

I Basic Policy on Audit

The FY2020 Audit Report constitutes the results of the audit conducted in 2021 based on the Basic Policy on Audit for 2021.

Basic Policy on Audit for 2021

Approved by
the Audit Commission
on September 9, 2020

To carry out audits for the year 2021 (audit implementation period: October 2020 - September 2021) efficiently and effectively and to perform its missions accurately in keeping with social and economic trends, the Board of Audit established its Basic Policy on Audit for the year 2021 as follows:

1. Missions of the Board of Audit

The Board of Audit (the Board) has the following missions as a constitutional organization independent from the Cabinet.

The Board audits all of the final accounts of the expenditures and revenues of the State every year, and also audits such accounts as provided by law.

The Board continuously conducts audits, supervises financial management, ensures its adequacy, and rectifies any defects. Also, the Board verifies the final accounts of the expenditures and revenues of the State through the results of its audits.

The Board prepares and sends the Audit Report to the Cabinet. This Report, together with the final accounts of the expenditures and revenues of the State, shall be submitted to the Diet.

2. Social and Economic Trends and the Situation Surrounding the Board of Audit

In recent years, Japan's society and economy have faced difficult challenges, such as accelerated depopulation, rising social security expenses due to the declining birthrate and the aging population, stagnant growth potential, and an increase in large-scale natural disasters. In addition, the ongoing COVID-19 pandemic has been seriously affecting Japan's society and economy, revealing various issues that call for urgent responses such as delay in digitalization of public administration.

In addition, reconstruction from the Great East Japan Earthquake (the earthquake and tsunami that occurred along the Pacific Ocean coast in the Tohoku Region on March 11, 2011, and the resultant accident at a nuclear power plant) has remained as an issue for Japan, therefore, the administrative authorities are required to deal with these challenges appropriately.

As for the fiscal position of the State government, continual issuance of government bonds, including those for COVID-19 countermeasures, is steadily increasing the outstanding debt, which is estimated to reach about 964 trillion yen at the end of FY2020. In the budget for FY2020 (after the approval of the supplementary budget), the level of dependence on government bonds is about 56% and the total expenditure required for redemption of national debt comprises about 15% of the general account expenditure, which imposes a major challenge in achieving a sound fiscal position.

Against this backdrop, the government has decided to move forward with integrated economic and fiscal reform to address structural problems relating to the sustainability of social security and public finance and to devise a concrete roadmap for implementing the reform by the end of 2020.

Moreover, the importance of grasping the results of the State budget execution and reflecting them in the following budgets is deliberated in the Diet from the viewpoint of enhancing and strengthening

fiscal administration control by the Diet.

Taking into consideration that the Diet requested the Cabinet to submit the final accounts of the State earlier, the Board has been striving to submit its Audit Report to the Cabinet earlier than before, which helps the Diet deliberate the final accounts of the State earlier and enables the audit results to be further reflected in the budget. Furthermore, the Board has been steadily undertaking audits requested by the Diet under the provisions of Article 105 of the Diet Act and reporting the audit results to the Diet, as well as issuing “Special Reports to the Diet and the Cabinet” on an as-needed basis every year for the purpose of contributing to enhancement of the Diet’s deliberations of the final accounts of the State.

Achievement of fiscal soundness has been an important issue, and importance is placed on the strict assessment and verification of the results of the State budget execution as well as the Government’s fulfillment of accountability to the public. Against this backdrop, the role of the Board, which has raised the awareness of the public on various issues relating to public administration and finance by such means as the Audit Report, has become even more important, and the public expectations for audit functions are also growing.

3. Basic Policy on Audit

The Board has been striving to conduct audits in order to respond to public expectations in light of social and economic trends at all times. With the aim of continuing to properly fulfill its missions in the situation mentioned above, the Board will make every effort to ensure the strict and fair discharge of its duties and maintain and further improve the quality of audit activities while paying due attention to the public interest, and will carry out audits in accordance with the following policies.

(1) Focus of audits

In response to Japan’s social and economic trends and its current financial condition, the Board has decided to focus its audit activities on the following policy areas of public administration:

- Social security
- Education, science and technology
- Public works
- Defense
- Agriculture, forestry and fisheries
- Environment and energy
- Economic cooperation
- Small and medium enterprises
- Information technology (IT)

In addition, the Board enhances cross-cutting audits on policies jointly executed by several ministries and agencies and cases commonly related with several ministries and agencies, and, if necessary, also responds to matters of great public concern by conducting prompt and flexible audit activities, in a timely and proper manner.

Furthermore, the Board appropriately and in a timely manner audits various measures for promoting the reconstruction from the Great East Japan Earthquake and for COVID-19 countermeasures according to the status of progress, noting that a large amount of national expenses will be spent during a certain period.

In particular, with regard to the COVID-19 countermeasures, various programs have been implemented based on the first and second supplementary budget for FY2020 to disburse additional expenses required for the countermeasures. In light of this, when it conducts the audit, the Board takes into account the urgency required for the implementation of these programs and responds to the situation in a prompt and flexible manner, monitoring policies and trends of the government's efforts.

(2) Audits with various audit objectives

The Board conducts audits not only to identify and disclose fraudulent and improper cases but also to evaluate the performance of operations and projects. Moreover, the Board conducts audits with a focus on the necessity of specific operational systems, if necessary.

The Board conducts audits with the following objectives:

- (a) Accuracy: whether the final accounts accurately reflect the financial status such as the execution of the budgets
- (b) Regularity: whether the financial management is properly conducted in conformity with the approved budgets, laws and regulations
- (c) Economy: whether the implementation of projects and programs or budget execution is administered with the minimum cost
- (d) Efficiency: whether the projects and programs gain the maximum results with the given cost or have the best cost-efficient outcome
- (e) Effectiveness: whether the projects and programs achieve the intended results and produce the expected effects
- (f) Other objectives necessary for auditing

As for the objectives of accuracy and regularity, the Board continues to duly conduct audits because there are still many cases of improprieties. The Board focuses on examining basic accountancy while considering the fact that there was fraud and improprieties in some ministries. Furthermore, the Board conducts audits bearing in mind the competitiveness and the transparency of bidding and contracts.

As for the objectives of economy, efficiency, and effectiveness, in light of the serious financial condition in recent years, the Board puts greater importance on these objectives. With the objective of effectiveness, in particular, the Board actively endeavors to review the results of operations, projects and budget execution. In such cases, the Board conducts audits with attention to auditees' self-evaluation of their policies and various measures carried out by the government for efficient and effective implementation of administrative work and projects. Also, the Board conducts audits with attention to the situations of the assets possessed by the State and funds developed by subsidies.

If there is any problem with the implementation of the operations and projects and the budget execution, the Board thoroughly investigates the causes and considers measures for improvement and if needed, abolishment of the program.

In addition, to contribute to the improvement of the transparency and accountability of public administration and finance as well as better project implementation, the Board analyzes the public finances of the State and evaluates the government's efforts toward fiscal consolidation, and more closely audits the financial status of the special accounts and the incorporated administrative agencies. In the above cases, the Board utilizes information on public accounting such as financial documents of special accounts prepared with reference to practices of corporate accounting.

(3) Approach corresponding to conditions of internal control

Since the conditions of internal control, such as internal audits and internal checks, in auditees affect the level of adequacy of financial management to be ensured in auditees, etc., the Board pays due attention to the effectiveness of the internal control. The Board also requests the auditees to improve

their internal control systems, if necessary, so that they ensure the adequate level of financial management, etc.

(4) Follow-up of the audit findings

The Board continually checks on the state of improvements made by remedial and preventative measures against improper and irregular cases to ensure that audit results are reflected in the State budget compilation as well as in project implementation adequately and effectively.

Moreover, concerning improper financial management in the Audit Report, the Board conducts audits necessary for improving similar cases with other auditees.

(5) Cooperation with the Diet

The Board always pays attention to the deliberations in the Diet. In auditing issues in response to audit requests from the Diet, the Board makes every effort to facilitate the Diet's examination and investigation by including the necessary research contents in the Board's audit activities, paying full attention to the intention of the Diet's request. In addition, to contribute to the Diet's sufficient examination on the final accounts, the Board makes efforts to actively submit reports to the Diet and the Cabinet whenever necessary.

(6) Improvement of audit capability and effectiveness of audit activities

The Board enhances its ability to conduct audits and the effectiveness of audit activities through efforts such as the development of new audit methods to respond to the more complicated society and economy, and the changing social environment derived from various factors, including the COVID-19 pandemic, as well as the accompanying changes in the State's financial and administrative operations.

The efforts include: research studies to vary the method and scope of audit activities, including those in light of international trends of auditing, human resource development for auditing areas of expertise as well as recruitment of personnel who have acquired practical skills and experts from the private sector, and more active use of IT in audit activities. By adopting these practices, the Board conducts a more fulfilling audit for project/program of auditee matters as a whole.

4. Designing an Appropriate Audit Plan

The Board designs appropriate audit plans and carries them out in order to conduct audits more effectively and efficiently and to achieve its mission, based on the above-mentioned Basic Policy on Audit.

In the audit plan, the Board establishes its priority audit issues, on which it should focus in audits, taking into full consideration the scale and content of the budgets of auditees, measures, projects and programs, the situations of internal control, the previous audits and results, etc.

Also, in auditing, the Board attempts to enhance and strengthen audit activities by promptly and flexibly responding to the progress status of audits as well as public interests, for example, by reviewing the audit plan when necessary.

In addition, the Board pays due attention to the effects of the COVID-19 pandemic on auditees.