

**INTOSAI Public Debt Committee Meeting  
Buenos Aires, Argentina  
5-6 June 2006**

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**Member States Questionnaire on  
Contingent Debt – Outcomes and  
Recommendations**

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# Reminder – work completed to date

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## **Mexico City 2003**

- the PDC agreed to undertake further work in the area of contingent debt. UK NAO was invited to prepare a draft questionnaire on contingent debt for circulation to PDC members.

## **Moscow 2004**

- draft questionnaire presented and agreed by the PDC. Subsequently, the questionnaire was circulated for completion by PDC members.

## **Bulgaria 2005**

- the results of the questionnaire were presented. UK NAO was invited to prepare a paper on the outcomes and recommendations arising from the questionnaire results.

# Current work

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## Buenos Aires 2006

- presentation of a paper on the outcomes and recommendations arising from the questionnaire results

## Approach

- the paper highlights the main conclusions arising from the questionnaire
- makes recommendation for SAIs to consider when planning work in the area of contingent debt
- recommendations are based around 7 specific areas

# Current work

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## Structure of paper

- definition of contingent debt
- identification and classification of contingent debt
- assessing the expected cost of contingent debt
- reporting of contingent debt
- budgeting for contingent debt
- control mechanisms and risk management
- role of the SAI

# Definition of contingent debt

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## Outcome

- there is general understanding of the concept of contingent debt. However, terminology and precise interpretations differ which creates a risk of misunderstanding.

## Recommendation 1

- when conducting work on contingent debt, and if not already in place, the SAI should at an early stage, seek agreement with relevant entities on the terminology to be used and its precise meaning.

# Identification & classification of contingent debt

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## Outcome

- not all countries have effective systems in place for the identification and classification of contingent debt
- those that do have systems in place adopt different approaches – (i) fiscal risk matrix (ii) debt spectrum (iii) GAAP approach

## Recommendation 2

- when conducting an audit of contingent debt figures, the SAI should consider the integrity of the systems that produced them – for example, to ensure the completeness and correct disclosure of the figures presented for audit. More generally, scope may exist for the SAI to add value through an examination of how the government identifies and classifies its liabilities, including contingent debt.

# Assessing the expected cost of contingent debt

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## Outcome

- most countries make some efforts to calculate the expected cost of at least some elements of the government's contingent debt
- government guarantees are the most common area where calculations of expected cost are made

# Assessing the expected cost of contingent debt

## Recommendation 3

- when examining the expected cost of contingent debt the SAI should include consideration of the following issues:
  - has the government attempted to assess (a) the total potential liability and (b) the expected cost, for each type of contingent debt identified. Does the assessment encompass a range of scenarios?
  - for those areas where no attempt has been made to assess the potential liability and expected cost – could such an assessment be made using practical and reliable techniques or is the contingent debt unquantifiable?
  - does the government produce appropriate descriptive information about non-quantifiable contingent debt?

# Assessing the expected cost of contingent debt

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## Recommendation 3

- when examining the expected cost of contingent debt the SAI should include consideration of the following issues:
  - for those areas where the potential liability and expected cost have been estimated – have suitable techniques been used to produce reliable figures?
  - is implicit debt a neglected subject? – given the potentially large scale of the contingencies that fall into this debt classification is there a need for work on the total value and expected cost of implicit contingent debt, taking into account the risk of ‘moral hazard’?

# Reporting of contingent debt

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## Outcome

- the ability of a country's Parliament to oversee effectively the contingent debt taken on by the government is determined largely by the adequacy of reporting arrangements. A wide variety of practice exists between different countries:
  - annual report from government to Parliament which includes a section on contingent debt
  - annual statement of guarantees
  - audited financial statements
  - government's annual budget statement
  - ad-hoc reports on specific aspects of contingent debt

# Reporting of contingent debt

## Recommendation 4

- when considering the adequacy of arrangements for the reporting of contingent debt information to Parliament, the SAI should assess whether the information is:
  - o complete – does it cover all material elements of contingent debt?
  - o understandable – can it be understood by those receiving it?
  - o accurate – where appropriate, does it reflect audited amounts?
  - o regular and consistent – does the frequency and form of the information provided facilitate effective ongoing oversight?

# Budgeting for contingent debt

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## Outcome

- many countries recognise the expected costs of certain contingent debts in the government's budget
- budgetary recognition of contingent debt is generally restricted to areas where the government expects costs to be incurred within the period covered by the budget.
- implicit contingent debt is generally not recognised in the government's budget.

# Budgeting for contingent debt

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## Recommendation 5

- when considering the government's budgetary arrangements for contingent debt, the SAI should consider whether budgetary outcomes are aligned with the government's work to assess the expected costs of contingent debt. In particular, do the budgeted amounts for contingent debt appear adequate to cover the costs likely to be incurred by the government?

# Control mechanisms and risk management

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## Outcome

- nature of control mechanisms – countries use both legal and administrative measures. Generally these impose some form of approval process around the take on of new contingent debt.
- risk management techniques – tend to be complex methodologies. Practice varies, but often involves estimating the expected costs of significant ‘risky’ contingent debts.
- variability of application – significant variations exist in the application of risk management techniques across the full range of contingent liabilities and the extent to which risk management is co-ordinated on a centralised basis.

# Control mechanisms and risk management

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## **Recommendation 6**

- when examining the control and risk management processes around contingent debt, the SAI should consider whether the arrangements in place are appropriate for the country's circumstances and whether there are practical improvements that should be made.

## **Recommendation 7**

- because of their potentially complex and specialised nature and prior to engaging in detailed work, the SAI should ensure that it has suitably skilled resources available to undertake an expert assessment of government risk management systems.

# Role of the SAI

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## Outcome

- given the potential significance of contingent debt to fiscal stability, the SAI's mandate should enable it to undertake financial or performance audit work in this area.

## Recommendation 8

- where SAIs do not have a mandate to undertake financial and performance audit on contingent debt, they should consider the merits of seeking to extend their powers to allow such work to take place.

## Recommendation 9

- the SAI should ensure that its work in respect of contingent debt reflects its own and Parliament's assessment of the relative importance of this subject area in their country while making an appropriate contribution to Parliamentary accountability.