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Host Country Systems and Harmonizing Donor Audit Requirements: A Case Study of Ghana*

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Host Country Systems and Harmonizing Donor Audit Requirements: A Case Study of Ghana

By Rob Kevlihan, MAcc, FCA, MA, Ph.D[1]

Abstract

In 2011 the author was commissioned to review current financial audit practices of the Government of Ghana (GoG) and twelve development partners (DPs) that relate to the provision of bilateral and multilateral assistance to the GoG and its constituent entities (including Ministries, Districts and Assemblies – MDAs).[2] The report was commissioned by the Ghana Audit Working Group (AWG), a sub-group of the Ghana Public Financial Management Working Group (a body that brings together the GoG and DPs) and was paid for by USAID. The purpose of the study is to analyze the various audit scopes of work (or terms of reference), criteria and requirements used by DPs and the Ghana Audit Service (GAS), extrapolate common standards, and develop consensus around commonalities within the audit process. This paper summarizes the findings of this research, making the findings available to a wider audience. This case study will be relevant to anyone interested in the nuts and bolts of efforts at donor harmonization, use of host country systems and public policy relevant to development assistance.[3]

Keywords: Ghana, Donor policies, audit policies, donor harmonization, host country systems, Public auditing, auditing standards, international auditing standards

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2 Including the African Development Bank (ADB), Canadian International Development Agency (CIDA), Danish International Development Assistance (Danida), the UK's Department for International Development (DFID), The European Union, Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ, formerly GTZ), Japan International Co-operation Agency (JICA), KFW Bankegruppen (KfW), the Governments of the Netherlands and Switzerland, the United States Agency for International Development (USAID) and The World Bank

3 The author would like to recognize the support and leadership of Mr. Richard Quartey, the Auditor General of the Republic of Ghana of this process and of Ms. Karen Fall (USAID), who as co-chair of the AWG during this period provided considerable assistance and support. The author would like to thank all members of the AWG for their support and input into this process, particularly the members of the task group formed to supervise this project, Ms. Lyne Paquette (USAID), Ms. Janet Mortoo (The European Union), Mr. Robert DeGraft-Hason (The World Bank) and Mr. Benjamin Codjoe (Ghana Audit Service). Any errors or omissions in this report are the responsibility of the author. All views expressed are the authors and do not reflect the views of any organization or government.

Abbreviations

AAS	Annual Audited (Financial) Statements
ADB	African Development Bank
AICPA	American Institute of Certified Public Accountants
AWG	Audit Working Group
CIDA	Canadian International Development Agency
CPE	Continuing Professional Education
Danida	Danish International Development Assistance
DFID	Department for International Development
DP	Development Partner
GAGAS	Generally Accepted Government Auditing Standards
GAO	Government Accountability Office
GAS	Ghana Audit Service
GBS	General Budget Support
GIFMIS	Ghana Integrated Financial Management System
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
GoG	Government of Ghana
IFAC	The International Federation of Accountants
INTOSAI	The International Organization of Supreme Audit Institutions
ISSAI	International Standards of Supreme Audit Institutions
ISA	International Standard on Auditing
JICA	Japan International Cooperation Agency
KfW	KfW Bankengruppe
MDAs	Ministries, Districts and Assemblies
MOU	Memorandum of Understanding
PCAOB	Public Company Accounting Oversight Board
PFM	Public Financial Management
RIG	Regional Inspector General
SAS	Statements of Auditing Standards
SECO	Swiss State Secretariat for Economic Affairs
SOW	Scope of Work
TOR	Terms of Reference
USAID	United States Agency for International Development
WB	The World Bank

Introduction

This paper reviews financial audit practices of the Government of Ghana (GoG) and twelve development partners (DPs) in place in 2011 that related to the provision of bilateral and multilateral assistance to the GoG and its constituent entities (including Ministries, Districts and Assemblies – MDAs). In addition to a review of Ghana Audit Service (GAS) requirements, a total of twelve DPs were approached to participate in this review. DPs included in the initial design of this study included: ADB, CIDA, Danida, DFID, The European Union, GIZ (formerly GTZ), JICA, KFW, the Governments of the Netherlands and Switzerland, USAID and The World Bank. Levels of participation and submission of audit guidelines varied, resulting in some limitations to this study. Where possible, the consultant supplemented material submitted with documentation available from on-line sources. Financial auditing is understood, in this context, to be concerned with the expression of an audit opinion on a set of financial statements and does not cover compliance or performance audit requirements.[4]

The paper begins with an overview of international auditing standards as they apply to the Government of Ghana and donor partners. The paper then delves into commonalities and differences in audit criteria between donor partners, considering issues that need to be addressed in seeking to harmonize donor approaches to the audit of funds provided to the government. The final section reviews next steps, including suggested ways forward towards greater harmonization of donor audit requirements.

As this paper will illustrate, while significant progress has been made at the international level in harmonizing auditing standards, common audit standards are only one piece of the puzzle when it comes to the harmonization of donor audits of funds provided to developing countries. Such harmonization is important in reducing the administrative burden on recipient governments while also streamlining donor processes and maximizing efficiencies to be gained from co-ordinated approaches to development assistance. Unfortunately, however, the devil, as with many such things, is in the detail. As this paper lays out, many practical issues remain to be addressed – both on the side of recipient governments and on the side of development partners – before the goal of a single consolidated audit of all donor funds, conducted at one time, in harmonization with recipient government audit procedures, can be achieved. The difficulty of achieving such a lofty goal should not act as an impediment to ambition, however. It is to be hoped that this case study will be useful in informing continuous improvements in public financial management systems – both recipient and donor systems – moving forward.

4 Financial auditing focuses on the audit of financial statements such as income and expenditure accounts, statements of cash flow and balance sheets. Compliance audits focus on compliance with other rules and regulations related to the utilization of public funds and are typically determined by national legislative frameworks. Performance audits are concerned with whether funds were well spent or not - in other words, on the impact of government expenditure, rather than on narrower questions of whether financial and legislative rules and regulations are followed.

Which Auditing Standards?

The starting point for any effort to harmonize approaches to auditing must be to consider the regulatory and professional frameworks which set out host country and donor audit requirements. While each country is required to adhere to procurement and public financial management rules that are set out within national legislative frameworks, as we shall see, the standards for auditing adherence to those national frameworks have to a large extent been internationalized and as a consequence, harmonized. This section begins with a comparison of international auditing standards between private and public sector auditing (both of which are utilized by DPs), before also discussing US auditing standards (which are relevant to US overseas development assistance in Ghana).

International Auditing Standards

With the exception of the US government (see below), all development partners reviewed in this case study, together with the Ghana Audit Service (GAS), rely on international auditing standards (either explicitly or implicitly) as the audit framework relevant to financial audits in Ghana; this manifests itself in a commitment to either International Statements of Auditing (ISAs) or International Standards of Supreme Audit Institutions (ISSAIs) or both.

The development of ISAs and ISSAIs as distinct sets of standards is related to historical differences between accounting and audit regulations in the private and public sectors that have been largely eroded in recent years. Internationally, there are two important audit standard setters; the International Federation of Accountants (IFAC) who promote International Statements of Auditing (ISAs) that are primarily intended for the private sector and the International Organization of Supreme Audit Institutions (INTOSAI) who promote International Standards of Supreme Audit Institutions (ISSAI) that are primarily intended for the public sector.

IFAC is an international association representing the accountancy profession. It has 159 accounting organizations affiliated to it as members or associates, drawn from 124 countries worldwide.[5] IFAC produces and promotes the use of ISAs. These standards have been developed in the public interest to promote best practices in the conduct of audits worldwide. At the time of this case study (2011), there were 32 ISAs relevant to financial audits. Historically these ISAs have been associated with private sector auditing – i.e. with the audit of private enterprises and non-governmental organizations by private audit firms.

INTOSAI is an umbrella organization of government audit agencies, including the Ghana Audit Service. Founded in 1959, as of 2011 INTOSAI had 189 full members and two associate members. INTOSAI provides an institutionalized framework for Supreme Audit Institutions (SAIs) to promote the development and transfer of knowledge, improve government auditing practices worldwide and enhance the professional capacities, standing and influence of member SAIs in their respective countries.[6] The term ISSAI is a relatively new designation, having been adopted at the 20th INTOSAI Congress, held in Johannesburg in November 2010. ISSAIs cover a number of areas of concern to public auditors, including financial, compliance and performance auditing. With respect to financial auditing, the new

5 IFAC, 2010, Handbook of International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements, p3.

6 INTOSAI website, available at http://www.intosai.org/en/portal/about_us/ [Accessed 28th March 2011].

ISSAIs (in the ISSAI 1000 series) adopted IFAC's ISAs with supplemental clarification notes (called Practice Notes) where necessary to adapt them to government auditing requirements.

Comparing ISAs and ISSAIs

Because ISSAIs relevant to financial auditing standards have incorporated ISAs (while also providing supplemental Practice Notes) there is now de facto convergence in terms of content between ISSAIs and ISAs. As a consequence, donor or host country compliance to either set of standards in financial audits will (with one or two caveats set out below) ensure a harmonized approach. Despite this convergence in content, however, potential for divergence in the application of this content can still arise.

ISSAI 1000, entitled "General Introduction to the INTOSAI Financial Audit Guidelines", highlights this potential difference. Section 35 of ISSAI 1000 makes clear that ISSAIs (unlike IFAC's ISAs) do not use the terms "shall" and "should". Instead, despite the use of the word 'standard' in their title, ISSAIs in fact represent guidelines only, and do not, as a consequence, override any national audit standards until such time as they are officially adopted or incorporated by the national system as binding. This provision is extended to the way in which ISAs are incorporated into ISSAIs. This has an important potential implication - that national SAIs could, in theory, claim adherence to ISSAIs while effectively opting out of certain provisions because of their voluntary nature.

There are two ways to overcome this potential problem – the first is to formally incorporate ISSAIs as national audit standards, making clear that adherence to them (and by extension to the ISAs contained therein) is required and that the terms of Section 35 of ISSAI 1000 do not apply. The manner of this incorporation should be flexible enough to allow for any future amendments or additions to ISSAIs to be easily added to national requirements. In the absence of such domestic incorporation, stating that audits were performed in accordance with ISSAIs leaves open some potential ambiguity as to the comprehensiveness of ISSAI standards applied.

Alternatively, SAIs can perform financial audits in accordance with both ISAs and ISSAIs; this binds SAIs to the required stipulations of ISAs, while also recognizing the additional relevance of the practice notes included in ISSAIs that provide guidance on how best the ISAs should be applied in the context of public sector auditing. As a consequence, stating that financial audits have been prepared in accordance with ISAs and ISSAIs represents a stronger statement than stating that audits have been prepared with respect to ISSAIs alone, or indeed, that they have been prepared with respect to ISAs alone.[7]

Despite these caveats, however, overall it is fair to say that with the exception of the US, reliance on international auditing standards by development partners greatly simplifies the degree of complexity faced in considering which audit standards to be adhered to in the conduct of financial audits of DP funds. Nonetheless, given that the objective is to harmonize all DP audit requirements, a further review and comparison of US standards to international standards is necessary to determine the full picture with respect to audit standards.

7 More generally, SAI adherence to ISSAIs is also beneficial as the scope of ISSAIs is much broader than financial audits, as they also encompass other issues of concern to SAIs, including compliance and performance audits.

US Auditing Standards
There are three primary auditing standard setters in the US – the Public Company Accounting Oversight Board (PCAOB), the American Institute of Certified Public Accountants (AICPA) and the Government Accountability Office (GAO).

The PCAOB was established under the Sarbanes-Oxley Act and is responsible for oversight of publicly listed companies in the US. The AICPA sets auditing standards for all other private companies and non-governmental organizations, while the GAO is responsible for establishing federal government auditing standards in the US (which are compiled in the so-called "Yellow Book"). GAO standards have also been widely accepted by other public sector institutions at state, municipal and local levels within the US and importantly, also apply to the audit of funds provided by the US government to other organizations, including funds provided by US government agencies working overseas.[8]

However, despite institutional differences between these three US standard setters, the actual core content of much of their standards is the same and derives from the AICPA's Statements of Auditing Standards (SAS). The Yellow Book explicitly notes this; section S1.15a states that the AICPA SAS's with respect to fieldwork and reporting have been directly incorporated into US Generally Accepted Government Auditing Standards (GAGAS).

Convergence in Auditing Standards
The common auditing framework in the US between AICPA SASs and GAGAS has been complemented by a related convergence between US and international auditing standards. The AICPA has, for example, been engaged in a re-presentation of its Statements of Auditing Standards to ensure consistency with IFAC's recently clarified ISAs. These revised (and converged) US auditing standards came into place for audits (that are not audits of publicly quoted companies covered by PCAOB standards) for periods commencing on or after the 11th December 2011.[9]

This process of re-presentation and consequent convergence is possible because of the basic similarities between these two sets of standards, a situation in stark contrast to the extended process (still on-going) of convergence in international and US financial accounting and reporting standards. While a detailed review of PCAOB standards (which apply to US publicly listed companies only and so are not directly relevant to this study) is outside the scope of this study, the similarity of PCAOB audit standards to AICPA SASs does provide us with some useful insights based on existing research. In 2009 the European Commission commissioned the University of Maastricht to compare ISAs with the PCAOB's Auditing Standards. The report concluded that only five areas of substantive difference existed between ISAs and the PCAOB standards.[10] These included US requirements (driven Sarbes-Oxley and applicable only to US listed companies) to report an opinion on the quality of internal controls, the inability under ISA standards to make reference to the work of another auditor, more prescriptive documentation requirements under PCAOB, differing approaches

8 Although derogations are permitted in certain circumstances – see discussion below for more detail.
9 Fraser, P. Nicholas. 2010. "A single set of worldwide auditing standards, The road is long..." International Journal of Disclosure and Governance 7 (4):298-309.
10 Vanstraelen, Ann, Roger Meuwissen, W. Robert Knechel, Heidi vander Bauwhede, Rogier Deumes, Caren Schelleman, Laury Bollen, and Harold Hassink. 2009. "Evaluation of the differences between International Standards on Auditing (ISA) and the standards of the US Public Company Accounting Oversight Board (PCAOB)." Maastricht, Netherlands: Maastricht Accounting, Auditing and Information Management Research Center (MARC).

to risk assessment and differing time horizons with respect to assessment of the going concern assumption (PCAOB 12 months, ISA at least, but not limited to, 12 months).

The report went on to conclude, on the basis of their comparative analysis and discussions with other experts in this field, that there was very little to no difference between ISAs and PCAOB standards that have an impact on general principles and responsibilities with respect to the audit of financial statements, quality control for audit firms, analytical procedures, written representations, comparative information in financial statements, the audit risk model and planning audits (exclusive of risk assessment and responses to assessed risk), materiality, sampling, fraud, illegal acts and compliance with laws and regulations, fair value accounting and auditing, confirmation processes, the audit of inventories, auditing estimates, subsequent events, auditing information from a service organization, use of specialists during audits, communication between predecessor and successor auditors and audit communications.

This general convergence in standards is also reflected in presentations made by senior US government officials and other experts in this area. In December 2010, for example, two senior GAO officials, a technical expert from IFAC and a senior government official from the South African government audit service made presentations in South Africa emphasizing this same point.[11] The presenters noted that in their view, the Yellow Book was fully consistent with ISSAIs because the Yellow Book incorporates the AICPA's SAS's which in turn have been converged with IFACs ISAs.[12] These presentations also noted that the GAO is on record in supporting global convergence in auditing standards, with GAO staff having provided support to the AICPA in the convergence of SASs with ISAs, while also supporting INTOSAI in the development of their practice notes. Furthermore, GAO staff have reportedly used the ISSAIs as a reference in writing proposed changes to the Yellow Book issued in August 2010 (and finalized in 2011).

The picture that emerges then, is of a broadly converging set of auditing standards for both commercial enterprises, non-governmental organizations and governmental units worldwide, with the possible exception of some audit requirements related to the audit of US publicly listed companies.

But some important areas of divergence remain

That said, a handful of significant content differences remain between GAGAS and ISSAIs, leaving aside the question of national incorporation and the voluntary / mandatory nature of these standards discussed in the context of ISAs above, which also apply to any comparison of GAGAS and ISSAIs. In terms of content, areas of notable difference include specific GAGAS requirements for the continuing professional education (CPE) of public auditors and provisions related to processes of peer review.[13]

11 Jeanette Franzel (Managing Director, GAO), Kelly Anerud (Senior Technical Manager, IFAC), Jan Van Schalkwyk (Corporate Executive, Auditor-General of South Africa) and Gail Flister Vallieres (Assistant Director, GAO), 2010, "Convergence of Public Sector Audit Standards".

12 The Yellow Book adding public sector considerations and requirements in the same manner as ISSAI practice notes.

13 This section provides an overview of important differences only. As the sections which follow makes clear, USAID acceptance of international standards in the conduct of audits by SAIs, and RIG/Dakar review and acceptance of the GAS as an eligible auditor for USAID purposes makes these difference irrelevant to the goal of audit harmonization in Ghana.

With respect to CPE, section 3.47 of the Yellow Book sets out a specific minimum requirement for public auditors. For those performing (but not planning, directing or reporting) audits, a minimum 24 CPE hours every two years directly relevant to government auditing is required. Those responsible for planning, directing or reporting are required to take an additional 56 hours CPE (making a total of 80 hours), with at least 20 hours CPE required per annum. These requirements remain unchanged in the current Exposure Draft released in 2010 and expected to be issued as the revised Yellow Book in 2011. This mandatory specification of required CPE hours for auditors differs from the non-specific approach adopted in ISSAIs. ISSAI 40, "Quality Control for Supreme Audit Institutions", for example, recommends that SAIs should have policies and procedures in place to ensure that personnel have the capacity to carry out work assigned, while also encouraging professional development. It does not specify any minimum hours of CPE required by audit staff.

A similar difference relates to requirements for peer review. Section 3.55 of the Yellow Book sets out a requirement for public auditors to be peer reviewed by an external reviewer at least once every three years. This requirement is also maintained in the current 2010 exposure draft. ISSAI 40, on the other hand, while encouraging SAIs to take advantage of peer review opportunities, does not require peer review.

These differences, while noteworthy, do not present insurmountable obstacles to a harmonized approach to auditing. The Yellow Book offers two possibilities if harmonization between GAGAS and ISSAIs is sought during the course of planning and implementing any particular audit; the first option allows for international auditing standards to be utilized in addition to GAGAS – what might be termed the GAGAS plus option. This would require auditors to meet US standards, including those provisions that relate to CPE and peer review discussed above. In the case of audits conducted by the Ghana Audit Service, this would necessitate a commitment to institute quality assurance processes that track CPE hours for individual auditors. In addition, while each auditor is responsible for his / her own adherence to the minimum CPE, as a practical matter, it is also likely that the GAS would need to co-ordinate and / or organize regular refresher and training courses to allow its auditors to reach these minimum CPE requirements on an on-going basis. The second requirement – for external peer review – appears, on the surface, to be more easily attainable, simply requiring a firm commitment from the GAS to institute such a review every three years, and actualization of this review within the requisite period. Engagement in peer review processes could also bring additional benefits to GAS, as it too could reciprocate in acting as a peer reviewer of other SAIs, if appropriate.

The second option allows for the possibility of a modified GAGAS audit opinion that specifies the areas of audit related work that were not conducted in accordance with GAGAS – i.e. a GAGAS minus option. This option has been commonly utilized by private audit firms in conducting recipient contracted financial audits of USAID funds. If the differences enumerated under the GAGAS minus option are not considered to have had a significant impact on the quality of the audit conducted, such audit reports can be accepted by US government agencies. It is to be noted that partial progress on CPE and peer review would still necessitate a modified opinion under GAGAS rules, but would reduce the weight given to these modifications and / or could eliminate some (for example, if peer review was instituted, but minimum CPE requirements were still in process). A third option, involving adherence to international auditing standards, is also open to GAS with respect to USAID funding.

To conclude then, US government audit requirements, while different in some respects from international auditing standards, are nonetheless broadly consistent with these standards and any differences can be addressed in a relatively straightforward manner. As a consequence, any divergences in auditing standards that currently exist between development partners do not present an insurmountable obstacle to audit harmonization. However, as the next section discusses in further detail, while auditing standards do not impede financial audit harmonization, other issues can be more difficult to overcome, including the use of diverse funding mechanisms by DPs, differences between financial audits and verifications in DP practice, issues related to the scope of financial audits, differences in reporting requirements and differences in contracting arrangements for auditors.

Commonalities & Differences in Audit Criteria

While the issue of which audit standards to use in the conduct of audits has been addressed in the preceding section and is not considered to be an impediment to donor harmonization of auditing practices, as we shall see, other stipulations of DPs related to audit and verification work (termed audit criteria) nonetheless diverge and as a consequence can act as impediments to harmonization. This section considers these other audit requirements. It necessarily takes a broad approach, considering donor requirements with respect to each of the following themes relevant to audit harmonization:

- Whether an audit opinion is required or not (financial audit versus verification)
- Internal Control Reviews
- Reporting currencies
- Synchronization and Diverse Funding Mechanisms
- Audit Scope
- Audit Opinions and Audit Reporting
- Contracting auditors

Annex 1 summarizes some of the most salient commonalities and differences with respect to DP audit practices between DPs for all but the last of these points, which will be dealt with separately. The sections that follow the table discuss each theme in greater detail.

Whether an audit opinion is required (Financial Audit versus Verification)

The first significant difference is between those DPs that conduct a financial audit and those that do not; while the majority of DPs conduct such audits, the EU and JICA are notable exceptions. JICA does not conduct financial audits as a matter of course except where it is a party to Multi Donor Budget Support (MDBS) or other sectoral support.

The EU has a distinct approach to fiduciary risk that can be contrasted with other DP approaches. While the majority of DPs conduct financial audits,[14] with the option of adding financial verification procedures if considered necessary, the EU typically conducts financial verifications instead of financial audits.[15]

14 The purpose of a financial audit is to allow auditors to express an opinion on the financial statements being audited. The audit opinion is based on detailed audited work conducted that typically allows auditors to place a certain level of assurance on the financial accounting and reporting system from which the financial information is drawn. Such assurance is often supported by a review of internal controls conducted as part of the financial audit process (although the testing and review of controls need not necessarily have taken place at year end).

15 With the exception of budget support funding where common audit arrangements are utilized.

In contrast to financial audits, the purpose of a financial verification is to check transactions against underlying documentation – either in whole or in part. A financial verification can be based on a financial report (i.e. can comprise a verification of transactions that accumulate to the figures presented in a financial report), but need not be. In some instances, for example, a verification exercise might occur on a transaction by transaction basis for very large purchases. The findings of verification exercises are typically used to allow or disallow expenditure or claims for payment; verification is often used in conjunction with funding mechanisms that adopt a reimbursement type approach, and is often considered necessary where DPs place little reliance on recipient financial control and reporting systems, as verifications do not place reliance on internal controls. DPs typically use external verifiers when conducting financial verifications; these DP led verification exercises can be distinguished from routine financial verifications conducted by an internal audit function which are not externally driven.

Verifications are utilized by some DPs (for example the European Union – see below) as an alternative to financial audits, while others use them in addition to financial audits. Verifications have the advantage of often providing higher levels of oversight and assurance than is usual in financial audits. However, they are typically more labor intensive / expensive and time consuming to administer, often do not seek to proactively strengthen host country PFM systems, and indeed, may act as a drain upon these systems because of heavy reporting requirements. That said, verifications do hold recipients, including MDAs, to an exacting standard, and as a consequence may encourage improved financial accounting and reporting practices to the extent MDAs will not receive DP funding until the required documentation is produced to satisfy the verification procedure.

A review of DP audit procedures highlighted the use of verification type approaches by at least three DPs – USAID, the European Union and DFID. However, it is unclear at this time whether DFID actually use its verification approach (termed 'continuous audit') for funding in Ghana. As a consequence, this section will deal with USAID and European Union verification approaches only.

USAID may use financial verifications when recipient organizations do not have adequate financial systems, weak internal controls and a large number of transactions are involved. Payment verification may also be used after an audit where an adverse or disclaimer opinion is issued in order to determine the specific costs that are reimbursable. Standard USAID requirements for financial audits continue to apply to funding in addition to these verification procedures regardless of the circumstances.

The European Union currently utilize a verification approach with respect to three types of funding arrangements – Programme Estimates (PEs), grant contracts and service contracts. While PEs and service contracts require a systematic and representative test of supporting documentation with a particular focus on high value items, grant contracts have more specific verification requirements – verification levels must reach an expenditure coverage ratio of 65% with an exception rate of less than 10%.[16] If the exception rate is over 10%, the coverage ratio should be increased to 85% before reporting. The results of the verification exercise are reported to the European Union who then arrive at their own opinion. In the case of PEs the European Union contracts a private audit firm to conduct this work directly; in both other cases the verifiers are recipient contracted. While the EU has preferred to engage private

16 Service contracts are not used to fund the GoG and are therefore not discussed further.

audit firms for the audit of PEs to date, their guidelines leave open the possibility of using GAS for this purposes.

USAID and the European Union therefore differ on when to utilize verifications, although purpose of a verification exercise once it occurs is quite similar. Nevertheless, because verification procedures are specific to each DP and of necessity will also involve reference to detailed rules related to allowable and disallowable expenditure which can vary by DP, harmonization in verification requirements will be difficult to achieve. However, greater use of host country systems in the processes of verification may prove to be effective in addressing underlying challenges of verification type activities while in the process also assisting in strengthening these same systems.

Options, in this respect include establishing a verification unit within GAS whose role would be to perform external verifications in accordance with individual DP requirements,[17] or alternatively, integrating particular DP verification requirements into joint audits by way of a separate annex to combined SoW/ToRs. Either approach could provide a number of advantages over current reliance on private audit firms; firstly, it would integrate these kinds of reviews into the regular work of GAS, providing them with further insights into the operation of MDA accounting and reporting systems; secondly, these insights could inform GAS risk assessment exercises in planning annual financial audit work; thirdly, integrating verification into GAS auditing would also make it easier for the GAS to ensure, as part of regular audit procedures, that no 'double dipping' is occurring – i.e. expenditure being charged to GoG accounts and also claimed for reimbursement from DPs, a practice that may be difficult to identify under the current verification arrangements using outside firms. Finally, the establishment of a verification unit would necessitate training GAS staff in donor requirements with respect to allowable expenditure etc., providing them with greater insight into DP policies. However, as with financial audits, use by DPs of a GoG verification unit in preference to private audit firms will necessarily be contingent upon any such GoG unit performing required tasks effectively, to a high standard and on a timely basis.

Internal Control Reviews

With the notable exception of JICA (who do not require an audit) and the EU (who conduct expenditure verifications only, and therefore do not normally require a review of internal controls), all other DPs typically include a review of internal controls as part of their approach to financial audits. In addition, both JICA and the EU accede to internal control reviews of budget support funding through the MDBS, while the EU also has a pro forma ToR for standalone internal control reviews. As a consequence, the principle of conducting internal control reviews as part of audit procedures is relatively uncontroversial among DPs.

Reporting Currency

While DPs appear to have become increasingly sensitive to issues of reporting currency in recent years, some divergence in policies continue to apply to particular tranches of funding provided to the GoG. Examples of DPs who may have to change some of their reporting requirements to support harmonization in audit approaches in this respect include: European Union grant and service contracts where the reporting requirement is currently specified in Euros, KFW direct disbursements where the reporting currency is not Ghana cedis, a Swiss funded sectoral budget support program with the Ministry of Energy that requires US dollar

17 Despite some issues related to the fiscal autonomy of the GAS from central government, the GAS, as an SAI, is generally considered to be independent of the rest of the Ghanaian government and can therefore be considered to be an external auditor.

reporting, USAID Fund Accountability Statements (which must be stated in US dollars) and World Bank funding that require US dollar reporting. While it is to be expected that some financial reports will continue to be required in currencies other than Ghana cedis – particularly where funding provided in a foreign currency is utilized to make foreign currency denominated purchases, and / or because of efforts to manage exchange risk, nonetheless, the logic of DP reliance on GoG financial reporting systems is that where possible, DPs should accept financial reports in Ghana cedis in preference to other currencies.

Audit Synchronization

The diversity of funding mechanisms between donors impacts on audit harmonization as requirements for financial audits typically accompany particular funding streams from donors. Diverse funding mechanisms create additional layers of complexity with respect to audit harmonization for a number of inter-related reasons, including issues related to audit synchronization, the number of separate audits actually required, the target audience for these audits, who can conduct these audits, and defining the audit scope and audit reporting requirements. This section will address audit synchronization issues and the number of audits required while the other issues will be addressed separately below.

Audit synchronization problems arise because financial audits are typically required at the end of funding periods. If funding periods of DPs do not correspond to the financial reporting period of the host country government – which in the case of Ghana, is the calendar year, then the audit work required for the financial audit of these funds will have to be conducted at a different time from all other financial audit work as a standalone exercise.[18]

A review of DP practices in this area highlight some differences. While those DP funds programmed as budget support are, by definition, synchronized with GoG financial reporting and audit cycles, other funding provided outside of budget support activities does not necessarily follow the same pattern, and require conscious action by DPs in order to ensure proper synchronization with the GoG fiscal calendar. Examples include:

- The European Union: Funding granted under programme estimates, grant and supply contracts
- GIZ: Short term projects that end before the end of the financial year
- KfW: Some funding under direct disbursement, disposition funds and reimbursement procedures
- Switzerland: Project based funding

Of those that submitted relevant information for review for this study, only two DPs build flexibility into their funding cycles to ease synchronization issues. The World Bank allows funding periods to range between 12 and 24 months in order to ensure that the end date of its funding periods synchronize with the GoG calendar year. USAID audit requirements, while triggered by particular funding thresholds, can be conducted in accordance with the recipient's fiscal year cut-off. USAID also allow recipients 9 months from the end of their fiscal year to complete these audits.

18 A separate but related problem relates to different deadlines for the submission of financial audit reports even when funding periods end at the same time, but is of relatively less importance.

A separate but related problem arises from the number of discrete financial audits actually required. Funding mechanisms that are not budget support or pool funding arrangements each require their own individual financial report and financial audit (or verification – see below), meaning that the number of audits required grows with the number of discrete funding mechanisms being used to disburse funds.

Audit Scope

The term audit scope relates to the breadth and depth of audit work required in order to express an opinion on a particular set of financial statements. Audit scope will be determined by the size and nature of the entity to be audited and its financial statements, together with the kind of audit opinion that is required. This section will address the first of these concerns while the following section will address issues related to audit opinions.

The size and nature of financial statements to be audited are in part determined by donor funding arrangements. Donor practice with respect to financial reporting affects audit harmonization because (in a manner similar to audit synchronization) if each DP requires its own financial report, and each report has to be audited, then a larger number of financial audits are required. One example of separate financial reporting and related auditing requirements relates to the ADB, whose financial reporting and audit guidelines assume the establishment of a standalone project implementation unit (PIU), responsible for the production of its own set of financial statements. Other examples of separate financial reporting requirements mirror those listed above under audit synchronization. One solution to this problem is relatively simple to state, but difficult to implement, and involves movement on both the part of the GoG, and in some cases, of DPs.

In the case of the GoG, it requires a financial accounting and reporting system that has the capacity to separately account for donor funding and expenditure financed by that funding when so required by DPs, and the capacity to produce comprehensive financial reports that can show these detailed expenditure breakdowns to a level of detail that will satisfy donor financial reporting requirements. While a review of the detailed specifications of the new Ghana Integrated Financial Management Information System (GIFMIS) was outside the scope of this case study, it is anticipated that this new system will have the capability to produce this kind of detailed financial information. However, full roll out of GIFMIS is still on-going, while arriving at the point where it will be possible for the GoG to produce comprehensive, consolidated financial reports that can be relied upon by DPs and that can receive a 'clean' audit opinion from the GAS will require continued commitment by the GoG and will take some time.

1.

On the DP side, reliance upon a single set of financial statements, even a set that provides, where necessary, a breakdown of DP contributions (recognized as income) and DP funded expenditure (recognized as expenditure), also requires DP flexibility on reporting currency and with respect to reporting formats. It also requires close co-ordination between DPs and the GoG to ensure that the GoG's financial accounting system properly captures all DP contributions, whatever the 'entry point' of these contributions into the GoG system. Ideally, such an accounting system should also capture DP donations in kind in addition to cash support.

Audit Opinions and Audit Reporting (including compliance issues)

A separate but related issue concerns the kind of audit opinion required. With respect to audit reporting, audit reports are commonly required to express an opinion on the whether the

financial statements reviewed offer a "true and fair" view; ISA 200, "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards of Auditing", expresses the overall objective of audits as follows:

> The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. In the case of most general purpose frameworks, that opinion is on whether the financial statements are presented fairly, in all material respects, or give a true and fair view in accordance with the framework. An audit conducted in accordance with ISAs and relevant ethical requirements enables the auditor to form that opinion (ISA 200, page 72, paragraph 3).

It is to be expected, in this regard, that audits of DP funds granted to recipients include a review to ensure that the expenditure has been spent in compliance with the underling funding or financing agreement. Because the terms and conditions of particular agreements can vary, it is understood that any such audit process will always need to refer back to underlying agreements to verify proper compliance. The only practical way in the short term in which divergent assessments of contract compliance between DPs could be comprehensively avoided would be for DPs to utilize pooled funding or budget support type funding arrangements which would result in the same contract terms and conditions between DPs and the GoG.[19] As a consequence, at this stage, any joint entity audit conducted by DPs, while specifying compliance as one of the objectives of the audit, will continue to require the auditors to perform distinct compliance work for each DP on how their funds were spent, and the extent to which the GoG was compliant with particular DP contractual terms and conditions.[20]

Looking beyond the question of compliance with funding contracts, a review of DP requirements also reveals some variation in requirements for the wording of audit opinions that could be avoided through modification of individual DP audit guidelines or ToRs for audit engagements. Examples of variations in required wording of audit opinions include a DANIDA requirement for auditors to report their opinion on whether the bookkeeping is in accordance with "sound bookkeeping principles" in their audit opinion,[21] standard provisions in KFW terms of reference for audit engagements (other than Audit of Disposition fund ToRs) that require a schedule to be included in the audit report showing receipts and

19 Although in the case of pooled arrangements, delegated responsibility may simply result in the divergent requirements being pushed up a level from the DP – GoG relationship to the DP – supervising DP relationship, unless both DPs agree to abide by the financial reporting and audit procedures of the other. This has actually occurred in the case of USAID support to BUSAC, a pooled funding arrangement managed by Danida, where USAID is permitted under its own funding criteria to place reliance on the financial accounting, reporting and auditing systems of another private international organization using the same mechanism it uses to fund UN and other multilateral agencies. It should be noted, however, that this approach, while reducing audit complexity, does not, in and of itself, further audit harmonization, as the audit requirements of the lead / managing DP will continue to apply to recipients.

20 However, a common entity approach will allow DPs to look at the narrower area of compliance for financial audit purposes in a co-ordinated manner; compliance is relevant to financial audits to the extent that it is necessary for auditors to consider the extent that non compliance could result in financial misstatement or impede a true and fair view of the financial statements.

21 In practice Danida standard Dandia ToRs for audits in Ghana use standard language in preference to the language set out in Danida guidelines; nonetheless, it is recommended that the wording of the guidelines be changed to reflect actual practice.

disbursements during the audit period, [22] and some redundant language in Swiss audit reports referring to SECO guidelines.

Contracting Auditors

Another area of potential commonality and divergence goes to the question of who can actually audit donor funds for development partners. Two questions arise in this respect – the role of the Ghana Audit Service, and the means utilized to identify suitable audit firms that have met donor requirements as competent auditors. An analysis of donor practice in this area shows considerable variation, with DPs engaging private audit firms directly, using GAS and in some instances utilizing private audit firms sub contracted by GAS. The table below summarizes DP practice in this regard.

Ref	Donor Partner	Number of Financing Models reviewed with distinct audit requirements	GAS or GAS Contracted Auditor	Direct Hire of Private Audit Firm (DP contracted)	Private Audit Firm or GAS (Recipient contracted)	No Audit or Not Applicable
1	ADB	1	0	0	1	0
2	CIDA[23]	1	1	0	0	0
2	Danida	5	3	0	2	0
4	DFID	4	3	0	1	0
5	European Union[24]	3	1	1	1	0
6	GIZ	1	1	0	0	0
7	JICA	3	2	0	0	1
8	KfW	4	1	0	2	1
9	Netherlands	1	1	0	0	0
10	Switzerland	5	5	0	0	0
11	USAID	4	0	0	4	0
12	World Bank	1	1	0	0	0
	Totals	33	19	1	11	2

Some clarification of the four different categories presented may be required. "GAS or GAS Contracted Auditor" refers to situations where GAS is the designated auditor but may choose, in discussion with DPs, to sub contract the required audit work to a private audit firm. "Direct Hire of Private Audit Firm" refers to situations when the DP directly hires a private firm to complete the required work. "Private Audit Firm or GAS" refers to situations where the recipient has the choice as to who to hire to complete the audit; in many cases this is because the funding mechanisms in question are used to finance both governmental and non-governmental counterparts; MDAs, in these circumstances, will typically have GAS (or possible a private audit firm sub contracted by GAS) to conduct their financial audit, while non-governmental organizations would hire a private audit firm directly. "No Audit or Not Applicable" is self explanatory.

22 This is unusual as audit reports typically do not include detailed schedules of this nature, but instead offer an opinion upon financial information presented by the entity being audited.

23 Note: CIDA and Netherlands statistics related only to MDBS activities. Further detail on other funding modalities was not provided for this review. DFID data is based on review of guidelines available on-line.

24 These include verification activities which take place in lieu of financial audits.

In the case of USAID and the World Bank, auditors are vetted in advance of engagement, while other DPs typically only require that auditors be properly qualified / recognized in Ghana. The EU and ADB adopt a slightly different approach, specifying in their standard ToRs the qualifications expected of the verification team supplied by the audit firm. The EU also appears to be something of an outlier with respect to direct hiring of auditors. It should also be noted that DPs appear to make extensive use of private audit firms sub-contracted through GAS, either as the primary auditor, or to provide additional audit services, as with respect to the audit of selected flows conducted on budget support funds.

Towards a single audit, one time

As the discussion in the previous section highlights, there are a number of practical impediments to audit harmonization between DPs and the GoG. A single audit, one time, that encompasses all donor funds and meets GoG audit requirements is a goal that in the short term, is perhaps unattainable, but nonetheless is one worthy of pursuit over the medium to longer term. Specifically, the title means that under ideal circumstances, the Government of Ghana should be obligated only to conduct a single financial audit process each year and that the audit reports produced by this financial audit process should be sufficient to meet Ghanaian statutory requirements and DP audit requirements.[25] The audit should include <u>all</u> resources (cash and in-kind) received and managed by the entity from all sources.

As the discussion set out above indicates, a number of inter-related issues need to be resolved in order to achieve this ideal. These include:

- A functioning and reliable consolidated Government of Ghana financial accounting system in operation that can capture all resources (cash and in kind) and provide breakdowns of donor funded contributions and expenditure in addition to all government expenditure; this consolidated financial accounting system needs to be modular (i.e. can report at the unit level) and cumulative (i.e. reports from individual units can be aggregated up to give accurate financial reports for the whole and for constituent aggregate units of the whole). The rollout of GIFMIS makes the realization of such an accounting system achievable; however, an effective consolidated financial accounting system requires more than accounting software; it also requires sufficient personnel with the skills to manage and oversee financial accounting and reporting processes, sustained commitment from senior managers and elected officials in ensuring these systems are effectively maintained and utilized, and that audit recommendations made by the external auditors are responded to in a timely manner to ensure that any weaknesses are addressed.

25 In practice, the single audit, one time, framework, if successfully implemented, would comprise a single audit for each constitutive auditable entity within the government system (requiring each such entity to produce financial statements that can be audited); these entity level audits could then be aggregated, and together with an audit of the consolidation process could be utilized to provide a comprehensive audit opinion on the government as a whole. This would occur in a manner similar to the audit of large private enterprises where audit reports on consolidated financial statements are based on audit work done on each subsidiary, and an audit of the consolidation process as a whole.

- A high capacity external audit function that can deliver financial audits for all constituent units and the aggregated whole using risk based methodologies that place particular emphasis where audit risk is considered to be highest and can report within the required reporting timetable to a standard consistent with international auditing standards, GoG and DP auditing requirements.

- Harmonization of DP audit reporting requirements, including (ideally) harmonization of contract terms and provisions; the shortest path to achieving this harmonization is through use of shared funding arrangements including budget support and pooled funding arrangements. Such comprehensive and wholesale harmonization (in contrast to partial use of these mechanisms by some DPs) would, practically speaking, be contingent upon DP confidence in GoG capacity to deliver on the objectives for which these funds are programmed and on DP confidence in the GoG's PFM system to manage funds entrusted to it. In the case of some DPs, domestic legislative obligations may also make such moves difficult.[26] In the absence of such harmonization, piecemeal harmonization of audit practices can reduce transaction costs and audit complexity while strengthening host country systems.

DP willingness to utilize host country systems in accordance with commitments made under the Paris Declaration on Aid Effectiveness and the Accra Agenda for Action does not necessarily imply a blanket commitment to budget support to host country governments,[27] nor given the weaknesses of some host country systems, should they. A blank check approach to funding in the absence of adequate systems to meet development objectives while managing fiduciary risk could be as detrimental to development objectives as DPs seeking to exert overly rigid financial oversight on host country governments through restrictive micromanagement of development assistance.

Ghana, while benefitting from extensive budget support, continues to also experience a relatively fractured aid giving environment. Ghana also presents a mixed picture in its efforts to reform and improve its PFM systems. While improvements have been made as part of a long term program of public sector reform, more still needs to be done. The most recent World Bank PEFA assessment noted that "when viewed from the perspective of the three main objectives of a sound PFM system, namely aggregate fiscal discipline, strategic allocation of resources and the efficient delivery of services; Ghana does not yet score well on all key aspects of aggregate fiscal discipline".[28]

These kinds of tensions – between commitments to host country systems, and fiduciary (and legal) responsibilities of DPs to their own governments and tax payers, also play out in differing DP attitudes towards risk and risk management.[29] This is reflected in different DP

26 US legislation, for example, places restrictions on the use of funding for certain kinds of activities.

27 Jeremy Cant, Rebecca Carter and Stephen Lister, 2008, "Stocktake on Donor Approaches to Managing Risk when Using Country Systems", London: CIPDA and Mokoro, p2.

28 Ronald E. Quist, Mary Betley, Dwight Alan Smith, Ranjan Ganguli, Maurice Ochieng and Ferrie Pot (2010), "Republic of Ghana Public Expenditure and Financial Accountability 2009, Public Financial Management Performance Assessment Report, Volume I: Central Government", Rotterdam: Ecorys Research and Consulting, p30.

29 See Cant, Carter and Lister (2008), cited above for a more detailed analysis and discussion of these issues. This review compared risk approaches of the following nine DPs, including Canada, France, Germany, the Netherlands, Sweden, the UK, the Asian Development Bank, the European Commission, and the World

approaches to reliance upon host country PFM systems. The European Union clearly states, for example, in its guidelines for budget support,[30] that it does not set 'absolute thresholds' with respect to the quality of PFM systems when budget support is being considered or initiated. From this perspective, provision of budget support is seen as a means of supporting improvement in recipient PFM systems. To this end European Union guidelines require that a plan to be in place for improvement in PFM systems at the time of initiation of budget support, while also anticipating that improvements will be made to this PFM system over time. By contrast DPs such as USAID appear to be considerably more risk averse on this point, requiring minimum standards for PFM systems before they can be relied upon for funding purposes. While these two positions are not inconsistent – assuming the anticipated improvements in PFM system occur over time to bring the systems in line with the expectations of all DPs, they can result in differences in DP approaches to the question of budget support.

This combination of circumstances mean that in the short term, audit harmonization issues need to be addressed on a piece meal basis, rather than through complete harmonization of funding arrangements. The remainder of this section will consider how best DPs and GAS can move forward on this basis, with a particular focus on potential quick wins.

Steps towards audit harmonization

This section sets out steps that DPs can take towards greater audit harmonization that is incremental in approach but manages to move the audit harmonization agenda of DPs forward in a meaningful manner. Common action points that can be addressed by all DPs include the following:

- All DPs to move towards using GAS as primary auditor for funding to GoG
- GAS, with the support of DPs, to pilot a joint audit on a selected number of GoG entities in accordance with international audit standards and conduct a lessons learned exercise thereafter
- GAS, with the support of DPs, design and implement a common internal control review to be conducted annually for financial audit purposes
- DPs should commission a review of the compliance requirements related to funding agreements and specific legislative and other rules and regulations of particular DPs to determine salient differences and consider how best compliance issues can be harmonized in the absence of consolidated funding arrangements
- DPs continue to support the GoG in the roll out of the GIFMIS system, including development of procedures to ensure that the GoG integrates all support received – both in cash and in kind – into its consolidated financial statements, regardless of the 'entry point' of that assistance

Bank.

30 The European Commission (2007), "Aid Delivery Methods, Guidelines on the Programming, Design and Management of General Budget Support", p31

- GAS, in consultation with DPs consider the feasibility of establishing a verification unit within GAS to carry out verification type activities instead of relying on outsourcing to private audit firms or integration of verification work into joint audits, if appropriate
- DPs work to synchronize project and pooled funding arrangements so that financial year end and audit requirements are synchronized with the government fiscal year.

The sections that follow discusses each of these steps in greater detail.

Use of GAS as primary auditor

While significant progress has been made in moving towards the use of GAS as the primary auditor of DP funding to the GoG, a heavy de facto reliance remains because of the use of private audit firms sub contracted to GAS. While this may be necessary in the short to medium term because of capacity constraints within GAS, DPs and GAS should together develop a joint strategy for how best to further strengthen GAS so that in time it will be able to take over these functions from private audit firms. Those DPs that do not currently use GAS as their primary auditor should also consider establishing arrangements to begin to work with GAS (using sub contracted private firms if necessary) in the conduct of financial audits. It is to be noted that use of GAS as a primary auditor does not necessarily preclude the possibility of DP commissioned audits, should circumstances require it (e.g. due to quality concerns with respect to the audit itself).

Pilot Joint Audit

As a stepping stone towards a more system-wide approach to joint auditing, DPs and GAS should plan a pilot joint audit approach for a selected number of government entities for the fiscal year ending 31st December 2011. The feasibility of such an approach is dependent upon the entities in question being capable of producing financial statements that can include DP contributions – both cash and in kind – that can then be audited on a joint basis. A relatively modest approach is recommended initially, concentrating on a small number of small or medium sized government entities in receipt of funds from multiple DPs that are capable of producing financial statements of the required quality. Ideally all DPs should be included, including any DPs not involved in this current process or AWG processes (including "off-shore" DPs such as The Global Fund).[31] While specific TORs may need to be written to reconcile particularly diverse DP requirements – such as those of USAID and the EU, for example, in situations of joint audits that do not involve either the US or the EU, it is suggested that the OECD's *Specimen Terms of Reference for External Auditors of Donor Support Projects and Sector Programs* may be used as a template for common SoWs/ToRs.[32]

Where USAID, the EU or other DPs with distinct requirements wish to harmonize on a pilot basis and need to go beyond the specimen ToR noted above, the best method of harmonizing SoWs / ToRs is to adopt an additive approach. In other words, where a particular DP has a

31 This point highlights the importance of sequencing PFM improvements; improvements to GoG financial reporting systems (facilitated by GIFMIS roll-out) should in turn make these kinds of joint audits possible for a larger number of government units over time.

32 OECD, 2003, DAC Guidelines and Reference Series, Harmonizing Donor Practices for Effective Aid Delivery, Good Practice Paper, p81 – 84, available at http://www.oecd.org/dataoecd/0/48/20896122.pdf [Accessed 4th May 2011].

higher level of detail and specificity to its requirements, joint SoWs/ToRs will include this higher level, while remaining focused on the principle of conducting an audit where the auditors express an opinion.

Design and implementation of a common internal control review

In the private sector, an internal control review is typically conducted as part of normal financial audit procedures to determine the effectiveness of systems of internal control and the extent to which reliance can be placed on these internal controls for financial audit purposes. It does not normally constitute a separate exercise for reporting purposes (unless it is required, as for example, with respect to PCAOB audit requirements of US listed companies), but instead represents an integral part of financial audit procedures, allowing auditors to evaluate how effectively internal controls are operating.[33]

Strong internal controls allow auditors to reduce the amount of substantive (i.e. detailed) testing they need to do after the year end as part of standard financial audit procedures. An internal control review differs from macro-type evaluations of PFM systems (such as PEFAs) because it is an integral part of financial audit procedures and because it typically includes detailed audit testing to determine the effectiveness of relatively low level, mundane financial accounting controls (in addition to more macro-level control issues). These reviews need not be conducted at year end; if properly designed, they could cover all internal control issues of concern to DPs and the GAS.[34]

DP Review of Contractual Language

Inevitably a core component of any audit of grants made to the GoG will include compliance issues – either overtly or implicitly. Compliance issues mean the extent to which the recipient of the funds adhered to the terms of the underlying funding contract / financing agreement. In the absence of a single comprehensive funding agreement for all DPs, consideration should be given to the extent to which the detailed language of various funding agreements can be harmonized so that the actual compliance work required of auditors is similar or substantially the same. As a first step in this process, DPs are encouraged to conduct a review of existing contracts and any other legislative and procedural laws, rules and regulations to determine the degree of divergence.

In the short term, however, a piecemeal approach to compliance issues can be adopted. Any SoW/ToR for pilot joint audit will need to require a compliance audit with all relevant

33 And can therefore be distinguished from exercises where a stand-alone opinion is required on internal control systems is required, from more general reviews of host country PFM systems (as with the WB's PEFA assessment, for example), and routine work on the effectiveness of internal controls performed by internal auditors. It should also be noted that while there is wide variance in national frameworks of risk management and internal control with respect to private companies – and indeed a strong demand for convergence in these frameworks (see for example, IFAC, 2001, "Global Survey of on Risk Management and Internal Control, Results, Analysis and Next Steps", Feb 2001, available at www.ifac.org), INTOSAI has issued two documents that provide a framework for the design of an appropriate common internal control review for public financial audit purposes – INTOSAI, "Guidelines for Internal Control Standards for the Public Sector" and ISSAI 1265, "Communicating Deficiencies in Internal Control to those Charged with Governance and Management." The former document is based on internal control framework developed by the Committee of Sponsoring Organizations (COSO), an organization that includes the AICPA and Institute of Internal Auditors among its sponsoring organizations – see www.coso.org.

34 The Auditor General is required under the Audit Service Act, 2000 (Act 584), to report on Internal Control matters and to indicate in his annual report whether applicable internal control and management measures are inefficient or ineffective. Per written submission from GAS in response to an earlier draft of this paper, GAS agrees that a common understanding or agreement on the features of internal control to meet the basic requirements of GAS and DPs is desirable.

funding contracts as part of the work to be done by auditors; this approach, while resulting in some efficiencies as compliance work will be conducted by only one auditor, will still be cumbersome, because of the divergence of particular (non-audit related) contractual requirements in individual DP funding contracts / financing agreements.

DP Support in GIFMIS roll out

As previously noted the roll out of the GIFMIS program provides an opportunity for a notable leap forward in the capabilities of the GoG with respect to its financial accounting and reporting systems. However, this will take time and significant effort on the part of the GoG together with sustained technical assistance from DPs to address issues as they arise. It will also require detailed consideration of GoG staffing requirements, including additional training and recruitment needs. A trend in the developing world has been towards the recruitment of professionally qualified accountants from the commercial sector into senior financial management positions within the public sector to support improvements in financial accounting and reporting systems; such recruitment moves necessarily involve the development of compensation packages that will attract suitably qualified people of a high enough caliber. While a detailed review of GIFMIS implementation is beyond the scope of this assignment, its success is crucial to the ability of GAS to place greater reliance on the accounting system, and to DPs, should they seek to depend on GAS audits of financial statements that include their funding to the GoG.

Integration of Verification Activities

As previously noted, consideration should also be given to the establishment and utilization by DPs of a verification unit within GAS specializing in external verification type activities in accordance with DP guidelines, or to the integration of verification into the work of audit teams engaged on joint audits. As these activities would comprise an external verification required by DPs, it is not anticipated that carrying out such activities would result in any conflict with GAS's audit responsibilities.

Synchronization with GoG fiscal year

As discussed in Part 1 of this report, certain DP funding mechanisms, including project and potentially pooled funding approaches, risk creating greater audit complexity because of differing time periods which typically trigger audit requirements at period end. In the design and roll out of such funding arrangements, DPs should consider timing and ways in which audit requirements can be synchronized with the GoG fiscal year to facilitate ease of cut-off and reconciliation for financial accounting purposes in GoG consolidated accounts, increase the likelihood of reliance upon joint internal control reviews (recommended above) and facilitate GAS takeover of these audits in a manner that corresponds to their normal work cycle.

Build Consensus on appropriate DP response to qualified or adverse audit opinions

An important implication of harmonized financial audit procedures amongst DPs is the possibility of an adverse or qualified audit opinion and the question of how DPs will respond under such circumstances. The development of a common DP approach to this question will strengthen DPs capabilities in dealing with such circumstances. It is suggested that DPs consider opportunities for joint action with existing parliamentary oversight mechanisms, or in support of these mechanisms where GAS financial audit reports are being relied upon, again with the objective of further strengthening host country systems, while retaining the ability for autonomous co-ordinated DP action to be taken if required.

Conclusion

To conclude, audit harmonization should be viewed as a process that can be worked on in an incremental fashion, but nonetheless should still keep in mind an end goal – to achieve a situation where a single audit is performed once each financial year to meet host country government and DP audit requirements. All efforts to improve financial systems and the auditing of financial reports that come out of these systems should be framed with such an objective in mind. Achieving a single audit, one time, will not be easy – not least because of the human capacity requirements that will need to be addressed in order to build reliable host country financial reporting and financial auditing systems; nonetheless remains a worthy goal for both the GoG and DPs to work together on over time.

Annex 1: Table: Summary of Commonalities and Differences

Entity	Financial Audit Opinion Required (Y/N) (Excluding MDBS/ SBS)[35]	International Auditing Standards are recognized (Y/N)[36]	Internal Control Review Required (excl MDBS/SBS)[37]	Reporting Currency in Ghana Cedis (All, Mixed, None)[38]	Funding to GoG synchronized to GoG fiscal year (All/Mixed/ None)[39]	Audit Opinion makes specific reference to contract or other compliance issues (Y/N)
GAS	Y	Y	Y	All	All	Y
ADB	Y	Y	Y	Not clear	Y	Y
CIDA	Y	Y	Y	All	All	Not clear
Danida	Y	Y	Y	All	All	Y
DFID	Y	Y	Not clear	Not clear	Not clear	Not clear
European Union	N	Y	N	Mixed	Mixed	Y
GIZ	Y	Y	Y	All	Mixed	Not clear
JICA	N	Y	N	Mixed	Mixed	Not Applicable
KFW	Y	Y	Y	Mixed	Mixed	Y
Netherlands	Y	Y	Y	All	Not clear	Not clear
Switzerland	Y	Y	Y	Mixed	Mixed	Y
USAID	Y	Y	Y	Mixed	All	Y
World Bank	Y	Y	Y	Mixed	All	Y

35 The EU requires audit verification instead of audit opinion, and subsequently draws its own opinion of verification work done. Per discussions with EU, it may be possible to seek a waiver from these requirements in favor of a financial audit on a pilot basis; alternatively, the EU may accept an audit opinion in addition to audit verification work; JICA does not normally require financial audits; however funds granted under MDBS and SBS funding mechanisms are audited in accordance with the joint financing agreements.

36 USAID normally requires GAGAS standards to be applied; however, where GAS is the auditor, ISAs are accepted, while a modified audit statement is also permitted where GAGAS is required but not completely followed.

37 The EU has a specific ToR for standalone internal control reviews; however these are not normally used in Ghana at present; JICA – Internal Control Reviews are required as part of MDBS and sectoral budget support, but not normally required for other types of funding.

38 # GIZ: Currency of contract is at the discretion of Accra office and can be in local currency; EU: contracts sometimes denominated in Euros to protect recipients from exchange rate risk; JICA: All cash transfers in local currency, but in kind donations to GoG are accounted for in Japanese Yen; KFW: While most funding mechanisms are denominated in local currency, some types of contracts, including direct disbursement and reimbursement procedures are sometimes denominated in foreign currency; Switzerland: Certain types of funding can be denominated in Swiss francs or US dollars; USAID: While current USAID funding mechanisms to GoG report in Ghana cedis, other types of funding mechanism used by USAID typically report in US dollars; also, the funds accountability statement must be provided in US dollars per current requirements; World Bank: Some reports are in US dollars.

39 EU: Funding dates dependent on contract / ToR; GIZ: contracts typically synchronized with fiscal year, unless contract less than one year; JICA: donations in kind not synchronized; KFW: disposition funds dependent upon project progress.