

WORKING GROUP ON PUBLIC DEBT

EVALUATION OF THE NEED AND OPORTUNITY OF REVISING WGPD'S PRODUCTS

REPORT BY SAI's OF MEXICO AND PORTUGAL

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1. INTRODUCTION

The WGPD, during its 2010 annual meeting in Mexico City, decided that “*Portugal and Mexico will undertake the analysis of the current WGPD’s official products so as to verify the need of updating them with regard to the ISSAI framework*”. This report is the result of the work the two SAIs undertook and its objective is to facilitate the discussion and the adoption of a decision on the revision process of the 5000-5999 ISSAI Specific Guidelines.

The ISSAI framework, as adopted by the 2010 INCOSAI (Johannesburg), comprises seven specific guidelines on audit of public debt (ISSAIs 5410, 5411, 5420, 5421, 5422, 5430 and 5440) and one INTOSAI GOV on definition and disclosure of public debt (INTOSAI GOV 9230). We examined this documents and also a document entitled “Guidance on the reporting of public debt” adopted by the Public Debt Committee in 2000 but not by INTOSAI.

The INTOSAI Professional Standards Committee (PSC) has a project of harmonization of the ISSAIs to be executed in the period 2010-2013. This project comprises the revision of ISSAIs 100-4999 and it may result in changes in the ISSAIs 5000-5999, which will be the responsibility of the INTOSAI Knowledge Sharing and Knowledge Services Committee. The harmonization will lead to the consolidation of the terminology used in ISSAIs 100-4999 in accordance with a general glossary for the ISSAI Framework.

Any revision the WGPD may decide will follow the “Due process for the development and endorsement of ISSAIs”.

2. CRITERIA OF EVALUATION

To evaluate the need and opportunity of the revision we defined five criteria. The first is related to the present and future usefulness of each ISSAI/INTOSAI GOV and will lead to the decision of maintaining or withdrawing the document from the ISSAI framework. The second and third criteria address the contents of the documents and are intend to assess if each one is updated and if together they form a coherent set of guidance. The

fourth and fifth criteria address the relation of the documents under examination with the other ISSAIs and INTOSAI GOVs now also being revised.

We proceeded by proposing an answer to the following questions:

- Are the ISSAIs and INTOSAI GOV still useful?
- Do they need to be updated and in what respects?
- Do they need to be harmonized with other WGPD products?
- Do they need to be aligned with the ISSAIs 100-4999?
- Do they need to be aligned with the general ISSAI terminology?

3. RESULTS OF THE EVALUATION

The last question can't be answered now because the general glossary isn't available yet. Specific information on this glossary disclosure will be disseminated by the PSC in due time. Thus, this criterion for revision has a pending status.

The fourth question can be answered for all the documents under examination: it doesn't make sense to harmonize these documents with the present versions of ISSAIs 100-4999 since they are also being revised. So far, there is no available information on the PSC's process to revise the set of ISSAI 100-4999. The WGPD Secretariat will contact the PSC Chair so as to get acquainted on the working plan and timetable for the Harmonization Project Proposal. This criterion for revision has also a pending status

We will now present our specific evaluation of each of the eight documents.

3.1. ISSAI 5410 Guidance for planning and conducting an audit of internal controls of public debt

The 1998 INCOSAI (Montevideo) approved the merge of two studies—one concerning performance auditing of public debt management and the other concerning its internal controls—into unified guidance for planning and conducting an audit of the internal controls of public debt. The resulting document is ISSAI 5410. It is divided into:

- “SAIs role” a section where a description of internal control is presented;
- “Audit objectives and procedures” a section where lists of possible audit objectives and related audit procedures are presented;
- A glossary of public debt terms,
- A bibliography

Although the question of auditing internal controls is still a basic one, with specificities in the case of public debt, the text makes references to a number of examples from member SAIs that may be clearly out of date. Also some concepts and definitions have to be harmonized. For example, the public debt is defined operationally and the definition defers in at least the terms used with the conceptualization of the ISSAI 5422. This standard mentions hidden liabilities and the ISSAI 5410 does not.

Another example of the necessity of harmonization is related to the risks evaluation. ISSAI 5410 makes reference only to the operational risks (even when the document considers different types of risk by mentioning monetary risks as part of the operational risk), and ISSAI 5422 mentions nine types of risks. In this respect, it is important to consider that the international financial practices acknowledge a two-type risk classification: a) financial, and b) operational. The market, credit and liquidity risks belong to the financial type, that include the risks from the volatility of interest rates and the exchange rates; on the other hand, the operational risks include the processes, the legal part and technological risks. It would be convenient to evaluate if the concepts must be harmonized with those accepted on the international financial scope.

Other example of the concepts difference could be found when referring to the debt sustainability, when the ISSAI 5410 mentions that: “Debt sustainability is the degree to which a government can maintain existing programs and meet existing creditor requirements without increasing the debt burden on the economy”, the ISSAI 5422 makes reference to a concept regarding to the fiscal sustainability and conceptualize it as “...whether the present value of its future revenues is greater than its expenditures, including debt service ...”.

This ISSA is also related to the theme being investigated by Brazil, auditing the information systems used in the management of public debt. And this subject is closely linked to the work of PSC Subcommittee on Internal Control Standards and to INTOSAI GOVs 9100-9150. A quick comparison of some major definitions used in these

documents shows ISSAI 5410 probably needs to be aligned with the new version of those INTOSAI GOVs.

3.2. ISSAI 5411 Debt indicators

This document was adopted by the 2010 INCOSAI (Johannesburg). Being such a new product we think it shouldn't be included in the present revision process. Possible need for harmonization with the new versions of ISSAIs 100-4999 and the general glossary will be discussed later.

3.3. ISSAI 5420 Public debt: management and fiscal vulnerability

This document, dated 2003, addresses the question of what roles the SAIs may play *“to help reduce fiscal vulnerability of governments and make financial crises less likely”*. It draws on 90's financial crises experienced by emerging economies and reach the following conclusion:

“SAIs may wish to play an active role in protecting the financial condition of governments by promoting the need for sound public debt strategies and risk management practices, data disclosure policies and effective supervisory-regulatory regime for the banking sector so that the risks associated with future obligations and claims of the public sector as well as possible contingent obligations from the private sector can be minimized.”

Recent developments in financial and economic crises show that the problem is still a significant concern so the guidance is still useful but the document could be updated by the introduction of information about the more recent crises. Would the new information lead to different conclusions about the roles of SAIs? It isn't clear.

3.4. ISSAI 5421 Guidance on definition and disclosure of public debt

The present document is the first product of the Public Debt Committee adopted by the 1995 INCOSAI (Cairo). It has a foreword by the Chairman of the Committee published as a separate appendix. This guidance addresses the following themes:

- The role of SAIs
- General guidance on definition

- General guidance on disclosure
- The medium for disclosure

It comprises also an illustration of a model for disclosing public debt. The same text, now in one document, was endorsed by the 2007 INCOSAI (Mexico City) under the designation of INTOSAI GOV 9230.

We think that guidance on this subject is still necessary and the text is useful (it has been used in training courses delivered by IDI); there is no significant updating needed; there are some references to debt indicators that could be aligned with ISSAI 5411 Debt indicators.

There seems to be no reason for the same text to be considered simultaneously an ISSAI and an INTOSAI GOV. Furthermore the Committee has adopted in 2000 another document along the same lines, “Guidance on reporting public debt” that was never adopted by the INTOSAI. This guidance includes the text of ISSAI 5410/INTOSAI GOV 9230 and another theme, identifying and measuring public debt, as well as several annexes presenting examples from the 90’s that could be replaced by newer ones.

3.5 ISSAI 5422 An exercise of reference terms to carry out performance audit of public debt

This guidance is still useful. Having documents that methodologically support the development of the audit work will always be necessary, even more when they integrate the best practices and have gathered the various audit institutions’ experiences as well as the public audit guidelines, issued by the international organisms.

The ISSAI 5422, issued in 2007, established in its introduction that “... the valuable contributions sent ... in 2004 have been incorporated”. The reference to 2004 seems very far away, especially if we consider the 2008 crisis events and others recent events (Greece, Spain and Portugal).

Due to the 2008 financial crisis, plus the economic problems in some European Union’s countries, relevant growths have been occurring on different nation’s public debt, which, also, have generated fiscal crisis. It will be important to review the international financial organisms’ posture as well as the experience of the involved countries, so

they could be incorporated in order to reconsider aspects related to the debt's management, its structure, strategy and vulnerability and sustainability analysis, and above all, its audit, if that is the case.

3.6 ISSAI 5430 Fiscal exposures: implications for debt management and the role of SAIs

This ISSAI is relevant for the INTOSAI community and must be kept updated, since it is the only WGPD's document providing the INTOSAI community with:

- A definition and an illustrative overview of fiscal exposures, which may have implications for long-term fiscal sustainability and for debt management,
- An explanation on the possible roles for SAIs regarding these items,
- A sound analysis on the issues and questions concerning the identification, assessment, reporting, budgeting, and monitoring of some key financial exposures, and
- Examples of approaches for the reporting, budgeting, controlling, and monitoring of fiscal exposures.

The document needs to be updated considering but not limited to INTOSAI current initiatives on topics such as:

- Evaluation of Program and Public Policies, particularly those focused on social security schemes, pensions, and health-related programs;
- Genesis and impact of financial crises,
- Government response during crisis (fiscal stimulus, financial interventions, broader interventions) and the aspects to consider so as to minimize the risks involved,
- Relevance of the regulatory framework to minimize the fiscal exposure,
- Impact of reforms on transparency and accountability,
- Proper accounting and reporting,
- Government intervention before natural disasters,
- Relationship between long-term fiscal and environmental sustainability, and particularly
- Challenges faced by SAIs and the role to be played, which is deemed as the main objective of this ISSAI.

INTOSAI's new findings and further information (specifically on the possible roles for SAIs) have been released for this document complete harmonization, since those topics have been dealt within the SAIs community during the last years by the Task Force on Global Financial Crisis, the Working Group on Key National Indicators, the Working Group on Value and Benefits of SAIs, the Working Group on Program Evaluation, the Accounting and Reporting Subcommittee, and the Project Group on Transparency and Accountability. Furthermore, a comprehensive approach on fiscal exposures and its implications for debt management could be gained if the perspective from other international organisms (i.e. UNCTAD Debt Management Conference and DMFAS Program) be incorporated to this work.

It is important to remember that this ISSAI main purpose is to provide an illustrative overview of this complex issue and explore the possible roles for SAIs. Thus, the focus should be kept on SAIs' contribution. Another aspect to be revised is the examples provided in the core sections regarding the Approaches to Reporting, Budgeting and Risk Mitigation, and the Possible Roles for SAIs. Most of them refer to relevant cases in the 90's or even late 80's, so the document could be enriched with best practices and case analyses on this topic.

Finally, the harmonization of the current WGPD's denomination and the correct reference¹ to its products are deemed pertinent during this revision process.

This document shall be aligned with WGPD's products not referred in its contents or which have recently been released, specifically the following:

- ISSAI 5421 (which shall be substituted by INTOSAI GOV 9230): "Guidance on the Reporting of Public Debt".
- ISSAI 5411: "Debt Indicators": this document is relevant since relevant entities should develop accurate cost measurements and integrate them into financial reporting, budgeting, and other policy processes.

Additionally, special attention shall be given to WGPD's current investigation themes, particularly those on:

¹ ISSAI 5430 includes certain references to the "Guidance on Definition and Disclosure of Public Debt" (which is a document to be withdrawn and substituted by the contents of the "Guidance on the Reporting of Public Debt", INTOSAI GOV 9230). Thus, the related bibliographic references shall be amended.

- the impact of financial crises on public debt (USA),
- the assessment of human resources employed in debt contracting (Fiji²)
- the risk assessment and reduction of probable effects on debt structure (Yemen),
- the evaluation of information systems related to public debt management (Brazil).

3.7 ISSAI 5440 Guidance for conducting a public debt audit – the use of substantive tests in financial audits

This ISSAI is still useful and must be kept updated, because this is a guide seeking to increase the Public Debt Auditing capacity by providing a general framework that can be used to approach the audit of public debt and specific advice on how to conduct substantive audit tests. Since the guide information is presented in general terms, the identification of concepts and issues by auditors is eased when examining public debt. Thus, the ISSAI is useful since it facilitates the development of relevant and effective audit processes by SAs, taking into account existing factors within national environments. Additionally, it comprises not only the INTOSAI work on public debt management, but also that of the IMF and the World Bank. (i.e. Guidelines for Public Debt Management). Furthermore, the guide is useful considering that it addresses specific substantive audit tests, and presents analytical procedures and substantive audit tests for derivatives.

The ISSAI 5440 draws on the INTOSAI Accounting Standards. Thus, the WGPD should be aware on the PSC's revision to the Fundamental Auditing Principles (particularly on ISSAIs 300: Field Standards). Besides, since this document assumes the conduct of a financial audit (not a performance review), attention should be paid to any relevant amendment by PSC to the set of ISSAIs 1000-2999 "Implementation Guidelines on Financial Audit". Additionally, this guide could be enriched considering INTOSAI's current work on:

- Principles and good practices on transparency and accountability,
- Monetary and fiscal policies,

² This investigation is led by Fiji and merged into the Investigation team that leads the theme of "Public Debt Management Office".

- Debt indicators,
- Debt management and fiscal vulnerability,
- Quality control for SAIs, and
- Proper accounting and reporting.

This guide addresses the audit of wholesale direct public debt instruments, it assumes the conduct of a financial audit with the aim of providing an opinion on a set of financial statements, and it does not include statistical sampling procedures. Therefore, any INTOSAI findings or investigations of retail debt, performance debt audits and statistical procedures may be subject of separate guides.

Finally, the harmonization of the current WGPD's denomination and the correct reference³ to it's products are deemed pertinent during this revision process.

Although this document has already been aligned with the ISSAI 5410 "Guidance for Planning and Conducting and Audit of Internal Controls of Public Debt" (specifically on the audit procedures for testing internal control), it would be appropriate to take into account the work on two additional specific topics:

- Public debt management strategy and inherent costs, which has been disseminated through the ISSAI 5420 "Public Debt Management and Fiscal Vulnerability: Potential Roles for SAIs". This ISSAI is also relevant because it comprises the relevance of SAIs to encourage data disclosure and the promotion of the need for a proper regulatory and supervisory framework to be adopted for the financial services sector.
- Debt indicators (ISSAI 5411), because it covers, among other topics, the financial indicators, which show the liabilities' market performance.

Besides, there are still references to the "Guidance on Definition and Disclosure of Public Debt", which must be amended so as to refer the "Guidance on the Reporting of Public Debt", which is an updated version.

³ ISSAI 5430 includes certain references to the "Guidance on Definition and Disclosure of Public Debt" (which is a document to be withdrawn and substituted by the contents of the "Guidance on the Reporting of Public Debt", INTOSAI GOV 9230). Thus, the related bibliographic references shall be amended.

Additionally, attention shall be given to WGPD's current investigation themes, particularly those on:

- Public debt management office (TBA),
- Contingent debt (Ukraine),
- Risk assessment and the reduction of probable effects on debt structure, and the internal control system on public debt management (Yemen), and
- Evaluation of information systems related to public debt management (Brazil).

3.8. INTOSAI GOV 9230 Guidance on definition and disclosure of public debt

See 3.4. above.

4. Recommendations to the WGPD

Taking this evaluation into account we recommend the homogenization of the concepts used in our documents. The priority will be to review the concepts of debt sustainability, vulnerability, its management and risk administration, as well as those related to audit. We also recommend that overlaps between documents should be eliminated during the revision process.

4.1 Documents to be revised

- ISSAI 5410 needs to be harmonized with the other Specific Guidelines on Audit of Public Debt and probably with ISSAIs 100-4999 as soon as their new versions will be available. In this case there is an opportunity to introduce modifications, in line with the ongoing work on information systems, and to update the text as well as to make some editorial changes.
- The ISSAI 5421, the INTOSAI GOV 9230 and the PDC document "Guidance on reporting public debt" should be merged, eventually updated with recent examples, and harmonized with the other Specific Guidelines on Audit of Public Debt. Editorial modifications could be introduced as well.
- ISSAI 5422 needs to be harmonized with the other Specific Guidelines on Audit of Public Debt.
- ISSAI 5430 needs to be harmonized with the other Specific Guidelines on Audit of Public Debt.

- ISSAI 5440 needs to be harmonized with the other Specific Guidelines on Audit of Public Debt.

4.2 Timetable

Since we can't conclude our revision before we have the results of the PSC revision, we propose that we start by undertaking the revision our documents along the lines defined above. This process will lead us to new versions of our documents, discussed and accepted by the WGPD by the end of 2012. The harmonization, if needed, with ISSAIs 100-4999 and the general glossary would take place as soon as possible but no later than 2014. The due process to get the approval by the INTOSAI members could be finished in the INCOSAI 2016.

4.3 Distribution of tasks

The WGPD should decide during the 2011 meeting which members are going to lead the task of revision of each document (or group of documents) and what are the contributions of the other members.

5. Further work

Having examined the ISSAIs produced by the WGPD we would like to open the discussion on the need to complete the present framework with other documents.