

INTOSAI



*Principles for
Best Audit
Arrangements for
International
Institutions*

INTOSAI PROFESSIONAL STANDARDS COMMITTEE

PSC-SECRETARIAT

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Introduction

International institutions are basically funded by public funds through contributions or guarantees from the member states. Supreme audit institutions (SAIs) have a fundamental interest in good governance, accountability and transparency in international institutions, and strongly believe that good, well-organised and independent audit systems will contribute to better and more transparent control of these institutions, thus contributing to their economy, efficiency and effectiveness.

A definition has been formulated for the purpose of describing the principles for best audit arrangements for international institutions:

“An international institution is an organisation whether or not established by a treaty, in which two or more states (or government agencies or publicly funded bodies) are members and in which a joint financial interest is overseen by a governing body.

The purpose of such an international institution could be to achieve international co-operation in dealing with issues of an economical, technical, social, cultural or humanitarian character. This could be co-operation in the field of governance, security, finance, scientific research, environment or the realisation of joint technical, economical, financial or social projects.”

The members of the International Organization of Supreme Audit Institutions (INTOSAI) are of the opinion that accountability in a number of international institutions could be enhanced to meet present standards for good governance, and that audit arrangements could be substantially improved. Audit arrangements were in many instances established many years ago, in an era where the focus was more on the success of establishing international cooperation, rather than on ensuring insight into prudent, effective and transparent spending of public money. As a result, audit mandates and arrangements are often outdated, and the accounts and audit more geared to the budgetary process than to ensuring that money is spent wisely and with transparency.

INTOSAI believes that an effective external audit is one decisive factor in better governance, and that INTOSAI members are uniquely placed to contribute to achieving this. INTOSAI collectively, and its members individually, have therefore undertaken to promote audit arrangements that encourage the auditing of international institutions by the community of

SAIs, recognising their expertise and independence in the regularity and performance auditing of public money.

In 2001, INTOSAI established a working group with the following mandate:

“Recognising the importance that SAIs place on establishing and maintaining adequate auditing of resources administered by international institutions, the XVII INCOSAI agreed to continue the work of establishing guidelines on recommended auditing arrangements for international institutions, and supplementary guidance on the application of auditing standards to the audit of such institutions.”

The following principles for best audit arrangements for international institutions were prepared by the Working Group on Audit of International Institutions and presented for approval by the INTOSAI Congress, XVIII INCOSAI, at its meeting in 2004. The principles are intended to be used by SAIs, international institutions and national representatives to such institutions, and governments.

Principles for best audit arrangements for international institutions

To be effective, the audit arrangements for international institutions should ensure that:

1. All international institutions financed with or supported by public money should be subject to audit by supreme audit institutions, to promote better governance, transparency and accountability,

and that the external auditor:

2. Is fully independent in the conduct of the audit,
3. Has sufficient authority to carry out the audit in a manner that meets best practice in the audit of public money,
4. Has adequate resources to carry out the audit,
5. Has the right and obligation to report on the results of the audit to the member states concerned through the governing body,
6. Meets relevant professional and ethical standards, and
7. Is appointed in an open, fair and transparent manner.

Commentary on the principles for best audit arrangements for international institutions

Principle 1

All international institutions financed with or supported by public money should be subject to audit by supreme audit institutions, to promote better governance, transparency and accountability

1.1. An international institution is, as an autonomous body, responsible for establishing its own rules and regulations, including the audit arrangements. The rules and regulations should be based on internationally accepted principles. International institutions vary in their set-up. Typically, however, they are constituted under international law as a legal entity and may enter into various commitments following their own established rules. A governing body consisting of representatives from all (or some of) the member states decides such rules, among which are financial rules and regulations covering financial management, budgets and accounting as well as auditing. Management carries out the day-to-day management of the international institutions within the framework laid down by the governing body.

1.2. The audit arrangements of international institutions must ensure that the audit of the institution is adequate and performed in an economical, efficient, and effective manner. At the same time, audit arrangements may have to reflect the member states' different legitimate interests, such as preferential treatment of developing nations, as decided by the rules of the international institution.

1.3. The international institution and the auditor should continually assess whether the evolution of the institution warrants a change in the audit arrangement. In case the scope or structure of the international institution changes fundamentally, the audit arrangements should be considered very carefully and updated if necessary.

1.4. Supreme audit institutions (SAIs) are uniquely positioned to assist international institutions in enhancing good governance, transparency and accountability. This follows from their statutory independence and their long tradition of providing the same assurance in a national

context. SAIs will also have experience in assessing carefully the need for the public to receive relevant information on financial issues. The added value to the international institution from an audit performed by an SAI will normally be the integrated audit work covering performance aspects.

1.5. It is normally most effective that a single SAI alone is responsible for the audit. However, as the international institution grows and particularly when the member states establish major programmes, it may be more suitable that two or more member SAIs are represented. Thus, the member states may decide to appoint a board of auditors to perform the audit. Only if the international institution is very large would it be reasonable to appoint a board of auditors-general, as seen in the UN system.

1.6. To the international institution, the appointment of one SAI means that the audit arrangement will be quite flexible with simple lines of communication. The relevant SAI gains substantial knowledge of the institution and the auditor will be able to work more or less as at home which means that only limited training will be needed. At the same time the SAI will be able to provide a wide range of skills and capabilities to ensure the maximum effect of the audit.

1.7. If two or more SAIs perform the audit, whether in the form of a board of auditors or not, the audit arrangement can still be quite flexible. Moreover the institution will benefit from the fact that different perspectives will be represented in the audit and the professional base of relevant audit expertise will be larger. Internally, however, the involved SAIs will spend some time communicating to ensure that everybody agrees on audit findings. Therefore, if the member states decide to form a board of auditors the number of SAIs should be kept relatively small, no more than three or four.

1.8. Some SAIs have extensive experience in auditing international institutions while other SAIs have less or none. Partnerships between well developed and experienced SAIs and other SAIs should be encouraged, and the regulations of international institutions should not obstruct them.

Principle 2

The external auditor is fully independent in the conduct of the audit

2.1 The external auditor must be free to determine the scope, methods and resources required to conduct the audit of the international institutions.

2.2 The auditor must be independent of the management of the international institution.

2.3 The auditor should neither seek nor receive instructions from an individual member state. Often the auditor needs to discuss issues concerning audit risk, methodology, etc. with management of the international institution and representatives of the governing body. This way of gathering necessary information is not discouraged, provided that solely the auditor decides on the audit.

2.4 The financial rules and regulations of the international institution should include provisions that ensure that the auditor is appointed by and responsible only to the governing body.

2.5 The financial rules and regulations of the international institution covering external audit should ensure that the auditor is not restricted in carrying out any audit task deemed necessary to fulfil the audit mandate.

2.6 The auditor must be solely responsible for the conduct of the audit, including the scope of the audit and the methods chosen.

2.7 Only the governing body can request the auditor to perform specific or additional audit work. Before accepting such a task, the auditor must ensure that resources are adequate to fulfil the specific or additional audit work requested in addition to the audit mandate. The auditor must also ensure that the specific or additional auditing is consistent with the mandate and competence of an external auditor. Having accepted the specific or additional audit work, it is for the auditor to determine the scope, methodology and resources of the audit.

2.8 The independence of the auditor should not be constrained by other factors, such as lack of authority, resources, mandate or reporting rights and obligations as described below in principles 3 - 5.

2.9 The auditor should be perceived to be independent. This implies that the auditor needs to be objective in dealing with the audit issues and free of personal interest and any external pressure, basing conclusions exclusively on audit evidence obtained in accordance with relevant standards.

Principle 3

The external auditor has sufficient authority to carry out the audit in a manner that meets best practice in the audit of public money

3.1 The governing body is responsible for establishing effective systems that promote good governance, transparency and accountability. This includes ensuring that all accounts are subject to review by the auditor, establishing reliable systems of accounting for the financial resources granted, and maintaining good systems for efficiency and value for money in order to ensure that resources are well spent. The auditor's task is to make an independent appraisal of these systems, but it should be clear that not even the best audit can correct a deficient management system.

3.2 It is the responsibility of the international institution to prepare and present its financial statements. The auditor's task is to audit these, and express an opinion on them.

3.3 The audit mandate should include regularity audit as well as performance audit, and should also allow for special audits, e.g. environmental audits. In this context the relevant INTOSAI auditing standards should apply as well as generally accepted best auditing practice.

3.4 INTOSAI's definitions on regularity audit and performance audit are found as an annex to this paper. For the entire texts, use the INTOSAI website. (www.intosai.org)

3.5 To guard against narrow interpretation of the mandate, the auditor needs to be able to report to the governing body on any matter deemed of significance.

3.6 The auditor and audit staff shall have unrestricted access to any information and staff of the international institution deemed necessary for the performance of the audit.

3.7 The auditor should have the authority to engage the services of specialists and experts required to undertake the audit.

3.8 The external auditor should assess the extent of reliance that might be placed on other auditors, for example internal audit.

Principle 4

The external auditor has adequate resources to carry out the audit

4.1 The international institution should provide adequate resources and facilities for the proper discharge of the audit, and bear the full cost of the audit.

4.2 The international institution should establish an adequate formal budget provision for the external audit services in consultation with the auditor.

4.3 To the extent that the costs of the audit for some reason are not fully covered, the auditor should make the full costs known to the governing body, in order to promote transparency. Some SAIs may not undertake the role of external auditor for international institutions unless all costs are covered; on the other hand, some SAIs are not allowed to receive money from anyone but their own state or legislature. The rules and regulations of the international institutions should not lead to discrimination between SAIs based on their national legislation.

4.4 If the auditor considers that the available resources are insufficient to carry out the audit, either in quantity or quality, this fact should be reported to the governing body, as well as the consequences of the problem and proposed solutions. Normally, in a competitive situation, issues relating to the budget are settled when the auditor is appointed.

4.5 The auditor should have the opportunity to present and discuss the budget requirements with the governing body of the institution, before the approval of the budget, especially when not in a competitive situation or where conditions have fundamentally changed since competition.

Principle 5

The external auditor has the right and obligation to report on the results of the audit to the member states concerned through the governing body

5.1 The auditor must issue a report on the audit of the financial statements to the governing body.

5.2 The auditor may issue reports to the governing body on financial issues, on performance audit and/or special reports on any issue deemed of significance by the auditor.

5.3 The auditor should report to the governing body on the status of management's implementation of the auditor's previous recommendations.

5.4 The auditor must report to the governing body in a timely manner.

5.5 The auditor should, in all reports, disclose relevant auditing standards observed.

5.6 The auditor is solely responsible for the content of the audit report. Before issuing the report, the auditor should submit it to management for comments.

5.7 The auditor should be invited to present the audit report to the governing body in the appropriate meeting.

5.8 The audit reports should be publicly available. Exceptions should be based on clear and relevant criteria concerning classified and confidential information.

5.9 The members of the governing body should be encouraged to forward the reports to the SAIs of the member states for information.

Principle 6

The external auditor meets relevant professional and ethical standards

6.1 The audit of international institutions shall be conducted in conformity with the INTOSAI Auditing Standards and other generally accepted international auditing standards, such as the IFAC auditing standards, issued by the International Federation of Accountants.

6.2 The conduct of the auditor shall be in conformity with the INTOSAI Code of Ethics and other generally accepted professional standards, ref. Annex 1.

Principle 7

The external auditor is appointed in an open, fair and transparent manner

The auditor should be appointed by the governing body independently of the management.

The selection process should allow participation of all member states to ensure that the process is fair and transparent.

The process for appointing the auditor should be established by the governing body, and laid down in the financial rules and regulations. Timely information on forthcoming appointments is essential.

The governing body should decide an appropriate length of appointment for the auditor. Factors that may influence the length of appointment are costs and benefits of changing auditors, the likely availability of auditors, and the complexity of the institution. In many instances an appointment of between 4 and 8 years will provide a reasonable balance between the additional costs of changing the external auditor and the benefits of the change.

There are no standard arrangements for selection of a new external auditor. There may be a process of inviting SAIs to undertake the audit in a specific order of rotation. There may be formal

requests for proposals (bids) from SAIs of the member states concerned. The selection process should nevertheless provide equal opportunity for all SAIs to be appointed as external auditor, as well as ensuring quality audit. Governing bodies may wish to establish selection criteria that provide scope and encouragement for SAIs from developing countries to undertake or contribute to the external audit.

The governing body should lay down clear and open criteria for the selection of the auditor. Selection criteria may include factors such as appropriate technical and professional competence for the audit and the costs thereof, sought by invitation from those SAIs that wish to undertake the audit. Selection should not be based on the basis of costs alone.

The institution should seek to get bids in an defined format. This means that specific guidelines and recommendations have to be applied when designing for bids. Such guidelines could include how to present various budget items, like cost for permanent staff, preparatory work in home country, travel plans, etc. It is also important to emphasize that competition between SAIs, in their efforts to be appointed as external auditor, should be fair and free from unnecessary imperfections of any kind. The principle of full cost coverage should be part of the guidelines and, consequently, part of the evaluation of bids.

When carrying out competitive bidding by calling in technical and financial bids from the SAIs, the international institution, its member states and the SAIs involved should apply standards for good procurement practise.

Candidates for an audit assignment must have a thorough knowledge of, and experience in auditing and examining government operations in accordance with the INTOSAI auditing standards, and a good working knowledge of at least one of the official working languages of the international institution.

Annex I

Excerpts from INTOSAI documents

(The full texts can be found on www.intosai.org)

INTOSAI Auditing Standards, Chapter I, paragraph 1.0.39

Regularity audit embraces:

- attestation of financial accountability of accountable entities, involving examination and evaluation of financial records and expression of opinions on financial statements;
- attestation of financial accountability of the administration as a whole
- audit of financial systems and transactions including an evaluation of compliance with applicable statutes and regulations;
- audit of internal control and internal audit functions;
- audit of the probity and propriety of administrative decisions taken within the audited entity and
- Reporting of any other matters arising from or relating to the audit that the SAI considers should be disclosed.

INTOSAI Auditing Standards, Chapter I, paragraph 1.0.40

Performance audit is concerned with the audit of economy, efficiency and effectiveness and embraces:

- audit of the economy of administrative activities in accordance with sound administrative principles and practices, and management policies;
- audit of the efficiency of utilisation of human, financial and other resources, including examination of information systems, performance measures and monitoring arrangements, and procedures followed by audited entities for remedying identified deficiencies; and
- audit of the effectiveness of performance in relation to the achievement of the objectives of the audited entity, and audit of the actual impact of activities compared with the intended impact.

The INTOSAI Implementation Guidelines for Performance Auditing

describe in its Part 1 the meaning of auditing economy, efficiency and effectiveness:

- Economy – keeping the cost low
- Efficiency – getting the most out of available resources
- Effectiveness – achieving the objectives

And define performance auditing:

Performance auditing is an independent examination of the efficiency and effectiveness of [international institutions'] undertakings and programs, with due regard to economy, and with the aim of leading to improvements.

Code of Ethics

The Code of Ethics is a statement of values and principles guiding the daily work of the auditors.

Annex II

Glossary

Audit arrangements

The organisational set-up of the external audit of an international institution. Two arrangements dominate: A single auditor and a board of auditors. Audit arrangements will normally be part of the financial rules and regulations.

Auditing standards

The most relevant, generally accepted auditing standards for regularity (financial) audit are the INTOSAI standards and the IFAC standards, issued by the International Federation of Accountants. Adherence to these standards will ensure the quality of work.

Auditor

In this paper used as generic term meant to cover the external auditor, whether single or in the form of a board of auditors.

Board of auditors

A group of auditors from different SAIs jointly responsible for conducting the audit.

Code of Ethics

Code of Ethics is a statement of values and principles guiding the daily work of the auditors.

Financial rules and regulations

Rules and regulations covering financial management of the international institution. They normally cover the budgetary process, accounting, and responsibilities for management, financial committees etc. They also cover rules governing the external audit.

Good governance

Generic term covering standards for decision-making, propriety, probity, accountability and transparency.

Governing body

Common term for the highest authority in an international institution. May in some institutions also include committees such as audit committee, financial committee, etc. The main common factor is that all governing bodies will consist of representatives from member states.

International institutions

An international institution is an organisation whether or not established by a treaty, in which two or more states (or government agencies or publicly funded bodies) are members and in which a joint financial interest is overseen by a governing body.

INTOSAI

An autonomous, independent and non-political organisation established as a permanent institution in order to foster the exchange of ideas and experiences among the SAIs on government auditing.

Management

The day-to-day executive administration, responsible for carrying out the decisions of the governing body.

Member states

The nations participating in the international institution.

SAIs

Supreme Audit Institutions. In general they are responsible for audit of the government, its administrative authorities and other subordinate institutions.