

# NEW MODEL OF INTERNAL CONTROL IN THE EUROPEAN UNION: ITS USEFULNESS FOR THE SUPREME AUDIT INSTITUTIONS

V JORNADAS EUROSAI/OLACEFS – LISBOA 2007)

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I have a modest objective with these words, that is not other but the one of sharing with you some reflections about the new theories and guidelines on the internal audit. systems in the public sector in Europe, especially its possible influence on the audit that we develop from the Supreme Audit Institutions.

For it, and more concretely, I would like to summarize before you the new developments or tendencies on internal control promoted by the European Commission in Europe, out of them the main exponent is the document of year 2006: «Welcome to the world of PIFC», of the Budget DG of the European Commission. There is no doubt that there are positions that are originated in the system of internal control implanted in the European Commission after the reform implemented with the White Book on the Administration Reform, of year 2000, one of whose pillars were in fact the audit, the financial administration and the control.

And, in second place, I try to make some reflections about the new model that, apparently, it has promoted or it promotes the European Commission in the candidate countries (today, new States of the European Union) or applicants of membership. The reasons of this interest I think that are not hidden to anybody: belonging to the Supreme Audit Institutions, it is essential the existence of a solid system of internal control in the entity that

is audited and one of the first and main tasks that are carried out at the beginning of the audit works is in fact the analysis of the system of internal control. If the external auditor's evaluation is unfavourable, if he/she expresses a negative opinion on the system of internal control as a whole, then the conclusion is the existence of a high level of risk in the activities of the entity. It conditions the external auditor's work since the intensity of the substantive tests that are carried out will have to be necessarily high. But, mainly, the faulty state of the system of internal control will reveal the potential existence of irregularities and, even frauds, what will be worrying and it will equally affect the work of the SAI.

Therefore, the establishment of solid systems of internal control by the subjects that conform the public sector turns out to be essential for a good administration of the public funds and the surveillance that it is this way it is equally mission of the SAI.

For this reason, in the European Commission, as it is well known, since year 2000, has carried out a reform of the financial administration, the control and the audit that it has consisted basically on the decentralization in the DGs of the control activities that before were developed under the responsibility of the Controller of the Commission. In summary, it has meant to make responsible each Director General of guaranteeing a control adapted in their services, promoting the «accountability» (obligation of surrendering accounts) for the results of the administration. We could say that it is to pass from a «culture of the suspicion» to a «culture of the responsibility», where what it cares is the achievement of objectives and for this reason it is granted autonomy to the managers that should respond for the results of the administration.

For this purpose, it starts from the principles and conceptual elements coming from the COSO Report of year 1991, an adaptation of which we find in the document entitled INTOSAI 1994, « Guides for standards of internal control of the public sector», and that it is well known by all us what saves me a detailed presentation of it. I will only add that, on the basis of the five components of any system of internal control as it is COSO (control environment; planning, objectives and risks analysis; information and communication; control activities; and follow up, audit and evaluation), the European Commission has established 24 internal control standards whose execution should be self-evaluated by the public agents.

The suppression of the central previous endorsement as part of an old culture of control has been compensated –independently of the *ex ante* y *ex post* controls that each Director General may decide, under his responsibility, to implementing - with the strengthening of the internal auditor's new figure in each DG, without neither forgetting certain coordination elements developed at central level, for the whole Commission, for the Central Financial Services and Service of Internal Audit.

Right now, this new administration and control model, already in operation in a modern Administration, with resources, in summary, ready, as it is it the European Community Administration, and whose results are still to be seen, somehow has been transferred toward the countries that were candidates recently and today they are already Member States of the European Union, as well as to the future Candidate countries with those ones which the European Union, by means of the ENP, (European Neighbourhood Policy), holds relations guided to reinforce the Institutions so that they start being homologated with those ones of the European Community.

It is a model whose English acronym is «PIFC», this is, «Public Internal Financial Control» and, that as said document reads «Welcome to the World of PIFC», it seeks to represent a structured model to guide the national Governments in the establishment of an environment of advanced control that provides reasonable security of execution of the principles of good financial administration («sound financial management»), transparency, efficiency, effectiveness and economy. It is underlined that, in front of the traditional systems of internal control that places particular emphasis in the former centralized *ex post* control, in the *ex post* investigation of accusations and in the punishment of human errors, in summary, in the legality and in the regularity, the modern systems of internal control underline the approaches of economy, efficiency and effectiveness in the administration and control of the public funds and they are centred in the transparency, understood as a manifestation of the principle that the government is forced to be accountable to the citizens that have designated it to collect revenues and to manage the expenses on their behalf.

And it is in this last aspect where it is, in my opinion, the kernel of the new system denominated «PIFC». Because the three key elements, as they are described in the mentioned document, are, in the first place, the obligation of surrendering accounts and provide information («managerial accountability») of the public managers for the operative policies and for the administration and financial control policies; in second place, the existence of a functionally independent internal auditor that supports the administration evaluating the systems of internal control implemented by the DG, to which they inform directly; and, lastly, the creation of the CHU (Central Harmonisation Unit), responsible for the development and promotion of the internal control and the audit methodologies and the coordination of the installation of a new legislation on the obligation of accountability by the public managers and on internal audit.

It is not difficult to notice the likeness among the pattern proposed in the new member countries or acceding countries (a model, by the way that is not generalized in all the old member countries of the European Union) and the existent pattern in the European Commission, previously described.

However, while the document «Welcome to the World of PIFC» grants an enormous importance to the different steps that are necessary for implementation of the PIFC and, very especially, to the function and role that it should play in all this the denominated «CHU» (equivalent to the Central Financial Service of the European Commission and, also, to the Internal Audit Service), it not so relevant the importance of the obligation of accountability for the public manager as an essential pillar of the new model, but rather it is presupposed, it is considered existent or already given and on it, the new building of the internal control is built.

And here, in my opinion, is where the biggest risks in the PIFC are located. Indeed, the traditional administrative culture of the countries of the former Eastern Europe was based partly on the existence of rigid centralized controls, *ex ante* and *ex post*, in meticulous procedures that completed a function of surveillance on the public managers. Certainly, such practices could not be in agreement with the most modern techniques in the public «management» and they were based on that that before was denominated «culture of suspicion», very far from what has to be nowadays an authentic culture of the responsibility. In that sense, those control techniques were and they could be professedly improved.

But equally I think that, as Michel Crozier said, « society is not changed by ordinance» and the old agents don't become responsible managers that assume their obligation of permanent accountability before the citizens because it is said in a document that has to happen. Many times it happens, in the radical reformations that seek to be carried out that the dirty water is also thrown at the bowl, and that when we abandon what we consider the worst practices we remain, if we don't have anything else to exchange, unable to substitute that considered old, without anything to be used as a replacement. And, to take the above-mentioned issues to our side, although the controls and endorsements or *ex ante* authorizations, carried out in a centralised way and from outside the administration, they cannot be a model to be imitated, its mere suppression appealing to the need of «accountability» of the public managers, with a absolutely new and unknown instrument of internal audit in those administrative cultures (and surely also in others that are not the Anglo-Saxons ones,) as a replacement, can end up in the appearance of irregularities and frauds that, although they will finally be detected by the SAI, they will be able to cause damages difficult to compensate.

And I am going to finish: I am not at all an enemy of novelties neither, particularly of the reformation undertaken in the European Commission. I follow with interest the developments of the new profession of internal audit and I consider essential the creation and the promotion of some administrative practices so that the public agents enjoy freedom in the achievement of the objectives that are fixed for them but, at the same time, be forced to be accountable for their performance and the necessary mechanisms can be activated for the demand of the responsibilities in which they may have been able to incur.

It, however, it is only possible in societies with mature and consolidated democracies, and by means of quiet and meditated reforms and through concrete steps that open the way, substituting procedures that are no longer considered adapted by others whose results may overcome, because will be contrasted this way, the previous ones. All this, always presupposing the existence of, appropriately rewarded professional public officers and managers, with high ethical approaches of behaviour and aware of their function of public servants, legitimated before society by the results achieved in their administration.

In the fight against irregularities, fraud and corruption, the SAIs, as it highlights the final Report of the Working Group on the protection of the financial interests, designated by the Contact Committee of the Presidents of the Supreme Audit Institution (SAI) of the European Union (2003), don't have competencies or direct responsibilities, but there are indeed instruments to prevent and to detect fraud and corruption and, moreover, those SAI with jurisdictional competencies in the demand of accounting responsibilities makes an additional contribution in that fight. The promotion of good governance in the public sector and of a good and healthy administrative culture that prevents against irregular practices it is also the mission of the SAI, through the recommendations contained in the audit reports. And, as a final point, I would like to meditate about how the systems of internal control in the public Administrations can be improved without presupposing in all the occasions the existence of a culture of «accountability» of the public managers; a necessary and indispensable pillar without the one the radical and imposed by acts of will reforms can end up causing higher damages that those ones that it tried to fight. Let us prevent the risks before we detect them in the inspection of the internal control and let us contribute to the improvement of the public administration retaining those instruments of the past that suppose a control to possible irregular behaviours until we are convinced that the new

practices have possibility to take root because they do not fall in breeding ground for it and may then, be substituted the old elements by new instruments that suppose a better administration without detriment of the protection of the public funds.

Thank you.