

IV EUROSAI-ARABOSAI Conference

Subtheme III: IMPORTANCE OF SPECIFYING THE LIMITS AND OBJECTIVES OF FINANCIAL PUBLIC CONTROL, BOTH EXTERNAL AND INTERNAL, FOR IMPROVING PUBLIC FINANCIAL MANAGEMENT

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1. INTRODUCTION

The present crisis which affects a large part of the developed countries and which is provoking adverse effects worldwide has its origins in the financial economy and is having full effects on it. The balance between the real economy and the financial economy has been altered in the last 30 years, with a disproportionate growth of the latter. In affected countries, the public sector is facing, on the one hand, a reduction in traditional budgetary resources, which has led to a considerable increase in the public deficit in a large number of national economies; and on the other hand, to greater difficulties when it comes to selling sovereign debt issues. In view of this situation, governments and supranational bodies, such as the European Union, have been adopting a series of measures aimed at guaranteeing budgetary stability and preventing the disproportionate growth in public borrowing.

The present economic and financial situation, including the new rules on fiscal consolidation that have been adopted, constitute a new scenario in which the control bodies of the public sector, both internal and external, have to undertake their activity. For that purpose, a precise demarcation of the aims, functions and objectives

of these bodies becomes essential, in such a way that the control system can be properly coordinated.

Below are to be found some thoughts on the scheme for controlling public economic-financial activity, the limits and objectives of public control, both external and internal, and the characteristic principles of the economic-financial control institutions existing in Spain. Finally, a separate section presents the challenges facing external control bodies in order to improve public financial management.

2. ECONOMIC AND FINANCIAL ACTIVITY CONTROL

The budgetary and financial regulations of the public sector are presided over by the idea of control and, indeed, all control institutions are aimed at evaluating the source and application which governments give to the public resources which they divert from private economies. The control function is inherent to a democratic state and, though not confined solely to financial activity, its special importance in this field is undeniable.

The democratic basis of the need for control is none other than the fact that public resources are being used which do not belong to those who use them, plus the fact that they concern scarce funds which have to be handled properly.

The control function means watching over the faithful execution of financial commitments, with the aim of guaranteeing a proper administration of public funds, in accordance with the principles of sound financial management. So, control is directed towards checking that the activity of the public sector accords with the

existing regulations and that it complies with the objectives, previously established, in an effective and efficient way and at a reasonable cost.

Therefore, the scope of the control consists of two main areas: regularity and the principles of sound financial management. The first includes the legality control, which has a fundamentally juridical nature, and the financial control of the financial statements that are submitted. Meanwhile, effectiveness, efficiency and economic controls, which are included in the performance control, have an essentially economic component.

Together with political control on public activity, which is that carried out by a body having such a nature, as is Parliament, one can also talk about technical control over the economic and financial activity of the public sector, which consists of an internal and external control on public finance. So, internal or administrative control is conducted by a body belonging to the Administration itself over its own acts, acting independently with regard to the body being controlled. The fundamental characteristic of this internal control is that, in the end, the body exercising it and the management body being controlled always have a common hierarchical superior. Also, external control is carried out by a body that is wholly outside of the Public Administration being controlled and which therefore does not come within the sphere of action of the latter but instead enjoys absolute independence.

In the Spanish case, the public sector, which constitutes the subjective scope of this control function, is structured into three levels: the first consists of the Central Administration of the State and Social Security; at a second level are the Autonomous Communities or the regions, with a broad system of autonomy and extensive powers (which, without reaching the point of forming a federal state, form a broadly decentralised system); and at a third level is the local public sector, essentially

consisting of municipalities. Moreover, in its different levels the public sector displays very varied kinds of entities, including both bodies and entities that are purely administrative and also corporations or foundations that are publicly owned, among other examples.

In this territorial framework, internal control in Spain is carried out by the General State Comptroller (Intervención General de la Administración del Estado, or IGAE), with regard to the state public sector, and by the Autonomous and Local Comptrollers in the autonomous and local public sectors, respectively; while external control is conducted by the Court of Audit, whose powers extend to all levels of the public sector, and by the Regional Audit Institutions (Órganos de Control Externo or OCEXs) for those Autonomous Communities which have them, with powers at the autonomous and local levels.

3. SHAPING OF THE INTERNAL CONTROL OF PUBLIC ECONOMIC AND FINANCIAL ACTIVITY IN SPAIN

3.1. Objectives

Internal control bodies are set up and work within the actual Administration, specifically within the different ministerial departments and other bodies of the public sector and organically they come under the leadership of the administrative organisation, although they enjoy functional and organisational independence. As has already been stated, internal control of the state public sector in Spain is entrusted to the IGAE, which organically comes under the Ministry of Finance and Public Administrations. The regional and local public sectors have their own comptroller bodies, whose activity is similar to that exercised by the IGAE.

As an internal control body, the IGAE is in charge of verifying by means of audit techniques that the economic and financial activity of the public sector accords with the principles of legality, economy, efficiency and effectiveness. Also, as an executive and management centre for public accounting it is responsible for issuing the necessary rules for the development of public accounting and guaranteeing that reliable, complete and suitable accounting information on public management is being provided.

Also coming within its scope of action are those functions deriving from the exercise of controlling EU funds, in particular those provided for in section 62 of the Regulation (EC) 1083/2006 of the Council, of 11 July 2006, with regard to the exercise of the functions of the audit authorities, in those programmes in which the IGAE has that capacity.

The main regulation of state internal control and of the organisation of the IGAE is found in the General Budgetary Act 47/2003, of 26 November 2003 (LGP). The categories of control comprise the comptroller function, financial control and public audit. The first category is exercised prior to carrying out the controlled activity (*a priori* control), basing itself exclusively on criteria of legality, the other two are applied once the activity has been carried out (*a posteriori* control) and also include other objectives such as control of the financial regulating of the accounts (public audit) or control of activity in its aspects of economy, effectiveness and efficiency (financial control).

3.2. Limits

The IGAE does not have any restrictions regarding its powers in relation to its internal control function and, with respect to the available resources, it has to be pointed out that its staff is essentially trained by public officials who occupy their work posts as a result of a rigorous competitive process by means of passing various eliminating tests. Moreover, in the event of the IGAE lacking sufficient resources for conducting its control function, the LGP provides for the possibility of requesting, with justifying arguments, the collaboration of private audit firms or officially registered accounts auditors in order to execute the Annual Plan of Audits.

The activity of internal control bodies can involve certain actions being carried out by the management bodies, as occurs in subsidies control, in which the IGAE can urge them to ask for their refund when they have not been properly justified, or it can halt any administrative management that fails to comply with the legal requisites, notwithstanding the possible disagreements which the heads of the management bodies might bring before the internal control body and which, as a last resort, is resolved by the Central Government. In order to apply this system of solving disagreements, there exists a regulated contradictory procedure between the parties involved.

4. EXTERNAL CONTROL OF PUBLIC ECONOMIC-FINANCIAL ACTIVITY IN SPAIN

4.1. Objectives

The main aim of external control over public economic-financial activity consists of verifying whether public funds are obtained and applied in accordance with regulations and the principles of effectiveness, efficiency and economy, as has been emphasised earlier. These principles constitute a guide for defining the objectives of the external control organisations and they highlight the importance of having a sufficiently broad mandate and fully discretionary powers for undertaking the functions proper to each Supreme Audit Institution (SAI), as recognised by Principle 3 of the Mexico Declaration of INTOSAI.

According to the said Mexico Declaration, the legal framework of the Spanish Court of Audit starts from the apex of the legal code, which is none other than the Constitution. Section 136 of the Spanish Constitution defines the Court of Audit as *“the supreme audit body of the State’s accounts and its economic management, as well as of the public sector”*. The legislative development of section 136 of the Spanish Constitution was carried out by means of Organic Act 2/1982, of 12 May 1982, on the Court of Audit (LOTCu) and Act 7/1988, of 5 April 1988, on the Functioning of the Court of Audit (LFTCu).

Section 2 of the LOTCu sets down that *“the functions proper to the Court of Audit are:*

- a) *The external, permanent and consenting audit [a posteriori] of the economic-financial activity of the public sector.*

b) *The judgement of the accounting responsibility incurred by those who are in charge of handling public wealth or effects” .*

Section 9 of the same legal text defines the scope of the audit function when stating that it includes the verification *“that the economic-financial activity of the public sector is being subjected to the principles of legality, efficiency and economy” .*

The audit function is the competence of the Plenary Session of the Court of Audit and is materialised in a set of actions aimed at checking that the economic-financial activity of the public sector is being subjected to the principles of legality and sound financial management, mentioned above, contributing to promoting the proper use of public funds. Via this activity of a technical nature, support is provided for the political control function which in their respective areas are exercised by Parliament, the Legislative Assemblies of the Autonomous Communities and the Plenary Sessions of the Local Authorities; also, as a last resort, social control exercised directly by citizens is facilitated.

4.2. Limits

As has been stated, in accordance with the LOTCu, the Court of Audit is the supreme audit body of the accounts and of the economic management of the Spanish public sector, adding that *“it is unique of its kind and its jurisdiction extends to the entire national territory, notwithstanding the accounts audit bodies which the Autonomous Communities might provide for in their Statutes” .* From this definition it is inferred that the Court of Audit has auditing powers over the entire public sector and also over those bodies which manage public funds, and that there does not exist, *a priori*, any significant regulating limits on the exercise of its audit function, which is fully in accord with the provisions set down in the Lima Declaration.

In terms of the objective scope over which this function extends, it falls to the Court of Audit to audit all public economic-financial activity and, in general, whatsoever use of public funds, irrespective of the public or private nature of the body managing them; including, therefore, subsidies, credits, bank guarantees and other assistance from the public sector received or managed by individuals or private legal persons. Also, the fact that Spain belongs to the European Union entails the use of European funds for financing expenditure and investments at the national level, over which the Court of Audit also exercises auditing powers together with the European Court of Audit, since these normally concern activities cofunded by member States.

A particular point in the scope of control exercised by the Spanish Court of Audit consists of its auditing powers over political parties and other entities linked to them, specifically, over the annual accounting of political formations having parliamentary representation, as well as the electoral accounting of those formations meeting the requisites for receiving subsidies for their participation in various electoral processes. It can be pointed out that the auditing of political parties extends to their entire activity, not just to those financed with public subsidies, and is exercised exclusively from the point of view of their accordance with regulations.

As has been stated above, the Court of Audit is not the only external control institution existing in Spain, since the majority of Autonomous Communities have their own external control bodies. The creation of these autonomous or regional control bodies does not imply any diminution or reduction at all of the auditing powers attributed to the Court of Audit which, by virtue of its own constitutional standing, maintains a position of supremacy, though not of hierarchic superiority over the OCEXs. The law states that the OCEXs shall have to coordinate their activity with that of the Court of Audit by means of establishing common criteria and

techniques for auditing that will guarantee the greatest effectiveness in the results and prevent duplication in control actions.

This concurrence in the same sphere of the control activity exercised by the Court of Audit and by the OCEX requires introducing coordination and cooperation mechanisms. Especially significant is collaboration in the field of accounts submitted by Local Authorities, a process that is carried out by means of the telematic sending of accounts both to the Court of Audit and to the great majority of the OCEXs via the web portal www.rendiciondecuentas.es. This system makes it easier for the Local Authorities to send their accounts to the Court of Audit and to the respective OCEX simultaneously by means of a single act. This procedure also allows automatic checks to be conducted and it notably increases transparency with regard to citizens, by providing them with the economic-financial information contained in the accounts of those Local Authorities. The appropriate measures are at this moment being adopted so that information on public contracts of the local public sector can be provided by telematic means using the same portal.

Aside from all the above, in the exercise of its control functions the Court of Audit is not faced with any restrictions of a budgetary, organisational or personnel nature, beyond the limits intrinsic to its legislation and to the inevitable scarcity of public resources.

The Spanish Court of Audit has an acknowledged budgetary autonomy and management of its own resources. The Court prepares its own budget, which is included in an independent section within the State General Budgets, for being jointly approved by the Parliament. Nevertheless, when it comes to budgetary credits, the Court of Audit is subject to the general directives of economic policy in terms of complying with the objectives of budgetary stability and financial

sustainability, and in its management it is currently following a line of maximum austerity that is shared with the entire Spanish public sector and with our European partners.

The Court of Audit also has a principle of organisational autonomy that is recognised by law, both in the assignment of areas or entities to the different auditing departments into which it is structured and with regard to the internal creation and organisation of them, which will be adapted to the needs established by the Plenary session of the Court.

Nevertheless, the most important asset of the control institutions is undoubtedly their auditing personnel. Human resources, like economic ones, are limited, therefore it becomes especially important to adapt their actions to the requirements of these new times, strengthening their motivation and training, especially in the use of new technologies and in the field of auditing. For this purpose, each year the Court of Audit approves an Annual Plan of Training and it is also currently designing an Administrative Modernisation Plan which will affect the exercise of all the activities of the Court.

5. CHALLENGES FACING EXTERNAL CONTROL FOR IMPROVING THE PUBLIC FINANCIAL MANAGEMENT

If the actions of the public control institutions are to be effective and efficient, and are to be carried out in a coordinated manner, it is necessary to start from a clear definition of their objectives and limits of action. Without this demarcation it is not possible to successfully confront the difficult challenges being faced at the current time for improving the economic-financial management of the public sector.

As a starting point, the importance of the independence of the control bodies needs to be highlighted which, in the case of external control, is an essential requisite. The Lima Declaration established the basic lines of auditing activity, emphasising that an effective audit cannot be conducted without a framework of independence. Recognition of that independence has to be made at the highest level of the legal code, as set down in section 5 of the Lima Declaration which states that *“The establishment of Supreme Audit Institutions and the necessary degree of their independence shall be laid down in the Constitution; details may be set out in legislation.”* This is the case, for example, with the regulation of the Court of Audit of Spain, referred to above, in which there exists a constitutional provision for its existence and basic shaping, and an express acknowledgement of the independence of its members, similar to that of judges.

Moreover, in advanced democratic societies there is an intensifying demand on the part of citizens for greater transparency in public economic-financial activity, so that it can be seen whether that activity has been carried out in accordance with the principles shaping a sound financial management, which permits demanding the responsibility to which the public managers are subject. In this regard, the

application of the principle of transparency has to be tackled by the SAIs from a dual perspective:

- a) Increment their own transparency and responsibility with regard to citizens, not just in terms of the results of their work but also with regard to the management of their own resources. SAIs must be perceived as key elements which, with the most efficient use of their resources, guarantee the best functioning of the public sector and, as such, they must be an example of transparency.
- b) Verify compliance with the obligations of transparency by the entities making up the public sector, via the exercise of their auditing function. The role of the SAIs must accord with the mandate set down in their regulations and with the values and principles in which their activity is framed, but they must also heed the growing social demands for greater transparency. In this regard, the need to properly transmit the results of the control activity over compliance with the principle of transparency to the ultimate recipients of it, which are none other than the citizens, takes on special relevance.

In Spain, the *Act on Transparency, Access to Public Information and Good Governance* is currently in passage through Parliament. This is a legal instrument that is going to be fundamental for increasing the transparency of Institutions and guaranteeing the right of all citizens to have access to public information, strengthening the responsibility of the managers in the exercise of their functions and in the handling of public resources, by means of a strict regime of sanctions.

The obligations on transparency provided in the new Act constitute a novel field for auditing on the part of the Court of Audit of Spain and, at the same time, a relevant source of information on budgetary and economic-financial matters which is going to facilitate control activity over the public sector.

In addition to the above, if external controls are going to be able to function properly, then it is an indispensable requisite that the public sector entities should comply with the obligation to submit accounts under the terms and within the periods established in law.

The submitting of accounts is shaped as a necessary element for carrying out the auditing of the public management but it essentially implies complying with a duty towards citizenry as a whole.

In the event of failing to comply with this obligation to submit accounts by those who manage public funds, the legislation of the Court of Audit of Spain sets down a series of measures, notwithstanding other kinds of liabilities to which such conduct might lead, among which the forthcoming Act on Transparency, Access to Public Information and Good Governance, referred to above, expressly provides for the imposing of sanctions. With regard to the coercive measures that can be applied by the Court of Audit, these include the possibility of issuing an admonishing requirement for the entity to proceed to submit its accounts and, if the non-compliance persists, the imposition of a fine is considered which can be repeated over time until the obligation is fulfilled. Provision is also made for informing Parliament of the lack of collaboration by those obliged to do so; and as the case might be, the proposal of the Government, Ministers or the respective Authorities to impose disciplinary sanctions, including the removal of the official from his or her post or the discontinuance of the authority responsible for the non-compliance.

As with the provisions made for the submitting of accounts, SAIs have to provide the appropriate attributions for having suitable, unlimited, direct and free access to the documentation and to the necessary information for the due compliance of their

functions, as postulated by both the Lima Declaration and the Mexico Declaration of INTOSAI. This principle related to the duty to collaborate is first of all directed at audited bodies, which must provide freedom of access for the auditing body to the economic-financial documentation held in them which needs to be known and analysed in order to be able to achieve the objectives of each audit. But, moreover, it must be extended to other institutions or entities holding information of any kind (tax, labour, etc.) which is relevant to the activity being audited.

The duty to collaborate with the Court of Audit constitutes one of the basic presuppositions on which the exercise of its auditing function is based, since it derives from the obligation of the audited bodies to provide whatsoever data, statements, documents, background or reports which the Court asks for. This duty to collaborate is therefore shaped as being an indispensable requisite for the exercise of external control, and it covers all the phases of economic-financial activity, extending to the managers of public funds, including the recipients of subsidies, whether they are natural or legal persons, public or private.

Having taken into account the growing quantity and importance of the information stored by public entities, this duty to collaborate with SAIs could find itself clashing with the right to protect personal data in relation to the citizens' data held by those entities. Although this right to privacy is safeguarded by the duty of professional secrecy on auditors and the prohibition contained in the regulations on not making use of the information to which access is had beyond that corresponding to the exercise of the control function, the legislation on protection of personal data has been invoked on some occasions as a justification for denying access to particular information.

In order to face up to this limitation on the duty to collaborate by means of invoking the right to privacy, the legislation relating to certain fields or to Spanish public entities (such as Social Security or the Inland Revenue Service) has expressly considered the collaboration of these Institutions with the Court of Audit in terms of supplying information on third parties, though specifying that this can only be properly demanded as part of an audit being conducted on those entities, which excludes such collaboration when the information is required in relation to other bodies being audited. This limitation on the exercise of the audit activity has been questioned by the Court of Audit itself which has informed Parliament of the need to remove all obstacles to accessing the information available in Institutions such as those mentioned.

In addition to the above, in the case of States belonging to the EU, the challenges facing them include, among others, the commitments deriving from the new institutional and Community framework. The Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (known as the Fiscal Compact), signed on 2 May 2012, is going to boost the establishment of the so-called "Golden Rule" of budgetary equilibrium in Euro zone countries, if possible in a constitutional rule. In this regard SAIs will have to pronounce on whether public management has accorded with the criteria guaranteeing the budgetary stability and financial sustainability of public accounts, which requires having the tools that will permit a comparison to be made of the models used and the estimates made, as well as providing training for staff in this matter.

Another relevant aspect is to do with the control of the so-called European Stability Mechanism (ESM), of a permanent and intergovernmental nature, which acts in cooperation with the European Central Bank and the International Monetary Fund. The EMS constitutes a decisive instrument for guaranteeing the solvency of member

States in difficulties, providing financing subject to compliance with strict conditions. The auditing of their functioning provides for the participation of SAIs of various member States, which also play an important role in controlling the destination of the funds received, compliance with the requirements demanded for their concession and their eventual return.

In short, the role of the control institutions at the international level needs to be strengthened in order to provide a response to the problems deriving from the financial crisis, just as it is also necessary for those institutions to accept responsibility for orientating their efforts and results towards these questions of special relevance for our societies. In this regard, it is appropriate to strengthen the role of SAIs in the field of new measures and instruments for fighting against the crisis, at both the national and international levels, in such way they play an important role in the auditing of the adopted measures and of the mechanisms created for financial supervision.

6. CONCLUSIONS

The economic-financial control del Public sector is consubstantial to the existence of democratic institutions and has a constitutional basis. External and internal controls, though they are highly coincident in terms of the bodies on which they act and, in the ultimate instance, of guaranteeing a proper use of public funds, are not wholly identified with each other, neither in their aims nor in their procedures. Nevertheless, it is fundamental that there should be close collaboration between the different control institutions in such a way that will give rise to the creation of a genuine "control system", in which the functions with regard to the respective sphere of competence are clearly defined, but that there should also exist a spirit of maximum

collaboration, cooperation and coordination, with the intention of providing a response to social demands by means of the sharing of information and experiences and the adoption, when possible and pertinent, of common criteria.

SAIs have certain limits which arise from the constitutional rules and the rest of the legal code applying to them. Within these limits they must have full powers for initiating their control procedures and for defining the content of their audit works with complete freedom, thereby guaranteeing the full exercise of their independence. Freedom, subject nevertheless to the law, which includes the bodies that are acknowledged to have the initiative for agreeing on an audit and on the destination of the report resulting from the audit.

SAIs, especially those belonging to EU countries, are currently passing through moments of change and challenge. The present economic and financial crisis has expanded the sphere towards which auditing efforts are being directed, including the bases used for drawing up budgets and the restrictions established in relation to the objective of the deficit which those budgets have to meet. Although in general the mandates of SAIs do not include the possibility of auditing government policy decisions, the new budgetary framework that is binding on member States of the Euro zone entail the necessity to evaluate the measures adopted for complying with the principles of budgetary stability and financial sustainability. In this regard, the technical task of SAIs as bodies at the service of the Legislative Power becomes strengthened from the very beginning of the budgetary cycle up to its completion.

In this context, SAIs must, today more than ever, contribute to creating a public awareness of control in all spheres, from Parliament to citizens, passing through public managers, of course. Control which has to be understood as a means which will contribute an ever more transparent and efficient management. There exists the

need to go beyond performance audits in order to probe into an evaluation of effectiveness, efficiency and economy, in line with the demands of citizens that public funds should be managed in the best possible way, which constitutes a challenge for the managers who have resources that are always limited. This need also appears in a context in which sustainable development is acquiring ever greater protagonism.

Transparency in all its scopes is another major challenge for external control, since it has become a priority objective for the improvement of governance. There is a need to support the maximum transparency in the management of public funds, in a way that is accessible for citizens, which have to have the support of SAIs in the exercise of their control over a field that is as specialised as is the economic-financial activity of the public sector.

For these purposes, it is fundamental to increase collaboration and cooperation among all control institutions in order to be able to satisfy the demands of the citizenry with regard to verifying that public management is, as well as legal, also adequate from the point of view of effectiveness, efficiency and economy. With the backing provided by all shared experiences and teachings that have been learned, especially at the regional levels such as ARABOSAI and EUROSAI, SAIs will continue to serve their societies in controlling more transparent and better managed public finances.