



SIGMA

Support for Improvement in Governance and Management

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ALBANIA

EXTERNAL AUDIT

ASSESSMENT MAY 2008

1. Legal Framework

The Supreme Audit Institution of the Republic of Albania, the High State Control (HSC), was established in 1992 as a parliamentary institution independent from the government. The HSC finds its legal basis in articles 162-165 of the Albanian Constitution. Concerning external audit, the Albanian Constitution establishes:

- the status of the HSC;
- the legal position (appointment, dismissal, protection) of the Chairman of the HSC;
- the remit of the HSC audit;
- reporting by the HSC to the National Assembly;
- relations of the HSC with the government.

The objectives, scope, powers, and organisational structure of the HSC are elaborated in the Law on the “State Supreme Audit Institution” of 1997 (SSAI Act), last amended by law in 2000 as well as by a Constitutional Court decision in 2002. The last amendment of the SSAI Act in 2002 reflects a decision of the Constitutional Court, which stated that in principle it would be possible for the National Assembly, upon the proposal of the President of the Republic, to dismiss the chairman of the HSC from office on any grounds. This decision is not in line with the INTOSAI Lima Declaration. Several international organisations have supported the view that the position of the chairman of the HSC should be regarded as a non-political post (article 1 of the SSAI Act states that the HSC is supposed to be a non-political organisation) and that any possible action taken with regard to the dismissal of the HSC chairman must be based on a limited number of criteria, preferably mentioned in the Constitution, but in any event in the SSAI Act. Criteria for dismissing the HSC chairman are missing in the current SSAI Act.

The SSAI Act gives authority to the HSC to audit the services of the state and “other state judicial (i.e. legal) persons”. Companies in which the state has a majority of shares or whose debts are guaranteed by the state can be audited by the HSC. It also has the right to audit state funds (employment, retirement and health) adopted by the National Assembly, funds provided to private organisations, and funds from foreign donors provided via the state budget. Regarding local government, the HSC audits the expenditures of local government entities and the use of state transfers to these entities.

The HSC has the authority, under the current Audit Act, to carry out the full scope of audit. This includes financial audit, performance audit and other specific audits (“legality; regularity; financial management; and performance aspects”).

The annual statutory audit covers the execution of the state budget and budget support to municipalities, state funds, and the National Bank.

The HSC is functionally, operationally and administratively independent. The Constitution provides a solid basis for its functioning. Its operations are financed by its own budget and approved by the National

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Assembly, and it can independently recruit and dismiss staff. Its operational independence has increased. Prior to 2007 the HSC's operational independence could be violated by the government. It was possible, following the approval of the budget by the National Assembly, for the government to cut the budget of the HSC, if deemed necessary. In that regard, cuts of up to 37% were imposed on HSC's 2005 budget. These budget cuts resulted in reducing the volume of audit work. As from 2008 only the Budget Committee of the Albanian Parliament reviews the HSC's budget proposal. However, like all other institutions, the HSC also has to deliver its share of general budget cuts aimed at stabilising the state budget.

Following an amendment of 1 June 2000 to the SSAI Act of 1997, the HSC has been established as an office-model institution, headed by a chairman. The National Assembly elects the chairman by majority vote, upon the proposal of the President of the Republic, for a term of seven years. This term can be renewed. The legal design of the institution, with a term of office of the HSC chairman of seven years, should promote a reasonable degree of stability and independence, as general elections to the National Assembly occur every four years.

Although the SSAI Act is in principle in line with the INTOSAI Lima Declaration and auditing standards, the remit and scope of audit of the HSC – in addition to the above-mentioned independence of the HSC chairman – need further clarification. The SSAI Act is unclear as to whether the HSC has the right to audit the end-users of EU resources and revenues, and as to whether the statutory audit leads to an opinion on the financial statements of the state and/or individual ministries. Furthermore, the Act should be modernised in the technical sphere, such as defining the status of the staff, clarifying the HSC's co-operation with Internal Audit services. Although contradictory procedures for presenting reports to the government and to the National Assembly, as well as procedures for the follow-up of HSC recommendations, are regulated in the HSC Internal Regulation, for reasons of transparency and equal treatment such procedures would be preferably incorporated into the SSAI Act.

As the new Organic Budget Law (OBL), which was presented to the National Assembly in March 2008, does not contain provisions for the role of the HSC in the annual budget cycle, it is of paramount importance that this role be precisely defined in the SSAI Act.

2. Institutional Framework

Internal reorganisation of the HSC took place following the latest legal amendment to the SSAI Act, and a director-general appointed by the HSC chairman is now second in command. To reinforce audit activity, the number of audit departments was reduced from six to five in mid-2007. Two of the three support departments were reorganised as well. Audit methodology has been transferred from the Department of Public Relations to the Department of Legal Affairs and Quality Control. The third support department, Department of Economy and Human Resources Management, has not changed. The total number of staff in the HSC is 160, of whom 110 are auditors.

In addition to the central headquarters, there are three local offices in Tirana, Skodër and Vlorë. The regional offices are not autonomous offices. The staff members, in total 22, are subordinated to the head of the audit departments for the state budget. The auditors in the regional offices collect information and submit this information to staff members of the central office for reporting purposes. Originally the regional offices were set up to fill the gap created by the lack of control of regional and municipal expenditures by the government. Violations of laws were not prosecuted. The regional offices pay particular attention to compliance with the laws.

Now that the government has taken the first steps (introduction of financial management, internal audit and inspection in the new OBL) to improve the financial management and control of budget activities all over the country, for efficiency reasons the HSC might reconsider the role, organisation and type of work of its regional offices.

The HSC is located in the building of the parliament's administration, but it will have to move to a new location. Since the beginning of 2007 the HSC management has been waiting for a decision by the Council of Ministers as to which building it will be occupying. The chairman of the HSC expects that a solution will be found in the next few months, although it is difficult to find a well-maintained and spacious building in Tirana. This delay in moving has negative consequences for the development of information technology within the HSC. Internet connections are not available for everyone, and Intranet is only accessible in the main office. Investments aimed at improving this IT environment are no longer made, for understandable reasons.

The HSC is a member of INTOSAI (1994) and EUROSAI (1996); it also participates in the co-operation network organised by the Presidents of SAIs in EU candidate and potential candidate countries and the European Court of Auditors.

3. Reform Agenda and Capacities

In the somewhat difficult public sector environment of Albania, the HSC has substantially progressed in its audit activities as well as in its internal management and organisation.

This is due in the first place to the efforts of the SAI itself and its staff. The role of technical assistance was also important in contributing to the drafting of a development strategy for the period 2005-2008. Exchange of experiences in the key areas of audit and audit support activities with the Polish Supreme Chamber of Control took place in 2006, with the support of Sigma. A twinning project with the National Audit Office of the United Kingdom and the Court of Audit of the Netherlands started in January 2007 and will continue until September 2008. The twinning project focuses on institutional reform, improvement of audit practices, reform of the legal framework, and improvement of support processes, such as HRM and communications. Due to capacity problems, a revision of the 2005-2008 strategy is foreseen to begin as soon as the twinning project has ended. This revision will be carried out by the HSC itself; the chairman does not foresee the need for any technical assistance after the current twinning project.

4. Assessment

The legal reform component of the twinning project focuses on reviewing the current law on compliance with EU requirements and on practical needs resulting from the pilot audits. The HSC declared that Sigma's remarks and suggestions for improving the SSAI, provided in section 1, will also be taken into account.

In the last few years Sigma has indicated that HSC's **core audit processes** were well functioning in its present stage of development and that suitable **support processes** for current operations had been developed, considering the resources at its disposal. During 2007 the HSC further developed its audit processes and support processes, with the assistance of the two twinning partners.

Although the legal framework to a great extent complies with INTOSAI standards, the current approach to statutory audits does not focus yet on certifying financial statements but rather concentrates on structural deficiencies in government operations, and mainly on detecting violations of laws. In 2007 the HSC carried out 146 audits and in these audits it found irregularities amounting to the equivalent of 2% of the annual state budget, i.e. 6 billion LEK. Of this amount, 2.4 billion LEK could be recovered. For the recovery of these sums the HSC undertakes follow-up audits each year in the period December/January (in 2007 these audits numbered 100, out of the total of 146 audits).

Performance audit is rather new for the HSC and is in its early days. IT audit is underdeveloped.

The twinning project pays special attention to improving the audit methodology and audit practices.

Under the component "Institutional Reform", a framework for audit planning has been developed. This framework defines criteria for using HSC's scarce resources and assists the HSC management in prioritising audit activities. The Annual Plan 2008 is based on this framework.

In addition, a tool for planning resources of individual audits has been developed. The drafting of a specific IT strategy is planned under this component as well, but has not yet been completed. Streamlining the planning processes of audits (annual and individual) is certainly a step forward in HSC's attempts to improve the efficiency of its operations. The real effects of using these tools will become more visible, however, when they are used in connection with the (revised) strategic objectives of the HSC.

The component "Audit Practices" focuses on training in financial audit and performance audit. The bases for these audits are the audit manuals, which were developed under a former twinning project. In 2007 two pilots of financial audits were carried out and four pilots will be undertaken in 2008. These audits follow the audit process for certifying financial statements according to INTOSAI standards. The pilots of performance audits required more intensive training support. The four pilots of performance audits are nevertheless on track. It should be noted that a full understanding of financial audit is needed to be able to carry out performance audit.

IT audit is not a part of the twinning project. Training in this type of audit will certainly be needed in the coming years.

Audit software has been acquired and some HSC staff have been trained, but the use of this software is still poor. In the pilot audits the IDEA tool is used.

In the fight against fraud and corruption the HSC monitors the government's activities but does not carry out specific audits. However, the twinning project foresees the organisation of training in integrity audit. During regular audits in 2007, a total of 29 uncovered cases of violation of laws was reported to the Prosecutor's Office; 6 of these cases were brought to court and 18 are still being prosecuted.

Quality control concentrates mainly on the legal aspects of the findings of the auditors (and on the use of auditing standards). Audit reports are first scrutinised at directorate level by a lawyer and subsequently by the Law, Quality Control and Audit Methodology Department on a central level; the General Director of IA reviews all reports before they are submitted to the HSC chairman. Quality control in individual audits is also part of the twinning project.

The relations of the HSC with the General Directorate of Internal Audit (IA) in the Ministry of Finance are strained. Both institutions concentrate on detecting violations of laws and seem to be competitors rather than allies in their attempts to help improve the government's operations.

Current working relations are formal and concentrate only on the exchange of planning documents.

The HSC assesses the activities of the IA and reports annually on the activities and quality of the IA in its annual activity report.

The current SSAI Act declares that the HSC audit standards are compulsory for the government's internal audit bodies. This is not in line with international standards and is in contradiction with the new draft Internal Audit Law, which gives to the Minister of Finance the authority to issue internal audit standards (article 6 of the draft Law on Internal Audit in the Public Sector). The HSC intends to revise this provision together with the other SSAI Act amendments.

The impact of HSC audit work is increasing. Every year the chairman of the HSC presents to the National Assembly two reports: an activity report in May and a report on the budget execution in October. The report on the budget execution includes violations of laws (including tax violations). After the Prime Minister issued a decree to ministers that HSC recommendations should be given follow-up, the rate of implementation of recommendations by the government increased from 48% in 2004 to 72% in 2005, 74% in 2006 and 77% in 2007. The HSC recommendations more and more often concern structural measures, although disciplinary measures for violations still constitute the main part of the HSC's reporting to the National Assembly.

Public awareness of the role and task of the HSC is growing. According to the chairman of the Standing Committee on Economy and Finance of the National Assembly, the quality of HSC products is improving. Compared with the reports of a few years ago, current HSC reports contain more information (for parliament) on important issues and on how public funds are used, focus more on performance, and show the relation between the HSC and the Prosecutor's Office. The Standing Committee also sees room for improvement: findings should be better presented, more attention should be paid to legislative issues and less to descriptions of the executive's functioning, and the contacts between the HSC and the Standing Committee should be intensified.

The Standing Committee evaluates the performance of the HSC every year and drafts a resolution which includes recommendations to the HSC. This resolution is based on the action plan of the HSC, presented in its annual report.

Article 3 of the SSAI Act refers to the audit of the accounts of the HSC by an independent body appointed by and reporting to the National Assembly. The HSC accounts have not been audited since 2002. The chairman of the Standing Committee acknowledged that from the point of view of transparency, it is recommended to carry out this audit annually. During the discussions in March 2008 on the HSC's 2007 report, this issue was raised, and the Standing Committee decided that as from 2008 the accounts and performance of the HSC should be audited by an external audit institution. This intention is laid down in the Standing Committee's resolution on the annual report 2007 of the HSC.

Regarding the *support processes*, the HSC – together with the twinning partner – has further developed its HRM system. A staff appraisal system has been introduced, and a training needs assessment framework has been set up. Improved prestige of the institution in the last few years has also been reflected in the staffing

situation, which has shown stability and a low turnover. The year 2007, however, was a turning point. Auditors have been leaving the HSC for better paid jobs, such as those offered by the recently established Anti-Corruption Committee. HSC salaries are not higher than those of comparable jobs in the public sector, as is usually the case in other countries, as the HSC salary scheme follows the civil servant salary scheme. IT audit capacity is not present and will be badly needed in the coming years.

5. Recommendations

In addition to the activities being carried out under the current twinning project, it is recommended that the HSC address the following issues:

- When revising the current SSAI Act, the remarks included in section 1 above (“Legal Framework”) should be taken into consideration and the new Organic Budget Law analysed carefully with regard to the implicit requirements for the HSC.
- Highest priority should be given to drafting a new strategy 2009-2011. The development of this strategy is key to the reform and should focus on further elaboration and implementation of a financial attestation audit process, audit of financial management systems (the core process in accordance with internationally accepted audit standards and guidelines), and performance and IT audit. At the same time, current developments in the budget process and in public internal financial control (including internal audit) must be taken into account. The strategy should also pay special attention to the further development of management and administrative processes affecting general management, human resources management, and external relations, and to the reassessment of the role and organisation of the local offices of the HSC.
- Although reform activities should be more and more initiated and brought forward by the HSC itself, technical assistance might be needed for further strengthening of the financial and performance audit capacity.

With the above in mind, it is further recommended to the HSC to:

- Draft, adopt and start to implement key substantive and support policies in the following areas:
 - contribution of the HSC to the fight against fraud and corruption in the public sector;
 - auditing of EU-funded projects in order to prepare the HSC for the future task of auditing EU funds;
 - elaboration of an IT strategy covering both the computerisation of the management of the HSC in the new building and a better use of available IT software in audit activities;
- Introduce management training in audit and HRM-related issues, such as quality control, staff appraisal, teamwork and coaching;
- Broaden the current quality control methodology by means of a wide range of activities (awareness training, pilot audits, additional guidelines, etc.);
- Foster a climate of trust and mutual assistance in HSC co-operation with other audit bodies and with the administration, in particular with the General Directorate of Internal Audit of the Ministry of Finance;
- Actively seek opportunities for intensifying contacts with the National Assembly and with the government in order to strengthen HSC relations with both bodies in terms of reporting and follow-up of actions taken on the basis of audit findings.

6. External Assistance

Other than the above-mentioned twinning activities, no external assistance is foreseen. However, as recommended above, further training in financial and performance auditing seems to be necessary. The current audit approach is not fully in line with INTOSAI standards for financial audit and performance audit and under the current twinning project only a small number of people have been trained in pilot audits.

The HSC participates in technical activities organised by the network of Presidents of candidate country and potential candidate country SAIs in co-operation with the European Court of Auditors and Sigma, and is

involved in various training activities supported by EUROSAI and INTOSAI, in particular the International Development Initiative (IDI) of this organisation.

In November 2006 the HSC signed a co-operation agreement with the Account Chamber of the Russian Federation, but there are also co-operation agreements with the SAIs of Denmark, Hungary and Poland, and it intends to sign similar agreements with France and the Netherlands in 2008.

The HSC has further plans to co-operate with neighbouring countries in “joint” audits.