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# The Framework of INTOSAI Government Auditing Standards: In the Stream of International Convergence

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## I Introduction

In the private sector, countries have increasingly adopted the International Financial Reporting Standards (IFRS) developed by the International Accounting Standards Board (IASB) as their domestic standards in line with the globalization of corporate activities, and financial and capital markets. In 2002, the IASB and U.S. Financial Accounting Standards Board (FASB), which are responsible for setting accounting standards in the United States, reached an agreement called the Norwalk Agreement to integrate their accounting standards. Amid this trend toward international convergence of accounting standards, for audits intended to ensure that financial reports are appropriate, more and more countries have adopted the International Standards on Auditing (ISA) developed by the International Auditing and Assurance Standards Board (IAASB), which is a review board for international standards for audit/assurance of the International Federation of Accountants (IFAC), as their domestic auditing standards. Thus, auditing standards are converging internationally<sup>1)</sup>.

The International Organization of Supreme Audit Institutions (INTOSAI), members of which are domestic Supreme Audit Institutions of countries, has developed standards and guidelines for government auditing as a reference for the member countries, and is now working on systematizing such standards, etc. for convergence with ISA. As a growing number of countries have introduced an accrual accounting system to their governmental sectors, it is considered that the same standards now applied to auditing in the private sector could be applied to government auditing (financial audits), to ensure the appropriateness of financial reports. (An overview of the international convergence of accounting standards and auditing standards is given in Figure 1.)

The objectives of audits of the government sector are different from those of audits of the private sector, and therefore, it is impossible to apply the International Standards on Auditing (ISA) developed by the International Auditing and Assurance Standards Board (IAASB), as they are, to government audits. Thus there is a limit to the convergence of government auditing standards and ISA. Notwithstanding, adopting ISA developed by IAASB, which is recognized as an international entity for establishing standards, would be more efficient than INTOSAI's developing standards on its own. How will the International Organization of Supreme Audit Institutions (INTOSAI) be systematizing government auditing standards toward convergence with ISA, taking into consideration the difference of the government sector from the private sector? This paper examines how INTOSAI has systematized government auditing standards to date amid the international trend toward convergence of such standards, and reviews past activities. (The views expressed in this paper are the personal views of the author and do not reflect the official view of the Board of Audit of Japan.)

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1) Anerud (2004), p. 21.

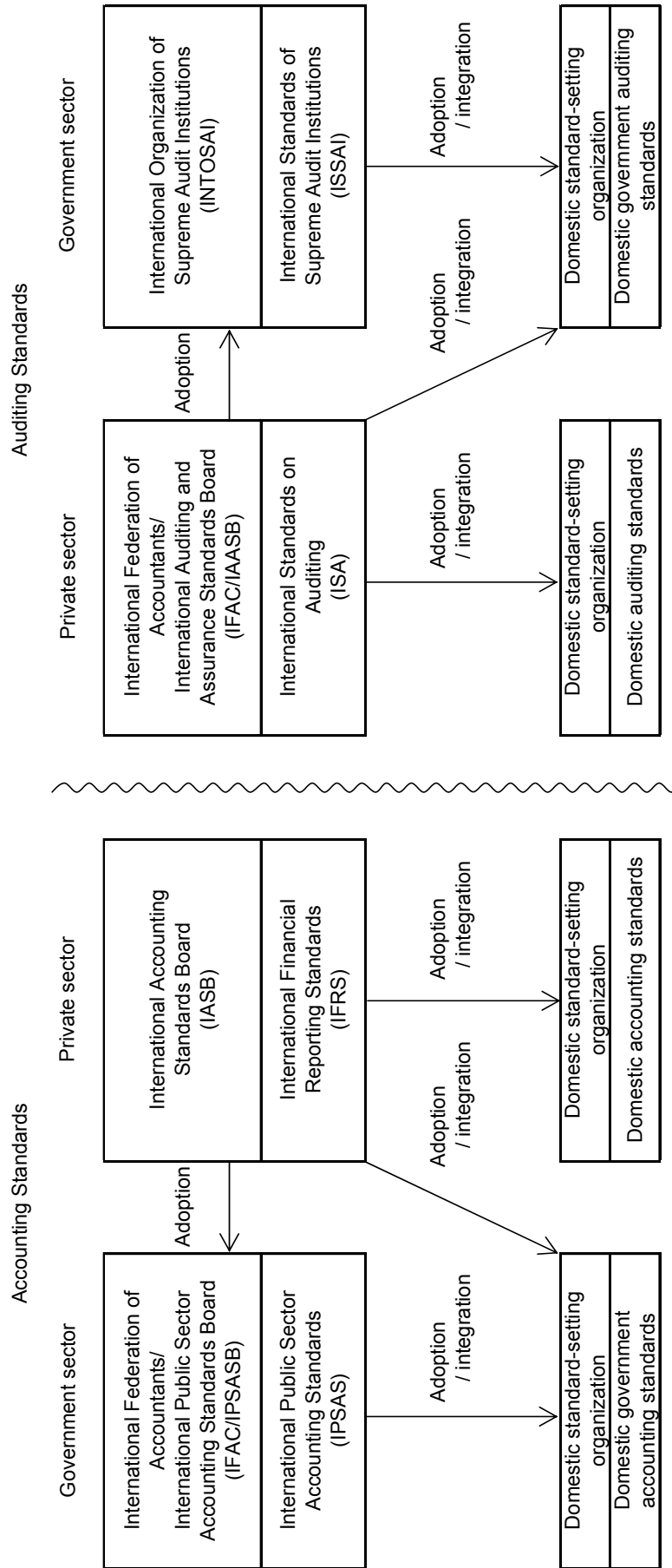
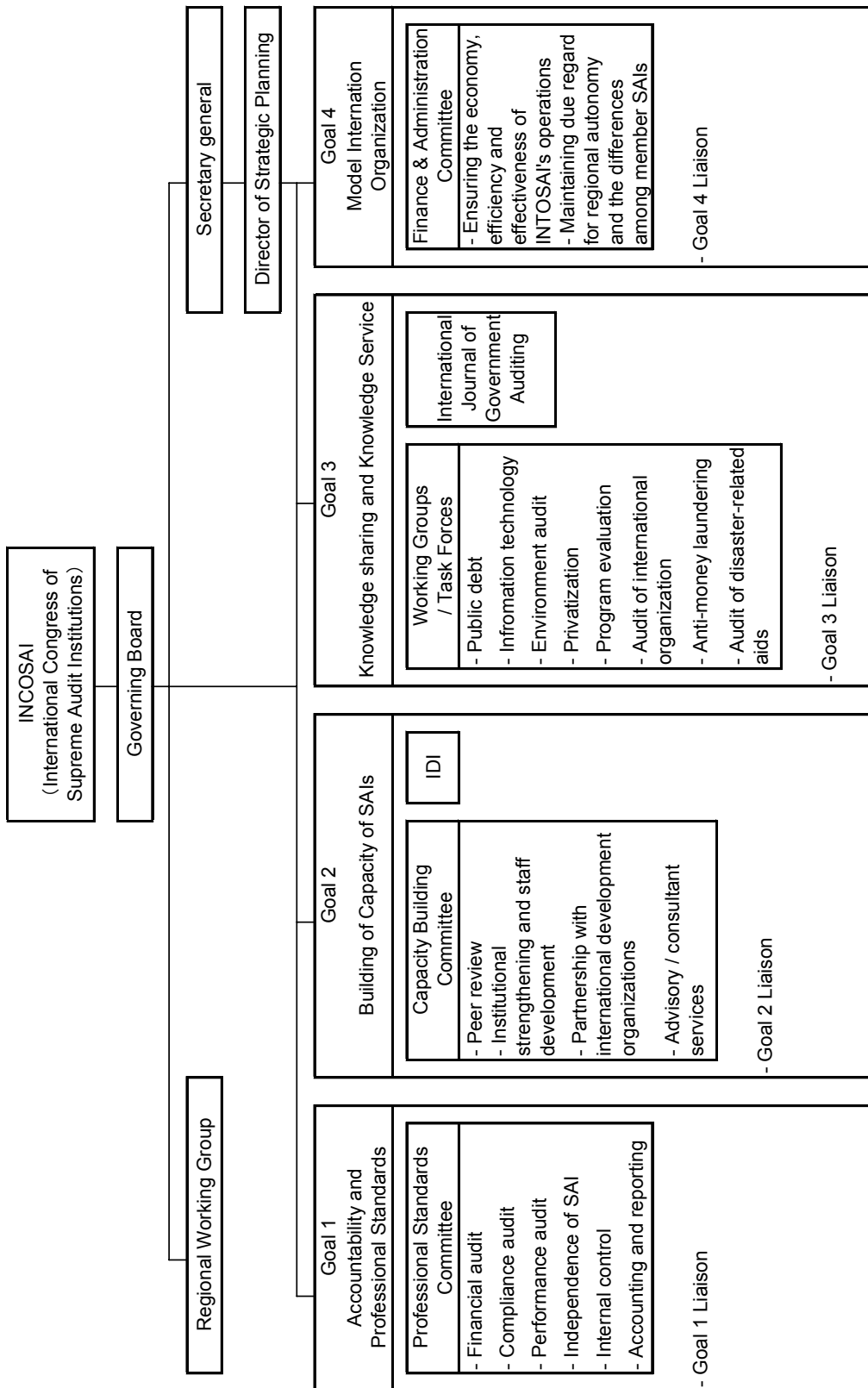


Figure 1 Overview of international convergence of accounting standards and audit standards



Source: INTOSAI (2005) APPENDIX III, INTOSAI website ([http://www.intosai.org/en/portal/about\\_us/organization/](http://www.intosai.org/en/portal/about_us/organization/) (July 11, 2007))

Figure 2 Chart of organs of INTOSAI

## II Activities of INTOSAI

### 1. Outline of INTOSAI

#### 1.1 Purpose of the establishment, and membership of SAIs

INTOSAI is an international organization that was established to foster the exchange of ideas and experiences among the Supreme Audit Institutions (SAIs) on government auditing<sup>2)</sup> in 1953<sup>3)</sup>, with the current membership of the SAIs of 185 countries and the European Union (EU) as of the end of 2004. Its headquarters are in Vienna, Austria. Participation as a Full Member in INTOSAI and all its organs and functions is open to: the Supreme Audit Institutions of all countries which are members of the United Nations Organization or any of its Specialized Agencies; and to the Supreme Audit Institutions of those supranational organizations which are subject to international law and are endowed with a legal status and an appropriate degree of economic, technical/organizational or financial integration. “Supreme Audit Institution” means such public body of a state or supranational organization which, however designated, constituted or organized, exercises, by virtue of law, or other formal action of the state or the supranational organization, the highest public auditing function of that state or supranational organization in an independent manner, with or without jurisdictional competence<sup>4)</sup>. In Japan, this is the Board of Audit.

#### 1.2 Organization

INTOSAI consists of: i) the International Congress of Supreme Audit Institutions (INCOSAI), ii) the Governing Board, iii) the General Secretariat, iv) the Regional Working Groups, and v) the Finance and Administration Committee (FAC) according to the Statutes of INTOSAI<sup>5),6)</sup>. It also has vi) Committees, Working Groups (WG) and Task Forces (TF), vii) the International Journal of Government Auditing (commonly called “INTOSAI Journal”), and viii) the INTOSAI Development Initiative (IDI) on the basis of resolutions of INCOSAI or the Governing Board. Those organs have been reorganized to correspond to Strategic Goals 1-4 in the Strategic Plan 2005-2010 decided at the 18<sup>th</sup> INCOSAI in 2004 (see Figure 2 Chart of organs of INTOSAI). Under Goal 1, of those goals, the Professional Standards Committee (PSC) has been established to develop standards, guidelines, etc. for government auditing, internal control, financial reports, etc. In particular, PSC functions as an international standard-setting organization for government auditing.

## 2. Professional documents of INTOSAI

INTOSAI has established Committees, Working Groups (WGs) and Task Forces (TFs) to study professional or technical issues common to member SAIs, and to develop the results into professional documents such as standards and guidelines. The Committees, WGs and TFs have been established on the basis of resolutions of INCOSAI or the Governing Board, and have different statuses according to the types of issues they cover. In other words, Committees are formed to deal with issues of significant, recurring interest to all members of INTOSAI, and WGs are formed as a result of INCOSAI recommendations to address SAIs’ interests in specific technical issues. In addition, TFs are formed to deal with issues of significant interest to many member SAIs for a finite period of time. The professional documents developed by the Committees, WGs and TFs are described according to the INTOSAI Goals as follows<sup>7)</sup>.

### 2.1 Documents related to Goal 1

In 1984, INTOSAI simultaneously established the Auditing Standards Committee, the Accounting Standards Committee, and the Internal Control Standards Committee as committees to study issues of significant,

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2) INTOSAI Statutes Article 1.

3) INTOSAI (2004), p. 10.

4) INTOSAI Statutes Article 2.

5) INTOSAI Statutes Article 3 and Article 8.

6) For the tasks of each organ, refer to Azuma (1990), pp. 74-88.

7) No professional documents under Goal 2 have yet been developed.

recurring interest to all members of INTOSAI. Those Committees developed professional documents related to audit, such as INTOSAI Auditing Standards and the Implementation Guidelines for Performance Auditing, and those related to governance, which has a close relationship with auditing, such as the Accounting Standards Framework and the Guidelines for Internal Control Standards for the Public Sector (for the results of development of professional documents related to Goal 1, refer to Table 1). Those Committees were put under PSC for Goal 1 in 2004 when Strategic Plan 2005-2010 was formulated. PSC now has: i) the Sub-Committee on Financial Audit Guidelines, ii) Sub-Committee on Compliance Audit, iii) Sub-Committee on Performance Audit, iv) Sub-Committee on SAI Independence, v) Sub-Committee on Internal Control Standards, and vi) Sub-Committee on Accounting and Reporting (for a chart of organs related to Goal 1, see Figure 3). Those Sub-Committees are developing professional documents related to auditing in general, such as Financial Audit Guidelines and Guidelines for Compliance Audit, for the 19<sup>th</sup> INCOSAI that will take place in November 2007 (for the professional documents for Goal 1 planned to be developed, refer to Table 2).

**Table 1 Professional documents related to Goal 1 (development results)**

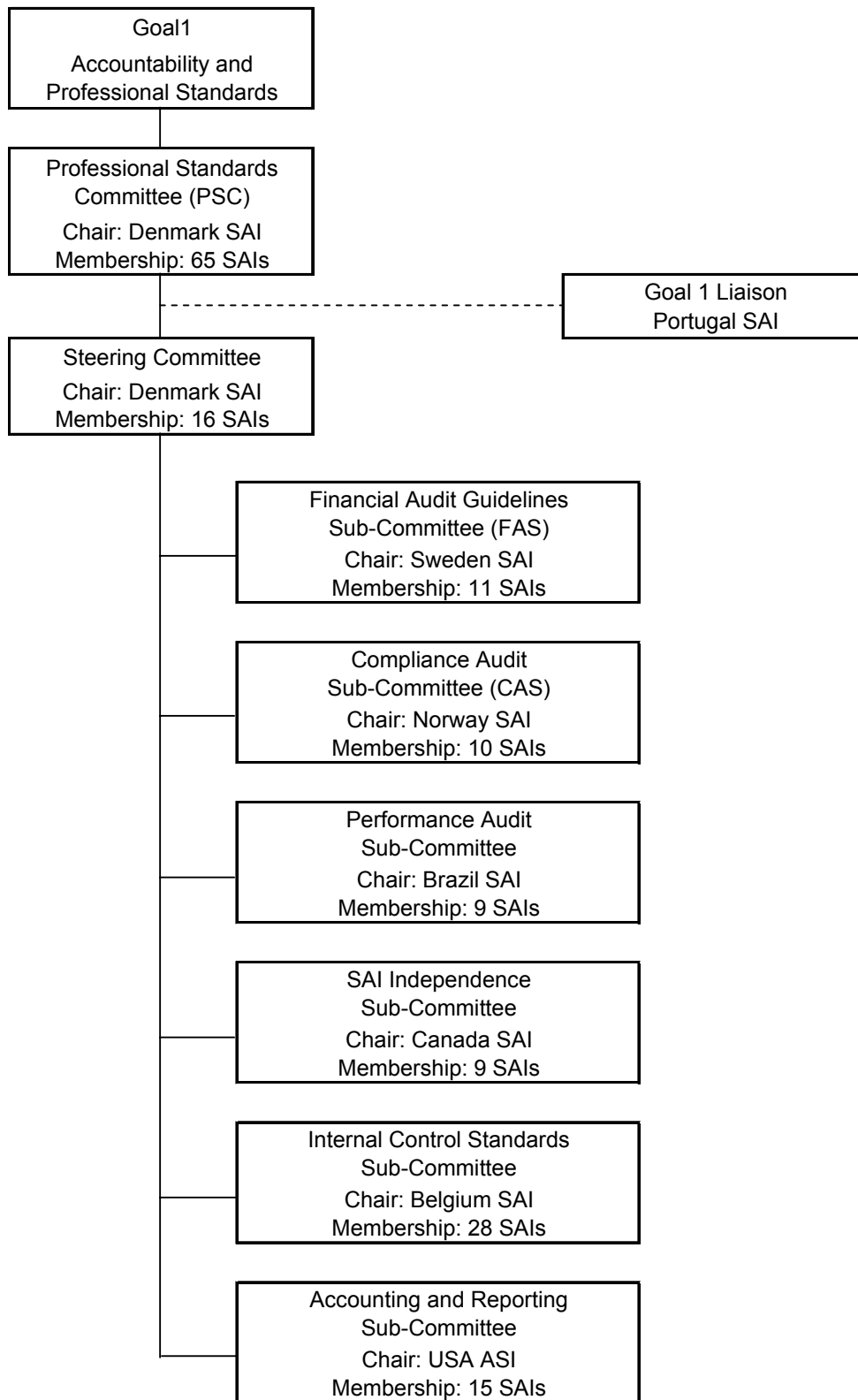
Committee	Name of document	Approved: (last revised:)
Auditing Standards Committee	INTOSAI Auditing Standards	October 1992 (October 2001)
	INTOSAI Code of Ethics	November 1998
	Independence of SAIs Project: Final Task Force Report	March 2001
	Implementation Guidelines for Performance Auditing	October 2004
Accounting Standards Committee	Accounting Standards Framework	October 1995
	Accounting Standards Framework Implementation Guide: Departmental and Government-wide Report	November 1998
	Accounting Standards Framework Implementation Guide for SAIs: Management Discussion and Analysis of Financial, Performance and Other Information	October 2001
Internal Control Standards Committee	Guidelines for Internal Control Standards for the Public Sector	October 1992 (October 2004)
	Guidance for Reporting on the Effectiveness of Internal Controls: SAI Experiences in Implementing and Evaluating Internal Controls	November 1997
	Internal Control: Providing a Foundation for Accountability in Government	October 2001

Source: INTOSAI website

([http://www.intosai.org/en/portal/documents/intosai/audit\\_related/documentsgoal1/](http://www.intosai.org/en/portal/documents/intosai/audit_related/documentsgoal1/),

[http://www.intosai.org/en/portal/documents/intosai/audit\\_related/documentsworkpap/](http://www.intosai.org/en/portal/documents/intosai/audit_related/documentsworkpap/)

(July 11, 2007))



Source: PSC website (<http://psc.rigsrevisionen.dk/composite-162.htm>,  
<http://psc.rigsrevisionen.dk/composite-163.htm> (July 11, 2007))

Figure 3 Chart of organs related to Goal 1

**Table 2 Professional documents related to Goal 1 (planned to be developed)**

Sub-Committee	Name of document	Expected to be approved:
Financial Audit Guidelines Sub-Committee	Financial Audit Guidelines	November 2007 and beyond
Compliance Audit Sub-Committee	Compliance Audit Guidelines	November 2007
SAI Independence Sub-Committee	Code of Independence of Supreme Audit Institutions	November 2007
	Guidelines and Good Practices related to SAI Independence	November 2007
	Code of Transparency and Accountability	November 2007

Source: INTOSAI/PSC (2007a)

## 2.2 Documents related to Goal 3

INTOSAI established the Committee on EDP Audit in 1989, the Public Debt Committee in 1991, the Working Group on Environmental Auditing in 1992, the Working Group on Programme Evaluation in 1992, the Working Group on Privatization in 1993, and the Working Group on the Audit of International Institutions in 2001, each to address technical issues of specific interest to SAIs. Those Committees and WGs developed professional documents related to specific audit issues, such as Information System Security Review Methodology and Guidance for Planning and Conducting an Audit of Internal Controls of Public Debt (for the results of development of professional documents related to Goal 3, refer to Table 3). Those Committees and WGs were incorporated into Goal 3 in 2004 when Strategic Plan 2005-2010 was formulated. For Goal 3, INTOSAI now has the i) Public Debt Committee, ii) Committee on IT Audit (former Committee on EDP Audit, renamed in 2002), iii) WG on Environmental Auditing, iv) WG on Privatization, v) WG on Programme Evaluation, vi) TF on the Audit of International Institutions (reorganized from the WG in 2004), vii) TF on the Fight Against International Money Laundering, and viii) TF on the Audit of Disaster-Related Aid (for a chart of organs related to Goal 3, see Figure 4).

## 3. Nature of professional documents

Professional documents such as standards and guidelines developed by the Committees, WGs and TFs are approved by INCOSAI or the Governing Board and then published on the INTOSAI website under the administration of the Secretary General. These can be viewed not only by member SAIs but also by the general public. It is not mandatory for member SAIs to apply the professional documents including the INTOSAI Auditing Standards to practices of government auditing, because SAIs are under different legal systems or have different audit practices, i.e., some SAIs have only limited authority of audit, or do not have fully discretionary power to set standards for government auditing. Therefore, the INTOSAI Auditing Standards are considered as a “best practices” consensus among SAIs, and each SAI must judge the extent to which the standards are compatible with achieving its mandate<sup>8)</sup>.

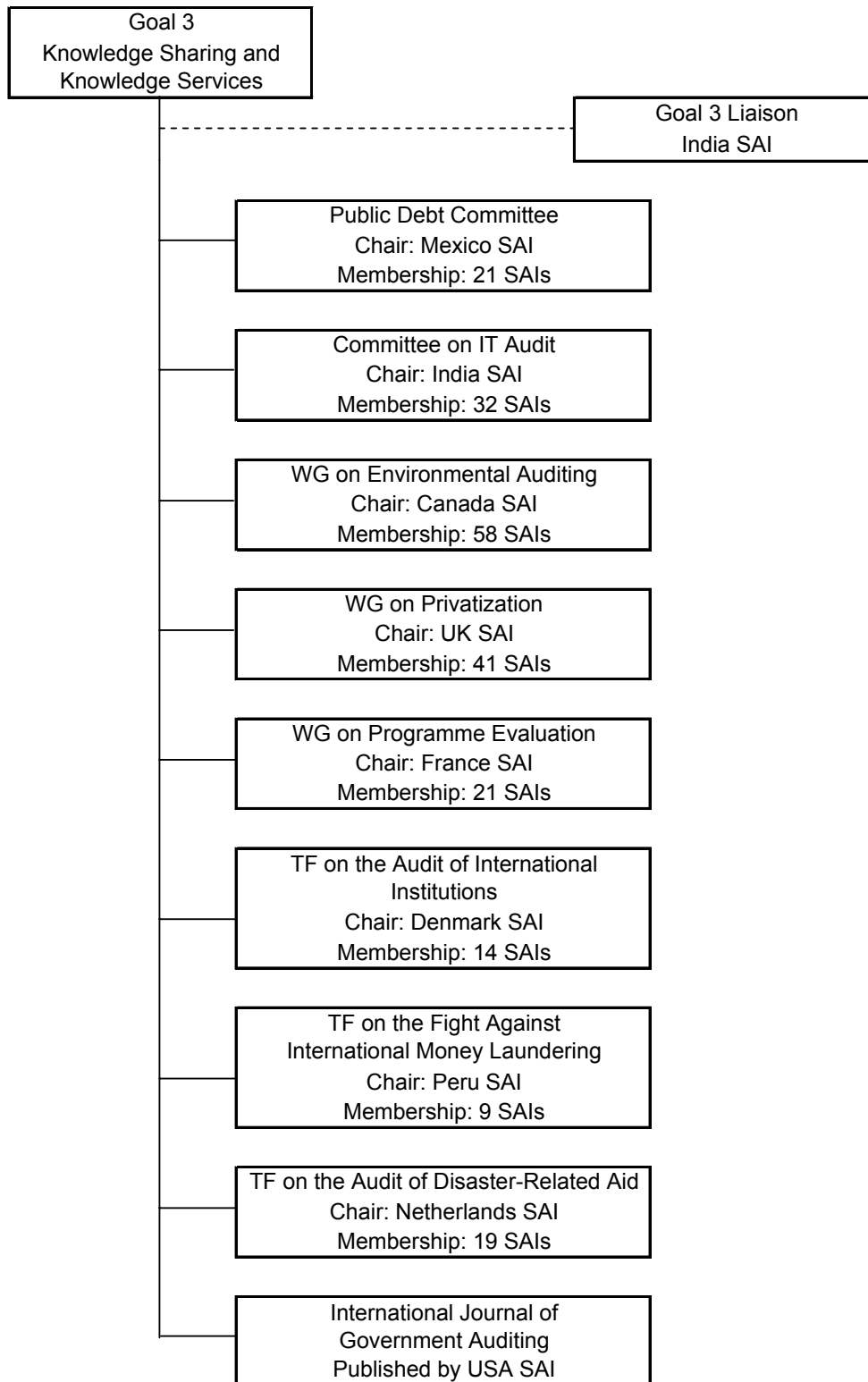
8) INTOSAI Auditing Standards, Foreword.

Table 3 Professional documents related to Goal 3 (development results)

Committee / WG / TF	Name of document	Approved: (last revised:)
Committee on EDP Audit	Information System Security Review Methodology: A Guide for Reviewing Information System Security in Government Organizations	October 1995
	Guide to Developing IT Strategies in Supreme Audit Institutions	October 1995
Public Debt Committee	Guidance on Definition and Disclosure of Public Debt	October 1995
	Guidance for Planning and Conducting an Audit of Internal Controls of Public Debt	November 1998 (May 2000)
	Guidance on the Reporting of Public Debt	November 1998 (May 2000)
	Public Debt Management and Fiscal Vulnerability: Potential Roles for SAIs	February 2003
	Fiscal Exposures: Implications for Debt Management and the Role for SAIs	February 2003
WG on Environmental Auditing	Natural Resource Accounting	May 1998
	How SAIs May Co-operate on the Audit of International Environmental Accords	November 1998
	Guidance on Conducting Audits of Activities with an Environmental Perspective	October 2001
	The Audit of International Environmental Accords	October 2001
	Environmental Audit and Regularity Auditing	October 2004
	Sustainable Development: The Role of Supreme Audit Institutions	October 2004
	Auditing Water Issues: Experiences of Supreme Audit Institutions	March 2004
	Towards Auditing Waste Management	May 2004
WG on Privatization	Guidelines on Best Practice for the Audit of Privatizations	November 1998
	Guidelines on Best Practice for the Audit of Public / Private Finance and Concessions	October 2001
	Guidelines on Best Practice for the Audit of Economic Regulation	October 2001
	Guidelines on Best Practice for the Audit of Risk in Public/Private Partnership (PPP)	October 2004
TF on the Audit of International Institutions	Principles for Best Audit Arrangements for International Institutions	October 2004
	Best Practice Example of Financial Rules and Regulations concerning Audit Arrangements in International Institutions	October 2004
	Audit of International Institutions: Guidance for Supreme Audit Institutions (SAIs)	October 2004

Source: INTOSAI website ([http://www.intosai.org/en/portal/documents/intosai/audit\\_related/documentsgoal3/](http://www.intosai.org/en/portal/documents/intosai/audit_related/documentsgoal3/), [http://www.intosai.org/en/portal/documents/intosai/audit\\_related/documentsworkpap/](http://www.intosai.org/en/portal/documents/intosai/audit_related/documentsworkpap/) (July 11, 2007))





Source: INTOSAI website  
 ([http://www.intosai.org/en/portal/committees\\_working\\_groups\\_task\\_forces/goal\\_3\\_knowledge\\_sharing/](http://www.intosai.org/en/portal/committees_working_groups_task_forces/goal_3_knowledge_sharing/)  
 (July 11, 2007))

Figure 4 Chart of organs related Goal 3

#### 4. Status of adoption of government auditing standards

PSC conducted a survey of all member SAIs (186 countries, etc.) during the period from November 2006 through February 2007 to grasp their needs for professional documents to be developed in the future. The survey also covered the status of adoption of government auditing standards by the member SAIs. As a result, as many as 76 SAIs of the 100 SAIs that responded to the questionnaire have adopted INTOSAI Auditing Standards for their financial audits, compliance audits or performance audits, showing that the INTOSAI Auditing Standards are now the mainstream in government auditing. Some SAIs have adopted standards other than the INTOSAI Auditing Standards for some areas of audit. The survey results revealed that 60 SAIs have adopted i) the International Standards on Auditing (ISA) developed by IAASB for their financial audits, compliance audits or performance audits; 50 SAIs have adopted ii) government auditing standards developed by domestic standard-setting organizations; 29 SAIs have adopted iii) government auditing standards developed by their Regional Working Groups; and 27 SAIs have adopted iv) auditing standards applicable to the private sector developed by domestic standard-setting organizations<sup>9)</sup>.

### III Systematization of government auditing standards

#### 1. INTOSAI's system of standards

INTOSAI's Committees, WGs and TFs have so far developed the professional documents as listed in Tables 1 and 3, and are planning to develop the documents listed in Table 2. Those professional documents have been developed by the Committees, WGs and TFs independently of one another without coordination. As a result, the relationships among those documents are unclear, i.e., some documents concerning government auditing are placed on a parallel with documents concerning governance, or the relationship between documents defining the principles of government auditing and those defining more detailed auditing procedures is unclear. Thus, INTOSAI is now considering integrating the existing and future documents developed by the Committees, WGs and TFs into a single system of standards, in order to clarify the documents, and their relationships and hierarchy, for the member SAIs. The system of standards is to consist of standards related to audit and those related to governance, as follows. (For INTOSAI's system of standards, refer to Table 4.)

##### 1.1 Standards related to audit

It is suggested that the name International Standards of Supreme Audit Institutions (ISSAI) be used as the common name for the body of documents related to audit. Each document will thus get an ISSAI-number. The system of standards consists of four levels in a hierarchy: Levels 1-4, and the number of digits in the ISSAI-number indicates the level in the hierarchy.

##### (1) Level 1

Level 1, which is the highest in the system of standards, contains the founding principles of government auditing. Specifically it includes the Lima Declaration adopted at the 9<sup>th</sup> INCOSAI in 1977, because the Lima Declaration is equally significant for all the member SAIs, no matter to what region they belong, how mature their government auditing has become, or how they are integrated into the system of government. The Declaration consists of 25 Sections that provide for i) the purpose of the SAI's government auditing, ii) the SAI's independence from the audited entities, iii) the SAI's relationship to the parliament, government and the administration, iv) the SAI's audit powers, v) the methods and procedures for the government auditing and so on. It provides the concepts to support the activities of INTOSAI.

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9) INTOSAI/PSC (2007b), pp. 3-4.

Table 4 INTOSAI's system of standards

1. International Standards of Supreme Audit Institutions (ISSA)		Name of document
Level	ISSA number	
1	Fundamental principles	1 The Lima Declaration
2	Prerequisites for the Functioning SAIs	10 Code of Independence of SAIs <sup>note1)</sup>
		11 Guidelines and Good Practices related to SAI Independence <sup>note1)</sup>
		20 Code of Transparency and Accountability
		30 INTOSAI Code of Ethics
3	Auditing principles	100 INTOSAI Auditing Standards (Basic Principles of Government Auditing)
		200 INTOSAI Auditing Standards (General Standards for Government Auditing)
		300 INTOSAI Auditing Standards (Field Standards for Government Auditing)
		400 INTOSAI Auditing Standards (Reporting Standards for Government Auditing)
4	Guidelines	1000 Implementation Guideline on Financial Audit - Introduction - <sup>note1)</sup>
		IFAC/IAASB 1... Implementation Guideline on Financial Audit <sup>note2)</sup>
		3000 Implementation Guideline on Performance Audit
		4000 Implementation Guideline on Compliance Audit <sup>note1)</sup>
		5000 Audit of International Institutions - Guidance for SAIs - Specific Guidelines
		5000 Audit of International Institutions
		5010 Principles for best audit arrangements for international institutions
		5010 Best practice example of financial rules and regulations concerning audit arrangements in international institutions (ISSAI 5010-Appendix)
		5110 Guidance on Conducting Audits of Activities with an Environmental Perspective
		5120 Environmental Audit and Regularity Auditing
		5130 Sustainable Development: The Role of SAIs
		5210 Guidelines on Best Practice for the Audit of Privatizations
		5220 Guidelines on Best Practice for the Audit of Public/Private Finance and Concessions
		5230 Guidelines on Best Practice for the Audit of Economic Regulations
5240 Guidelines on Best Practice for the Audit of Risk in Public/Private Partnerships		
5310 Information System Security Review Methodology - A Guide for Reviewing Information System Security in Government Organizations		
Public debt	5410 Guidance for Planning and Conducting an Audit of Internal Controls of Public Debt	
	5420 Public Debt: Management and Fiscal Vulnerability: Potential Roles for SAIs	
	5430 Fiscal Exposures: Implications for Debt Management and the Role for SAIs	

Note1: This document is expected to be adopted.

Note 2: "ISSA 1..." refers to International Standards on Auditing (ISA) developed by the International Auditing and Assurance Standards Board (IAASB) of the International Federation of Accountants (IFAC), and "... " means an ISA number or an ISQC (International Standards on Quality Control) number. Each "ISSA 1..." contains practice notes (PN) developed by INTOSAI.

2. INTOSAI Guidance on Good Governance (INTOSAI GOV)		Name of document
INTOSAI GOV number		
Guidance on standards for internal control (9100-9199)	9100	Guidelines for Internal Control Standards for the Public Sector
	9110	Guidance for Reporting on Effectiveness of Internal Controls: SAI Experiences in Implementing and Evaluating Internal Controls
Guidance on accounting standards (9200-9299)	9120	Internal Control: Providing a Foundation for Accountability in Government
	9200	Accounting Standards Framework
	9210	Accounting Standards Framework Implementation Guide: Departmental and Government-wide Reporting
	9220	Accounting Standards Framework Implementation Guide for SAIs: Management Discussion and Analysis of Financial, Performance and Other Information
	9230	Guidance on Definition and Disclosure of Public Debt

Source: INTOSAI/PSC (2007a) p. 6, PSC/ISSAI website (<http://www.issai.org/composite-191.htm>, <http://www.issai.org/composite-192.htm>, <http://www.issai.org/composite-194.htm> (July 20, 2007))

(2) Level 2

Level 2 contains codes/principles for the organization and management of member SAIs. Specifically, it includes the Code of Independence of SAI, the Code of Transparency and Accountability, and the INTOSAI Code of Ethics, because the SAI's independence from the audited entities, the transparency of the SAI's organization and management, and the ethical views of the staff of the SAI addressed by those codes greatly enhance the effectiveness of audits and the reliability of the results. Those codes provide fundamental principles, as the Lima Declaration does, and so should not be revised so often.

(3) Level 3

Level 3 contains standards on government auditing. Specifically it includes the INTOSAI Auditing Standards adopted at the 14<sup>th</sup> INCOSAI in 1992. Those Standards consist of Basic Principles, General Standards, Field Standards and Reporting Standards, and provide a framework with which member SAIs can establish principles that they follow in implementing audits, and important procedures for audits. INTOSAI Auditing Standards – Basic Principles divide the scope of government auditing into regularity audit and performance audit<sup>10</sup>.

(4) Level 4

Level 4, which is the lowest in the system of standards, contains guidelines for government auditing. Specifically, it includes Financial Audit Guidelines, Compliance Audit Guidelines, Performance Audit Guidelines, and guidelines on specific audit subjects. Those guidelines provide detailed procedures for auditing practices by which INTOSAI Auditing Standards at Level 3 are actually applied in audits. At Level 4, regularity audit is further divided into financial audit and compliance audit. Thus the government auditing is finally divided into financial audit, compliance audit and performance audit. As for Financial Audit Guidelines, they are intended to converge with the International Standards on Auditing (ISA). They are composed of ISAs and Practice Notes developed by INTOSAI independently.

## 1.2 Standards related to governance

INTOSAI is considering incorporating developed documents concerning the governance of government institutions in the areas of internal control, accounting, etc. that are closely related to government auditing, into its system of standards. It is suggested that the name INTOSAI Guidance on Good Governance (INTOSAI GOV) be used as the common name for the body of documents related to governance. Each document will thus get an INTOSAI GOV-number. The INTOSAI GOV-number consists of four digits, so the document corresponds to Level 4 in ISSAI.

## 2. Public sector considerations

At the Level 4 of ISSAI, the government auditing is divided into financial audit, compliance audit and performance audit. This division corresponds to the following government sector considerations.

### 2.1 Necessity of compliance audit

The principle of administrative and financial activities of the government sector is to allocate revenues from taxes that it levies according to policy goals. Because people have various interests, such revenues are allocated according to budgets deliberated and decided in the parliament that consists of representatives of the people. Thus the administrative and financial activities of the government sector are controlled through budgets by the parliament. It is therefore necessary for the member SAIs to check whether the accounting is carried out properly according to the budgets in order to confirm that the control through budgets functions effectively. Regarding the accounting principles and procedures to be followed in the implementation of budgets, the basic matters are provided in laws, and the matters

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10) INTOSAI Auditing Standards 1.0.38. Regularity audit includes audits implemented to ensure the appropriateness of financial reports, and audits implemented to check on the compliance of financial systems and transactions with applicable statutes and regulations (INTOSAI Auditing Standards 1.0.39). Performance audits include audits implemented from a perspective of economy, efficiency and effectiveness (INTOSAI Auditing Standards 1.0.40).

related to accounting practices are set forth in governmental or ministerial ordinances. Similarly, regarding the principles and procedures for managing assets/liabilities acquired/incurred in the implementation of budgets, the basic matters are provided in laws, and the matters related to management practices are set forth in governmental or ministerial ordinances. Thus the administrative and financial activities of the government sector are controlled through laws and regulations. It is therefore necessary for the member SAI to check whether the accounting and the management of assets are carried out properly according to the laws and regulations in order to confirm that the control by laws and regulations functions effectively.

## 2.2 Necessity of financial audit

Because the administrative and financial activities of the government sector are controlled through budgets by the parliament, the government sector is accountable to the parliament for its accounting that should be carried out properly according to the budgets. The government sector fulfills this accountability by preparing and submitting to the parliament the closing accounts according to the budget items where the budget amounts are compared with the actual expenditures (financial reports on the flow). In addition, because the financial status of the government sector is directly related to the burden on the people, the government sector is accountable to the parliament for the status of assets/liabilities that it has acquired/incurred in the process of implementing the budgets. The government sector fulfills this accountability by preparing and submitting to the parliament financial reports on the stock. The government sector's financial reports on the flow and the stock are used by the parliament to evaluate how well the government is fulfilling its accountability and to make rational decisions in controlling the government through budget. It is therefore necessary for the member SAIs to check whether the government sector's financial reports properly reflect the status of implementation of the budgets and that of management of assets in order to confirm that the government sector fulfills its accountability properly.

## 2.3 Necessity of performance audit

Because the private sector is subject to competition and the market mechanism, private enterprises will be selected by the market and forced out of the market if they operate uneconomically and inefficiently. Thus enterprises in the private sector have an incentive to operate economically and efficiently. On the other hand, the government sector does not provide administrative services through the market mechanism, and so has no incentive to carry out its administrative activities economically and efficiently. In addition, because the government sector is under the financial control of the parliament and the cabinet, it tends to give priority to compliance with the budgets, laws and regulations over economy and efficiency. In view of the fact that the government sector has no incentive to be economical and efficient in its administrative activities, the member SAIs must check whether administrative operations are performed with the minimum inputs of resources, and whether the maximum administrative services are provided with certain inputs of resources, to ensure that budgets are used economically and efficiently.

In addition, enterprises in the private sector operate to gain profits. They procure funds necessary to produce goods or services through the market mechanism, and provide those goods or services to consumers who are willing to pay for them through the market mechanism. Because such enterprises are evaluated on the principles of competition in the market mechanism, their performance is reflected in the financial data, i.e., profits obtained by subtracting the cost from the revenue. On the other hand, the government sector carries out administrative activities to achieve policy goals such as improving the welfare of the people. Institutions in the government sector use financial resources of taxes that they levy on the people, and provide administrative services for the people without going through the market mechanism. Thus the administrative operations of the public sector are not evaluated on the principles of competition, and therefore, it is impossible to evaluate its performance only on the basis of financial data. Since it is impossible to evaluate the state of achievement of policy goals of the government sector only on the basis of financial data, the member SAIs must check whether the policies have led to the achievement of their goals or have been effective for society, in order to promote the effective use of budgets.

## IV Convergence of government auditing standards and ISA

### 1. INTOSAI's strategy on financial audit

In INTOSAI's system of standards, the government auditing is divided into regularity audit and performance audit at Level 3, and further into financial audit, compliance audit and performance audit at Level 4. The financial audit at Level 4 means the audit of financial statements, in the category of regularity audit at Level 3, that is carried out to ensure the appropriateness of financial reports, and is basically the same as the audit of financial reports implemented in the private sector. INTOSAI has adopted the strategy of leveraging the expertise and resources of the International Auditing and Assurance Standards Board (IAASB), an international audit standard-setting organization, of the International Federation of Accountants (IFAC) in order to develop guidelines for financial audit that can be accepted by as many member SAIs as possible<sup>11)</sup>. The background is that many more countries have introduced the accrual accounting system into the government sector, creating an environment where the standards for auditing financial statements in the private sector can be applied to financial audits of the government sector. Accordingly, the Financial Audit Guidelines at Level 4 consist of i) a document that describes the relationship of INTOSAI's auditing standards with the International Standards on Auditing (ISA) developed by the IAASB, ii) ISAs developed by IAASB, iii) Practice Notes (PN) by which the auditing procedures provided in ISAs are modified or new such procedures are added to accommodate the considerations specific to government auditing, and iv) documents that provide for practical audit procedures in the areas where ISAs have not been developed<sup>12)</sup>.

### 2. Relationship of INTOSAI with IAASB

#### 2.1 Organization of IAASB

The International Auditing Practices Committee (IAPC) of the IFAC, an international organization of associations of accountants in the world, has developed ISAs since the 1980s. The Committee was integrated into the International Auditing and Assurance Standards Board (IAASB) in 2002 when the IFAC was reorganized. The IAASB is composed of i) 18 Board members (ten members from accountant associations, five representatives from the Forum of Firms, and three public members), ii) the Steering Committee, and iii) the Consultative Advisory Group (CAG), and acts as an independent standard-setting body under the umbrella of the IFAC. As international standards converge, it is essential to ensure the reliability of such standards, so the Public Interest Oversight Board was formed in 2005 to oversee the activities of the IFAC including the IAASB in terms of the public interest. As for relations with INTOSAI, one of the public members is the Auditor-General for the Commonwealth of Australia, and another is an ex-Auditor-General of the Swedish National Audit Office, and a staff member of the Swedish National Audit Office is on the CAG as a representative of INTOSAI.

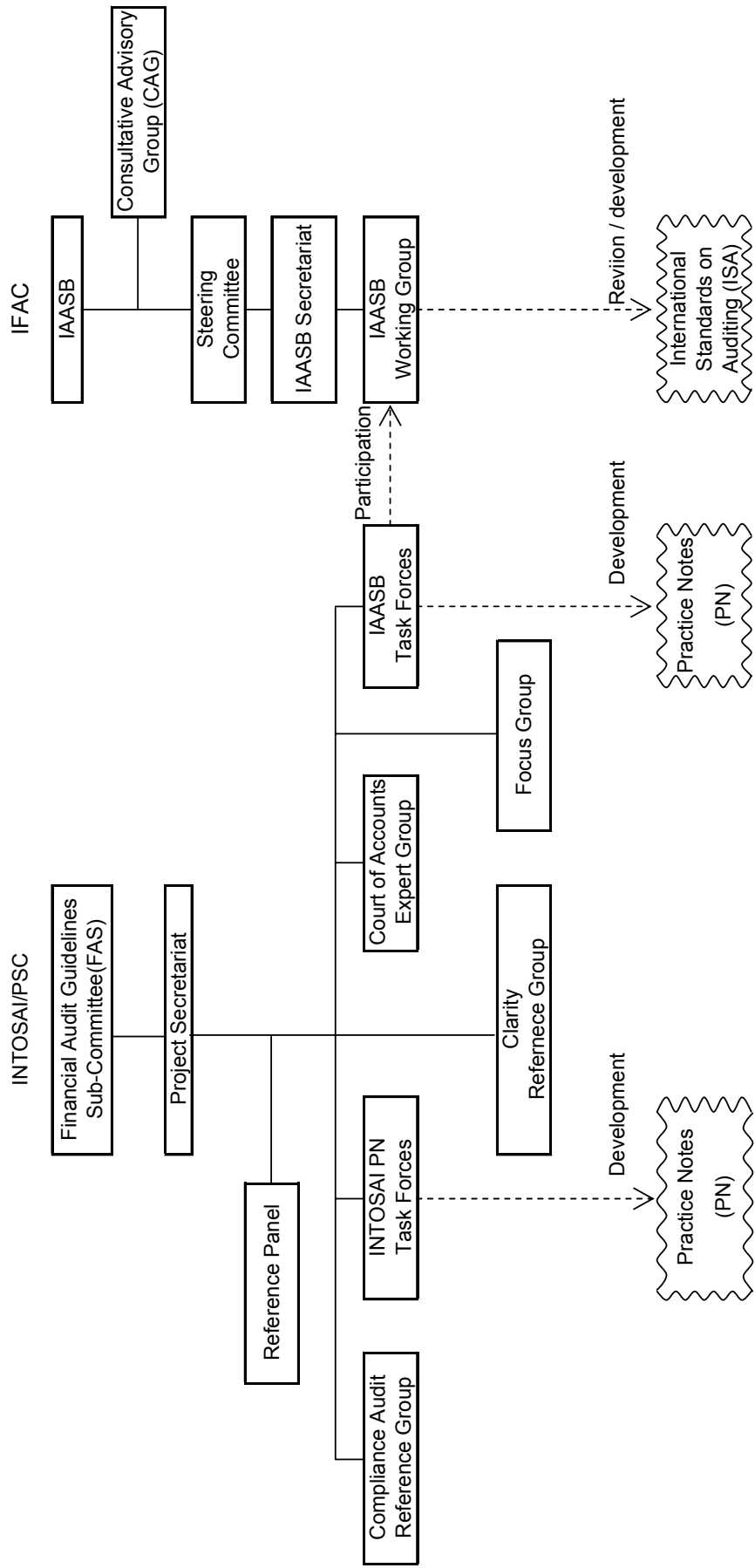
#### 2.2 IAASB standards

The IAASB has been developing i) International Standards on Auditing (ISA) to be applied in the audit of historical financial information, ii) International Standards on Review Engagements (ISRE) to be applied in the review of historical financial information, iii) International Standards on Assurance Engagements (ISAE) to be applied in assurance engagements dealing with information other than historical financial information, iv) International Standards on Related Services (ISRS) to be applied in related services engagements, and v) International Standards on Quality Control (ISQC) to be applied to all auditing/assurance services falling within the scope of ISA, ISRE and ISRS. The ISA, among others, will be adopted by INTOSAI as a part of the Financial Auditing Guidelines, and given the ISA-numbers of 100-999 according to the subject, with each ISA accompanied by guidelines, basic principles, and important procedures.

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11) INTOSAI/FAS (2005), p. 1.

12) INTOSAI/FAS (2005), p. 2.



Source: INTOSAI/FAS (2006a), p.9, PSC website (<http://psc.rigsrevisionen.dk/composite-136.htm> (July 11, 2007))

Figure 5 Scheme for convergence of Financial Audit Guidelines and ISAs

## 2.3 Agreement between INTOSAI and the IAASB

INTOSAI and the IAASB have agreed to cooperate with each other in the development of ISAs in order to share resources, minimize duplicated efforts, try to reach agreement in an early stage of development of ISAs, and achieve a convergence of such standards. To materialize their agreement, the Committee on Auditing Standards of INTOSAI (integrated into the Professional Standards Committee (PSC) later) and the IAASB made a Memorandum of Understanding (MOU) in 2004 to construct a scheme in which they would implement a cooperative project to ensure a convergence of INTOSAI's Financial Audit Guidelines and ISAs. The MOU was revised in 2006, and the current scheme is as follows (for the scheme for convergence of the Financial Audit Guidelines and ISAs, see Figure 5).

## 3. Convergence of Financial Audit Guidelines and ISAs

### 3.1 Scheme

#### (1) Project Secretariat

In order to implement the cooperative project of INTOSAI and the IAASB, a Project Secretariat was established in the Financial Audit Guidelines Sub-Committee (FAS) under PSC. The Secretariat is comprised of a Project Director and six staff members, and is located in the Swedish National Audit Office. The Project Secretariat requests the member SAIs to register their staff members with practical experience of auditing and knowledge of government auditing standards every year in order to ensure human resources who can revise or develop ISAs together with the IAASB.

#### (2) Reference Panel

The staff members of the member SAIs that are registered at the request of the Project Secretariat compose a Reference Panel. This Reference Panel had 150 registrations from 70 SAIs in 2006<sup>13)</sup>. The FAS appoints experts from the Reference Panel to participate in i) IAASB Task Forces, ii) INTOSAI PN Task Forces, iii) the Focus Group, iv) the Court of Accounts Expert Group, v) the Clarity Reference Expert Group, and vi) the Compliance Audit Reference Expert Group. Those experts include ordinary ones who attend meetings with the IAASB or meetings at the Project Secretariat, and supporting ones who stay at their own SAIs without attending such meetings, but give support to the former ones. In 2006, 44 members from the 150 registrations were appointed as such experts and supporting experts<sup>14)</sup>.

#### (3) IAASB Task Forces

For an IAASB Task Force, one INTOSAI expert and at least one supporting expert are appointed from the Reference Panel to participate in a working group that the IAASB creates to revise/develop existing/new ISAs. The experts who participate in the working group are tasked with ensuring that the considerations specific to government auditing are reflected in those ISAs in order to make them applicable to the government sector, where possible. In addition, each IAASB Task Force develops Practice Notes for the ISAs that it has helped to revise or develop within nine months after they were revised or developed. Those PNs provide for detailed procedures to be used when those ISAs are applied to the government sector, or new procedures unnecessary for the private sector but used to adapt those ISAs to the government sector consideration in the audit. With an IAASB Task Force appointed, Financial Audit Guidelines are composed of the ISAs of which the Task Force has contributed to the revision or development, and the Practice Notes that it has developed on its own<sup>15)</sup>.

#### (4) INTOSAI Practice Note Task Forces

For an INTOSAI Practice Note Task Force, two experts and a few supporting experts are appointed from the Reference Panel to develop Practice Notes for ISAs for which the IAASB is not likely to set up Task Forces during the coming years. Each INTOSAI PN Task Force typically develops 1-4 Practical Notes for ISAs that are related to one another, with advice from the technical staff of the IAASB if necessary. With an INTOSAI PN Task Force appointed,

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13) INTOSAI/FAS (2006a), p. 1.

14) INTOSAI/FAS (2006a), p. 2.

15) INTOSAI/FAS (2006c), pp. 1-2.



Financial Audit Guidelines are composed of the ISAs to which the Practice Notes are related, and the Practice Notes that it has developed on its own<sup>16)</sup>.

#### (5) Focus Group

For a Focus Group, at least five experts are appointed from the Reference Group to give expert comments to i) the IAASB, ii) the IAASB members who represent INTOSAI, iii) the members of IAASB Consultative Advisory Group (CAG) who represent INTOSAI, iv) IAASB Task Forces, v) INTOSAI PN Task Forces, and vi) the Court of Accounts Expert Group. The Focus Group is responsible for considering the necessity of creating a working group to revise existing ISAs or develop new ISAs when the IAASB makes a proposal to INTOSAI for the working group<sup>17)</sup>. Nowadays, members from Swedish National Audit Office, Cameroon Supreme State Control, Indian Office of the Comptroller and Auditor General, South African Office of the Auditor General, and Greek Court of Audit are appointed.

#### (6) Court of Accounts Expert Group

Some member SAIs are vested with a judicial authority in government auditing. For the Court of Accounts Expert Group, at least five experts are appointed from the Reference Panel to give expert comments to i) the IAASB members who represent INTOSAI, ii) the members of IAASB Consultative Advisory Group (CAG) who represent INTOSAI, iii) IAASB Task Forces, iv) INTOSAI PN Task Forces, and v) the Focus Group to ensure that the considerations specific to the government auditing in so-called Court of Accounts systems are reflected in Financial Audit Guidelines<sup>18)</sup>. Nowadays, members of the Hellenic Court of Audit (chair), Brazilian Tribunal of Accounts, Turkish Court of Accounts, and Tunisian Court of Accounts are appointed.

#### (7) Clarity Reference Group

The IAASB has implemented the Clarity Project since 2005 to clarify whether auditing procedures, etc. Provided in ISAs are essential. For some ISAs checked or reviewed in the Project, Public Sector Perspectives (PSPs) in audit procedures have been developed separately. For the Clarity Reference Group, at least two experts are appointed from the Reference Panel to support not only the work of the IAASB to clarify whether audit procedures provided in PSPs are essential, but also its work to incorporate PSPs into the relevant ISAs<sup>19)</sup>.

#### (8) Compliance Audit Reference Group

The Regularity Audit defined at Level 3 in INTOSAI's system of standards is further divided into Financial Audit and Compliance Audit at Level 4. Thus it is necessary to ensure the consistency between guidelines developed by FAS and the Compliance Audit Subcommittee (CAS) under PSC independently of each other. FAS and CAS consulted with each other and agreed to cooperate in the development of the audit procedures in Compliance Audit Guidelines that have relations with the financial audit. For the Compliance Audit Reference Group, at least four experts are appointed from the Reference Panel to support the development of Compliance Audit Guidelines by CAS according to the agreement between FAS and CAS<sup>20)</sup>. FAS decided to incorporate the audit procedures in Compliance Audit Guidelines that have relations with the financial audit into Financial Audit Guidelines in order to ensure that the latter guidelines are consistent with the former.

### 3.2 Results

#### (1) IAASB Task Forces

Since INTOSAI and the IAASB made the Memorandum of Understanding (MOU) in 2004, 10 IAASB Task Forces have been formed to work for nine revisions of ISAs and the development of one new ISA, with nine

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16) INTOSAI/FAS (2006e), pp. 1-2.

17) INTOSAI/FAS (2006d), pp. 1-2.

18) INTOSAI/FAS (2006b), pp. 1-2.

19) INTOSAI/FAS (2007a), pp. 1-2

20) INTOSAI/FAS (2007b), p.2

experts and 18 supporting experts of INTOSAI appointed for them (for the organizations of the IAASB Task Forces, refer to Table 5). Most of those experts belong to the SAIs of countries that have introduced the accrual accounting system into the government sector, such as Canada, the Netherlands, New Zealand, Sweden, UK and USA. The Task Forces that worked on ISA230, ISA260 and ISA800, among others, finished the respective revisions, and the revised Standards were approved by the IAASB. The Task Force on ISA230 finished the development of Practice Notes related to ISA230, and the PN was approved at the meeting of the Governing Board of INTOSAI in November 2006. Accordingly the Task Force on ISA230 ended its activities as an IAASB Task Force; however, the members of that Task force are working in the Clarity Reference Group for ISA230 to clarify whether audit procedures in the standard are essential. In the Clarity Project, it is expected to take a few years to check and review one ISA. The Task Forces on ISA260 and ISA800 have almost finished developing Practice Notes for ISA260 and ISA800, respectively, and the standards were in the stage of Exposure Drafts as of March 2007.

The Task Forces other than those working on ISA230, ISA260 and ISA800 are still working on the revision or development of those ISAs, and on the development of Practice Notes for them. It is expected to take two or three years to finally revise or develops the ISAs.

**Table 5 Organization of IAASB Task Forces**

ISA-number	Name of ISA	Expert's SAI	Remarks
ISA230	Documentation	Norway SAI (Sweden SAI and USA SAI)	Revision
ISA260	Communications with Those Charged with Governance	Norway SAI (Sweden SAI and USA SAI)	Revision
ISA402	Use of Service Organizations	Norway SAI (vacant)	Revision
ISA505	External Confirmations	Canada SAI (vacant)	Revision
ISA550	Related Parties	UK SAI (Germany SAI and Malaysia SAI)	Revision
ISA580	Management Representations	Vacant (Chile SAI and Italy SAI)	Revision
ISA620	Using the Work of an Expert	Brazil SAI (Hungary SAI and Lesotho SAI)	Revision
ISA800	Auditor's Report on Special Purpose Audit Engagements	Sweden SAI (Ethiopia SAI, Netherlands SAI and New Zealand SAI)	Revision
ISA805	Engagements to Report on Summary Financial Statements	Sweden SAI (Ethiopia SAI, Netherlands SAI and New Zealand SAI)	Revision
Reserved	The Auditors Response to Material Weaknesses in Internal Controls	Saudi Arabia SAI (New Zealand SAI and Sweden SAI)	New development

Note: ( ) in the column of Expert's SAI contains the SAIs to which the supporting experts belong.

Source: INTOSAI/FAS (2007c), Appendix 1

## (2) INTOSAI PN Task Force

Since INTOSAI and the IAASB made the Memorandum of Understanding (MOU) in 2004, three INTOSAI PN Task Forces have been formed with seven experts and five supporting experts appointed for them to develop Practice Notes for ISAs for which the IAASB is not likely to set up Task Forces during the coming years. (For the organization of INTOSAI PN Task Forces, refer to Table 6). Task Force 1 is developing Practice Notes for ISQC (International Standards on Quality Control) 1 and ISA220; SWAT 1 for those for ISA300, ISA315, ISA320, ISA330 and ISA450; and Task Force 240 for those for ISA240. As of March 2007, the Practice Notes for ISA220, ISA300, ISA315, ISA320, ISA330 and ISA450 were in the stage of Exposure Drafts. FAS is planning to finish 12 Practice Notes including those developed by IAASB Task Forces and submit them to INCOSAI to be held in November 2007 for its approval.

Table 6 Organization of INTOSAI PN Task Forces

	ISA-number	Name of ISA	Expert's SAI
Task Force 1	ISQC1	Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements	Netherlands SAI and UK SAI (Jordan SAI and New Zealand SAI)
	ISA220	Quality Control for Audits of Historical Financial Information	
SWAT 1	ISA300	Planning an Audit of Financial Statements	Canada SAI, Norway SAI, Sweden SAI and USA SAI (China SAI, Scotland SAI and Turkey SAI)
	ISA315	Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatements	
	ISA320	Materiality in Planning and Performing an Audit and Evaluation of Misstatements Identified during the Audit	
	ISA330	The Auditor's Procedures in Response to Assessed Risks	
	ISA450	Evaluation of Misstatements Identified during an Audit	
Task Force 240	ISA240	Auditor's Responsibility to Consider Fraud in an Audit of Financial Statements	Norway SAI (vacant)

Note: ( ) in the column of Expert's SAI contains the SAIs to which the supporting experts belong.

Source: INTOSAI/FAS (2007c), Appendix 2

## V Conclusion

On the occasion of its 50<sup>th</sup> anniversary, INTOSAI formulated Strategic Plan 2005-2010 with four goals, reorganized itself according to those goals, and initiated activities to achieve them. Goal 1 is to induce member SAIs to be strong, independent, and active in many more professional areas by contributing to the development and adoption of appropriate and effective professional standards. Toward that end, INTOSAI is implementing a project to incorporate all existing and future professional documents developed by its Committees, etc. into a single system of standards in order to clarify the natures of those documents, and the relationships, including hierarchy of them, for the member SAIs.

In the project to systematize professional documents, INTOSAI classified the government auditing into financial audit, compliance audit and performance audit, and decided to develop and adopt Compliance Audit Guidelines and Performance Audit Guidelines on its own, but to adopt Financial Audit Guidelines that converge with ISAs of the IAASB, because the audit in the government sector and that in the private sector have different objectives. In this way, with regard to financial audit, INTOSAI cooperates with the IAASB in revising or developing ISAs, which makes it possible for SAIs to apply standards of high quality to their government auditing with minimum resource input. The background is that many more countries have introduced the accrual accounting system into the government sector, creating an environment where the standards for auditing financial reports in the private sector can be applied to financial audits of the government sector.

INTOSAI has constructed a scheme to ensure that Financial Audit Guidelines and ISAs converge, in which experts from member SAIs are participating in the revision or development of ISAs, or developing Practice Notes. The convergence of accounting standards and auditing standards is an international trend that is expanding from the private sector to the government sector. Of course, member SAIs are not forced to adopt International Standards of Supreme Audit Institutions (ISSAI); however, if they do not adopt ISSAIs as they are, instead member SAIs that currently have no domestic standards on government auditing may refer to the ISSAIs as a model for their domestic standards that reflect their legal system and audit practices when they develop them.

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