

## **Promoting Independent External Audits on Credibility of Government Budgets Collaboration between IBP and UNDESA-DPIDG on the production of a handbook on how SAIs can shed light on budget credibility**

### **Concept Note**

Given their mandates and essential roles auditing government finances, supreme audit institutions (SAIs) are uniquely placed to assess budget deviations and the justifications offered for and consequences of such deviations. However, few SAIs are currently systematically auditing budget deviations or assessing trends in budget credibility. In this concept note, the International Budget Partnership (IBP) and the Division for Public Institutions and Digital Government of the United Nations Department for Economic and Social Affairs (DPIDG) describe a planned effort to develop a handbook to support SAIs in conducting analyses of the credibility of government budgets through external audits.

### **Why is Budget Credibility Important?**

Budgets are considered “credible” when governments collect and spend funds according to their approved budgets. The ability of a government to meet its revenue and expenditure targets during a financial year determines the credibility of the budget approved by the legislature. There are several reasons why it is important that budgets be credible:

- The national budget is a roadmap to the effective delivery of public services and to progress on sustainable development. Veering off course can impact both the provision of essential services and the achievement of national development objectives.
- A persistent lack of budget credibility can reflect poor public finance management practices in countries, which in turn can jeopardize the integrity of public funds and increase the risks of misuse and corrupt practices.
- Governments’ repeated failure to collect and spend funds according to approved budgets often feeds into an ongoing narrative that governments cannot be trusted.

The importance of budget credibility for effective, accountable and transparent institutions has been made clear by the inclusion of a dedicated indicator (indicator 16.6.1) in the list of global indicators agreed by United Nations Member States to monitor progress on the Sustainable Development Goals (SDGs) at the global level.

## **How can SAI work inform analyses of budget credibility?**

The literature on public finance management is very sparse on how SAIs have contributed to understanding and assessing budget credibility. A recent source of information on this topic is a short paper (which is still in draft form) developed by DPIDG. The paper uses examples of audits issued by 20 SAIs from around the world to assess how SAIs have—and have not—covered budget credibility issues in their audits. It shows that information and reports already produced by SAIs can directly inform analyses of budget credibility (see Annex 2).

## **Rationale for and objectives of the elaboration of a handbook for SAIs**

Over the past couple of years, IBP and DPIDG have discussed the topic with SAI officials from several countries, including at the sidelines of SDG-related events at the UN in 2019 and in several meetings organized by IBP. These discussions have been welcomed by SAI officials who were present at the events. SAI officials have recognized that budget credibility is an important issue that merits further attention from the SAI community. The discussions also suggest that there would be a value in sharing audit practices being followed by some SAIs who are already assessing budget credibility more widely among the SAI community.

The production of a handbook on how SAIs can inform analyses of budget credibility through their work would aim to directly contribute to this objective, and ultimately support building the capacity of SAIs in different national contexts to produce and inform analyses of budget credibility by drawing on existing audit work.

The handbook would (see Annex 3):

- Expose to SAIs how their work can inform analyses of budget credibility;
- Illustrate how audit work already conducted by SAIs across the world provides insight on budget credibility;
- Outline and illustrate key steps that SAIs can contemplate when aiming to assess and address budget credibility;
- Share practices from SAIs in this regard.

## **Plans for the production of the handbook**

IBP and DPIDG will join efforts to elaborate the handbook, in close consultation with potential SAI users as well as relevant SAI groupings. The production of the handbook is a component of a three-year IBP initiative called the *Strengthening Budget Credibility for Service Delivery* project, launched in 2020. The project builds on previous work on budget credibility and engagement with SAIs on this subject (see Annex 4).

The production of the handbook is expected to span the years 2021-2023. The following set of activities are contemplated by IBP and DPIDG (dates are indicative only):

- Collection of feedback from SAI practitioners, including through dissemination of this concept note (December 2020-Spring 2021);

- Expert meeting with interested SAIs to define the scope and expected content of the handbook (May 2021);
- Work with interested SAIs to elaborate country case studies for the handbook (second half of 2021);
- Validation of the handbook content with SAI and other experts (March 2022);
- Finalization and launch of the handbook (December 2022 – March 2023).

## **Annex 1: What do we know about Budget Credibility?**

Through its pilot phase of work on budget credibility, IBP has identified and examined several trends pertaining to the lack of credibility in government budgets:

***National budgets are plagued by underspending:*** IBP's research across 35 countries shows that, on average, governments are underspending their annual national budgets by nearly 10% (above the 5% deviation standard set forth by international standards). This level of underspending equals the average total health budgets in many countries. Levels of underspending are even higher in low-income countries, averaging approximately 14%.

***Underspending in budgets is most common in key social sectors and service delivery programs:*** IBP's research reveals that underspending in specific sectors—such as health, education, water and sanitation, and agriculture—is often significantly higher than the aggregate levels of underspending. For example, an IBP study revealed that nearly 30% of the budgets for purchasing vaccines across 22 countries was unspent over a multi-year period, even as these governments reported vaccine shortages.

***Lack of credibility is driven by both technical and political factors and is often associated with donor funding:*** IBP's research has identified a variety of technical factors that contribute to lack of budget credibility, including faulty revenue forecasting, weak procurement systems, and inadequate policies to control the shifting of funds. However, political factors also frequently contribute to countries' budget credibility problems. Further, IBP's research indicates that external financing from donors is associated with nearly 40% of identified underspending.

***Governments rarely explain the reasons for their budget deviations:*** During the pilot phase of its budget credibility project, IBP successfully tested a standard on budget justification across a range of countries. IBP's research shows that many countries either do not provide explanations for budget deviations or provide explanations that lack essential explanatory details. Repeated budget deviations in the absence of adequate and reliable justifications erode confidence in the ability of a government to make realistic plans and adhere to commitments.

## **Annex 2: Some insights from the draft DPIDG paper on SAIs and budget credibility**

Some of the main findings of the review conducted by DPIDG are as follows:

- SAIs are producing a variety of reports that help shine a light on the extent and causes of budget deviations in countries, but SAIs do not typically classify such deviations as matters of budget credibility. Thus, even though limited or absent documentation for expenditures, unexplained expenditures, expenditures used for purposes that were not authorized in budgets, non-compliance with fiscal laws and regulations, and weak internal controls are all problems commonly associated with lack of budget credibility, they are rarely identified by SAIs under that specific heading or linked to overall deviations in revenues or expenditures. However, audit reports issued by SAIs in Ghana and Uganda that discuss weaknesses in revenue and expenditure forecasting models, and explain how these trends are driving deviations between planned and implemented budgets, are unique and noteworthy examples of audit reports that draw explicit attention to the over-arching issue of lack of budget credibility.
- Many SAI reports simply identify overruns or underspending in budgets without providing additional assessment of the justifications offered for budget deviations or analyzing broader trends when such deviations recur. For example, the Colombian SAI produces a monthly report analyzing deviations between the approved budget and monthly expenditures incurred by the government, but it only provides financial information without analyzing the causes for any deviations. That said, some SAIs, such as those in Mexico and Uganda, have begun issuing audit reports that help assess budget credibility in specific government programs. The Brazilian SAI has analyzed parliamentary amendments to the draft budgets submitted to parliament, which also have an impact on budget credibility. These reports point the way to the kinds of broader analyses of trends in budget deviations that SAIs can conduct.
- Several SAI audits explicitly discuss how limited transparency and challenges in reporting on budgets and expenditures (e.g., quality and disaggregation of information) hampers a proper assessment of government finances. Some SAIs are also reviewing the adequacy of performance information as well as linkages between performance information and financial data produced by governments. The provision of good quality performance data is critical to assessing the impact of budget deviations on the achievement of development objectives.

### **Annex 3: Potential Content of the Handbook**

*The structure below is indicative. The structure and content of the handbook will be refined following consultations with SAIs.*

Chapter 1 will begin to define budget credibility, explain its importance to national development and the promotion by SAIs of the public interest, and describe the various causes of lack of budget credibility that SAI audits have already uncovered.

Chapter 2 will provide a methodological framework for the rest of the handbook, mapping how different types of audits and reviews conducted by SAIs can inform various aspects of budget credibility, and illustrating how the conclusions from different types of audits conducted within a SAI can be combined to produce comprehensive analyses of budget credibility.

Chapter 3 will provide five to six practical case studies examining the budget credibility assessments that have already been conducted by SAIs and that can be replicated by others. These may be organized under various themes, such as the following:

- Assessing the extent of budget deviations by programmatic sectors and budget codes and the reasons for deviations;
- Analyzing justifications for budget deviations and the adequacy of such explanations;
- Investigating the impact of budget deviations on the provision of essential services;
- Evaluating transparency and reporting of financial and performance data by governments
- Strategically communicating audit findings and following up on audits to ensure action is taken

#### **Annex 4: About IBP and DPIDG**

IBP works in collaboration with multiple actors – including civil society, state actors, international institutions, and the private sector – to bring about a world in which empowered citizens participate in open, inclusive budgeting processes to shape policies and practices that promote equity and justice on a sustainable basis.

For a number of years, IBP has been working to support efforts to improve the credibility of national budgets. In 2020, IBP launched a three-year initiative called the *Strengthening Budget Credibility for Service Delivery* project. This project seeks to expand understanding of the causes and consequents of deviations from national budgets for the delivery of public services. The initiative is also raising awareness of the effects of lack of budget credibility and promoting reforms to address key causes of deviations from budgets. The project builds on a pilot phase of work that IBP, with DPIDG's engagement, undertook to understand the extent and causes of lack of budget credibility in countries in the years 2018 and 2019. Annex 1 provides an overview of lessons learned from the pilot phase of work on budget credibility.

Within the United Nations Department for Economic and Social Affairs, the Division for Public Institutions and Digital Government (DPIDG) focuses on analyzing and supporting efforts to make institutions inclusive, effective, accountable and well-equipped to achieve the Sustainable Development Goals (SDGs), as reflected in SDG 16. By focusing on building strong institutions and governance for the 2030 Agenda, the Division assists UN intergovernmental bodies in reflecting on the role of institutions as an integral part of their examination of the SDGs and supports the Committee of Experts on Public Administration (CEPA).

The Division supports the efforts of Supreme Audit Institutions (SAIs) to audit the implementation of the SDGs. DPIDG's longstanding collaboration with INTOSAI has included the organization of biannual joint symposiums, joint publications, workshops and high-level events. Since 2016, DPIDG has supported INTOSAI's efforts to contribute to the follow up and review of the SDGs, including by contributing to a global capacity building programme on auditing SDGs of the INTOSAI Development Initiative (IDI).