

# 2006 Joint Review Audit Working Group Report

## INTERNAL AUDIT

**PAF Indicator/Target:** *Implementation of priority components of the strategic plan in internal audit*

### *1. Executive Summary*

**In 2005, the PAF target for internal audit was partially met.** Although progress can be noted in terms of internal audit performance and of new ongoing initiatives, IGF as well as the Subsystem of Internal Audit (SCI) experienced delays and no fulfilment of some priority activities. The reasons that could explain this no fulfilment include: the change of Government which limited the possibility to carry out audits effectively during the first quarter 2005; not planned requests by superiors; joint audits which involved the on-job training of sectorial inspectors and the increase of audited entities; and the weak capacities of IGF civil servants at intermediate level. Progress was made in the area of developing human capacities through training of new staff. In general, performance of the internal audit area in 2005 can be considered mixed with a positive perspective of improvement for 2006.

In order to make effective the SCI, it is necessary to: (i) adopt as soon as possible a legal instrument which allows for the institutionalization of audit committees, key means for improving the quality of audits, the participation and the follow-up of the recommendations; and (ii) continue the institutionalization of internal audit bodies in each institution at central and provincial level. The reinforcement of SCI would permit that the OCIs could gradually assume the actual role of IGF allowing this latter to focus on more cross-cutting or bigger impact issues.

Audit is not an objective *per se*: it is important to reinforce the interaction of IGF and SCI with the other components of the Public Finance Reform (SISTAFE, procurement, public sector (payroll control), and decentralization), in order to ensure that the auditing activity can adapt with the new environment and that the reforms can consider lessons and experience from the realised audits. Similarly, it should be taken into account whether the relationships and the information flow between IGF and its interlocutors can be optimized. In particular, this is important with the Tribunal Administrativo for what concerns the opinions about the municipality accounts and with the Anti-Corruption Unit, in order to get benefit from their results in a more efficient manner.

### *2. Performance assessment in 2005*

In the area of internal audit, the PAF target for 2005 (*implementation of priority components of the strategic plan in internal audit*) was partially met.

## **2.1 Execution of the 2005 strategic plan**

### **2.1.1 IGF**

**The IGF performance was mixed in terms of implementation of its 2005 plan.**

IGF implemented 79% of the planned activities. This corresponds to 150 inspections, with completed field work, compared to the 191 annually programmed. This amount includes 31 actions passed from 2004 and 27 not planned, but carried out by superior request. Although IGF had established its priorities for 2005, its work has been partially affected by specific and high-level requests by the Anti-corruption Unit and/or by sectorial Ministries. In 2005, the number of these requests was 22 (6 in 2004). The increase in the number of not planned requests by new Ministries in 2005 (the number of these requests is always higher at the beginning of a new Government) can be seen as a positive signal of reinforcement of trust in the role and impact of internal audit.

The number of inspections carried out in 2005 seems to reflect a reduction compared to 2004. However, the number of audits is not a valid indicator for such a comparison since IGF is in the process of changing its way of working that is implementing more cross-cutting activities. This will involve more institutions for the same activity (for example, the procurement audit). Compared to 2004, the number of institutions visited and audited in 2005 increased substantially.

The reasons that could explain this no fulfilment include: the change of Government which limited the possibility to carry out audits effectively during the first quarter 2005; not planned requests by superiors; joint audits which involved the on-job training of sectorial inspectors and the increase of audited entities; and the weak capacities of IGF civil servants at intermediate level.

Progress was made in the area of developing human capacities through training activities, in particular of the 35 new staff contracted at mid 2004.

### **2.1.2 SCI**

Regarding the SCI, a rather weak performance is noted. However, it should be considered that 2005 was the first year of activity for the SCI. Among the planned activities, some important ones have not been carried out, such as the creation of audit committees, the institutionalisation of internal audit bodies in the municipalities of the Provinces capitals, the encouragement of functionaries in the different sectors to create OCIs at intermediate level, the production of manuals of auditing/inspecting procedures for the financial and patrimonial management. It should be underlined that the majority of these activities were not initiated before the end of the year.

Positive developments were achieved in carrying out joint audits on: (i) the *procurement* process in the country, including 6 Ministries e 5 Provinces, involving 5 institutions in each

province; (ii) the diagnostic study, carried out for the first time, about the financial and patrimonial management of 39 districts, (iii) INAS, e (iv) PROAGRI and the State Property.

Some first steps in the creation of the audit committees were made in the province of Niassa. However, it is believed more adequate that this instrument is approved by a decree by the Council of Ministers. Considering the positive environment in Niassa province as well as in MINED, IGF believes that it will be possible to start the activities already in the second semester of 2006.

The intention to take advantage from the work done by ESAAG, so to have an appropriate international benchmark, it is delaying the production of a basic auditing manual. A competition was launched in order to contract a short term consultancy that will be in charge for its elaboration.

Improvements have been also made in terms of training and recruitment of new personnel.

## **2.2 Budget Execution**

According to the 2005 budget execution report, the execution rate of liquidated recurrent expenditures, mainly salaries and retributions, is 50.4%. IGF underlines that there are discrepancies between their budget execution report, where the execution rate is 59%, and the figures reflected in the State budget execution report. This difference is explained by the payments not yet registered by the National Directorate for Public Accounting and it should be rightly included in the State General Account.

In addition, the Budget Execution Report reports that 1.200 million meticaís allocated to the Delegation in Beira for investment expenditures have not been used. However, IGF states that these funds were almost totally spent (1.108 million meticaís) during the last quarter of 2005.

As said during the last MYR, the principal causes for this low execution are identified in the late approval of the State Budget for 2005 and in the integration of 35 new staff in IGF organigramme, concluded only in December 2005. Until this date the personnel was paid with external project funds and by the State Budget.

## ***3. Future Perspectives***

Looking at the results achieved during 2005, it is clear that additional efforts are necessary to make dynamic the creation and development of OCIs. The creation of audit committees and regulation of their functioning are fundamental for the effective implementation of the recommendations. The reinforcement of capacities and competencies of the human resources of this area are a priority for the increase of its coverage, quality and follow-up. In 2006 it foreseen the recruitment of 10 additional people for IGF and 50 for the SCI. IGF is currently preparing a financing proposal for 2006-2008. Although initially supported by donors' resources, the State Budget will gradually incorporate the costs related to the SCI.

In order to have a more complete overview of the priorities and the coverage of this area, the 2006 IGF activity plan and the one of the SCI could be integrated. The group noted that the internal monitoring system is still weak. However, there is an improving trend, thanks to the development of a new information management system that will make possible to have a more complete overview on the cycle of the implemented activities from 2006. IN particular, it will be possible to know the value of audited public expenditures, the number of audited

entities, and the follow up to the level of implementation of the recommendations. The group thinks that this new instrument will facilitate the monitoring of the new strategic plan.

Regarding the link and coordination with key reforms, such as procurement, decentralisation and other SISTAFE sub-components, IGF is working for the reinforcement of such relationships. A team was created to work in the area of decentralisation and a lawyer was made responsible for creating the links with the procurement area. Regarding internal control for no salary expenditures, IGF intends to advance with it in 2006.

The **2006 PES** refers to the PAF indicator related to IGF. However, it is important that future Government key documents deal with IGF objectives and activities and SCI development more in detail. Furthermore, donors' funds in support of IGF are not included in the 2006 State Budget. It is recommended that this situation is resolved in 2007.

The strategic objectives of SCI for 2005-2009 are:

- To ensure the institutionalization of the OCIs in each sector by enabling them with adequate resources and a "privileged" role in the Ministry where they are operating;
- To assess the quality of its performance;
- To promote the professional development, the methodology and competences of the SCI components;
- To implement auditing/inspection activities in coordination with other institutions of internal audit, the Tribunal Administrativo and the other SISTAFE subcomponents, taking into account the basic principles of sufficiency, complementarity and relevance.

In general, the group recommends that additional efforts are made in order to develop the SCI that still needs instruments and adequate support.

In future, particular attention should be paid to three aspects:

- In order to make effective the SCI, it is necessary to: (i) adopt as soon as possible a legal instrument which allows for the institutionalization of audit committees, key means for improving the quality of sectorial audits at central and local level, the participation and the follow-up of recommendations provided by the audit reports and (ii) continue the institutionalization of internal audit bodies in each institution at central and provincial level. The reinforcement of SCI would permit that the OCIs could gradually assume the actual role of IGF allowing this latter to focus on more cross-cutting or bigger impact issues.
- It is important to reinforce the interaction of IGF and SCI with the other components of the Public Finance Reform (SISTAFE, procurement, public sector (payroll control), and decentralization - district administration audits-), in order to ensure that the auditing activity can adapt with the new environment and that the reforms can consider the lessons and the experience from the realised audits.
- It should be taken into account whether the relationships and the information flow between IGF and its interlocutors can be optimized. In particular, this is important with the Tribunal Administrativo for what concerns the opinions about the municipality accounts and with the Anti-Corruption Unit.

#### Documentation:

The group based its analysis on the following documents:

- IGF Activity Plan for 2005;
- Implementation Report of IGF Activity Plan for 2005;
- IGF Strategic Activity Plan for 2000-2005;
- IGF Strategic Activity Plan for 2006-2010 (Draft);
- SCI Activity Plan for 2005;
- Implementation Report of SCI Activity Plan for 2005;
- SCI Strategic Activity Plan for 2005-2009.
- Budget Execution Report Jan - Dez 2005
- PES 2006
- BdPES 2005

## **Non-PAF issues: MoU Audit requirements**

The MoU foresees the delivery of 3 annual Audits:

### **1. Value for Money Audit:**

The MoU foresees annual value for money audits on a sample of activities relevant for poverty reduction. Those audits should be delivered by IGF with the support of qualified and independent experts. Sectors or areas as well as ToRs and financing should be agreed upon between PAPS and GoM.

The second VfM audit undertaken in the framework of the MoU was related to road sector. Presentation and discussion of the results (draft presented in the 2005 Joint Review) occurred in the 1st semester 2005. The work was concluded in 2005 and approved by the Minister of Finance in March 2006. It is essential that the follow up of the implementation of the recommendations are part of IGF and road sector 2006 activity plans. It is recommended that the conclusion and formal approval of the annual reports are done in a shorter period.

The third VfM audit is being undertaken in the water sector. Due to delays from the initial calendar, only the draft has been released at the time of this Joint Review. This draft will be assessed by PAPs and GOM but a concern was raised on the definition and objectives of this type of audits in Mozambique. Based on this experience, it is recommended for future exercises, the work of IGF and of the independent consultants be more coordinated from the planning phase, the choice of the consultants well thought in view of IGF capacity needs to perform such type of audits, and that terms of reference be discussed widely to agree on objectives and expectations.

A new VfM audit will be carried out during 2006. The preparatory work should start immediately after the Joint Review to avoid recurrent delays and in order to have a final product to be part of the analysis of the 2007 Joint Review. As agreed in the 2005 Mid Year Review, the justice sector will be chosen for this exercise (and agriculture in 2007). The financing support from a PAP should be identified as soon as possible.

As specified in the MoU, one VFM audit will take place yearly until the capacity of IGF has made it possible to undertake this type of audits from the regular activity plan of the competent Mozambican audit authorities. In this regard, IGF has informed the PAPs that based on the already existing experience, it foresees during 2006 the creation of a new specific unit within its organic structure that will be charged with the realisation of VfM audits.

### **2. Audit of the financial records of the Programme aid**

The financial audit of the flow of budget support funds into the Treasury Account in 2005 is about to be released to the PAPs (31/03/2006).

### **3. Audit of the General State Accounts**

The Administrative Court audits annually the State Accounts. PAPs received in December 2005 the report and opinion of the TA on the 2004 State Accounts. These documents have been debated in Parliament in ....

These two documents provide an essential basis to feed the dialogue between the PAPs and the Government on public finance management issues, in particular budget allocations, execution and transparency of state accounts for the previous year. Following the experience initiated in the 2005 Joint Review and the respective recommendation, a dialogue has been opened between PAPs and the Ministry of Finance on the follow up given to the TA report. It is planned to deepen this dialogue after the Joint Review with the presence of the TA, in particular to tackle recurrent recommendations that are not taken on board by the MF for specific reasons.

Scope and quality of the TA reports are treated in the respective PFM part of the Aide Memoire.