



SIGMA

Support for Improvement in Governance and Management

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LITHUANIA PUBLIC SECTOR EXTERNAL AUDIT¹ ASSESSMENT 2003

1. Introduction

The supreme audit institution of Lithuania (*Valstybes Kontrole, VK*) was established by articles 133 and 134 of the 1992 Constitution and the Law on the Amendment of the Law on State Control of 13 December 2001, which introduced significant changes in the management and operating mode of the VK. The VK is structured hierarchically, headed by the State Controller and two deputies. The Board of Control, consisting of the deputies and heads of departments, assist the State Controller in the discharge of his duties. In addition to the headquarters in Vilnius, there are three regional offices.

The State Controller is elected by the Lithuanian Parliament (*Seimas*) on the proposal of the President of the Republic. The VK currently numbers 295 staff, of which 167 (65 per cent) are actually assigned to audit tasks. The regional divisions account for 65 out of the total number of staff. The 2003 budget of the VK was 17.1 million litas (plus 1.6 million compared to the year before), equivalent to 4.9 million euros. Due to a wider introduction of performance audit and the abolition of inspections and revisions, the total number of audit reports has gradually decreased from a maximum of 1,220 in 1995 to 297 in 2002. Since May 2002, the VK has benefited from a Phare-supported twinning project with the UK National Audit Office, which will continue through October 2003.

2. Baseline Questions

2.1 *Does the SAI have clear authority to satisfactorily audit all public and statutory funds and resources, bodies and entities, including EU resources?*

Baseline achieved (1999, 2000, 2001 and 2002 baselines achieved). The VK has a wide remit to audit the entire public sector, including any enterprise, institution or organisation in which the state holds the ownership of at least half of all voting shares. In accordance with the audit law, the Office carries out an audit of the management, use and disposal of state budgetary funds and state property by local governments. Since April 2000, the VK has the right to audit the management of EU funds and their use by final beneficiaries, as well as the implementation of programmes in which Lithuania participates.

The issue of local government auditing of own resources still remains unclear. In the framework of a working group under the auspices of the *Seimas* and in co-operation with the Ministry of Finance, the VK has developed proposals that would clearly empower existing control units within municipalities with the capacity to carry out public external audit. These audits would be performed on the basis of the methodology defined by the VK and by applying the Public Auditing Requirements, and would be subject to quality control and quality assurance

¹ The rating is comprised of four categories: baseline achieved; baseline substantially achieved; baseline partially achieved; baseline not achieved.

arrangements in which the VK would play a role. These proposals are contained in the draft Concept of Public Audit, which should be approved in July.

2.2 *Does the type of audit work carried out cover the full range of regularity and performance audit set out in INTOSAI auditing standards?*

Baseline substantially achieved (1999, 2000, 2001 and 2002 baselines partially achieved). According to the audit law, the VK must conduct its audits in accordance with international standards, which focus more on management control and the quality of internal control.

The VK carries out financial (regularity) audits of institutions within its mandate in state institutions and agencies. Financial statements of appropriation managers are audited on an annual basis. The audit law also entitles the VK to carry out financial audit of other entities that are not subject to statutory annual audit carried out by an audit firm. Minor entities and institutions are audited at least every five years. The VK has undertaken to provide audit opinions on the accounts produced by ca. 280 appropriations managers.

In addition, the VK is entitled to carry out performance audits of state institutions and agencies, local authorities; enterprises of all types in which the state owns at least half of the shares; agencies, and organisations and other legal entities to which a state institution or local authority has allocated funds or transferred property. It also carries out performance audits of the implementation of the budget of the State Social Insurance Fund and the budget of the Compulsory Health Insurance Fund. In 2002 the VK carried out 58 audits, examining the implementation of budget programmes, management and use of budgetary funds and state property in large-scale enterprises, funds, agencies and public institutions.

The obligations of the audit law represent a big challenge for the VK, in terms of both quality and the use of scarce resources. Audit needs have to be carefully analysed and addressed, and clear audit priorities have to be identified in the form of an audit strategy. Such a strategy is currently being developed with the assistance of the UK twinning partner for the financial audit, and has already been completed for the performance audit (three-year strategy).

2.3 *Does the SAI have the necessary operational and functional independence required to fulfil its tasks?*

Baseline substantially achieved (1999, 2000, 2001 and 2002 baselines substantially achieved). The audit law satisfies the major formal independence recommendations of INTOSAI. The State Controller is appointed by the *Seimas* on the proposal of the President of the Republic for a fixed five-year term and must not recently have been a member of the cabinet or leader of a political party. There are strict requirements for avoiding staff conflicts of interest.

The financial independence of the SAI remains limited, as it is not different from other state organisations. The VK is financed from the state budget, and the *Seimas* determines the amount of appropriations for the budget. This situation does not divert from the still mainstream practice among supreme audit institutions, but the VK considers that improvements in that respect are in any event needed, as its working capacity may be affected by these restrictions. This has, for instance, the impact that resources are in particular insufficient to develop the use of external expertise.

During the last few years and especially in connection with the process of developing the renewed legal framework, the interference of external partners, especially law enforcement bodies, in the programming of the

audit has completely disappeared. In 2002 all audits were performed according to the annual audit programme. The only exception – which is fully acceptable – is the possibility given to the *Seimas* to request special audits from the VK. Such special audits can only occur through a specific procedure involving the audit sub-committee of the budget and finance committee, and indeed this has happened only twice so far in 2003.

2.4 *Are the SAI's annual and other reports prepared in a fair, factual and timely manner?*

Baseline substantially achieved (1999, 2000, 2001 and 2002 baselines substantially achieved). Each year the VK submits to the *Seimas* its conclusions on the annual account of the execution of the state budget (article 134 of the Constitution), its conclusions on the draft state budget (article 173 of the Statute of the *Seimas*), and its conclusions on Public Debt (under article 11 of the Law on Public Debt). Since 2002 the VK has had to also submit to the *Seimas* its conclusions on the management and use of state property (under the article of the law on use and disposal of state property), which actually focuses mainly on the management of state shares in companies. The first opinions on the accounts of appropriation managers are expected by the end of September, which may appear to be rather late.

Furthermore, the VK submits to the *Seimas* an annual report on its operational performance (article 206 of the Statute of the *Seimas*).

According to the current law, a financial audit must be concluded by an audit report and an audit opinion. A performance audit results in an audit report. The audit opinion is signed by the auditor who performed the audit and by the director of the relevant audit department. A first audit report signed by the relevant auditor is to be sent to the auditee for comments that are attached to the final audit report.

In case of violations reported during the audit, a statement is made by the State Controller, or the deputies, against which the auditee may appeal to the court, according to the procedure established by the law on administrative proceedings.

2.5 *Is the work of the SAI effectively considered by government and parliament, e.g. by a designated committee that also reports on its own findings?*

Baseline substantially achieved (1999, 2000 2001 and 2002 baselines partially achieved). The VK's relationship with the *Seimas* remains as well developed as one would assume from the institutional linkage. For this reason the establishment in September 2002 of an audit sub-committee within the committee on budget and finance should be regarded as significant progress in this relationship, paving the way for further strengthening of the impact of audit work. This sub-committee was established in accordance with the *Seimas* Resolution of 7 July 2001 no. IX-465. The internal regulations adopted in February 2003 stipulate that the sub-committee will consider the audit reports sent by the State Controller and will implement parliamentary means to assist the VK in the follow-up of audit work. This set-up may be too recent to allow a real assessment of its effectiveness. It would seem, however, that cumbersome procedures have already resulted from the fact that the final decision on issues remains with the Budget and Finance Committee. This problem could have been avoided by the establishment of a self-standing, fully empowered State Control Committee.

The State Control Law stipulates that the public must be informed about audit activities through the mass media. This obligation is now regulated by a specific procedure approved by the State Controller in January 2003. The Annual Report on the VK's activities is made public. Reports of public-sensitive audits are published on the VK's official Internet site. In 2002 representatives of the VK took part again in several TV programmes and press

conferences, gave interviews and published articles in the press. The publication of the VK Journal, which was temporarily suspended for budget motives, resumed in early 2003.

2.6 *Has the SAI adopted internationally and generally recognised auditing standards compatible with EU requirements, and how far have they been implemented?*

Baseline substantially achieved (1999, 2000, 2001 and 2002 baselines partially achieved). The VK is an active member of INTOSAI and EUROSAI. Relevant international standards have been published in Lithuania and are available to VK auditors. The audit law requires that audits shall be carried out in accordance with the requirements for government auditing, developed in line with INTOSAI standards. In February 2002, in compliance with the law, the State Controller approved and specified these requirements in the Public Auditing Requirements.

This should provide a basis for harmonisation of auditing procedures with international auditing standards. Special training programmes have now been designed to prepare VK staff for implementation of these standards. Methodological and practical assistance was delivered by the Swedish Audit Office in a bilateral project and by the UK NAO twinning project. A significant outcome of the latter assistance has been the production of a financial audit manual and a performance audit manual. These manuals are fairly recent: they were respectively approved in December 2002 and January 2003, so that it is now too early to assess their relevance and current use in the VK.

2.7 *Is the SAI appropriately aware of the requirements of the EU accession process?*

Baseline substantially achieved (1999 and 2000 baselines not achieved, 2001 and 2002 partially achieved). In order to strengthen its capacity to deal with EU matters, the VK has established a new division dealing specifically with European and international relations. The aims are to implement the VK policy of international co-operation; maintaining and developing contacts with international professional organisations and managing international projects.

Furthermore, the VK is linked to the National Committee dealing with European integration issues, to which it regularly submits reports. This committee has played a significant role in the successful provisional closure on the EU accession negotiation chapter 28 on financial control.

The VK is also involved in the Working Group of central and eastern European SAIs, which addresses issues of the *acquis communautaire* and its consequences for public external audit. Concern about EU accession is now taken into account in VK activities, above all with regard to the development and implementation of the Strategic Development Plan.

In that respect, one of the financial audit departments (no. 7) is specifically entrusted with the audit of EU funds, and was significantly reinforced in 2002 in terms of both new staff and increased experience. Three of its auditors spent a five-month internship in the European Court of Auditors (ECA). The department has carried out two joint audits on EU projects with the ECA, and pilot audits of the SAPARD and ISPA programmes were performed in the framework of the twinning project. The department is now searching for partners likely to help with the issues relating to the Cohesion Fund audit.

The VK will propose to assume the role of appointed certifying body for SAPARD, and is now confident in its capacity to fulfil this role, which it had to renounce previously because of a lack of training.

In general, the VK also regards the external audit of EU funds as a major challenge in terms of resources, and has requested additional means from the *Seimas* in order to carry out this new task.

3. Capacity to Further Develop the System

The VK appears to be a well-established institution, to which due respect is paid by its potential auditees. However, the current leadership acknowledges the need for developing and improving the capacities of the VK. The current change process is still based on the Strategic Development Plan for 2001-2006, which was adopted by the State Controller in August 2001 following a Sigma peer review in 2000.

The Law on the Amendment of the Law on State Control of 13 December 2001 provided a clear legal basis for changes to be introduced, and strengthened institutional independence and the status of the staff. The development of secondary legislation, the adoption of the Public Auditing Requirements (February 2002), the development of a methodological framework (including financial and performance audit manuals), instructions, audit documentation, etc. and training programmes (including on management issues, human resources, and IT support strategies) should contribute to ensuring an external audit in line with good European practice.

In addition, the VK is desirous to continue the co-operation with European peer institutions. This co-operation will take place through a new twinning project expected to start in 2004. The VK is also involved in specific audit activities with partners from Spain, Germany and France.

The number and intensity of training and development activities has grown significantly in a small period of time and contrasts considerably with the situation of only a few years ago. This is a very good evolution, but there could also be a need to refrain from overloading an already limited absorption capacity.

4. Summary and Next Steps

External audit substantially meets the requirements of the INTOSAI Auditing Standards/EU Implementing Guidelines for adequate audit of public funds and expenditure, and the VK's strategic objective is to ensure full conformity with the above requirements. The audit mandate and powers given in the audit law provide the VK with a solid base for becoming a strong SAI. Very significant progress has been achieved in a short period of time.

Priority should be given to the following actions:

A. Should be applied (or started) in the short term (next 12 months):

- Continue to implement the Strategic Development Plan in co-operation with the available technical assistance.
- Implement and test the Public Auditing Requirements as well as the new audit manuals; to be useful, these documents should be regarded as living documents, placed permanently under scrutiny.
- Develop a contradiction procedure and quality control.
- Introduce an Audit Strategy based on an assessment of risk and materiality.
- Carefully assess the training requirements for progressively implementing the revised audit approaches and techniques, with sufficient attention paid to the need for ownership among audit staff and efficient dissemination of new audit instruments.

- Contribute through its activities to the development and improvement of the new public internal financial control systems and procedures in Lithuania.
- Take the lead in helping the government and Parliament develop a good policy and strategy for the audits of local government (and to play an active audit role if necessary), as the implementation of effective and efficient arrangements for such audits is a priority. The policy and strategy for local government external audit should ensure that financial, legality and performance audits are performed to an acceptable standard and quality, equivalent to the standards applied by the VK.

B. Should be applied (or started) in the medium term (next two years):

- Make full use of the new possibilities provided by the creation of the sub-committee on audit of the Budget and Finance Committee of the *Seimas*, and also reflect on possible improvements, including a self-standing committee for public external audit issues.
- Review the budget arrangements to improve the level of autonomy of the VK in this area.
- Ensure the updating of the Strategic Development Plan.
- Ensure that any new developments in the Lithuanian public administration are quickly taken into account in audit activities, including the performance of the audit.
- Maintain the right balance between training and development activities and daily audit work, also taking into account the reality of the absorption capacity.
- The VK should seek peer assurance to assess the progress resulting from the current changes and reform process.