Public Sector Accounting Standards) and national regulations	Consolidated financial information from the fiscal year.  Data on critical transactions	Financial statements and accounting notes  Statements related to financial transactions in the public sector	Financial audit of the government's accounting statements  Compliance audit procedure	Identify any limitations associated with the information required, planned methodology or your general ability to answer the audit question.  Limitations could include questionable data quality or reliability, inability to access some information, constraints on staffing or travel funds, or inability to generalize or extrapolate findings to the universe.	An opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework.  This strengthens budget credibility by furnishing independent assurance on the adequacy of public-sector financial information.

AUDIT QUESTION	AUDIT CRITERIA	REQUIRED INFORMATION	SOURCES OF INFORMATION	PROCEDURE RELATING TO ANALYSIS OF DATA	LIMITATIONS <sup>2</sup>	WHAT CONCLUSIONS CAN BE DRAWN FROM THE ANALYSES
Has the budget execution during the year been compatible with legislative authorizations?	Budget law and legislation governing budget execution	Information on budgetary execution, regarding revenue collection and expenditure disbursement  Legal criteria that govern budget execution	Approved budget legislation and regulations  Statements related to government revenue and expenditures in the fiscal year  Prior recurring audits and standalone audits conducted by the SAI	[Compliance audit procedures on budget execution statements, with a focus on legislative authorizations for the fiscal year]	Identify any limitations associated with the information required, planned methodology or your general ability to answer the audit question.  Limitations could include questionable data quality or reliability, inability to access some information, constraints on staffing or travel funds, or inability to generalize or extrapolate findings to the universe.	A conclusion on the regularity of budget execution considering legislative authorizations applicable for the fiscal year.  The verification of the regularity of budget appropriations conveys the lawfulness of the government's discharge of fiscal management, thereby underscoring credibility in public finance.
Have applicable fiscal rules been followed during budget execution?	Legislation governing budget execution Best practices on budget execution	Information on budget execution, regarding revenue collection and expenditure disbursement.  Legal criteria and best practices that promote sound fiscal management	Statements related to government revenue and expenditures in the fiscal year  Permanent domestic fiscal rules.  International best practices on budget execution (e.g., OECD Principles for Budgetary Governance).  Prior recurring audits and standalone audits conducted by the SAI.	[Compliance audit procedures on budget execution statements, with a focus on fiscal rules and best practices criteria]	Identify any limitations associated with the information required, planned methodology or your general ability to answer the audit question.  Limitations could include questionable data quality or reliability, inability to access some information, constraints on staffing or travel funds, or inability to generalize or extrapolate findings to the universe.	A conclusion on the regularity of budget execution considering fiscal rules and applicable international best practices.  Auditors' oversight considering fiscal rules provides additional assurance at a higher level, beyond that of individual procedures, that budgetary management warrants credibility, in terms of rules and best practices on fiscal targets, general budgeting principles, and other overarching criteria.
Are macroeconomic assumptions that underlie the budget adequate?	Market projections for macroeconomic variables	Information on the assumptions that led the government to propose and approve the budget, regarding revenues and expenditures.	Budget draft and ancillary reports (such as the pre-budget statement) published prior to budget approval  Independent public- and private-sector projections for macroeconomic variables.  Prior recurring audits and standalone audits conducted by the SAI.	[Compliance audit procedures on the assumptions that underlie the budget]	Identify any limitations associated with the information required, planned methodology or your general ability to answer the audit question.  Limitations could include questionable data quality or reliability, inability to access some information, constraints on staffing or travel funds, or inability to generalize or extrapolate findings to the universe.	A conclusion on the regularity of the macroeconomic assumptions that substantiate projected revenues and expenses for the fiscal year.  This contributes to the credibility of budget preparation and its feasibility. Incorrect assumptions tend to be overly optimistic, inflating figures that may prove to be unrealistic during and after budget execution.

AUDIT QUESTION	AUDIT CRITERIA	REQUIRED INFORMATION	SOURCES OF INFORMATION	PROCEDURE RELATING TO ANALYSIS OF DATA	LIMITATIONS <sup>2</sup>	WHAT CONCLUSIONS CAN BE DRAWN FROM THE ANALYSES
Has the government delivered goods and services in an effective manner?	Technical benchmarks and best practices on policy evaluation	Information on the economy, efficacy and effectiveness of public policies in the fiscal year.	Government reports on policy results, results from critical indicators and target attainment for policy outcomes in the fiscal year.  Independent public- and private-sector reports on public policy outcomes in the fiscal year.  Prior recurring audits and standalone audits conducted by the SAI.	[Performance audit procedures on public policy outcomes in the fiscal year]	Identify any limitations associated with the information required, planned methodology or your general ability to answer the audit question.  Limitations could include questionable data quality or reliability, inability to access some information, constraints on staffing or travel funds, or inability to generalize or extrapolate findings to the universe.	A conclusion on the outcomes of selected government programs in the fiscal year.  This ratifies the credibility of the government's aptitude to deliver the goods and services outlined in the budget.
Does the national public debt have a sustainable outlook?	Technical benchmarks and best practices on public debt management	Government data describing the trajectory of public debt and budget balance  Independent opinions on the outlook of the public debt.	Government reports on the evolution of public debt.  Government reports on budget execution and projected trajectory in the future.  Independent public- and private-sector reports on the evolution of public debt.  Prior recurring audits and standalone audits conducted by the SAI.	[Compliance audit procedures on the projection for public debt]  Financial audit procedure	Identify any limitations associated with the information required, planned methodology or your general ability to answer the audit question.  Limitations could include questionable data quality or reliability, inability to access some information, constraints on staffing or travel funds, or inability to generalize or extrapolate findings to the universe.	A conclusion on the regularity of public debt outlook considering its projected trajectory and desirable debt sustainability.  The verification of the trajectory of public-sector indebtedness corroborates credibility in the government's capacity to finance its activities.

<sup>2</sup> Adapted from: <https://www.idi.no/elibrary/professional-sais/issai-implementation-handbooks/handbooks-english/performance-audit-v1-2021/1342-chapter-4-pa-handbook-v1-2021/file>

### ANNEX 6.1. Selection criteria for budget credibility audits

Criteria <sup>3</sup>		Factor (generic) <sup>4</sup>	Budget credibility aligned questions
1	Materiality	<ul style="list-style-type: none"> <li>Is the topic important to the government/the public/the audited entity (national priority) and does it involve a critical area?</li> </ul>	<ul style="list-style-type: none"> <li>Is the government program/activity financially and operationally significant to the government, the public, or the audited entity?</li> </ul>
2	Possible impact	<ul style="list-style-type: none"> <li>Will the topic have a powerful effect on enhancing the economy, efficiency, and effectiveness of government undertakings?</li> </ul>	<ul style="list-style-type: none"> <li>Will the topic have a positive effect on the planning and spending capacities and arrangements of government entities?</li> <li>Will the audit lead to the achievement of the set goals and priorities in government programs, activities, and projects?</li> </ul>
3	Improvement	<ul style="list-style-type: none"> <li>Will the audit lead to improvements in government?</li> </ul>	<ul style="list-style-type: none"> <li>Will the audit evaluate significant governance aspects of government entities in relation to budget execution?</li> <li>Will the audit provide advice/recommendations to ensure that there will be fewer or no deviations in government entities' budgets?</li> </ul>
4	Legislative or public interest	<ul style="list-style-type: none"> <li>Will the topic address a legal concern or otherwise be to the advantage of the community?</li> </ul>	<ul style="list-style-type: none"> <li>Will the audit cover budget aspects and considerations involving the legislature?</li> <li>Is the topic responsive to the interest of the general public pertaining to the allocation and use of the budget?</li> </ul>
5	Risks to SAIs	<ul style="list-style-type: none"> <li>Will the topic present risk/s (strategic or reputational) to the SAI?</li> </ul>	<ul style="list-style-type: none"> <li>Does the SAI have the technical expertise to undertake the audit of budget credibility for this government program/activity?</li> </ul>
6	Relevance	<ul style="list-style-type: none"> <li>Does the topic have some bearing on, or importance for, real-world issues, present-day events, or the current state of society?</li> </ul>	<ul style="list-style-type: none"> <li>Will the audit of budget credibility for this government program/activity provide bearing information regarding the country/public/world's concern, example SDGs?</li> </ul>
7	Timeliness	<ul style="list-style-type: none"> <li>Is this the right or appropriate time to audit the topic?</li> </ul>	<ul style="list-style-type: none"> <li>What current issue/s or concern/s will the audit of this government program/entity resolve?</li> <li>Is there another program/activity that is of urgent concern for an audit?</li> </ul>
8	Auditability	<ul style="list-style-type: none"> <li>Can the topic be audited? Is it practical to audit? Does it fall within the legal mandate of the SAI? Does audit evidence exist and is it accessible by the audit team in a format that can be easily collected and analyzed?</li> </ul>	
9	Other major works planned or in progress	<ul style="list-style-type: none"> <li>Is there work being planned or done on the topic?</li> </ul>	<ul style="list-style-type: none"> <li>Will the audit of this program/activity be supplemental or congruent with work that is currently being implemented or planned?</li> </ul>
10	Request for audit	<ul style="list-style-type: none"> <li>Have any special requests been made for audits to be done?</li> </ul>	

<sup>3</sup>The INTOSAI PAS Guideline on selecting PA topics presents 15 criteria. Out of the 15, ten were used and aligned with the budget credibility lens.

<sup>4</sup>Adopted from INTOSAI PAS Guideline on selecting PA topics. Retrieved from: PAS Guideline 1 Selecting Performance Audit Topics - 2013 - AFROSAI-E

## ANNEX 6.2. Self-checklist for assessment of budget credibility risks at program/entity level

This checklist provides basic guidance for auditors to verify the activities performed and their compliance with the recommended direction. It may be used for monitoring purposes during the audit or for quality assurance after the audit process. To keep it relevant to the audit environment, the list can be enhanced or modified depending on the SAI context and the recommendations of the SAI's audit authorities. It can also be integrated with the SAI's quality control checklist/s to ensure that the activities comply with applicable audit standards.

ANNEX 6.2. Self-checklist for assessment of budget credibility risks at program/entity level						
Entity audited		:				
Program/Project/Activity/Accounts Audited		:				
Period covered		:				
Auditor/Names of Audit Team Members		:				
Activities / Questions		Yes	No	NA	Remarks	Audit WP Reference
<b>Mandate and independence of the SAI to conduct budget credibility audit</b>						
1	The SAI is free from direction and interference in the selection of audit issues, planning, conduct, reporting, and follow-up of their audits (ISSAI 10:3).					
2	There is a law that provides the SAI with unrestricted right of access to records, documents, and information (ISSAI 1:10).					
3	The SAI has the right to decide which information it needs for its audits (ISSAI 1:10).					
4	The SAI staff have the right of access to the premises of audited bodies in order to do the fieldwork the SAI deems necessary. (ISSAI 1:10).					
<b>Selecting audit topic</b>						
5	Budget credibility audits are included in the SAI's strategic audit plan for the year.					
6	In case the SAI does not specify the budget credibility area as a priority theme in its audit plan, there are specific sectoral/office audit instructions from appropriate officials within the SAI.					
7	The SAI has undergone the process of understanding the risk factors for critical areas for audit (sectoral programs and government-wide activities).					
8	The SAI determined the selection criteria in determining the audit topic.					

<b>ANNEX 6.2. Self-checklist for assessment of budget credibility risks at program/entity level</b>							
<b>Planning</b>							
9	The auditor performed a pre-study for the selected audit topic.						
10	The auditor determined whether to conduct a risk assessment on budget credibility separately/integrated with the general audit of the program/entity.						
11	The auditor conducted a risk assessment for the selected topic based on the budget credibility risk factors.						
12	The auditor identified a budget credibility-aligned risk response to the risk identified.						
13	The auditor determined the audit approach (exclusive audit focus; integrated with another audit; relating the findings with budget credibility).						
14	The auditor defined distinct audit objective/s and questions for assessing budget credibility risks.						
15	The auditor defined the scope of the audit based on the selected budget credibility approach.						
16	The auditor identified budget credibility-related criteria.						
17	The auditor specified budget credibility in preparing the audit plan and overall strategy.						
<b>Conducting</b>							
18	The auditor collected and analyzed budget-related evidence against the identified audit criteria.						
19	The auditor formulated audit findings and related their elements (criteria, condition, cause, and effect) to budget credibility.						
20	The auditor developed audit conclusions and recommendations based on audit findings on budget credibility.						
21	The auditor linked the analysis of deviation/discrepancy with performance and estimated the impacts of the recommendation where possible.						

## ANNEX 7.1. Opportunities to integrate budget credibility in the audit process with stakeholders

Stage of the audit process	Recommended actions/resources	Examples
Audit topic selection and planning	<p>Discuss topics, root cause analysis, and risks with stakeholders who analyze budget credibility, e.g., with authors of SDG budget credibility briefs/reports; budget credibility in COVID fiscal management analysis; sector and program budget credibility analysis; PEFA assessments.</p> <p>SAI online tools/apps.</p>	<p>Stakeholder workshops including expert panels, and focus group discussions.</p> <p>Online platforms for citizen inputs, e.g., CITIZENEYE in Ghana (Box 7.5), Republic of Korea, and Georgia platforms.</p>
Audit execution	<p>Review/include evidence from budget credibility analyses. From authors of SDG budget credibility briefs/reports; budget credibility in COVID fiscal management; sector and program budget credibility; PEFA assessments.</p> <p>Review/include data from social audits indicating significant budget deviations.</p> <p>Review/include data from SAI online tools and apps.</p> <p>Citizen participatory audits on budget credibility issues. Analyze the extent to which auditees provide reasonable justification for budget deviations.</p>	<p>Citizen-led social audits in Indonesia, Senegal, and South Africa.</p> <p>Citizen participatory audits in the Philippines.</p>
Audit reporting	<p>Publish findings and provide recommendations to address budget credibility issues, e.g.: the root causes of budget deviations such as poor coordination, inadequate forecasting and procurement, and delayed donor funds.</p> <p>Report the extent to which auditees provide reasonable justification for budget deviations.</p> <p>Report in a timely manner to help rectify budget credibility issues.</p>	
Audit follow-up	<p>Develop and implement strategies with stakeholders to address budget credibility issues, e.g.:</p> <ul style="list-style-type: none"> <li>w/those affected by underspending in critical sectors, with CSO partnership.</li> <li>w/the executive/auditees.</li> <li>w/ the legislature: organize hearings or simple oral presentations for legislators and the public.</li> <li>w/budget credibility analysts and development partners.</li> <li>w/media: prepare accurate and online press releases; publish the same date that the report is tabled in the legislature for maximum impact.</li> </ul>	<p>Joint follow-up, e.g., Argentina: SAI/ACIJ on Chagas containment (Box 7.11) and Colombia's Articulated Audits (AA) (Box 7.13).</p> <p>Multi-stakeholder COVID committee in Senegal.</p>

## **Strengthening Budget Credibility through External Audits: A Handbook for Auditors**

Supreme Audit Institutions (SAIs) have an important role to play in strengthening the implementation of sustainable development promises and ensuring that their country's budget is on track. Drawing on SAI's experience, the handbook explores different approaches to auditing that can contribute to improving budget credibility.

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