



# Guidance on how to use PEFA for fiduciary assurance

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**PEFA Secretariat**

1818 H Street NW  
Washington DC 20433, USA



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# LIST OF ABBREVIATIONS AND ACRONYMS

<b>BCG</b>	Budgetary Central Government
<b>CG</b>	Central Government
<b>CSO</b>	Civil Society Organizations
<b>EBU</b>	Extra Budgetary Units
<b>IIA</b>	Institute of Internal Auditors
<b>IPSAS</b>	International Public Sector Accounting Standards
<b>ISSAI</b>	International Standards of Supreme Audit Institutions
<b>PEFA</b>	Public Expenditure and Financial Accountability
<b>PFM</b>	Public Financial Management







## PART 1: ABOUT PEFA

PEFA (Public Expenditure and Financial Accountability) is a partnership program of the European Commission, the International Monetary Fund, the World Bank, and the governments of France, Luxembourg, Norway, Slovak Republic, Switzerland, and United Kingdom.

The PEFA program provides a framework for assessing and reporting on the strengths and weaknesses of Public Financial management (PFM) using quantitative indicators to measure performance. PEFA is designed to provide a snapshot of PFM performance at specific points in time using a methodology that can be replicated in successive assessments, giving a summary of changes over time.

The PEFA framework provides an overview of the PFM system and evidence-based measurement against 31 performance indicators and 94 dimensions. It also provides an assessment of the implications for overall system performance and desirable PFM outcomes. It provides a foundation for planning reform, discussing strategy and priorities, and monitoring progress.

PEFA is a tool that helps governments to achieve sustainable improvements in PFM practices by providing a means to measure and monitor performance against a set of indicators across the range of important PFM institutions, systems, and processes. In addition to governments, other users of PEFA include civil society organizations and international development partner institutions. PEFA scores and reports allow users to gain a quick overview of the strengths and weaknesses of a country's PFM system. Users also see the implications of the overall performance results for the key goals of fiscal discipline, strategic resource allocation, and efficient service delivery. The PEFA analysis thereby contributes to dialogue on the need and priorities for improving PFM.

The PEFA methodology draws on international standards and good practices on crucial aspects of PFM, as identified by experienced practitioners. PEFA incorporates a PFM performance report for the subject government that presents evidence-based indicator scores and analyzes the results based on existing evidence. It emphasizes a country-led approach to improve performance and align stakeholders around common goals.

In addition to guidance for analysis and reporting, the PEFA program provides support, monitoring, and analysis of PEFA assessments.

For more information on PEFA, visit the PEFA website, [www.pefa.org](http://www.pefa.org).



## PART 2: ABOUT THE GUIDANCE

### 2.1. Background

The goals of the PEFA Program are to strengthen capacities to assess the status of country PFM systems and develop a practical sequence of reform and capacity development actions, in a manner that (i) encourages country ownership, (ii) reduces the transaction costs to countries, (iii) enhances donor harmonization, (iv) allows monitoring of progress of country PFM performance over time, (v) better addresses developmental and fiduciary concerns, and (vi) leads to improved impact of reform. Contribution to the assessment of fiduciary risk has been one of the main goals of the program since its creation.

International development partner institutions, that we will call in this guidance development agencies, need to ensure appropriate use of the resources that they provide for development projects. For that purpose, development agencies have specific operational requirements, that consider the existing elements of partner government's financial management systems to support and strengthen existing systems to maximize capacity building and development impact. For doing such assessment the development institutions have in place different methodologies aligned with the institutional consideration of fiduciary risk<sup>1</sup> and identification of mitigation measures that may include identification of actions for strengthening such systems and institutions.

The approach for assessing government's financial management systems very often use PEFA assessments as input for the fiduciary work with variations in different aspects as:

- the level of reliance on country PFM systems,
- the extent of the PEFA performance indicators they consider in their assessment: the whole range or a selection,
- how they prioritize, within the selected ranges, some PEFA indicators as seen as more critical than others,
- the extent to which they use the PEFA scores: keeping them or aggregating them in specific combined scores for fiduciary areas,
- the way they connect the PEFA scores to the level of fiduciary risk,
- the inputs they use in addition to PEFA, for areas not covered by the PEFA framework (e.g.: corruption) or digging into some fiduciary area (e.g.: procurement, external audit).

### 2.2. Purpose

This guidance is not a methodology in itself, it aims to enhance the use of PEFA reports for fiduciary considerations on country systems. As it follows the standard PEFA methodology, its focus is on central government (CG), with deeper emphasis on the Budgetary Central Government (BCG). The guidance focuses on the elements of information in the PEFA report to consider in country systems from a fiduciary standpoint. It does not draw conclusions or prescribe mitigating measures in relation with the elements assessed.

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<sup>1</sup> Fiduciary Risk understood as the risk of the resources not used with economy and efficiency for intended purposes.

The present document does not aim at substituting the fiduciary methodologies developed by the development agencies. Its intent is to help the fiduciary works by providing a guidance on how to use the PEFA reports as an input. It includes a correspondence table between fiduciary risk areas, and PEFA dimensions, and an analysis of the extent to which the PEFA dimensions can contribute to the fiduciary assessment. The use of PEFA for Fiduciary consideration has the advantage of being based on an established methodology used by development partners that could promote and support the donor harmonization agenda. As different institutions may have different risk appetites, they may conclude differently with the same information.

This guidance is based on the seven key fiduciary key areas of the PFM cycle: (i) budgeting, (ii) flow of funds, (iii) internal controls, (iv) procurement, (v) accounting, (vi) financial reporting, and (vii) auditing. Each fiduciary area is broken down in critical PFM processes identified as fiduciary processes, which are linked to corresponding PEFA dimensions. Those fiduciary processes that are not covered by PEFA are not included in this guidance. The guidance is prepared with focus on using the PEFA reports as source of information. However, in case of an ongoing assessment which will be used also for fiduciary assessment consideration, the guidance provides complementary questions in the different dimensions. These questions could help gather more specific information. This information is not necessarily included in a PEFA report but could be included as part of the underlying causes of performance or for clarification.

Most of the processes identified correspond perfectly to a PEFA indicator: all the dimensions identified are useful for fiduciary assessments, and no dimension from another indicator is needed. Correspondence is partial for some other processes:

- either they rely on dimensions belonging to different indicators,
- or part of the dimensions of an indicator are useful to assess the fiduciary risk.

In the third section, Fiduciary area and PEFA dimensions, the guidance provides a short description of the seven fiduciary areas, and all the critical processes. For each process, the corresponding PEFA dimensions are briefly described, highlighting what can be found in the narrative, and what is the specific meaning of a D score, which corresponds to a level of performance below the basics. The coverage of the PEFA indicators and dimensions is explained as those vary among the different processes, being the Budgetary Central Government (BCG) the principal focus but, with also reference to Central Government (CG), Extra Budgetary Units (EBU) and Public Corporations (PC).

In addition, for each fiduciary process a list of additional questions is provided. These questions can be used during the PEFA assessment if one of its purposes is to provide information for a fiduciary assessment. The information and questions to be collected could be also complemented by other more specific analytical tools (for example MAPS in procurement, IA-CM in internal audit, SAI PMF in external audit) that would depend on the availability of those reports.

In the Annex, the guidance provides a table for recording the main observations related to the fiduciary risks that can be found in the related PEFA dimensions. The second column is for recording the score of the dimension. It is not considered to provide a score at the level of the fiduciary process.

# PART 3:

## FIDUCIARY AREAS AND PEFA DIMENSIONS



### Fiduciary area 1 - Budgeting

#### 1.1 - Reliability of the budget

Budget reliability is affected by deviations of the total expenditure compared to originally approved budget, and variations between the main aggregates of the budget.

This area is captured by 4 dimensions, covering BCG, pertaining to three different indicators:

- **PI-1.1.** Aggregate expenditure outturn, which gives the magnitude of the deviation of the expenditure outturn with the originally approved budget for the last three completed fiscal years. The score is given by comparing the best two deviation rates out of the three years with the PEFA defined range.
- **PI-2.1.** Expenditure composition outturn by function, which gives the magnitude of the variation between the allocation of actual expenditure between main functions, programs, or administrative heads and what was approved in the budget, for the last three completed fiscal years. The score is given by comparing the best two deviation rates out of the three years with the PEFA defined range.
- **PI-2.2.** Expenditure composition outturn by economic type, which also gives the magnitude of the variation, but for the main heads of the economic classification.
- **PI-21.4.** Significance of in-year budget adjustments measures the frequency and transparency of significant in-year budget adjustments.

#### *Complementary questions:*

1. Is there any indication of issues related to overall budget allocation and execution?
2. Is there any indication of an underlying cause that may produce the reallocation?

## 1.2 - Consistency of the budget classification

A budget classification aligned to international standards ensures that budget information is consistent and enables to track expenditure all along the budget cycle.

This area is captured by indicator PI-4. Budget classification, based on BCG, which assesses the:

- comprehensiveness of the classification: existence of different categories of classification – economic, functional, administrative, programmatic,
- level of detail: number of digits
- alignment to international standards: COFOG for the functional classification, GFS for the economic classification

### *Complementary questions:*

1. Does the budget classification allow to track the program expenditures and distinguish between categories?
2. Can the budget classification be used for reporting program/ project/activities categories?
3. Can the budget clearly segregate between source of funds?

## 1.3 - Compliance of the budget preparation process

An orderly budget process ensures that adequate time and information on procedures and assumptions are provided to allow budget proposals to be developed taking into account all important factors. If there is insufficient information in advance of preparing budget proposals, or inadequate time to produce fully considered submissions, the chances of weak and ill-considered proposals increase.

This area is captured by indicator PI-17. Budget preparation process, and its three dimensions, which cover BCG:

- **PI-17.1.** Budget calendar, which assesses the existence of a budget calendar, the level of compliance with it, and that budgetary units have enough time to complete their estimates. A D score means either that there is no budget calendar, or that the budget calendar steps and deadlines are not complied with.
- **PI-17.2.** Guidance on budget preparation, which gives information on the clarity and comprehensiveness of the budget circular, and the setting of expenditure ceilings. A D score means either that circulars are not issued, or do not contain expenditure ceilings, or do not cover the whole year, or that ceilings are not approved by the cabinet.
- **PI-17.3.** Budget submission to the legislature, which gives an indication on the time available to the legislature for ensuring a proper scrutiny of the budget before the fiscal year starts. A D score means, that the legislature has received the budget proposal less than a month before the start of the year, for at least two out of the last three completed fiscal years.

### *Complementary questions:*

1. Is there any indication of non-compliance in the budget calendar?
2. Are the deadlines respected? If not, is it justified?
3. Is there any issue regarding the budget guidelines affecting the budget process?
4. Have the budgets been approved before the start of the fiscal year?

## 1.4- Scrutiny of the budget process

The government's authority to spend is awarded by the legislature, through its passage of the annual budget law. If the legislature does not rigorously examine and debate the law, its power is not being effectively exercised, and the government's accountability to the electorate is undermined.

This area is captured by indicator PI-18. Budget preparation process, and its four dimensions, which cover BCG:

- **PI-18.1.** Scope of budget scrutiny, which gives an indication of the comprehensiveness of the scrutiny of the budget conducted by the legislature. A D score means that the legislature's review has been insufficient because it has not even covered the details of expenditure and revenue. In this case, the legislature does not assume its scrutiny role, not balancing the power of the executive.
- **PI-18.2.** Legislative procedures for budget scrutiny, which assesses the extent to which the scrutiny of the budget is supported by established rules, such as specialized committees, technical support, negotiation procedures, arrangements for public consultation. A D score means that either there are no specific procedures approved in advance of the scrutiny, or they are not adhered to. In both, the capacity of the legislature to undertake a proper scrutiny of the budget proposal is weakened.
- **PI-18.3.** Timing of budget approval, which ensures that the budget is approved before the start of the year, or not too late after the start of the year. A D score means that the budget has been approved more than one year after the start of the year for two or more of the last three completed fiscal years. It increases the risk that expenditures occur whereas they have not been budgeted.
- **PI-18.4.** Rules for budget adjustments by the executive, which assesses the existence of rules limiting in-year budget adjustments by the executive. Both the nature of adjustments and the magnitude of reallocation must be limited. A D score means that either there are no rules, or they are not adhered to. Such lack of rules poses the risk for both the budget reliability, and the budget execution control process.

### *Complementary questions:*

1. Are there any weakness identified that affects the budget process?
2. What were the significant adjustments which were made to the budget by the executive during the year?



## Fiduciary area 2 - Flow of funds

### 2.1 - Resource allocation

Efficient resource allocation requires that the government has the most current information on and is able to forecast the cash availability during the year, and that the budgetary units are provided with reliable information on their cash commitments.

This area is captured by three dimensions of PI-21, which cover BCG:

- **PI-21.1.** Consolidation of cash balances, which informs on the frequency and extent of the consolidation of cash balances. A D score indicates a situation where either the cash balances are not consolidated, or consolidated less frequently than monthly, or the consolidation covers less than 75% of the cash balances. In either case, it corresponds to a situation where the government does not have available enough information on its cash availability, which could lead to perturbations in the execution of the budget and use of useless liquidity facilities. In addition, it means that some cash balances might be out of the oversight of the treasury, which raises the risk of misuses. The existence of a treasury single account generally helps to increase the performance of this dimension. However, there might also be frequent and comprehensive consolidation in countries which have not implemented a TSA, and the existence of a TSA does not prevent from the existence of side accounts.
- **PI-21.2.** Cash forecasting and monitoring, which informs on the ability of the government to forecast the evolutions of the cash availability, which requires to anticipate the inflows and outflow during the year. The dimension does not require that the forecast is accurate, but only that it is updated based on actual inflows and outflows, for a B and an A score. A D score corresponds to a situation where a cash flow forecast is not prepared for the year, which makes difficult the planning of the commitments, and thus the execution of the budget as planned.
- **PI-21.3.** Information on commitment ceilings, which assesses the reliability of in-year information available to budgetary units on ceilings for expenditure commitment for specific periods. A D score means that either budgetary units do not receive information on their commitment ceilings, or the information is not reliable, or covers a less than a month horizon. In any case, a weakness in this dimension is likely to hamper the execution of the budget. Predictability for budgetary units as to the availability of funds for commitment is necessary to facilitate planning of activities and procurement of inputs for effective service delivery and to avoid disruption of the implementation of these plans once they are under way. It shows a risk on the capacity of the government to deliver on its programs.

#### *Complementary questions:*

1. Is there any problem with the management of Treasury accounts during the last two years?
2. Are any issues identified on the cash forecast that could affect budget execution?
3. Is there any issue that could affect cash plan or execution?
4. Is the timing of information adequate for cash planning?

## 2.2 - Funding of service delivery units

Problems frequently arise in front-line service delivery units providing services at the community level in obtaining resources that were intended for their use, whether in terms of cash transfers, distribution of materials in kind or provision of centrally recruited and paid personnel. Information about the receipt of resources by service units is often lacking.

This area is captured by one dimension of indicator PI-8, which covers CG:

- **PI-8.3.** Resources received by service delivery units, which measures the extent to which information is available on the level of resources actually received by service delivery units of at least two large ministries (such as schools and primary health clinics) and the sources of those funds. A D score means that there has not been any information on the resources received by the service delivery units of any large ministry for the last three completed fiscal years, even through a survey. It means that there is no oversight of the resources of service delivery units, which could lead to unidentified shortage of resources or inappropriate allocation between services, weakening the delivery of the services, and implementation of policies. It could also mean that collection of some resources, like fees or other users' payments is not tracked, which could lead to misuses. The dimension covers CG, including the services managed and funded by other tiers of government if the CG significantly finances such services.

### *Complementary questions:*

1. What system used to produce information on service delivery resource allocation?
2. Is there any other digital system used for gathering information about service delivery unit resources (e.g., webservice, social media)?
3. Has there been any recent survey on service delivery allocation?
4. Are the payments from the TSA allocated and programed in an automatized way for the service units?

## 2.3 - Expenditure arrears

Arrears are at the same time a PFM issue, and a symptom of structural weakness of the PFM system. On one hand, they can have a significant impact on fiscal discipline because they constitute a failure in controlling commitments and making payments when obligations are due. If arrears are allowed to occur and grow, they can place a burden on future budgets to meet the unauthorized or excessive obligations of the past. On the other hand, arrears can also indicate an unintended expansion of expenditures that could distort the allocation of resources. They can be an indication that more resources are needed to achieve the service levels expected, levels that cannot be attained without incurring unauthorized additional expenditures. Arrears can also be an indication that cash is not being provided to meet obligations when needed, implying that cash allocation arrangements are not fully effective.

This area is captured by the two dimensions of indicator PI-22, which covers BCG:

- **PI-22.1.** Stock of expenditure arrears, which assesses the extent to which there is a stock of arrears, and its magnitude. A D score means that the stock of expenditure arrears is deemed significant, i.e., more than 10% of total expenditure in at least two of the last three completed fiscal years. In a number of PEFA reports, it also might mean that there is not



enough information on the stock of arrears to ascertain its magnitude. A high level of arrears can indicate a number of different problems such as inadequate commitment controls, cash rationing, inadequate budgeting for contracts, under-budgeting of specific items and lack of information.

- **PI-22.2.** Expenditure arrears monitoring, which assesses the extent to which any expenditure arrears are identified and monitored. It focuses on which aspects of arrears are monitored and how frequently and quickly the information is generated. A D score means that either there is no information on the stock and/or the composition of arrears, or it's produced less regularly than yearly. In some instances, payment rules, like ex-ante controls of the commitments, make impossible the production of arrears. However, generally, by not monitoring their arrears, the governments are less likely to control their evolution. It can lead to the shortage of cash for the execution of the annual budget, due to its use for covering previous years' arrears.

### *Complementary questions:*

1. Is the level of arrears significant?<sup>2</sup>
2. Was there any underlying cause identified?
3. Is there any indication on composition of arrears by responsible entity and type of arrears, such as arrears for goods and services, salary payments, pension payments or others?

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<sup>2</sup> According to the PEFA Framework, stock of arrears is considered significant when it represents more than 10% of annual expenditure.



## Fiduciary area 3 - Internal controls

### 3.1 - Control of payrolls

Salary expenditure are usually among the biggest items of government expenditure and susceptible to weak control and corruption.

This area is captured by three of the four dimensions of the indicator PI-23. Payroll controls. They all cover central government, i.e., budgetary and extrabudgetary units (EBUs) of the government:

- **PI-23.1.** Integration of payroll and personnel records, which assesses the degree of integration between personnel, payroll, and budget data. A D score means that there is no direct linkage between the systems, and either no reconciliation more frequently than six months, and/or there is no check of hiring and promotion against the approved budget. Insufficient linkage of personnel and payroll systems not mitigated by regular reconciliation between the two systems increases the risk of error and fraud. It is particularly the case when hiring and promotion can be done without reference to budget approval.
- **PI-23.2.** Management of payroll changes, which measures the frequency of the updates of the payroll and personnel data, and the magnitude of retroactive adjustments. A D score means that update of information is less than quarterly and/or is so inefficient that it requires significant adjustments (more than 25% of the salary expenditure). The lack of regular update means that risk of payroll error is high, and the percentage of adjustments informs on the magnitude of these errors.
- **PI-23.3.** Internal control of payroll, which assesses that the integrity of payroll data is guaranteed by an adequate system of control. A D score means that the system of controls is insufficient to ensure the integrity of the payroll data. In such a situation, the risk of unjustified changes to payroll data is high.

#### *Complementary questions:*

1. Are there any significant deficiencies in payroll process control identified?
2. If yes, is there any underlying cause identified?
3. Is an audit trail in the changes?
4. Are there automatized audits to detect fraud or overpayments?

## 3.2 - Control of other expenditures

Internal controls provide assurance that transactions are performed as intended and resources are used only where appropriate authority has been verified. This process ensures that fiscal discipline is maintained at the micro- as well as the macro-level. It also ensures that resources are allocated as intended and properly authorized and that service delivery has access to and uses the resources provided under legal and regulatory authority and are used only for those purposes.

This area is captured by the three dimensions of indicator PI-25. Internal controls on nonsalary expenditure, which dimensions, all cover central government:

- **PI-25.1.** Segregation of duties, which assesses how the duties are segregated in the expenditure chain. The dimension assesses the appropriateness of the segregation of duties only for an A score. A D score means that duties are not segregated in the chain of expenditure and/or that there is no definition of the main responsibilities. Absence of segregation of duties, or inadequate segregation of duty poses the risk does not prevent an employee or group of employees from being in a position both to perpetrate and to conceal errors or fraud in the normal course of their duties.
- **PI-25.2.** Effectiveness of expenditure commitment controls, which ensures that through an adequate system of controls, the government's payment obligations remain within the limits of annual budget allocations and within projected cash availability. A D score means that either there is no control of commitment, or its coverage is insufficient, or the system is not efficient. The system of control must cover cash availability and approved budget allocations for a B and an A scores.
- **PI-25.3.** Compliance with payment rules and procedures measures the magnitude of the compliance with the regular payment procedure and the extent to which exceptions to the regular procedures are authorized and justified. A D score means that less than 50% of payments (in value) are compliant with the regular procedures, and/or less than 50% of the exception (in value) are properly authorized and justified. Hence, this dimension gives a direct evaluation of the risk by providing the percentage of payments that are not properly authorized and justified.

### *Complementary questions:*

1. Is the report identifying any significant incompatibility in the duty assignment?
2. Has there been any issue related to duty assignment regarding segregation of responsibilities?
3. What type of PFM system is being described as used for payments? Does it have authorization officers?
4. Has this system been assessed through international standards (e.g., COSO ERM, COBIT, ITIL 4)?
5. Are different systems of commitment controls being used in different agencies?
6. Is the information disaggregated by Budgetary Units and extrabudgetary units?
7. Do those commitment controls systems work similarly?
8. Is there an information system on internal control performance?
9. Are internal control reports available informing on internal control performance?
10. Do external audit reports, and internal audit reports identify significant internal control deficiencies?

### 3.3 - Investment monitoring

Investments are a large part of public expenditure. Characteristics of the investment projects that are factors of risks: financial significance, complexity of the contracts, number of contractors, involvement of different parts of the governments, potential remoteness of the projects, etc. Hence, a well-structured monitoring of financial and physical advancement of investment project is crucial.

This area is captured by one dimension of PI-11. Public investment management, which covers CG:

- **PI-11.4.** Investment project monitoring assesses the extent to which prudent project monitoring and reporting arrangements are in place to ensure value for money and fiduciary integrity. The dimension could provide information on the existence of standard procedures for monitoring and reporting on the advancement of major investment projects, and the level of compliance with them. A D score could mean several situations: lack of financial monitoring, lack of physical advancement monitoring, absence of preparation of annual information on advancement. Existence of standard procedure is required for a B score, and compliance with it for an A score. This dimension covers Central Government, and focuses on the major investment projects, which are defined as those of which the total capital cost exceeds 1% of annual expenditure. It means that the dimension is not supposed to cover all the investment projects of the government, but a limited number of them.

#### *Complementary questions:*

1. Is the level of compliance disclosed?
2. Does the report mention any issue of compliance with standards and regulations?
3. Does the country system utilize digital technologies to track public investment?

### 3.4 - Control of nonfinancial assets

The effective management of assets ensures that resources owned and controlled by government are used efficiently and effectively in the implementation of policy objectives. If governments do not have sufficient knowledge of the existence and application of assets, it is possible that the assets are not being used effectively and may not be properly applied. Adequate control over assets is an important part of the government fiduciary responsibility and it should be in place a system of adequate safeguards to protect assets from fraud, waste, and abuse of the entrusted assets to the public sector. Adequate control includes also control, information and transparency of transfers and disposal of financial and non-financial asset.

This area is captured by two dimensions of PI-12. Public asset management that covers BCG for nonfinancial assets and CG for financial assets:

- **PI-12.2.** Nonfinancial asset monitoring, which assesses the features of nonfinancial asset monitoring, through the maintenance of a register. A D Score indicates that there is no register, or it does not record information on usage and/ or age of the nonfinancial assets. It may also mean that the registers are not considered to be complete and current for all material assets. This dimension covers BCG.

- **PI-12.3.** Transparency of asset disposal, which assesses that procedures for transfer, including transfer of usage, and disposal of assets are established, and information is provided on transfer and disposal operations. A D score means that there is no established procedure, and/or that information on the original purchase cost and disposal value is not produced. Level of compliance with the established procedure is not assessed by the dimension.

*Complementary questions:*

1. Is the information of disposal included in government financial reports?
2. Are the guidelines on disposal of assets complied with?
3. Is there any internal audit or external audit documentation on the process compliance and efficiency?

## 3.5 - Control of debt

The size and management of debt and guarantee obligations can have a substantial impact on a country's capacity to maintain fiscal discipline. Effective management is necessary to ensure that the cost of such obligations is minimized in the long term and that the country has the capacity to meet all obligations when they are due. Governments that fail to monitor the financial liabilities that arise from domestic, foreign, and guaranteed debt or from payment arrears, including salaries, may create unnecessarily high debt service costs and are unlikely to be able to deliver planned services.

This area is captured by one dimension of PI-13. Debt management, which covers CG:

- **PI-13.1** Recording and reporting of debt and guarantees, which assesses whether there is a system in place to monitor and report regularly on the main features of the debt portfolio. It is critical for ensuring data integrity and effective management, such as accurate debt service budgeting, making timely debt service payments, and ensuring well-planned debt rollovers. A D score means that records on debt are not updated nor reconciled on a yearly basis.

*Complementary questions:*

1. Does the report identify compliance issues?
2. If any, are underlying causes identified?
3. Is there any issue regarding the accuracy of information on government reports?

## 3.6 - Internal audit

Regular and adequate feedback to management is required on the performance of the internal control systems, through an internal audit function (or equivalent systems monitoring function). Such a function should use a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes. In the public sector, the function is primarily focused on assuring the adequacy and effectiveness of internal controls: the reliability and integrity of financial and operational information; the effectiveness and efficiency of operations and programs; the safeguarding of assets; and compliance with laws, regulations, and contracts.

Effectiveness of risk management, control, and governance processes should be evaluated by following professional standards such as the International Standards for the Professional Practice of Internal Auditing, issued by the Institute of Internal Auditors (IIA). These include: (a) appropriate structure particularly with regard to organizational independence; (b) sufficient breadth of mandate, access to information; and power to report; and (c) use of professional audit methods, including risk assessment techniques. Internal audit provides assurance that systems are operating to achieve government objectives efficiently and effectively. It leads to timely recommendations to management regarding corrective action necessary when weaknesses are identified.

This area is captured by the four dimensions of indicator PI-26. Internal audit, which covers CG:

- **PI-26.1.** Coverage of internal audit, which measures the coverage of CG entities covered by an operational internal audit. The measurement is based on the percentage of revenue collected and expenditure spent by the entities. Coverage does not mean that an internal audit has been performed for a certain percentage of expenditure, but that internal audit is operational for entities representing a certain percentage of expenditure (and revenue). Operability is assessed by referring to a set of typical features. A D score means that operational internal audit covers CG entities representing less than 50% of expenditure, and/or less than 50% of revenue.
- **PI-26.2.** Nature of audits and standards applied, which assesses whether internal audits rely on professional standards, and are primarily focused on financial compliance or also cover internal controls. A D score means that internal audits could not even qualify as financial compliance audits. Audit of effectiveness of internal control systems corresponds to a B score.
- **PI-26.3.** Implementation of internal audits and reporting, which assesses the existence of an audit plan and measures its completion. Completion is defined by the fact that the report is distributed to the appropriate parties. Hence, the requirements of this dimension inform about the actual activity of the internal audit system, in complement to the first dimension which informs on the existence of the units. A D score means either that an audit plan did not exist during the last completed fiscal year, or that less than 50% of the planned audits were actually completed.
- **PI-26.4.** Response to internal audits, which assesses whether internal audit recommendations are effectively followed. The dimension informs about both the appropriateness, the timeliness, and the coverage of the management response to internal audit recommendations. A D score means that either management did not provide a response to the recommendations, or it was for less than 50% of the audited entities, or the response was less than partial, i.e. not containing actions to implement the recommendations.

### *Complementary questions:*

1. Do financial audits and compliance audits provide information on significant fiduciary deficiencies?
2. Is the completeness of audit plans against original audit plans consistent among the entities?
3. Are significant and repetitive issues and linked recommendations consistently ignored?



## Fiduciary area 4 - Procurement

### 4.1 - Procurement

Significant public spending takes place through the public procurement system. A well-functioning procurement system ensures that money is used effectively in acquiring inputs for, and achieving value for money in, the delivery of programs and services by a government. Key procurement principles include the use of transparency and competition as means to obtain fair and reasonable prices and overall value for money.

This area is captured by the four dimensions of indicator PI-24. Procurement, which covers CG:

- **PI-24.1.** Procurement monitoring, which measures the percentage of procurement for which databases or records are accurate and complete. Elements of information to be recorded are what has been procured, value of procurement, and who has been awarded contract. A D score means that the information is accurately recorded for less than 50% of procurement in value.
- **PI-24.2.** Procurement methods, which measures the percentage of procurement awarded through competitive methods. Use of competitive methods ensures value for money and limits the risk of misuse. A D score means that less than 60% of the total value of contracts was awarded through competitive methods. In several PEFA reports, this dimension is scored D\* because procurement records (previous dimension) are not complete, hence the percentage of competitive procurement cannot be calculated accurately.
- **PI-24.3.** Public access to procurement information, which reviews the level of public access to complete, reliable, and timely procurement information. Public dissemination of information on procurement processes and their outcomes are key elements of transparency. There are 6 elements of information: (i) legal and regulatory framework for procurement, (ii) government procurement plans, (iii) bidding opportunities, (iv) contract awards (purpose, contractor and value), (v) data on resolution of procurement complaints, (vi) annual procurement statistics. A D score means that less than three elements are published or that the published elements cover less than 50% of the procurement operations.
- **PI-24.4.** Procurement complaints management, which assesses the characteristics of the resolution mechanism. Scoring is based on a list of characteristics, of which independence is the most important. A D score means that the body in charge of reviewing the complaints is involved in procurement transactions or in the process leading to contract award decisions, or when it is not involved that neither of the other characteristics is fulfilled.

#### *Complementary questions:*

1. Is there a well-defined legal and regulatory procurement framework?
2. Does the procurement function adhere to the core principles of public procurement, namely: efficiency, effectiveness, economy, transparency, fairness, competition, and value for money?
3. Is the public procurement system integrated with the financial management system?



## Fiduciary area 5 - Accounting

### 5.1 - Accounting

Reliable reporting of financial information requires constant checking and verification of the recording practices of government accountants – this is an important part of internal control and a foundation for good quality information for management and for external reports. Timely and frequent reconciliation of data from different sources is fundamental for data reliability.

This area is captured by the four dimensions of indicator PI-27. Financial data integrity:

- **PI-27.1.** Bank account reconciliation, which assesses the regularity of bank reconciliation between government bank account (central or commercial) transaction data and government cash books. Such reconciliation is fundamental to the integrity of the accounting records and the financial statements. A D score means that the reconciliation covers less than 90% of the bank accounts (in value), and/or that the reconciliation is less regular than quarterly or is done more than 8 weeks after the end of the quarter. This dimension covers CG.
- **PI-27.2.** Suspense accounts, which assesses the regularity and timeliness of the reconciliation and clearance of suspense accounts. Failure to clear suspense accounts can distort financial reports and provide an opportunity for fraudulent or corrupt behaviors. A D score might mean that an annual reconciliation is not performed or performed with too important delays (more than two months after the end of the year), or that the accounts are not cleared before the end of the year. This dimension covers BCG.
- **PI-27.3.** Advance accounts, which assesses the regularity and timeliness of the reconciliation and clearance of advance accounts. Complete, accurate, reliable, and timely information is essential to support the internal controls system. A D score might mean that an annual reconciliation is not performed or performed with important delays (more than two months after the end of the year), or that accounts are not cleared regularly and timely. This dimension covers BCG.
- **PI-27.4.** Financial data integrity processes, which assess the extent to which processes support the delivery of financial information and focuses on data integrity defined as accuracy and completeness of data. This dimension is focused on the integrity of financial data only. Separate systems for other types of data may exist and be linked to or overlap with financial data systems, e.g., personnel and payroll data and procurement data. A D score means that there is no restriction and/or record of access and/or changes to financial data. An audit trail is needed only for a B and an A scores. This dimension covers BCG.

#### *Complementary questions:*

1. Are the accounts reconciliations made regularly and in proper manner?
2. Are significant differences identified in the reconciliations? Have these differences caused any issue?
3. Is there any underlying cause identified?
4. Is the internal audit checking on financial data integrity?





## Fiduciary area 6 - Reporting

### 6.1 - In-year reporting

Information on budget execution that includes revenue and expenditure data is required to facilitate performance monitoring and, where necessary, help identify actions needed to maintain or adjust planned budget outturns. Regular reporting is part of an effective monitoring and control system to ensure that budgets are executed as intended, and that deviations from plans, if any, are highlighted for consideration by decision makers adjusting budget execution to better meet objectives and achieve desired outcomes.

This area is captured by the three dimensions of indicator PI-28. In-year budget reports, which covers BCG:

- **PI-28.1.** Coverage and comparability of reports, which assesses the extent to which information is presented in in-year reports and with the same coverage, basis of accounting, and presentation as the original budget. A D score means that comparison is not possible between in-year budget reports and the original budget.
- **PI-28.2.** Timing of in-year budget reports, which assesses the frequency and timeliness of the issuance of in-year budget reports. A D score means that frequency is less than quarterly, and/or reports are issued more than 8 weeks after the end of the quarter.
- **PI-28.3.** Accuracy of in-year budget reports, which assesses the accuracy and usefulness of the information submitted in in-year budget reports, including whether expenditure for both the commitment and the payment stage is provided. A D score means that the data is not useful for the analysis of the budget and/or information is not captured at the payment stage. A C score does not mean that the data is necessarily accurate.

#### *Complementary questions:*

1. Is the internal audit checking on financial data integrity?
2. Is there any specific problem identified that prevent to have a wider coverage and in the same format as the approved ones?
3. Is there any specific problem identified that prevent financial information to be presented regularly and promptly?

## 6.2 - Reporting on fiscal risks

Central government usually has a formal oversight role in relation to units in other parts of the public sector and should be aware of, monitor, and manage at a central level any fiscal risks posed by those units. In addition, central government may be obliged, for political reasons, to assume responsibility for a financial default of other entities, such as the banking sector, even when no formal oversight role or legal obligation exists, thus adequate procedures to monitor those risks at the level of the whole of the public sector should be in place. Such risks can undermine fiscal discipline.

This area is captured by the three dimensions of indicator PI-10. Fiscal risk reporting, which covers CG. The three dimensions can provide relevant information for operations involving public corporations, a lower tier of governments, or private sector through public private partnerships, regarding the ability of the central government to monitor the fiscal risks these entities pose:

- **PI-10.1.** Monitoring of public corporations (PC), which assesses the extent to which information on the financial performance and associated fiscal risks of the central government's public corporations is available through audited annual financial statements. A D score means that the government receives the financial reports of less than 75% of the public corporations it controls, or that the reports are received more than 9 months after the end of the year.
- **PI-10.2.** Monitoring of subnational governments, which assesses the extent to which information on financial performance, including the central government's potential exposure to fiscal risks, is available through the audited annual financial statements of subnational governments. A D score means that either less than 50% of subnational governments publish their financial reports, or they do it more than 9 months after the end of the year.
- **PI-10.3.** Contingent liabilities and other fiscal risks, which assesses the monitoring and reporting of the central government's explicit contingent liabilities from its own programs and projects. Explicit contingent liabilities include umbrella state guarantees, state insurance schemes, financial implications of ongoing litigation and court cases and public-private partnerships (PPPs). This dimension only covers the contingent liabilities that are significant according to the PEFA definition: those with a potential cost in excess of 0.5 percent of total BCG expenditure and for which an additional appropriation by the legislature would be required. When there are no such contingent liabilities, this dimension is NA. A D score means that more than 75% of the significant contingent liabilities are not quantified.

### *Complementary questions:*

1. Are PC financial reports reviewed after submission?
2. Is there any kind of internal or public report on PCs performance?
3. What is the status of PCs external audit?
4. Does the reports show any strength/ weaknesses in the reporting of contingent liabilities and/ or guarantees?

## 6.3 - Extrabudgetary operations

Ex-post financial reports available to the government should cover all budgetary and extrabudgetary activities of central government to allow a complete picture of revenue and expenditures across every category. This will be the case if expenditure of EBUs and related to extrabudgetary activities of budgetary units are insignificant or if such revenues and expenditures are included in central government ex post financial reports. A complete picture also helps ensure that resources not covered in financial reports are adequately managed in a manner consistent with government policies and procedures. It will show whether external financed projects are included in financial reports, even when they are executed by government extrabudgetary units

This area is captured by two dimensions of indicator PI-6. Central government operations outside financial reports, which both cover CG:

- **PI-6.1.** Expenditure outside financial reports, which measures the magnitude of expenditures incurred by budgetary and extrabudgetary units (including social security funds) that are not reported in the government's financial reports. Such expenditures may include expenditures on externally funded projects and activities where these are not reported in central government financial reports. A D score means that these expenditure amount to more than 10% of total BCG expenditure. In a significant number of reports, this dimension is scored D\* as the amount of unreported expenditure is unknown.
- **PI-6.3.** Financial reports of extrabudgetary units, which assessed the extent to which ex-post financial reports of extrabudgetary units are provided to central government. A D score is provided when the reports representing less than 50% of EBU expenditure are provided to CG within 9 months.

### *Complementary questions:*

1. In which detail external financed projects are included in the government financial reports?
2. Is there any other control on externally funded projects if those are not included in the government's financial reports?
3. Does the format provide sufficient detail for fiduciary purposes?
4. In which detail external financed projects are included in the government financial reports?
5. Is there any other control on extrabudgetary units with externally funded projects if those are not included in the government's financial reports?

## 6.4 - Annual reporting

Consolidated year-end financial statements are critical for transparency in the PFM system. To be complete they must be based on details for all ministries, independent departments, and deconcentrated units. In addition, the ability to prepare year-end financial statements in a timely fashion is a key indicator of how well the accounting system is operating, and the quality of records maintained. In some systems, individual ministries, departments, and deconcentrated units issue financial statements that are subsequently consolidated by the ministry of finance. In more centralized systems, all information for the statements is held by the ministry of finance.

This area is captured by the three dimensions of indicator PI-29. Annual financial reports, which cover BCG:

- **PI-29.1.** Completeness of annual financial reports, which assesses the extent to which annual financial reports are comparable to approved budgets, and include full information on revenue, expenditure, assets, liabilities, guarantees, and long-term obligations. A D score means that either there is no annual financial report, or they are not comparable with originally approved budgets, or do not include one of the basic elements of information – expenditure, revenue, cash balances.
- **PI-29.2.** Submission of reports for external audits, which assesses the timeliness of submission of reconciled year-end financial reports for external audit as a key indicator of the effectiveness of the accounting and financial reporting system. A D score means that the completed financial reports are submitted more than 9 months after the end of the year they cover.
- **PI-29.3.** Accounting standards, which assesses the extent to which annual financial reports are understandable to the intended users and contribute to accountability and transparency. For A and B scores, national standards should be aligned to international standards – IPSAS<sup>3</sup> or regional standards. A D score means that either the accounting standards are not disclosed in the annual financial reports, or the reports are not consistent over time.

### *Complementary questions:*

1. In which detail external financed projects are included in the government financial reports?
2. Is there any specific reason why some of the required statements are not included in annual financial statements?
3. What are the reasons why the financial reports are completed and submitted to the external audit with delay?
4. Is there any inconsistency in the application of accounting or reporting standards?
5. If international standards are expressed to be complied with, is there any divergence or non-compliance disclosed in the annual reports?

## 6.5 - Fiscal transparency

Fiscal transparency depends on whether information on government fiscal plans, positions, and performance is easily accessible to the general public. The range and relevance of information available to the public affects their ability to engage with government and understand how public resources are being used. It contributes directly to government's accountability.

This area is captured by indicator PI-9. Public access to fiscal information, which applies to BCG. The indicator scoring is based on a list of basic and additional elements of information. Publication of basic elements are a cornerstone for budget transparency. Among the additional elements are some that are critical for fiduciary considerations as the publication of other External Audit Reports.

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3 International Public Sector Accounting Standards



## Fiduciary area 7 - Auditing

### 7.1 - External audit

Reliable and extensive external audit is an essential requirement for ensuring accountability and creating transparency in the use of public funds. Such an audit provides assurance that information in financial reports is accurate and contains no material errors that would affect the reports' interpretation. This helps to ensure budget outcomes by giving stakeholders an accurate picture of financial results.

This area is covered by the four dimensions of indicator PI-30. External audit, which applies to CG. The three dimensions apply to the financial audit of financial reports. Other kinds of audits – compliance and performance – are not covered:

- **PI-30.1.** Audit coverage and standards, which assesses key elements of external audit in terms of the scope and coverage of audit, as well as adherence to auditing standards. A D score can come from a weakness in the coverage, the efficiency, or the compliance with standards of the external audit. Either the financial audit has covered less than 50% of the revenue and expenditure, or it has not highlighted the significant issues, or it has not relied on ISSAI or national audit standards.
- **PI-30.2.** Submission of audit reports to the legislature, which measures the timeliness of submission of the audit report(s) on budget execution to the legislature, or those charged with governance of the audited entity, as a key element in ensuring timely accountability of the executive to the legislature and the public. A D score means that the audit reports have been submitted more than 9 months after the receipt of the financial reports.
- **PI-30.3.** External audit follow-up, which assesses the extent to which effective and timely follow-up on external audit recommendations or observations is undertaken by the executive or audited entity. A D score means that no response addressing the findings and recommendations has been made by the executive.
- **PI-30.4.** Supreme Audit Institution independence, which assesses the independence of the SAI from the executive, characterized by the following criteria: the arrangements for the appointment and removal of the Head of the SAI, noninterference in the planning and implementation of the SAI's audit work, the approval and execution of the SAI budget, the unrestricted access to documents, records, and information. Independence is essential for an effective and credible system of financial accountability and should be laid down in the constitution or comparable legal framework. A D score means that either the access to the documents is restricted, or the procedure for the appointment and removal of the head or the execution of the budget are not independent.

#### *Complementary questions:*

1. Are auditing standards consistently applied to entities?
2. What are the reasons explaining that the coverage of the audit has been limited?
3. Is there any explanation of the lack of coverage of significant issues?
4. Is there any identified cause explaining why the timeline for submission of the audit reports to the legislature could not be complied with?
5. Are significant issues repeatedly identified in audit reports?
6. Why have the executive ignored audit recommendations?
7. Is the SAI sufficiently independent regarding audit planning, publication of the reports, and approval of the budgets?
8. Does the system utilize digital technologies to facilitate reporting related to misuse of public funds to SAI or other relevant control units and agencies?

## 7.2 - Legislative scrutiny of the audit

The legislature has a key role in exercising scrutiny over the execution of the budget that it approved. A common way in which this is done is through legislative committees or commissions that examines the external audit reports and questions responsible parties about the findings of the reports. A report on the results of review of the external audit reports by any mandated committee should be submitted for consideration in the full chamber of the legislature in order to constitute a completed scrutiny. This is usually necessary before the executive can formally respond, though corrective action may be taken at any time. The operation of the committees will depend on adequate financial and technical resources, and on adequate time being allocated to keep up to date on reviewing audit reports.

The area is captured by the four dimensions of indicator PI-31. Legislative scrutiny of audit reports, which covers CG:

- **PI-31.1.** Timing of audit report scrutiny, which assesses the timeliness of the legislature's scrutiny, which is a key factor in the effectiveness of the accountability function. A D score means that either the scrutiny is not performed, or it is performed in more than 12 months after the audit reports are received.
- **PI-31.2.** Hearings on audit findings, which assesses the extent to which hearings on key findings of the SAI take place. A D score means that no in-depth hearings have taken place.
- **PI-31.3.** Recommendations on audit by legislature, which the extent to which the legislature issues recommendations and follows up on their implementation. A D score means that the legislature has not issued any recommendations, nor has it formally endorsed the recommendations made by the SAI.
- **PI-31.4.** Transparency of legislative scrutiny of audit reports, which the transparency of the scrutiny function in terms of public access. A D score means that the scrutiny reports are not published.

### *Complementary questions:*

1. If the scrutiny is not performed in accordance with the PEFA requirements, is there any underlying cause identified?
2. Are there recommendations that are not followed?

## Annex

### Table summarizing the fiduciary observations

Fiduciary area	Corresponding PEFA dimension	PEFA Score	Fiduciary observations collected in the PEFA report
<b>Fiduciary area 1 - Budgeting</b>			
<b>1. Reliability of the budget</b>	PI-1. Aggregate expenditure outturn		
	PI-2.1 Expenditure composition outturn by function		
	PI-2.2 Expenditure composition outturn by economic type		
	PI-21.4 Significance of in-year budget adjustments		
<b>1-2. Consistency of the budget classification</b>	PI-4 Budget classification		
<b>1.3- Compliance of the budget preparation process</b>	PI-17.1 Budget calendar		
	PI-17.2 Guidance on budget preparation		
	PI-17.3 Budget submission to the legislature		
<b>1.4- Scrutiny of the budget process</b>	PI-18.1 Scope of budget scrutiny		
	PI-18.2 Legislative procedures for budget scrutiny		
	PI-18.3 Timing of budget approval		
	PI-18.4 Rules for budget adjustment by the executive		
<b>Fiduciary area 2 - Flow of funds</b>			
<b>2.1- Resource allocation</b>	PI-21.1 Consolidation of cash balances		
	PI-21.2 Cash forecasting and monitoring		
	PI-21.3 Information on commitment ceilings		
<b>2.2- Funding of service delivery units</b>	PI-8.3 Resources received by service delivery units		
<b>2.3- Expenditure arrears</b>	PI-22.1 Stock of expenditure arrears		
	PI-22.2 Expenditure arrears monitoring		

Fiduciary area	Corresponding PEFA dimension	PEFA Score	Fiduciary observations collected in the PEFA report
<b>Fiduciary area 3 - Internal controls</b>			
<b>3.1- Control of payroll</b>	PI-23.1 Integration of payroll and personnel records PI-23.2 Management of payroll changes PI-23.3 Internal control of payroll		
<b>3.2- Control of other expenditure</b>	PI-25.1 Segregation of duties PI-25.2 Effectiveness of expenditure commitment controls PI-25.3 Compliance with payment rules and procedures		
<b>3.3- Investment monitoring</b>	PI-11.4 Investment project monitoring Additional information		
<b>3.4- Control of nonfinancial assets</b>	PI-12.2 Nonfinancial asset monitoring PI-12.3 Transparency of asset disposal		
<b>3.5- Control of debt</b>	PI-13.1 Recording and reporting of debt and guarantees		
<b>3.6- Internal audits</b>	PI-26.1 Coverage of internal audit PI-26.2 Nature of audits and standards applied PI-26.3 Implementation of internal audits and reporting PI-26.4 Response to internal audits		
<b>Fiduciary area 4 - Procurement</b>			
<b>4.1- Procurement</b>	PI-24.1 Procurement monitoring PI-24.2 Procurement methods PI-24.3 Public access to procurement information PI-24.4 Procurement complaints management		



Fiduciary area	Corresponding PEFA dimension	PEFA Score	Fiduciary observations collected in the PEFA report
<b>Fiduciary area 5 - Accounting</b>			
<b>5.1 - Accounting</b>	PI-27.1 Bank account reconciliation		
	PI-27.2 Suspense accounts		
	PI-27.3 Advance accounts		
	PI-27.4 Financial data integrity processes		
<b>Fiduciary area 6 - Financial reporting</b>			
<b>6.1- In-year reporting</b>	PI-28.1 Coverage and comparability of reports		
	PI-28.2 Timing of in-year budget reports		
	PI-28.3 Accuracy of in-year budget reports		
<b>6.2- Reporting on risk</b>	PI-10.1 Monitoring of public corporations		
	PI-10.2 Monitoring of subnational governments		
	PI-10.3 Contingent liabilities and other fiscal risks		
<b>6.3-Extrabudgetary operations</b>	PI-6.1 Expenditure outside financial reports		
	PI-6.3 Financial reports of extrabudgetary units		
<b>6.4- Annual reporting</b>	PI-29.1 Completeness of annual financial reports		
	PI-29.2 Submission of reports for external audit		
	PI-29.3 Accounting standards		
<b>6.5- Fiscal transparency</b>	PI-9 Public access to fiscal information		

Fiduciary area	Corresponding PEFA dimension	PEFA Score	Fiduciary observations collected in the PEFA report
<b>Fiduciary area 7 - Auditing</b>			
<b>7.1- External audit</b>	PI-30.1 Audit coverage PI-30.2 Submission of audit reports to the subnational council PI-30.3 External audit follow-up PI-30.4 Independence of the supreme audit institution		
<b>7.2- Legislative scrutiny of the audits</b>	PI-31.1 Timing of audit report scrutiny PI-31.2 Hearings on audit findings PI-31.3 Recommendations on audit by the legislature PI-31.4 Transparency of legislative scrutiny of audit reports		





## PEFA Secretariat

1818 H Street NW  
Washington DC 20433, USA  
[services@pefa.org](mailto:services@pefa.org)  
[pefa.org](http://pefa.org)

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