

# Audit Manual





# Foreword

Sida has given priority to combating corruption in programmes of development cooperation. The Government's annual directives and letter of appropriations to Sida state that Sida shall take measures that have the aim of preventing corruption in contributions financed by Swedish development cooperation funds.

The Manual is intended for all members of staff at Sida who, in one way or another, come into contact with auditing.

The Audit Manual is intended to function as a reference book. For example, it provides guidance on ways in which audit reports should be dealt with, on procurements of audit services, on aspects that should be given special consideration in cases of suspicion of corruption, and on ways in which terms of reference for audits should be written. Examples of different types of terms of reference are included as appendices. The Audit Manual is also intended to provide an insight into auditing, the role of auditors, and what can be achieved with audits.

The Manual will be distributed to all members of staff at Sida, including those working at embassies and field offices.

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# Introduction

## **Why do we have audits?**

Audits are aimed at giving us confidence in information provided by an organisation/country etc. Audits should be used as a control instrument in the follow-up process.

Auditing is to critically examine, assess, and express an opinion on the accounts and administration of a company or a government agency. The concept of auditing can also include examining whether operations are being pursued effectively and fulfil the goals. The audit shall be performed independently of the client, the auditee and other stakeholders. The auditor shall be independent and qualified for the assignment, and make clear and unambiguous statements on the audit certificate.

However, auditing does not provide a guarantee that the funds have been administered in a secure manner or that the financial reports are of high quality. On the other hand, a correctly performed audit shall lead to the identification and rectification of shortcomings in the accounts and in the internal controls. It can also have a preventive effect since the attention of management is drawn to problem areas and management can thus take appropriate action to avoid errors occurring.

Auditing is one of several methods for exercising control, preventing corruption and ensuring that funds are used in the correct way. Different control steps are, for example, built into Sida's project cycle in the form of project reviews. Normally, agreements lay down that it is the partner in cooperation that has the responsibility for the audit. However, Sida retains the right to make a follow-up with the aid of audits or evaluations.

As an agency under the Government, Sida receives appropriations via the government budget. This entitles us to use government funds for the purposes of the appropriation. Sida has the responsibility for exercising controls on behalf of Swedish taxpayers for all the activities financed by Sida. However, Sida also has a responsibility towards those who benefit from development cooperation – the poor – to ensure that Sida's contributions for poverty reduction are used appropriately by those who represent the target group – Sida's partners in cooperation.

The anti-corruption regulation, which contains rules for the auditing of activities, shall be used in Sida's work throughout the entire project cycle in addition to the Sida at Work manual. Sida's work shall also be performed in a cost-effective manner. This means, among other things, that the cost of controls and audits is in reasonable proportion to their utility. Budgets and cost controls, follow-ups of financial and operations-

based reports, as well as follow-ups of measures taken to rectify faults etc are duties of central importance to enable Sida to shoulder its responsibility for controls. At the same time, an indirect purpose is to strengthen the administration of our partners in cooperation. This is, in itself, an important form of support.

### **Sida's anti-corruption regulation**

One important aim of the audit is to guard against, prevent and counteract corruption. Sida's anti-corruption regulation states that Sida should conclude agreements with partners in cooperation in respect of reports and audits, which should be made annually. However, Sida should reserve the right to have a separate audit made in cases where it considers that a separate audit is necessary. The regulation also states that companies, consultants, non-governmental organisations and other implementing organisations that receive or administer Swedish development cooperation funds via Sida's contractual partners shall be audited in accordance with the criteria of materiality and risk, and that such organisations are also responsible for ensuring that audits based on Sida's anti-corruption regulation are performed at all organisations to which they channel Sida's funds further. Special external audits shall be made in cases where mismanagement or corruption is suspected. If it is provided that mismanagement or corruption exists Sida should consider cancelling the contribution and demanding repayment of the funds involved. (See further Sida's anti-corruption regulation.)

In order to give members of staff at Sida guidance in ways in which the anti-corruption regulation shall be applied, the publications Acting on suspicions of corruption - a guide and Manual for the application of Sida's anti-corruption regulation and Checklist for Sida's managers on suspicions of corruption have been produced. The Audit Guide supplements these documents in those cases where you suspect corruption and it is appropriate to perform an audit.

### **Aim of the manual**

The aim of the Manual is to make things easier for you when you come into contact with audits. The Manual is intended to function as a reference book and therefore some information is repeated. Among other things, the Manual provides guidance on ways in which you should deal with audit reports, make procurements of auditing services, and write terms of reference for audits. At the same time the Manual is intended to give members of staff at Sida and the embassies an understanding of auditing, the role of the auditor, and what can be achieved with audits.

It should be emphasised that the Audit Manual is only intended for Sida and embassies/field offices. (Embassies/field offices are referred to hereinafter as embassies.) It does not take up issues that relate to the external audit of Sida made by the Swedish National Audit Office or the internal audits performed by Sida's Department for Evaluation and Internal Audit (UTV) on behalf of the Board of Sida.

### **How to read the manual**

There is a checklist at the beginning of the Manual. There you can find brief questions and answers that are common in connection with audits. The answers contain references to relevant sections of the Manual.

Thereafter, there are three sections that describe what you should do before you commission an audit, how you should commission an audit, and finally what you should do when the audit has been completed.

In the fourth section, you will find information on ways in which you can make surveys of audit capacity. In section five, you will find the support functions that you can use in audit matters. The final chapter contains facts for those of you who wish to know more about important concepts in auditing, experience gained from audits, reading suggestions etc.

At the end of the Manual, there are appendices that provide practical suggestions and examples of different documents in the audit field. Note that these are merely examples. Each case is unique and you must always make necessary adjustments to the situation in question.

The headings in the table of contents are intended to provide guidance in cases where you want to read more about a specific section. There are also references in the text to sections where you can read more about a specific aspect.

# Checklist for audits

A checklist is provided below of a number of brief questions and answers on topics that are common in connection with audits. A reference to relevant sections in the Manual is provided after each answer.

## **On what occasions should sida perform an audit?**

There are several different occasions when Sida should perform an audit. We can, for example, perform an audit for preventive purposes in connection with the planning of a project, as a way of to regularly monitor an ongoing project, or in connection with the completion of a project. Normally, the partner in cooperation is responsible for the audit but, if no audit has been made for various reasons, it is Sida that must take the initiative to have an audit performed. Dissatisfaction with an audit that has been performed or a need to check up on the partner in cooperation for other reasons can also be reasons for Sida to make an audit. If we suspect any type of corruption or any other improprieties, it is our responsibility to make an audit of the activity immediately. Read more in section 2.5.

## **Who is responsible at sida for ensuring that an audit is performed?**

The responsibility lies with the member of staff who has the right to use the budget for the contribution. However, the programme officer responsible for a contribution or a component is usually the person in the best position to know when there is a need to make an audit, particularly if the audit has arisen as a result of something that has happened in the programme of cooperation. It is the duty of the programme officer responsible for the contribution to take up any problems and to propose an audit. Read more in section 1.1.

## **I have received a report on an audit – what should i do?**

First of all, you should check that the requirements in the agreement have been audited. It is important that you know what has been included in the audit assignment. You can assume that everything not included in the assignment has not been audited. The fact that the audit report is “unqualified” is no guarantee that everything is in order. In order to find out what observations the auditor has made, you need to have access to a more detailed audit report. It is therefore important to demand an audit memorandum/management letter in order to have access to all the

observations the auditor has made in the auditing process to reach his/her audit statement. Read more in section 3.1.

#### **I shall commission an audit – who at Sida can give me advice?**

EVU/Ekonomi know all about auditing and have a focal point. In addition, the departmental controllers or the field controller often have experience of similar cases. Read more in section 5.1.

#### **What type of preparations do I need to make when I commission an audit?**

Give the auditor basic information on the partner in cooperation and the activity. Add background information in the terms of reference on the amount of the support, the duration of the support, the number of staff in the organisation, the number of offices and where they are located. Also provide information if there is a special aspect or a part of the activity that the auditor should examine in particular, or if there is important information (for example rumours of improprieties, or that the financial reports seem to be odd) that the auditor should be aware of. Note that the proposed terms of reference are only templates. First of all, you must conduct your own risk assessment so that you can cross out less important areas in the terms of reference. Otherwise the audit will be either very expensive or general. You should bear in mind that it is Sida (and not the auditor) that determines the level of ambition of the audit and that the audit should preferably be arranged in such a way that it also offers support to the partner in cooperation at the same time. Read more in section 2.

#### **Which firm of auditors should I contact?**

Sida has framework agreements with several Swedish firms of auditors. Many embassies have made their own procurements of framework agreements with local firms of auditors. If, for any reason, you cannot use these framework agreements, you will need to make a special procurement of audit services. Read more in section 2.2.

#### **I work at an embassy and intend to commission an audit**

##### **– can I use Sida's framework agreements?**

Yes. Sometimes it can be preferable due to challenging situations, corruption or other political reasons. The big firms of auditors sometimes use local auditors in the country in question to keep the costs down or because they need their language skills, but the audit is always led by the Swedish auditors. Read more in section 2.2.

#### **Who pays for the audit?**

The cost is normally debited against Sida's contribution. However, this should have been agreed with the partner in cooperation. In special cases – particularly in the case of anti-corruption audits – Sida may need to use other funds especially for the audit, but this should be an exception. EVU/Ekonomi make a review of consultants once a year and this review is financed by EVU. In addition to this, departments at Sida can finance audits on the basis of a predetermined annual audit plan. Read more in section 1.1 and 2.2.

#### **What are the different stages of an audit?**

Before you contact a firm of auditors, you must first collect information. The areas that need to be audited are the point of departure. Then you plan the audit together with the firm of auditors. After the audit, the firm

of auditors submits a report based on the conditions you have stipulated. Finally, you make up your mind about the report and reach a decision on any measures that need to be taken. It may also be necessary in some cases to make a follow-up audit. Read more in section 2.3.

### **How should i formulate the terms of reference**

Every audit requires unique terms of reference. As your point of departure, you should always have the agreement in question or a relevant directive. The character of terms of reference will vary slightly depending on the type of audit in question. Note that the terms of reference suggested at the back of this guide are templates. Conduct your own risk assessment and cross out those parts that do not need to be audited in as much detail. It is a good idea to add that the auditor may propose changes to the terms of reference during the course of the work after approval by Sida. Request that the audit report ends with clear recommendations in priority order so that you do not have to interpret the report. Read more in section 2.4.

### **I suspect corruption – what shall i do?**

If you suspect corruption, you will find information on what you should do in, for example, Acting on suspicions of corruption – a guide and the Manual for the application of Sida's anti-corruption regulation. A suspicion of this type often has the effect that you have to commission a special audit to investigate what has happened. Read more on what you should bear in mind in this type of audit in sections 1.2 and 2.5.

### **What is a management letter?**

It is a letter containing the auditor's observations during the audit to reach his/her audit statement. Essential are required to influence the audit statement, but Sida is interested in all observations. For some auditors (those who use the American auditing standard), the term means a statement on internal control. Many have misunderstood our wording and think that a management letter requires an extra audit and costs more money. That is wrong. We have therefore made changes to the new agreement templates to say audit memorandum/management letter.

In cases where the auditor has provided detailed information on observations in the audit report, no separate management letter/audit memorandum is needed.

### **What applies to audits of contributions for swedish authorities?**

Sida makes no exceptions in its rules and regulations for audits of authorities. The audit requirements are the same for contributions to another authority as they are for other contributions, i.e., an annual audit. The audit by the Swedish National Audit Office is not enough. That is based on a risk assessment of the activity of the whole authority and it is unlikely that Sida's contribution will be audited, as it often forms a small part of the authority's total funding. The Audit Office rarely audits at the detailed level we normally require. If the Audit Office audits Sida's contributions, any failings are reported to the relevant authority and not to Sida. Note that if it concerns an assignment, the audit should be conducted based on the criteria of risk and importance.

# 1 To bear in mind before you commission an audit

## 1.1 Sida's right to have an audit performed

Sida's policy is that all programmes of development cooperation shall be audited annually (read more in Sida's anti-corruption regulation) and that this shall be done in a satisfactory manner, taking all circumstances into consideration. However, the cost of the audit must be reasonable in relation to the expected usefulness of the audit. The aim is to meet the requirements of both partners in cooperation in respect of control, insight, cost-efficiency and goal fulfilment. The agreement with Sida's partner in cooperation determines whether it is possible to commission an audit.

The question of how, when and of whom controls shall be exercised in the project cycle, preferably in the form of audits, should be evident from the assessment memorandum and then from the agreement and project document. Primarily, this is always the responsibility of the partner in cooperation.

Sometimes, proposing audits can be a sensitive matter. The partner in cooperation can perceive a proposal of this type as a violation of its integrity and thus a negative situation for cooperation can be created. Therefore, start audits first after consultations have been held with the partner in cooperation on when and how they should be performed etc. In the first place, the audit should be a form of support for the partner in cooperation, providing assistance for the partner in cooperation to shoulder its responsibility to exercise controls, not an indication that there is a conflict between the recipient and the donor. However, if you suspect improprieties, you should take the initiative for an audit without informing the partner in cooperation of this in advance.

If the partners in cooperation have the same views on the purpose of the audit, they can jointly indicate to the auditors that critical observations in the audit report will be welcomed as part of the openness and willingness to cooperate that exists between them. Agreement should also be reached on aspects that should possibly only be the subject of an oral report and, in such cases, the partner to whom this type of report should be addressed.

### What does the agreement say on audits?

According to Sida's views on ownership of the activities we support, it is the partner in cooperation that is responsible for exercising controls of the activity and for implementing the audit. Sida's agreement templates

therefore state that it is the partner in cooperation that is responsible for implementing the audit. If this has been agreed, but the partner in cooperation has not been able to perform a satisfactory audit, Sida is always entitled to take the initiative itself and have an audit made.

Normally, the partner in cooperation's regular external auditor performs the audit as part of the annual financial audit. In particular, this is the case when Sida provides a non-earmarked contribution to the activity (for example budget support, sector programme support or organisation support). In such cases Sida receives a copy of the audit report that covers all the activities pursued by the partner in cooperation during the year – in other words not merely the activities that Sida has supported. However, the regular external auditor can also make a special examination of the activity supported by Sida, for example a project, and then write a special report on that component. Sida is then interested in a financial report in which the expenses are compared against the budget. The auditor shall state that the funds have been used in accordance with the agreement.

If the partner in cooperation is a UN agency, it is normally not possible for Sida to engage any other auditors than the UN's regular auditors. (However, it is not always possible to engage them on behalf of Sida.) Audits of the partner countries' governments, ministries, agencies, municipalities and other public or publicly-owned organisations are normally performed by the Supreme Audit Institutions (SAI) in these countries. These audits are performed in accordance with legislation or the constitution but, by means of an agreement between Sweden and the government of a partner country, other auditors can make supplementary audits. This situation can arise, for example, if the country's SAI is not able to perform the audit within a reasonable period of time or if there is a need to make a special examination of a certain part of the activity. Both the agreement and the audit itself should always be subject to consultations with the country's SAI.

The regular auditors are also often engaged to examine a certain part of activities in which Swedish or foreign NGOs or companies are involved. However, it must be stated in the agreement with the organisation or company that Sida is entitled to receive a copy of the audit report or a report on the examination of a certain activity supported by Sida, and to have an audit performed whenever necessary. Read more in the Audit Guide for NGOs and their auditors produced by SEKA.

If Sida wishes to obtain copies of any other documents than the audit report, this must be stated in the agreement. This can refer, for example, to audit memoranda and management responses. Examples of sections on auditing in the agreement template for foreign organisations can be found in appendix 8.

## **1.2 Different types of audits**

The annual audit results in an audit report. In this report the auditor expresses an opinion on the annual accounts and on the administration of the organisation by the board and management during the period. The audit thus provides reliable financial information on the organisation. The statement made by the auditor shall follow the requirements laid down in the rules in the country concerned. These rules do not oblige the auditor to express an opinion on whether the work has been appropriate, the goals have been achieved, or agreements have been followed. The auditor only expresses an opinion on whether the accounts reflect what has happened in a reliable way. Therefore, you may need to

let the auditors make other types of examinations that provide answers to other types of questions. This section provides an overall picture of different types of audits. In many cases, the different types overlap each other, but they have a different focus. There is no scientific distinction between the different types of audit. At Sida, we have chosen to divide the audits into three areas: Financial Audit, Forensic Audit and Performance Audit.

### **Financial audit**

The aim of the financial audit is to examine whether the accounts are true and fair, i.e. that the financial accounts provide a correct picture of the organisation's work. This means that an examination is made of the annual accounts or other types of reports that have been drawn up on the basis of the accounts and their underlying documents (supporting vouchers). Where an individual project is concerned, the examination can include an annual follow-up of the project's expenditure or other financial reports agreed between the parties.

Two types of methods are used in the financial audit: substantive testing and examination of internal controls

- *Substantive testing*  
Substantive testing means that the auditor examines the content of different items in the accounts, i.e. the amounts presented in the report (for example, fees). However, the auditor does not examine all the vouchers. Therefore, the auditor must first decide on the proportion of the vouchers that are to be examined. The size of the sample depends on the assessment made by the auditor of risks of material errors and the wishes of the client. Sometimes, the auditor makes a spot check of one type or another, for example of a certain period, a certain project or a certain type of expense. The auditor can use purely statistical methods, for example every tenth voucher, regardless of size. Read more on materiality and risk in section 6.1.
- *Examination of internal controls*  
Examination of internal controls means that the auditor identifies, tests and examines the organisation's systems for internal control. Are, for example, regular reconciliations made between the accounts and the bank statements so that errors are discovered in good time? Does anyone check whether the right account is used for each amount? With the aid of this type of examination the auditor can make an assessment of the probability that the organisation's accounting system provides correct and complete information. A certain amount of substantive testing is also performed in the examination of internal controls, for example through spot checks of transactions in which vouchers and other supporting documents are examined.

### **Management audit**

Management audit (or operational audit) means that the auditor examines management's administration of the organisation (for example by examining systems for internal control). The examination investigates how the budgeting and accounting are done, how results are followed up, how risk analyses are made, as well the underlying documentation used by management for decision-making purposes etc. It can also include an examination of how laws, regulations and agreements are followed, a so-called Compliance audit (see below).

Accordingly, the borderline between financial audit and management audit is not clear-cut. Observations made during the examinations can often be used in both types of audits.

### **Performance audit**

Performance audit (or Value for Money Audit) is based on examining how well the organisation has achieved its goals (goal fulfilment), the relationship between resources used and results (cost efficiency), or how well the results contribute to the effects the organisation wishes to achieve (appropriateness).

Performance audit is a combination of traditional auditing and evaluation, where the borderline between auditing and evaluation is not clear-cut. The group making the audit can consist of both auditors and technical experts. The result of an audit of this type can be very valuable for both control purposes and for management, and as an instrument that can be used against corruption.

It is often necessary to make the examination of cost-efficiency and goal fulfilment of operations with the aid of technical experts. It is difficult to provide general guidance on the ways in which an audit of this type is best made since it is totally dependent on the prevailing conditions in each assignment.

### **Capacity studies**

A capacity study examines the organisation's capacity in respect of goal fulfilment, planning, administration, resources etc. The aim is to determine the quality of the activities pursued by the organisation. The focus is broad and perspicuous. It can, for example, include examining whether the organisation has access to staff that can work with payments, accounting and controls, and examining whether the organisation has adequate internal controls. The basic idea is that the study focuses on those aspects and routines in the organisation or project where, it has been assessed, the greatest risks lie.

### **Systems-based audits**

A systems-based audit analyses how the organisation works by examining the routines and systems in the organisation that are intended to guarantee reliability in its work and reports. The focus is narrow and more comprehensive than in a capacity study.

### **Compliance audit**

This type of audit can, for example, be included in a management audit. It has the aim of examining whether the organisation or the implementer of the project follows the legislation, other rules, agreements etc.

### **Preventive audits**

A preventive audit can be included with advantage in the assessment stage of a contribution. The auditor examines whether the organisation's stability and structure, management capacity and manning, financing and control functions etc are such that the planned activity can be expected to be pursued in a secure and successful manner. In other words, it is a type of capacity study.

### **Audits when corruption is suspected/Forensic audit**

A normal financial audit provides no guarantee that corruption will be detected. For example, it can be easy to falsify receipts or to receive bribes on bank accounts that are not examined by the auditor. However, if you commission a forensic audit to examine a suspected case of corruption, it may be possible to detect irregularities. The purpose of a forensic audit is to serve as a basis in possible legal disputes. In this type of audit, it is particularly important to ensure that the auditor is independent in relation to the auditee (read more on the formulation of terms of reference for this type of audit in section 2.5). A forensic audit may be either an investigation in the event of suspected financial irregularities, a programme to discover irregularities or an audit of protection against irregularities.

### **Internal audit**

Internal auditors are employees of the organisation and work on behalf of its management or board. An internal auditor shall have an independent position in the organisation and work impartially. However, it is common for internal auditors and external auditors to cooperate with each other. This enables the external auditors, for example, to make use of internal audits by using their results (if they are reliable), instead of making an examination of exactly the same material or material with the same focus.

Internal auditors can work with all different types of audits. One of their main tasks is to ensure that the organisation's systems for internal control work properly. The reports written by the auditors have the primary aim of improving routines and working methods. Their work can also have a preventive function in connection with the production of the organisation's annual accounts by enabling the organisation to detect and correct any errors before the final version is approved. It is the head of the organisation or the board that receives the internal audit reports.

## **1.3 Different types of audit reports**

In the auditing field there are a number of different technical terms that can be difficult to keep apart. A summary of the most important concepts, and how they should be interpreted, is provided below.

Audit report	Report on the regular audit of legal entities, performed in accordance with Swedish legislation. (Note that an audit opinion is a statement included in an audit report.)
Audit memorandum	All other types of reports on audits. Is not always an official document (unless the audit has been commissioned by Sida). Note that the term Management letter has a narrower meaning and mostly takes up issues concerning routines and internal control.

The terms audit report, reporting or report will be used below as generic concepts for different types of reports used in the Audit Manual.

## **1.4 When should an audit be performed?**

Auditing can be divided into three phases

- interim audit
- annual audit
- final audit

In a follow-up audit you can check in arrears how the recommendations made in an earlier audit report have been followed. You can also commission a special one-off audit of aspects that appear to be uncertain or suspicious. Before writing the terms of reference, you have a discussion with the auditor on the ways in which best use can be made of different parts of the audit.

### **Interim audit**

Normally the auditors do not wait until the books have been closed before they start to examine the annual accounts. Instead, they prepare the work earlier during the year in the so-called interim audit. In the interim audit they examine vouchers and other documents. After the closing of the books, they can concentrate on, for example, corrections to the bookkeeping, particularly year-end transactions, and controls of various summaries. The interim audit can result in yearly reports and audit reports, but can also be more limited, for example quarterly reports or half-yearly reports. It is also common that, in the interim audit, auditors make examinations that provide data for the assessment of the organisation's internal controls and the capacity of management. With the aid of this method, they can spread their work over a longer period of time.

### **Yearly financial audit**

The yearly financial audit is normally the financial audit and then the auditor expresses an opinion on the accounts, the annual accounts and the administration of the organisation. For example, the auditor investigates whether the annual accounts provide a true and fair picture of the financial outcome and financial position (statement of financial performance and statement of financial position), of disbursements made during the period, or other information that the statements of account shall reflect. The yearly audit also often includes audits of systems and routines that safeguard good internal controls and true and fair accounts.

### **Final audit**

In connection with the end of a project, a final audit shall be made of the entire project. If the auditors have made interim audits and have followed up how recommendations have been followed, they can make the final audit less comprehensive. If the first audit is performed when the project has ended, the work will be more extensive and more difficult. Perhaps, the documentation and persons responsible are no longer available and it will be difficult to correct any mistakes or demand accountability.

# 2 Commissioning an audit

In this chapter, we describe aspects that you must reach a decision on when you plan to commission an audit. As mentioned above, it is in the first place the responsibility of the partner in cooperation to ensure that an audit is performed. The section below only describes occasions when, for one reason or another, it is Sida that initiates the audit. This can, for example, be due to the fact that the audit that has been performed did not make a special examination of that particular part of the activity to which Sida contributed, that you are not entirely satisfied with the report, that you have not received audit reports as stipulated in the agreement, or that you suspect corruption.<sup>1</sup>

## 2.1 What should the audit include?

It is Sida's policy that all programmes of support shall be audited annually (see further, Sida's anti-corruption regulation). However, this must be placed against the cost-efficiency of the audit. Perhaps it is not reasonable to make an audit each year of all the activities in a major programme or project. Thus, you should plan the audits with a long-term perspective. In other words, one year you can have certain elements or sub-projects audited and the following year audits can be made of some other activities.

The auditor normally uses spot checks or assessments of materiality and risk (see further, section 6.1), which means that errors can remain undetected. It would be unreasonable to employ such large resources that all possible errors would be detected. If the examination shows that the internal controls function satisfactorily, the auditor can make the assessment that there is only a small risk of major errors.

Using development cooperation funds for intended purposes means that it is not just a case of true and fair accounts, it is also a case of achieving the poverty goal and programme or project goals. This can, in turn, mean that both the financial audit and the performance audit need to examine a holistic picture of the activity.

In addition to the necessity of performing the audit in such a way that sufficiently high levels of quality are achieved at as low a cost as possible, the audit shall also result in good advice and proposals to the organisation. The examination thus contributes to giving the partner in cooperation assistance in rectifying problems in its organisation and improving its capacity, which is a development contribution in itself.

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<sup>1</sup> Read more on audits in cases where you suspect corruption in section 2.5.

The result of an examination depends on how much knowledge is transferred in connection with the audit and what this has led to, together with the measures taken as a result of the audit's recommendations. If the personnel responsible know that activities will be audited regularly, or with a certain frequency, this very fact can contribute to improving the administration. The risk of improprieties and corrupt behaviour will thus be reduced. The risk of detection and legal consequences are also a deterrent.

Demand that the auditor prioritise the observations in order of importance. The program officer should not have to try to interpret the audit report. Make sure this is written into the terms of reference when Sida procures its own audits as well as when it is able to approve the partner in cooperation's terms of reference.

## **2.2 Making a procurement of an audit**

Normally, it is always the responsibility of the partner in cooperation for ensuring that audits are performed periodically. However, sometimes situations can arise in which Sida itself needs to take the initiative to have an audit performed or to engage a firm of auditors for another type of assignment. In the following two sections we describe what you should do when you wish to make a procurement through Sida's framework agreements or outside the framework agreements. Several departments have experience of making procurements of different types of audits. Contact the controller in your department or the focal point of the audit for more information.

### **Making a procurement via Sida's framework agreements**

Sida in Stockholm has concluded framework agreements with several Swedish firms of auditors. This means that you have a duty to use these for assignments for Sida Stockholm. Services can also be called off against these framework agreements by embassies/field offices. The framework agreements are valid for the period January 2007 to December 2008 (with the possibility of prolongation by two more years). With the aid of the framework agreements, we can simplify the procurement procedure and hold down costs, at the same time as we have access to auditors with experience of development cooperation who can step in at short notice. The agreements do not contain any guarantees in respect of volume for the auditors.

For each assignment there must be terms of reference that contain information on background, purpose, assignment, time schedule and reporting requirements. The fees charged for different categories of personnel are based on an agreed tariff in the framework agreements with maximum amounts. Therefore, all you need to do is to determine the amount of time that auditors in the different categories need to spend on the assignment and to specify other costs, for example journeys. The firms of auditors engaged in the framework agreements are entitled to request an annual upward adjustment of their fees based on an index calculated by Statistics Sweden. Presentations of the companies included in the framework agreements and information on fees can be found on Sida's Intranet, iNSIDE. Go in under the heading Supporting Functions/Law & Procurement/Procurement & Contracts/5. Framework Agreements/Sida's own Framework Agreements. Then click on Framework Agreements for Financial, Forensic and Performance Audits. Alternatively, go to Support Functions/Audit at Sida/Framework Agreements where there is a direct link to the audit agreements.

In Sida's framework agreements we distinguish between financial audits, forensic audits and performance audits (see definition in appendix 10). There is an instruction for call-offs on the intranet under the audit framework agreements. For the areas Financial Audit and Forensic Audit, Sida has agreements with E & Y, KPMG and Öhrlings PriceWaterhouseCoopers. For the area Performance Audit, Sida has agreements with Sipu International, Swedish Development Advisers, Jarskog Konsult, BDO Nordic, Professional Management Arne, Barbro Svensson and KPMG. For up-to-date information, see the intranet, which also has information on fees, contact details and CVs.

Assignments of more than five consultancy days require a renewed competitive tender, which means that you must send an inquiry to all the companies within the relevant audit areas. A copy of the call-off should be sent to the focal point for audit.

The levels of fees specified in the framework agreements apply to consultants in Sweden. Per diem, travel expenses etc must be added for Swedish auditors travelling abroad. If the assignment has the effect that the firm of auditors in Sweden has to engage a local office abroad, the level of fees for the foreign staff is a matter of negotiation, though not more than in the framework agreement.

For an embassy/field office it can be less expensive and better to engage a local consultant who, in addition to professional expertise, also knows the local culture and its risks. This assumes that the consultant is independent of the organisation to be audited and its staff. Sometimes the best alternative can be to engage Swedish auditors who work together with local auditors.

The division commissioning the audit finances the audit. EVU/ Ekonomi can, on request, provide support, for example in the formulation of the terms of reference for the audit assignment. Read more in section 5.1. Support at Sida.

Suggestions for the content of terms of reference for audit services are included in appendix 1-1b. Examples of terms of reference are included in appendix 2 (financial audits + performance audits) and in appendix 3 (system-based audits).

### **Procurements outside Sida's framework agreements or of new framework agreements for embassies/field offices**

Embassies/field offices are not bound to use the framework agreements for any type of audit, but have the right to use them.

On certain occasions, it can be advantageous for an embassy/field office to have contact with a local firm of auditors. This can be the case for issues where you want local knowledge, a rapid intervention, advice etc. However, note that you must follow the provisions of the Public Procurement Act in all procurements made by Sida and embassies. If you want to know more about the rules and how you should best proceed, contact one of Sida's procurement advisers. An example of terms of reference for a framework agreement for audit services (embassies) is included in appendix 6a. An example of a invitation to tender is included in appendix 6b.

The most important requirement you should stipulate when making a procurement of audit services is that the firm of auditors or the auditor is independent of the auditee. You should also ensure that you get qualified persons to perform the assignment. Perhaps it is not the auditor you negotiate with who will perform the assignment but much more junior staff. It is therefore a good idea if the contract states the name and

category of each auditor. OECD's Development Assistance Committee (DAC) has formulated recommendations for the requirements that should be made in respect of audit services. Read more in section 6.3.

When you are going to make a procurement of a suitable firm of auditors or auditor, you can use the following checklist:

- What experience is there in the country of auditing in general and of auditing different sectors, both financial and performance audits?
- What services over and above traditional auditing services are provided, for example various forms of training and advisory services?
- Is there a local system for the authorisation of auditors?
- What is the manning structure of the firm (CVs for individual auditors)?
- Does the firm have a human resource development policy?
- What other clients does the firm have and what is their experience of the services provide by the firm?
- Does the firm have method handbooks, and sensitivity and flexibility in respect of the requirements of the assignment?
- Are there ethical guidelines?
- Request a presentation of the firm.
- Make a test by giving the firm a minor assignment.
- Check with other donors with high demands to see if they have any experience of the firm (or any other valuable information).
- Investigate whether the firm or the auditor is/has been involved in legal disputes, has been given reprimands or warnings.

## **2.3 Different stages in Sida's procurements of audits**

### **Preparatory collection of information**

As a first step you should compile general information on the organisation or activity that is to be audited. This information forms the basis of the auditor's work. Examples of material that can be included here are:

- agreement
- plan of operations
- budget
- minutes or notes from important meetings
- reports as specified in the agreement
- the annual accounts of the company or organisation, including the annual report
- earlier audit reports
- evaluations
- experience of other donors
- information from the financial follow-up of contributions
- other relevant material from the contribution file and the archives.

The collection of material is governed by the type of audit that is to be performed, for example a financial audit, a systems-based audit or a capacity study. Read more in section 1.2. It may also need to be supplemented with interviews made by the auditor. The staff of the client (Sida) and the partner in cooperation should take an active role in the process. The point of departure is that Sida and the partner in cooperation agree that the accounts are to be correct and that any problems will be solved.

### **Planning of the audit**

Decide what should be audited and how exhaustive the audit needs to be. Should the entire activity be audited or merely certain parts of it? Should it cover all types of costs or merely some types? Should it cover the entire agreement period or a certain year – or even parts of an earlier agreement period? The planning is of decisive importance for the quality of the entire audit. The auditor's point of departure is the terms of reference and any other information you provide prior to the audit. On the basis of this information, the auditor draws up an audit plan.

This planning process results in a concrete audit programme that clearly specifies the steps the auditor will perform and the method that will be used. It is at this stage that selection criteria such as materiality and risk are applied.

In section 2.4 you will find examples of questions that you should take into consideration in the terms of reference.

### **The audit**

After the planning stage, the actual audit starts. The auditor continuously evaluates the results of the audit. This can sometimes lead to a re-evaluation of risks. For example, the scope of the audit can change from that originally planned by the auditor.

### **Reports**

The auditor then reports the results of the audit to you and possibly to other interested parties, in accordance with your agreement with the auditor. The audit report presents observations and recommendations for action to be taken.

The terms of reference should specify how the auditor should report the audit. A written report, an audit report, is always included. Moreover, it is usually a good idea to request information on concrete observations through a special audit report. The auditor's reports should focus on deviations, and state observations and recommendations in order of materiality. They ought also state the latest time by which the recommendations ought to be implemented. Unless otherwise stated in the report, the auditor should have covered all the areas specified in the terms of reference. An oral report from the auditor can also be valuable. At a meeting of this type, the auditor can explain the content of the written report and provide information on other observations or reflections in connection with the audit, which the auditor did not consider to be important enough (or far too sensitive) to include in the report.

The partner in cooperation shall naturally be informed. This can be done at the same time as you receive the report, or in connection with a meeting. The audit of public bodies in a programme of cooperation should normally be done by – or at least in consultations with – the country's supreme audit institution. One minimum requirement is that reports made by any other auditor should be passed on to the national audit institution.

If the audit is part of the ordinary audit (i.e. not commissioned by Sida), there will always be an audit report. You should follow up an audit report that contains qualifications by finding out about their causes and effects. It is sometimes the case that the regular auditor summarises his/her observations in a special memorandum to management (audit memorandum/management letter), which management should have responded to in writing (management response). Sida can make a request to receive these documents.

Another form of auditing is an examination in which the auditor issues an audit certificate for a special purpose. Sida can request an audit of this type and it is done either by the auditor of the company or organisation or by an auditor engaged by Sida. The statements made in the certificate are governed by the request that Sida has specified in the terms of reference.

### **Documentation**

Information that shall be documented in respect of the contribution includes, for example

- long-term audit plan
- documentation on the procurement of the audit, including terms of reference
- audit reports
- minutes of meetings with partners in cooperation
- positions/standpoints adopted
- plans for corrective action agreed by the partner in cooperation
- follow-up of results
- possible follow-up audit.

## **2.4 Terms of reference for an audit or capacity study**

### **Terms of reference for an audit**

Making audits is a way for Sida to assume its responsibility for exercising controls. If Sida or an embassy commissions the audit, the terms of reference must reflect this responsibility. At the same time Sida shall take into consideration the needs of the partner in cooperation. In this way the audit can be valuable for all parties involved.

It is Sida or the embassy that is the client and shall decide on the focus of the audit. Normally, we can do this in consultations with the partner in cooperation, and the auditor can submit proposals for terms of reference. However, if the audit refers to suspicions of corruption, it is sometimes necessary to keep the real purpose of the audit secret so that evidence cannot be destroyed.<sup>2</sup> As the client, you need to specify what the auditor should examine on the basis of the criteria of materiality and risk. You should do this in the light of agreements, project documents, sector reviews, financial and operational reports, previous audit reports, rumours and suspicions etc. The auditor must be given all the relevant material. It is often also appropriate to provide information orally before the auditor plans the audit.

As the point of departure for audits, you should have the (planned) agreement and underlying programme or project documents. In cases where you particularly wish to prevent improprieties, or if you suspect corruption, this shall be specified in the terms of reference. **N.B.** Bear in mind that the terms of reference is a public document (but it is possible to classify it as confidential). In some cases, it is appropriate to specify certain audit areas in the terms of reference, for example individual projects, particularly risky areas such as goods that are liable to theft, or major procurements. Give the auditor basic information for planning the audit. The auditor needs sufficient information to:

- create an idea of the expectations in the terms of reference
- identify problem areas, for example in accounts and reports, at early stage

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<sup>2</sup> Read more on audits in cases where you suspect corruption in section 2.5.

- make a time schedule for the audit
- select colleagues with suitable experience and specialist know-how for the assignment.

Sometimes, it can be necessary to change the terms of reference during an ongoing audit as a result of observations made by the auditor. Therefore, for major audits, the auditor should make a report, for example, at the half-way stage of the audit, or if a significant observation is made. In this context, a significant observation can be, for example, that the quality of the administration makes the audit difficult, or that the auditor has detected mismanagement of resources, improprieties or corruption.<sup>3</sup>

In all terms of reference you should stipulate that the auditor should analyse observed problems and submit concrete recommendations within his field of competence. If the auditor has this advisory function, the auditee can also benefit from it. Since the personnel involved are actively involved, the audit can contribute to building up knowledge. The auditor should also, as far as possible, look ahead and draw attention to potential problem areas. These can refer, for example, to management functions, manning, recruitment needs, issues relating to skills, technical quality development, changes in needs of systems and routines, or improvements in the control environment (performance audit issues).

Finally, you should make an overall assessment of the entire terms of reference to ensure that that it corresponds to expectations, both those of Sida and the partner in cooperation. The scope of the audit can be made infinite – choose therefore a reasonable and appropriate level of ambition!

Suggestions for the content of terms of reference for audit services can be found in appendix 1-1b. Examples of terms of reference can be found in appendix 2 (financial audit) and in appendix 3 (systems-based audit).

### **Capacity study of a partner in cooperation's organisation**

A capacity study can, for instance, investigate a ministry or a part of a ministry, a local administration, or a non-governmental organisation. The study can include the organisations that the partner in cooperation, in turn, has reason to cooperate with, or is administratively dependent on in other ways for implementing the project.

This type of study is within the competence of an authorised auditor. The points below can constitute a basis for the terms of reference. The study can, for example, include the organisation's activities, management and reports as well as knowledge development:

#### *Activities*

- Policy and strategies
- Focus of activities, for example by operational areas and scope
- Sources of finance
- Systems and methods for planning and coordination, management of implementation, controls and follow-up, and evaluation.

#### *Management and reports*

- Budget system
- Accounting system
- Systems for internal control
- Payment routines

<sup>3</sup> Read more on audits in cases where you suspect corruption in section 2.5.

- Reporting systems
- Rules and routines for procurements
- Allocation of powers and responsibilities
- Reconciliation routines
- Controls and planning of audits

*Development of knowledge*

- Existing skills in the organisation and needs of new skills
- Activities designed to enhance skills
- Feedback of experience from audits and evaluations

An example of terms of reference for a capacity study can be found in appendix 4.

## **2.5 Terms of reference for an audit where corruption is suspected**

In order for an audit to be effective in the context of corruption, it must focus particularly on risks of corruption. A combination of different types of audits can be necessary to counteract or detect corruption.<sup>4</sup> A financial audit will not detect, for example, if receipts are false or if material supplied has been used for private purposes. There can be detailed rules which are nonetheless inappropriate: use can be made of loopholes. A performance audit can be required for anti-corruption purposes. In this type of audit, it is particularly important to check that the auditor is independent of the auditee.

Normally, the agreement between Sida and the partner in cooperation states that the two parties will cooperate to counteract and detect corruption. It is usually the partner in cooperation that is responsible for ensuring that the activity is audited regularly. However, with the exception of UN agencies, Sida usually includes its right to commission its own audits in agreements.

Accordingly, it is the partner in cooperation, or organisations with which the partner in cooperation has agreements, that are to be audited. Corruption normally occurs through a network of individuals in an organisation, in collusion with suppliers or beneficiaries outside the organisation. A bribe does not pass through the organisation's cashier's office or the accounts, it goes directly from the person who received a grant on wrong grounds to the person who approved the grant. It is not stated on the invoice that the supplier is a cousin of the purchaser or that competitors in a procurement were threatened. Therefore, you must be aware that the audit cannot deal with risks of corruption alone.

It is important that the audit is performed rapidly and efficiently and that it is started as soon as possible. Otherwise, there is a great risk that accounting documents disappear, personnel leave the organisation and so on. It is important that the audit can state quite clearly whether or not improprieties have occurred. The audit assignment to the firm of auditors must be specific. In cases of suspicion of corruption, the audit shall answer the question of whether corruption has occurred or not. If it has, it shall be possible to verify the improprieties through copies of original documents. It shall be stated on the copies where the original documents are kept and on which day and by whom the copy was made.

<sup>4</sup> Read more about different types of audits in section 1.2.

In the terms of reference, you shall describe the focus of the audit. The point of departure must be the concrete situation in question. This should preferably be done in consultation with the auditor who is to perform the audit. The terms of reference are crucial for the efficiency of the audit, i.e. whether it can prevent or detect corruption. The focus of the audit will vary, depending on whether you suspect corruption or want to prevent corruption. The design of the audit shall also be based on an assessment of materiality and risk (see further in the section on Risk assessment below). Resources should be focused on the most important areas, which means that minor errors can remain undetected. There is an example of content for terms of reference in appendix 5. EVU/ Ekonomi, departmental controllers and the field controller can also provide support.

There are also other approaches to detect corruption. You can, for example, contact national sections of Transparency International, or voluntary organisations that specialise in monitoring corruption, or independent media. You can also study police investigations and the experience gained by other donors. You can also listen to the target group that would benefit from a contribution.

### **Risk assessment**

Before you draw up the terms of reference, it is important to make a risk assessment. This means that you try to identify the risks that exist in the project or the organisation that is to be audited. The objective is to classify the risks in the organisation or project. This assessment is of decisive importance for the formulation of the terms of reference.

When it is easy to identify the risks, the assignment can be limited in scope and the audit can concentrate on high risk areas. If this is not possible, the assignment must be made broader and include more areas with larger volumes of accounts.

Examples of ways in which risk assessments of projects can be made:

- What have the funds been used for?
- Divide the contributions provided into three to five groups on the basis of your assessment of the risk that funds may be used in an improper way.
- Review what most of the funds are used for and whether there are any special risks in these uses.
- Check whether there have been any signs of an increase in risk in any area or project (for example, incomplete reports or reports received late).
- If you have obtained information from external sources, compare how this information corresponds with the above points.

With the aid of the risk assessment, it is possible to identify the areas that should be given priority in the audit. Sometimes, the conclusion reached in the assessment is that one or more areas shall be the subject of a special audit, for example payments of suppliers' invoices, purchases of petrol, or wage payments. Sometimes, the risk assessment provides no concrete results but indicates general uncertainty. There can be, for example, information that improprieties are occurring in a programme but no information on what they are exactly. In cases of this type, the audit must include both routines and internal controls. However, with the aid of the risk assessment you may possibly identify that fifty per cent of the funds are used for purchases of material that is supplied by an

internationally well-known company that Sida has good experience of. In such cases the audits can concentrate on the use of the other funds.

With the aid of your risk assessment and other information you have on the programme or the organisation that is to be audited, you shall formulate your terms of reference. In appendix 5, there are examples that you can use. However, it is important to bear in mind that these provide guidance. You yourself must consider whether there are any special circumstances that you should take into consideration. You can contact EVU/Ekonomi if you need advice and assistance.

## **2.6 Audits of consultants**

Consultants are used to a great extent in development cooperation activities. In this context, consultants includes both one-man companies and private or publicly owned companies, institutions and government agencies. Most of the consultancy services procured by Sida refer to participation in, for example, the planning, management and administration of projects. We also engage consultants for the recruitment of personnel, procurement and shipping of goods, and for different forms of evaluations.

Sida stipulates in its agreements that it may audit the activities of the consultants it engages. This is regulated in Sida's Standard Conditions for Short-term and Long-term Consulting Services 2002, section 11.12.

### **Sida's annual audits of consultants**

Each year the Head of the Department for Finance and Corporate Development approves a plan for the audit of a number of consultants. EVU/Ekonomi draw up the plan on the basis of proposals made by the sector departments. It is the controllers in these departments who propose suitable subjects for audits to the contact person at EVU/Ekonomi for audit matters. Thereafter, EVU/Ekonomi decides on the consultants that shall be audited and also finances the audits. The results of the audits are forwarded to the departments concerned and are evaluated together with the contact person for audit at EVU/Ekonomi. The audits made by EVU/Ekonomi supplement the examinations made by the departments.

The background to the need of additional controls in the form of these examinations is, among other things, that there are examples of consultants and partners in cooperation who have collaborated with each other, resulting in the misuse of development cooperation funds. Therefore, Sida make these examinations in order to verify that the administration of development cooperation funds, internal controls, accounting and invoicing of services performed by consultants are in accordance with the agreements that have been concluded and in accordance with generally accepted accounting principles in Sweden.

# 3 Read audit reports and follow up audits in this way

If the auditor makes an oral report on completion of the audit, you will have the opportunity to ask questions and request explanations of matters that appear to be unclear. Bear in mind that this does not make you appear to be unintelligent, it is necessary for you to take your share of the responsibility for the programme of cooperation. Sometimes, it is not possible to make a review of this type for reasons of cost or lack of time. The following section provides guidance on ways in which you can interpret the written report on your own.

## **3.1 What information can you obtain from the audit report?**

The information you can obtain from an audit report depends in the first place on what you have requested in the terms of reference. However, sometimes there is no clear specification of the aspects that shall be included in an audit. This is particularly the case when Sida and the partner in cooperation have agreed that Sida shall receive a copy of the regular audit of the annual accounts. This is often a standard audit, made in accordance with the rules and traditions in the country, for example the legislation governing what the state audit institution shall audit.

There are some (Anglo-Saxon) standard formats for audit reports, in which a great deal of space is devoted to descriptions of what the auditor has examined. This is normally a standard text that reminds the reader that an examination has not been made of all the documentation, that a sample has been made on the basis of materiality and risk, and that the auditor does not guarantee that he/she has noticed all possible errors (freedom from responsibility). Here there is usually also an explanation of the different roles of the company/organisation (in respect of its obligation to maintain accounts) and the auditor.

The most important sentence in the text is usually whether the auditor makes the assessment that the annual accounts have been drawn up in accordance with current legislation and are, in essentials, free from material errors, and provide a true and fair picture of the result and position of the activity. If the audit report does not contain any remarks (qualifications), it is referred to as an unqualified report. However, even if the report is unqualified, there can be serious errors and shortcomings. If there are any qualifications, you should be additionally attentive. If, for example, the auditor states that it has not been possible to perform the audit according to plan (since not all the documentation was available,

that there were systematic shortcomings in the accounts or internal controls, or that management was unwilling to cooperate), this is a clear warning signal.

In a regular audit you should be aware that the auditor has probably not examined risks of corruption or the observance of agreements unless the auditor makes the assessment that these areas constitute a special risk and therefore they should be given attention in the audit. On the other hand, examinations of this type are often included in the audits commissioned by Sida.<sup>5</sup>

In order to know what concrete observations the auditor has made that form the foundation for the statement on discharge from liability or true and fair accounts, you need access to other audit reports in addition to the audit report (the audit memorandum/management letter). Normally, for Sida to have access to such reports, it is necessary that this has been included in the agreement (shown in the agreement templates), or that the climate of cooperation is so good that they can be obtained without this being explicitly included in the agreement. These types of audit reports are formulated in a freer manner. They can contain a description of the observations made by the auditor and the recommendations for measures to be taken that the auditor considers justified. However, where public agencies are concerned, there may be legal rules that prevent the audit institution from providing such information.

If you feel that it is difficult to make up your mind in respect of the seriousness of the shortcomings that the auditor has pointed out in the report, you can contact one of the support functions to obtain advice. In some cases you may have received signals that something is not as it should be, despite the fact that the partner in cooperation has been given an unqualified audit report. In such cases you should consider having a special examination made of the risk areas.

## **3.2 Follow-up of audits**

### **Follow-up and action plans**

After the audit comes the important follow-up work. Discuss the report with the partner in cooperation and agree what you should do. Make an action plan that specifies who is responsible for different stages of the follow-up and the point in time by which corrective action shall have been taken. There can be reason to demand that the measures shall be taken before we make further transfers of resources. Make this clear and do it in writing.

Follow-up work creates opportunities to have a dialogue with partners in cooperation. In addition, it is possible to discuss experience gained from audits in connection with annual reviews, preferably in the presence of the regular auditor.

If the question of a follow-up audit arises, it is often appropriate for this to be done by the auditor who did the original audit, since he/she has valuable insight into the activity.

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<sup>5</sup> Read more on audits in cases where you suspect corruption in section 2.5.

# 4 Surveys and donor coordination of audits

## 4.1 Make a survey of audit capacity in this way

To be able to formulate clauses on controls and audit in agreements, you should be aware of the capacity and expertise that exists in the partner country in this field. It is partly a question of the audits of activities in the public sector that are made by the country's supreme audit institution, SAI. It also a question of the expertise possessed by private firms of auditors that Sida or an embassy may need to engage to examine non-governmental organisations or companies and – in some cases in consultations with the SAI – public organisations. Bear in mind that the fact that a firm of auditors is part of a major international firm is no guarantee of good work, but it often provides a certain degree of quality assurance. Embassies should make surveys, based possibly on the following questions:

- Is the audit independent?
- Does it have sufficient resources
- Does it use generally accepted auditing standards based on approved international standards?
- Is its expertise continuously developed?
- What is the normal content of terms of reference?
- What qualifications and experience does the auditor in question possess?
- How much time is usually allocated for an audit?
- Is the audit performed in close connection with the actual activity?
- What measures does it usually lead to?

Distinguish between what can be expected from a country's SAI and from auditors in the private sector. The terms of reference for a SAI are, in principle, the same as its mandate in the constitution or in the legislation. In many cases, this means that it only makes a traditional examination of figures and rules. However, sometimes a SAI can receive an extended mandate, for example to make a performance audit. These issues are usually covered in the Country Financial Accountability Assessment (CFAA) that the World Bank commissions in countries that have applied for debt write-off under the Heavily Indebted Poor Countries (HIPC) scheme. However, it is not certain that the study is based on long-term and deep knowledge of the country. You should therefore

supplement this with information from, for example, other bilateral donors.

The results of the surveys above can affect the content of the country strategies, particularly in respect of the question of budget support or sector programme support.

For more information, refer to the handbook Public Financial Management.

#### **DAC's basic requirements for the audit of development cooperation funds**

OECD's Development Assistance Committee (DAC) has established basic requirements for auditing: DAC's Harmonising Donor Practices for Effective Aid Delivery<sup>6</sup>, which Sida has adopted. These include a number of points that take up ways in which audits of development cooperation programmes should be made. Below a summary is provided of these requirements. You can use them as a checklist when you make a survey. Always consider the aspect of corruption when you engage a firm of auditors.

- Accept a country's Supreme Audit Institution for the audit of activities supported by Sida, provided that it has acceptable capacity and expertise. Donors should contribute support for capacity development if needed.
- Normally, you should make an evaluation of their capacity and experience before you use private firms of auditors.
- One single audit should cover control needs for both donors and recipients. Reach agreement on the terms of reference for the audit together.
- Ensure that audits are performed in accordance with generally accepted auditing standards. This means that the auditors either follow and international standard (INTOSAI or IFAC) or a national standard that does not deviate in essentials from the international standards.
- An independent audit, performed by a qualified auditor, ensures that the financial reports are reliable and that the donors' support has been used for the right purpose.
- When financial reports on budget support and sector programme support are concerned, the donors' needs of audits are normally covered by the audit made by the partner country's SAI (provided that it has acceptable expertise). If special projects or programmes are to be audited by the SAI, the partners in cooperation should have obtained the assent of the SAI before an agreement is concluded on the audit procedure.
- Decide on the terms of reference for the audit during the preparation stage of the project. They should contain a description of the project or programme, who will implement it, what accounting principles will be used, what reports are required, what the audit shall cover, and (where necessary), what requirements should be made of the auditor in respect of qualifications.
- Ensure that the audited annual financial accounts are submitted within an agreed period after the end of the financial year – four to six months is regarded to be of good standard. If the report covers all financing and if the agreement contains special financial conditions, all donors can normally expect that the auditors will report any breaches of the conditions of the agreement.

<sup>6</sup> Paper 5 – Financial Reporting and Auditing

- The auditor will express an opinion in the audit report. When the audit is complete, the auditor should also submit a management letter/ audit memorandum that describes any shortcomings in internal control. Even if these observations merely apply to the project or programme that has been audited, they often provide valuable information on the way in which the entire financial control system functions at the implementing organisation, for example in respect of systematic errors and shortcomings.

### **Donor coordination of audits**

Good experience has been gained of coordinating audits between donors. You can save money by avoiding duplication of work. Cooperating can have the effect that:

- the donors survey administrative systems etc together
- the donors make a thorough audit that covers the areas of cooperation of several donors in a sector. This can provide a better overview than limited isolated measures.
- the donors check that the same expenditure has not been reported to more than one partner in cooperation
- it is easier for the recipient to have one coordinated audit instead of several.

One risk with coordination is that a group of donors can be unacceptably dominant. Encourage therefore the recipient to take the initiative for coordination and then allow the recipient to be responsible for the management of control interventions and audit interventions in the programme of cooperation.

With coordination of audit work between donors, you place the emphasis on the whole rather than on the parts and avoid the traditional focus on examination of projects. Coordination can also lead to the donors developing a common approach in respect of their requirements for reports.

# 5 Support functions

Sometimes it can be difficult to know whether you need to take the initiative to have an audit performed. It can also be difficult to interpret the results of an audit. In such cases, it is reassuring to know that there are several support functions, both at Sida and at firms of auditors that Sida or the embassy have framework agreements with, that can provide advice.

## 5.1 Support at Sida

There are several functions at Sida that can provide good advice if you have any questions relating to audit.

- EVU/Ekonomi (Sida's focal point for audit issues):
  - has knowledge about audit issues in general
  - is responsible for the framework agreements with the firms of auditors
  - can provide concrete support in the formulation of terms of reference, contacts with firms of auditors, interpretation of audit memoranda etc
  - is Sida's contact vis-à-vis the Swedish National Audit Office.

The departmental controllers often have experience of different types of audits.

Sida's field controller has experience of audits at embassies/field offices.

Sida's Department for Internal Audit (UTV) knows all about auditing in general. UTV can also, in certain cases, support the departments, resources permitting, and if it does not affect the department's independence.

Sida's procurement advisers provide advice if an embassy wants to make a local procurement of audit services.

## 5.2 Firms of auditors as support

In development cooperation there are many examples of fields in which we can use auditors. Often other consulting services can also come into question. However, bear in mind that the auditor can certainly make proposals for ways in which Sida should act, but can never be responsible for the implementation of the actions! Nor may the auditor end up in a situation where he or she combines the role as an auditor and consultant,

which would disqualify him. Here are some examples of fields in which you can use the expertise of a firm of auditors.

#### **At country level**

- Survey of the partner country's administrative systems, for example budgeting, accounting and reporting systems
- Survey of the partner country's procurement rules and material administration, i.e. the entire procurement process from identification of the need and establishment of a specification of requirements to stores administration, final delivery and consumption.
- Corruption studies, i.e. studies of risks or existence of corrupt behaviour
- Survey of capacity and expertise in the audit field in the public and private sector.

The survey can include an assessment of whether the systems are appropriate and whether they are used in a correct and uniform way. A study of this type should serve as a basis for the country strategy work and for reaching a standpoint on suitable forms of cooperation, disbursement channels and transfers of resources, control structures and audit programmes. Document them in writing and design them pedagogically, taking into consideration the embassy's need of information for its daily work. Update them when necessary. Cooperate with other donors and preferably allow the partner country to coordinate the surveys.

#### **At contribution level or prior to an agreement with a partner in cooperation (including framework agreements with a non-governmental organisation)**

##### *Preparation*

- Capacity studies or a preparatory audit of the partner in cooperation's organisation, general and administrative capacity and skills, stability, structure, accounting system, reporting system, internal control system etc.
- Examination of whether the project proposals are reasonable
- Assessment of the needs of Sida and the partner in cooperation for reports, control structures and organisation for audit planning.

##### *Implementation*

- Regular examination of the partner in cooperation's financial quarterly, half-yearly and yearly accounts. However, note that it is not the consultant but the person who has the right to use the appropriation who takes a standpoint on the basis of an analysis of reports and recommendations. Document this in the contribution file.
- Examination of major procurements
- Forward-looking analyses of potential problem areas, audits prior to sector reviews
- Examination of the quality of internal reports and follow-up of project planning
- Examination of internal controls
- Providing advice and participating in training for capacity development purposes. Examination of implementing consultants

- Special audits in cases where there is suspicion of mismanagement, improprieties and corruption

*End of contribution*

- Final audit (for parts of the project period or the entire period since the start of the project)

**Other aspects**

Procurements of the services of firms of auditors in the private sector can also be made when a certain type of professional expertise is need temporarily, for example for

- education and training (for example in the field of financial administration or internal control) but not for specific government subjects in Sweden or in the partner country, since private firms of auditors rarely have sufficient knowledge about this
- examination of regular financial reports
- examination of internal controls in connection with decentralisation ambitions
- examination of the organisation of audit programmes initiated by the partner in cooperation
- examination of individual major procurements.

# 6 For those of you who wish to know more

## 6.1 Important concepts in auditing and accounting

Below there is a review of some technical terms and expressions in the audit field. The aim of the review is, among other things, to enable you to make specific choices when you commission audits.

### Materiality and risk

No auditor can examine all the material that is available in an assignment. Therefore, the auditor uses various types of methods to select the areas that are to be audited. The concept of materiality and risk is fundamental to all auditing. The auditor obtains a further foundation for the focus of the audit by making an analysis of, for example, the processes, systems and routines in the activities that generate financial transactions, as well as the views of management on ways in which these risks are met and the internal control measures that have been taken. In other words, materiality and risk are used to assess how the auditor shall structure the audit work and how extensive the audit should be. By taking generally accepted auditing standards into consideration (see more below), the auditor selects the audit methods that will be effective to achieve the purpose of the audit and provide a basis for statements. Materiality and risk are guiding principles in Sweden. However, various types of statistical selection methods are common in many of Sida's partner countries.

What is to be regarded as material is determined by the auditor from case to case. According to the Swedish Institute of Authorized Public Accountants (FAR), materiality is expressed in accordance with Swedish audit standards in the following way:

*Information is material if an omission or an error can influence the decisions the user makes on the basis of the information in the financial reports.*

Accordingly, the materiality concept usually refers to considerable amounts or values. However, in some cases even small amounts can be material, for example since they are important in principle.

*Risk* is defined normally as the probability of a negative event occurring which will have the effect that the organisation cannot achieve its goals. When the auditor plans an audit, and determines the audit method that is to be used, the auditor analyses important risk areas. These can be reporting systems, cash holdings, complicated contractual arrangements, administrative problems to which attention was drawn earlier, and so on. The auditor can make the risk analysis before you finalise the terms of reference and the focus of the audit. Otherwise the auditor does it himself in connection with the start of the audit.

### **Generally accepted auditing standards**

All auditing shall be performed in accordance with generally accepted auditing standards. FAR publishes auditing standards that can be considered to be generally accepted standards in Sweden. The standards shall be used in the audit of annual accounts and bookkeeping, and in the audit of administration by management.

Internationally generally accepted auditing standards for the public sector are created by the International Organisation of Supreme Audit Institutions (INTOSAI) and for the private sector by the International Federation of Accountants (IFAC). Generally accepted internal auditing standards are created by the Institute of Internal Auditors (IIA).

However, the application of generally accepted auditing standards can vary from country to country. Sweden's auditing standards are based on international standards, the International Standards of Accounting (ISA), issued by IFAC. By contacting FAR's counterpart in "your" country, you can find out what applies there.

### **Classification of auditors in Sweden and abroad**

There are a number of different types of auditors. In Sweden there are authorized public accountants and approved public accountants, internal auditors and accounting consultants who call themselves auditors, the auditors of the Swedish National Audit Office, the National Tax Board's auditors etc. The title of auditor is not protected, which has the effect that anyone can call himself an auditor. On the other hand, there are special requirements for those who call themselves authorised or approved public accountants:

#### *Authorised public accountant*

A person who fulfils predetermined (higher) requirements in respect of education, professional experience and suitability can be authorised by the Supervisory Board of Public Accountants for a period of five years at a time.

#### *Approved public accountant*

A person who fulfils predetermined (lower) requirements in respect of education, professional experience and suitability can be approved by the Supervisory Board of Public Accountants for a period of five years at a time.

#### *Internal auditor*

There are no official requirements in respect of qualifications but, since an internal auditor reports directly to top management in the organisation, management has an interest in ensuring that internal auditors have high levels of professional qualifications and experience.

It is difficult to compare auditors in different countries. What we call an auditor in Sweden is included in the wider concept of "accountant" in English. In addition to auditors, the group of accountants includes other qualified persons who work with accounting. The auditing functions are referred to as audit and auditors in the Anglo-Saxon countries. Where qualified auditors are concerned, there are the concepts of CA (Chartered Accountant) and CPA (Certified Public Accountant). There are many different designations and classifications of auditors in all the countries in which Sida has programmes of cooperation. This can lead to problems when you plan to engage local auditors. However, one basic

condition is that there should be a central certification organisation of one type or another that stipulates criteria in respect of the auditor's qualifications. You can find further information in each country's auditors' organisation.

*DAC's Harmonising Donor Practices for Effective Aid Delivery*<sup>7</sup> contains examples of what you should require of an auditor. In the terms of reference you should stipulate that the auditor must be impartial and independent in all respects where the auditee is concerned. The auditor must have experience of performing audits in accordance with current standards for ISA or INTOSAI (read more in section 6.1, International auditing standards), and of earlier audits that are comparable in size and complexity. The client shall receive the CVs of the proposed auditors. It should be evident from the CVs what audits the auditors have performed and any ongoing assignments.

If you intend to engage a foreign firm of auditors, it is important that you first try to obtain a picture of how the firm works. There is a form that can be used for this purpose in DAC's document.<sup>8</sup> Points included in the questionnaire are (in addition to basic information on the name of the firm, its address and licence) questions on its independence, any cooperation with other firms, quality assurance, composition of its staff, human resource development and so on. Read more about making procurements of firms of auditors in section 2.2.

### **Code of professional ethics for auditors**

There is a code of professional ethics for auditors. (There are special ethical rules for internal auditors.) Among other things, auditors shall behave in a professional manner and inspire confidence, be independent and not be engaged in activities that are incompatible with their role as auditors. They shall charge reasonable fees, observe professional secrecy, and apply generally accepted auditing standards in the exercise of their profession.

In addition to auditing, the auditor, by dint of his experience and broad accounting skills, often has an advisory role (similar to that of a consultant). However, this role is not part of the auditor's traditional auditing duties and may not be in conflict with requirements in respect of his independence. Read more in section 5.2.

### **International auditing standards**

A country's Supreme Audit Institution (SAI) issues standards for the audit of the country's leading bodies and agencies. Within the framework of cooperation in INTOSAI (International Organisation of Supreme Audit Institutions), agreement has been reached on international standards for the public sector.

For the private sector, there is ISA (International Standards for Auditing) which was set up by IFAC (International Federation of Accountants). However, what applies to NGOs in the partner country can vary and is sometimes regulated in national legislation.

Audits shall be performed in accordance with international standards. However, national standards should also be accepted if a legally constituted body has issued them.

<sup>7</sup> Note 8 Qualifications of an Auditor

<sup>8</sup> Note 6 Private Sector Audit Firm Application for Eligibility Questionnaire

### **International accounting standards**

The International Accounting Standards Board (IASB) issues international accounting standards (IFRS) for the private sector. This organisation replaced the International Accounting Standards Committee (IASC) which had issued international accounting standards up to 2001 that were designated IAS. Standards that have already been published will continue to be known as IAS in the future.

In the public sector, there is the International Public Sector Accounting Standards (IPSAS), which are published by the International Federation of Accountants/Public Sector Committee (IFAC/PSC). As opposed to INTOSAI<sup>9</sup>, which consist of the supreme audit institution in each country, IFAC does not have any formal status which gives the organisation the right to issue regulations for ministries of finance in sovereign states. On the contrary, public accounting is most often governed by the country's own laws. Now that donors, particularly multilateral donors (World Bank and IMF etc), have started to insist that recipient countries use IPSAS as a condition for debt write-off, loans or grants, countries often have, in practice, no other choice.

For most of Sida's partner countries, it is a question of "cash basis IPSAS" if the accounting is cash-based. This is intended for countries that base their accounting completely on payment transactions, but do not take into consideration the year to which the payments refer (expenditure-based or cost-based accounting). Since the standard is based on the private sector's (cost-based) accounting, it does not include important matters for governments, for example how taxes and grants received or debt write-offs shall be accounted for. It is in the process of being further developed.

### **Internal control**

The concept of internal control is used sometimes with different definitions. In Sweden, the Swedish Institute of Authorized Public Accountants (FAR) uses a definition that is based on the wording of the Swedish Companies Act and which is somewhat narrower than the definition (COSO) that has a considerable international impact, particularly after it was adopted by FAR's American counterpart, AICPA.

Internal control (according to COSO) is a process through which the company's board, management and other personnel obtain reasonable certainty that the company's goals are being achieved in the following areas:

- appropriateness and efficiency of operations
- reliability in financial reports
- observance of applicable laws and ordinances

To make an assessment of this, the auditor makes a review of the control environment, risk assessments, control measures, information and communication, as well as supervision and follow-up.

In Sweden FAR uses the following definition which is based on the wording of the Companies Act:

*Controls that the accounting, administration of funds and the company's financial situation in all other respects include the parts of the company's organisation and routines that ensure that the accounts are correct and complete, and that the company's resources (within the framework of the Companies Act, the articles of association of the company and any directives given by the annual general meeting) are used only in accordance with the intentions of the board and the managing director.*

<sup>9</sup> Read more under "International Auditing Standards"

Good internal control means, among other things, that responsibilities, powers and routines are allocated in such a way that the risk of errors or improprieties is minimised and that the accounts are correct and complete. It also means that the organisation's resources are used in accordance with the intentions of the board and management. This should be documented in descriptions of routines in order, for example, to guarantee secure administration of funds, appropriateness, thrift, observance of the rules, and efficiency. The descriptions of the routines state how, when and by whom different stages of the work shall be performed.

Internal controls are usually broken down into general controls (for example in the division of responsibilities, powers and work) and in routine-oriented controls (for example various control points, regular reconciliations, important accounts etc), which are included in systems and methods. This is done regardless of whether the controls are manual or computerised.

### **Control environment**

The control environment is the basis of internal control and checks. It specifies how the organisation views the importance of internal control. The control environment is affected by the management's integrity and ethics, responsibility and authority, organisation, staff policy, view on competence and actions.

### **Accountability**

Every organisation that administers funds has a responsibility to report on the use of its funds. This responsibility is referred to as accountability.

There are different types of obligations to maintain accounts and provide reports. We often associate the concept with financial accountability. However, there is a wider meaning of the concept which has the effect that a report shall also be made on whether goals have been achieved and on the measures the organisation has taken to achieve the goals. This aspect is often examined by the organisation making its own evaluations or by engaging an external consultant to make an independent assessment.

### **Professional secrecy**

Auditors are obliged to observe professional secrecy and may not pass on information that they acquire in their work. The only information that an outsider obtains is, in principle, the information that can be read in the audit report or the information contained in the written audit report on special audits commissioned by Sida. Nor may the auditor use his knowledge for personal gain. However, there are exemptions from the rules on professional secrecy – sometimes the auditor is obliged to disclose information, for example if a crime is suspected. This also applies, in principle, in other countries than Sweden.

## **6.2 Experience gained from audits**

Here we give some advice and examples of problems that can be worth thinking about in your practical work.

- Audit assignments that are given to Swedish auditors can be performed, with advantage, *together with local auditors*. The local auditors often have better knowledge of local languages, geography, government regulations (for example on procurements), administrative systems for budgeting, accounting and reporting, laws, common corrupt behaviour locally, skills profiles and knowledge of prices.

However, you should be aware that there may be a greater risk that the auditor does not act completely independently in relation to the auditee.

- *If agreements are worded imprecisely* in respect of the content of the reports to be made by the partner in cooperation and the form in which they shall be presented, there is a risk that the audit will be made difficult and the report will be of inferior quality.
- *It is often the case that only a financial audit is made* and not a management audit or a performance audit. This means that you will not receive information on the quality of the management function, on cost efficiency or on whether the activity is achieving the results the organisation has planned.
- *If you do not follow-up the partner in cooperation's reports*, and if there are no action plans or they are not followed up, there is a risk that audits will never be started.
- *Amendments to agreements must always be made in writing*. If changes are made in such a way that the agreement is applied in another way than what you have agreed in writing, this constitutes a breach of agreement. This happens both in respect of agreements with the partner in cooperation are concerned and agreements between the partner in cooperation and consultants. It reduces the credibility of the entire agreement and leads to uncertainty in respect of what really applies. It has the effect that the audit is made difficult to a considerable degree.
- It is a good idea if a preparatory audit or a corresponding examination is included as a step in the project preparations. For example, a study can be made of whether the accounting system is suitable for follow-up and control, i.e. whether the financial reports are compiled in such a way that budget follow-up and comparisons between resources used and results achieved are possible.
- It is an indispensable requirement that the *auditor is independent* of the auditee.
- If you have agreed that *the regular auditors* in a partner country or an organisation shall be *responsible for the audit* of a certain activity, this does not provide a guarantee that Sida's projects will be audited. This is due to the fact that audit is normally based on spot checks. If it is essential that a special area or aspect is audited, you should therefore make a special agreement with the regular auditors or initiate an audit yourself (in consultations with the partner in cooperation).
- An auditor can encounter many *practical problems* in connection with an audit. Possibly the personnel concerned are not willing to cooperate with the auditor, they feel threatened by the effects the auditor's observations may lead to for them, documents are dispersed or cannot be produced, and language problems can make contacts difficult and create misunderstandings. These problems can result in delays and make the audit more expensive. As the client you should therefore have a certain amount of long-term planning and make preparations wherever possible.
- Shortcomings in documentation and in internal control, a lack of order in the accounts or poor quality reports can make follow-up difficult and increase the risk that advantage is taken of the poor controls. Sometimes this can be a *sign of improprieties*. However, it is often difficult to find evidence for this. With the aid of regular audits

and follow-up audits, including examinations of budget outcome and outputs, you can minimise the risks and in some cases rectify the problems.<sup>10</sup>

- A weak internal control can *create temptations* for the personnel to undertake improprieties with possibly very serious consequences for them and their families when they are detected. In consideration of this, it is important to work for good internal control.
- Sometimes the *auditor's role is misunderstood*, which can create irritation and a negative attitude towards both the auditor and audits in general. If, for example, the auditor discovers something that is clearly a theft or embezzlement, the auditor shall call attention to this and present the facts that have emerged. On the other hand, it is not the auditor's responsibility to track down the thief or to investigate the embezzlement and try to recover the funds. It is the organisation being audited that shall report the matter to the police. It is true that an auditor can be engaged to make an investigation of this type, but this is an assignment outside than the original assignment, which possibility lies outside the traditional role of the auditor.<sup>11</sup>

### 6.3 Links to other organisations and documents

If you want to read more or if you need further support you can obtain more information from the following documents:

#### **DAC's Harmonising Practices for Effective Aid Delivery**

Sida has adopted the recommendations made by OECD's Development Assistance Committee (DAC) on how the world's development cooperation should be harmonised: *Harmonising Practices for Effective Aid Delivery*. The aim of the recommendations is to harmonise and coordinate the administration of the support provided by different donors in order to avoid an unnecessarily high workload for the recipient country. Where audit matters are concerned, the aim is to define an internationally accepted standard for audits. In turn this shall guarantee the reliability of the financial reports for both donors and recipients. In addition to this, the audit shall be able to examine whether the requirements stipulated by donors for the use of funds have been fulfilled.

By working with audit matters in the partner countries, it is hoped that it will be possible to contribute to improving capacity and quality where auditing is concerned.

You can download the recommendations from OECD's website ([www.oecd.org](http://www.oecd.org)). Paper 5 and the Technical Guidance Notes 5, 6, 7, 8 and 9 take up auditing.

### 6.4 Read more

Sida has produced the following documents in order to provide the staff with support. You will find most of them on Sida's Intranet. (The department in brackets is the department at Sida responsible for the document.)

- Audit at Sida (intranet under Support Functions)
- Financial handbook (EVU/Ekonomi)
- Acting on suspicions of corruption – a guide (Policy and Methodology Department)

<sup>10</sup> Read more on audits in cases where you suspect corruption in section 2.5.

<sup>11</sup> Read more on audits in cases where you suspect corruption in section 2.5.

- Manual for the application of Sida's anti-corruption regulation (Policy and Methodology Department)
- Audit guide for NGOs and their auditors (SEKA)
- Sida's Regulations for organisation, delegation of work and decision-making procedure (DG-secretariat)
- Sida's anti-corruption regulation (EVU/JUR)
- Sida's management of contributions in corruption-prone environments (Audit memorandum UTV, 2004)
- Sida's use of audits in development cooperation programmes (Audit memorandum UTV, 2004)
- Sida's Guidelines for Planning, Reporting and Audit (JUR)
- Sida's manual on development cooperation agreements (JUR)
- Sida's manual on procurement (JUR)

Suggestions for useful websites on the Internet:

- FAR            [www.far.se](http://www.far.se)
- OECD         [www.oecd.org](http://www.oecd.org)
- IIA            [www.theiaa.org](http://www.theiaa.org)
- IFAC          [www.ifac.org](http://www.ifac.org)
- INTOSAI     [www.intosai.org](http://www.intosai.org)

# Appendix 1

## Proposal for the content of terms of reference (ToR) for audits

This is a brief description of the headings and content of terms of reference for audits. The aim is to provide general guidance – this is not a template that works in all situations. *Include the points that are appropriate for the audit in question, and exclude those that are not applicable.* You may also need to add completely different points. It is important to bear in mind that many audits are unique and require their own terms of reference.

If it is a question of a regular audit, the auditor will plan the audit in accordance with generally accepted auditing standards. However, Sida may have agreed with the company or organisation that it should also commission the normal auditor to make a special examination based on Sida's request (special terms of reference). On the basis of this audit, the auditor can submit a special auditor's certificate or report.

The points below are based partly on the disposition in DAC's document *Harmonising Donor Practices for Effective Aid Delivery*, Note 7. See further there.

### **Background and aim**

Provide a brief description of the project or activity, for example what activities are being pursued, their goals, duration of the project/activity, the costs, the phase the project is currently in, special known problems, number of staff, turnover, number of offices, etc. The auditor should obtain a picture of the aim of the activity, both what it is expected to result in and its budget.

Also state the aim of the audit. Why is the activity being audited? Explain how the information the audit is expected to provide will be used. Has the audit been made necessary by special circumstances, for example suspicions of improprieties or mismanagement?<sup>12</sup>

Provide a brief description of the administrative routines for the specific programme of cooperation between Sida and the partner in cooperation (reporting procedures, disbursements etc). Have they functioned hitherto as intended and agreed?

### **Information on the partner in cooperation**

Describe the partner in cooperation that is responsible for implementing the activity, its address, telephone, fax number, website and general e-

<sup>12</sup> More specific information on ways in which terms of reference shall be written in cases where corruption is suspected can be found in Appendix 5.

mail address. What agencies, organisations or departments are involved? What mutual links do they have to each other? A brief summary of the administration of funds for the activity can also be included, together with information on how the financial information will be made available to the auditor by the partner in cooperation.

Other information that can be included here is (best obtained from the partner in cooperation):

- An organisation chart
- A list of administrators and contact persons responsible for accounting, financial management and internal audit. Information on how to contact them.
- A project description that includes the agreed budget for the activity, broken down into main types of costs, and information on how the activity is otherwise financed.
- A statement that a project evaluation (if one exists) will be made available to the auditor.

### **Accounting standards**

If possible, describe in brief the accounting principles followed by the organisation. State any deviations for that part of the activity that is to be audited. If International Accounting Standards (IAS) or International Public Sector Accounting Standards (IPSAS) are not followed by the organisation, this can also be mentioned.

### **Financial reports of the partner in cooperation**

Describe the procedure for financial reports. These are often cash-based reports (describe receipts and payments) for a project, but in some cases the reports can refer to revenue/expenditure or income/costs.

The financial reports normally cover a certain accounting period (calendar year, budget year, half-year) with a comparison against budget. Normally, the accumulated outcome from the start of the project is usually compared with the total budget (in cases of projects).

### **Available material**

Describe the type of material that is available for auditing and where it is kept. If the accounting or other types of information have been computerised, you should state the software that is being used since the auditor can need to make special checks of the software.

The agreement with the partner in cooperation should give the auditor the right to have access to relevant documents at any time, for example accounting records, agreements, minutes of meetings, bank statements, invoices, contracts etc. The auditor should also be given the opportunity to meet all employees at the unit concerned. If access of the auditor to the above is limited for any reason, this, and the reasons for it, should be clearly stated in the terms of reference.

### **Scope and focus of the audit**

The scope of the audit shall be specified in such a way that makes it clear what shall be examined, what is expected of the auditor, and how the report shall be structured, e.g., the report should result in recommendations in order of importance. For more concrete examples of aspects that can be included in financial audits and management audits, see appendices 1a-1b.

Examples of information that should be included:

- The type of audit that is to be made (see section 1.2).
- A financial audit should be performed in accordance with international audit practices (ISA or INTOSAI).
- State the period that is to be audited. Information can in certain cases be obtained from earlier audits, thus avoiding duplication of effort.
- State whether it is the entire organisation (partner in cooperation) that is to be audited, or a certain part of the activity or the organisation.
- If Sida's grants or payments are based on costs presented by the organisation, the audit shall include an examination of whether these costs correspond to what has been regulated in agreements.
- If a special bank account is used for Sida funds, the audit shall check that the balance of the account corresponds with unused funds as shown in the accounts.
- If the organisation being audited channels Sida funds further to other organisations, the auditor should check that these funds are audited at subsequent steps in the chain.
- If any point included in the terms of reference is not covered in the audit, this shall be evident from the auditor's report.

#### **Compliance with Funding Agreement Covenants**

The terms of reference shall specify if the auditor is expected to express an opinion on whether the partner in cooperation has fulfilled the requirements of the cooperation agreement. This section should include the following:

- A statement that the auditor will not be an arbitrator in any possible disputes between the donor and the recipient
- The agreement(s) that you want comments on, possibly through a reference to the sections and paragraphs in question.
- A copy of the current cooperation agreement – to be provided to the auditor.
- Copies of relevant correspondence between the parties involved – to be provided to the auditor.

#### **The auditor's report**

The terms of reference shall specify when the auditor shall submit his report after the completion of the audit. This section should include the dates when the draft report and the final report on the audit are to be presented. The auditor should be given guidance on the headings that are to be included in the report. If there are specific questions that you wish to have comments on or answers to, they should be specified here. As a minimum, the headings/subjects below should be included:

- Whether the report is an audit report (audited annual accounts) or an audit certificate (for part of the activity/year). Since an organisation's annual report is normally audited by its regular auditors, the examinations that Sida has commissioned are usually presented in the form of an audit certificate.
- Whether the report has a special purpose and what it is expected to be used for.
- The language the report shall be written in and whether it shall be supplemented with an oral report.

- The accounting standard that is used and the effect of any deviations from this standard.
- The audit standard that is used (INTOSAI or ISA, or national standard which, in all essentials, corresponds to them).
- Audited period
- If the audited financial report's appendices correspond with the accounting, receipts and other vouchers, and whether the funds have been used for intended purposes.
- If the report shall be submitted to other financiers or donors and the way in which it shall be presented to the partner in cooperation.

# Appendix 1a

## Content of terms of reference – financial audits

A list is provided below of aspects that can be included in the terms of reference for an audit under “scope and focus of the assignment”. (Appendix 2, which is a combination of 1a and 1b, is usually used.)

The auditor can examine whether the partner in cooperation’s routines and systems are appropriate and whether they are known and used in the organisation. The content is determined by the aim of the audit. Consider what you want to investigate/achieve. What is the correct level of ambition? The greater the scope and depth of the audit, the more expensive it will be.

### **Financial administration**

- Invoice procedures
- Payroll administration and other forms of remuneration, including taxes
- Payment channels and bank accounts
- Interest income and expenses
- Currency transactions, exchange rates and differences
- Administration of loans and advances
- Cash holdings, stores and stock, other assets
- Disposition of the chart of accounts and whether it corresponds to the disposition of the budget
- Regular bookkeeping
- Internal charges
- Cost allocation
- Accounting of assets and liabilities
- Reconciliation of bookkeeping accounts, bank accounts, cash books and stock lists
- Interim and final accounts
- Agreement between the accounts and reports to Sida
- Budget follow-up according to agreement
- Are there instructions and policies?
- Vouchers:
  - Completeness

- Quality of supporting documents
- Approved by authorised officials
- Reconciliation against the accounts

#### **Division of responsibilities and powers**

- Delegation of the right to make decisions, e.g. the right to use budgets and to approve payment orders
- Delegation of authorisation, e.g. right to sign cheques, agreements, contracts
- Routines for internal follow-up
- Corrective measures when errors are detected.

#### **Procurements**

- Drawing up specifications of requirements
- Initiations to tender
- Evaluations of tenders and decisions to make procurements
- Procurements of insurance and transportation services
- Preshipment inspection
- Special examinations of major procurements.

#### **Inventory and stock**

- Goods received routines, and stock-keeping and inventories
- Physical stock checks of goods over a certain value reconciled against registers, decisions to sell stock, depreciation and scrapping
- Are there instructions and policies?

#### **Follow-up audit**

- Assessment of the need to make a follow-up audit and, if so, drawing up proposals for the terms of reference.

# Appendix 1b

## Content of terms of reference – management audits

Can include an examination of the appropriateness of approved routines, systems etc and their application in respect of the aspects listed below. The content is determined by the aim of the audit. Consider what you want to investigate/achieve. What is the correct level of ambition? The greater the scope and depth of the audit, the more expensive it will be. (Appendix 2, which is a combination of 1a and 1b, is usually used.)

### **Agreements**

- Follow up of contractual obligations (including any changes) – financial and activity oriented – and of measures taken as a result of breaches of agreements (=compliance audit).

### **Plan of operations and budget**

- Operational planning (for different periods of time)
- Budgeting
- What budget documentation is produced
- How budgets are approved, follow-up, revised and agreed between the parties
- Integration in the government budget or in the organisation's overall budget
- Reconciliations of funds transferred to and received by the partner country, partner in cooperation, ministry and district or within/ between organisations
- Routines for reports on financial outcome and project implementation
- Audits of funds that are channelled further to other organisations
- Analysis of deviations between budgets and outcome

### **Vehicles**

- Follow-up of operating costs
- Checks of logbooks and authorised use.

### **Project activities**

- Financial reports and activity-oriented reports
- Checks that unused funds are returned from one part of the organisa-

tion to another or from other organisations that have had funds channelled to them.

- Follow up of consulting contracts and activities
- Checks that the project uses the administrative systems and rules of the partner country/organisation in respect of, for example, budgeting, accounting, procurements, follow-up and reports.
- Quality of documentation on which decisions for different activities are based.

### **Personnel**

- The capacity and proficiency of personnel in the management function, and in accounting, personnel and operating functions
- Assessment of the recruitment function
- Travel policy, for example mode of transport used and levels of allowances, and other aspects of cost efficiency
- Housing costs, for example clauses in housing contracts in respect of rent and maintenance, and operating costs
- How personnel mobility is handled in the light of, for example, HIV/Aids. Is there a personnel strategy?

### **Controls**

The role of management in respect of

- Controls and directives
- Audit planning
- Auditors engaged and terms of reference for audits
- Follow-up of audit reports and planning of actions to be taken
- How risk analyses have been made of control structures and audit planning

### **Documentation**

- Job descriptions
- Descriptions of routines
- Rules for internal control
- Procurement documentation
- Reports
- Minutes
- Safekeeping of important documents

### **Computer security**

- Back-up
- Electricity supplies, virus protection. Physical environment for hardware, passwords, communication etc.

### **Organisation**

- Organisational stability and structure in relation to the requirements of operations
- Division of responsibilities, powers and work
- Allocation of authorisations, for example in respect of signing on behalf of the organisation and signing cheques (authorisation list)
- Ways in which capacity studies are made.

# Appendix 2

## Example of terms of reference for financial audits and management audits

### **Terms of reference**

For audit of XX, for its work with XX in XX.

### **Background and objectives**

Since XXXX Sida has supported XXX for its work with XXX in XXX. XXX is also implementing similar programs in XXX as well as in XXX. In all, Sida has allocated XXX SEK for XXX activities since XXXX. Apart from this, Sida also finances agricultural components through XXX in XXX, which are partly connected to XXX financed by Sida but implemented by other organisations.

The overall objectives of the XXX are to recreate the civil society, to build peace and to support the return of refugees and IDPs (Internally Displaced Persons) in accordance with the Dayton agreement, and to support democratic development in XXX.

The programme includes providing building material to the beneficiaries. The majority of the projects are implemented through self help, but in some specific cases, assistance with construction is provided. The programs also include components of local infrastructure as well as employment creation, mainly within the field of agriculture.

Fill in with background information about the organisation, for example, no. of staff, location, etc.

### **Objectives**

In view of the large amounts of financing that have been provided for the XXX, Sida finds it important to perform thorough audits of some of the implementing partners in XXX. The Audit of XXX should ascertain that the Sida funds are handled in accordance with the agreement, and secondly the audit shall tell Sida whether XXX managerial and financial systems are in order and all Sida contribution is used according to the stated objectives. The Audit shall supply XXX with all sorts of advice and suggestions regarding the improvements to financial or management systems. The auditor shall also respond to XXX genuine needs and wishes to promote further capacity building within XXX.

## Assignment

The auditor shall make a financial and management audit of the XXX program.

The audit will be concentrated on either one financial year or a specific program, or a combination of both, which will be determined after discussions between the auditor and XXX. The audit shall also review the budget, accounting and reporting system used within XXX both in the office in XXX (where the financial management of the projects is handled) and in the office at XXX.

The auditor has the right to suggest changes to these Terms of Reference during the work. Any possible changes should be approved by Sida.

Special emphasis shall be given to the following areas (please reduce areas according to your risk assessment):

### *Financial Management*

- Have the Swedish funds been used for intended purposes stipulated in the agreement/s and in accordance with Sida's General Conditions and Guidelines?
- The overall structure and control of the financial management.
- The budget system at different levels, the accounting system, the handling of cash and the reporting systems regarding all this, taking into account that the work is performed in different geographical places.
- Handling of funds, transactions and access to the bank accounts
- The system for auditing at all levels regarding the organisation and its projects
- Does XXX budget system correspond to and is easily comparable or compatible with that of XXX?
- The follow-up of the financial management at XXX
- Payment of social fees and taxes for the employed staff
- Fixed assets register

### *Project Management*

- Are XXX annual reports and follow-up of the projects of satisfactory quality (including methods for risk assessment of the projects)?
- Is there a Project Management System (with methods for planning, coordination, management and control of implementation etc.) in place and used for the actual projects?
- Do the projects have work plans with time schedules for the activities which are followed?
- Adequate project accounting and the co-ordination between the project accounting and the general ledger

### *Human Resources Management*

- Employment contracts, job descriptions and the division of duties regarding the financial management and the projects.

### *Other Supporting Processes*

- Procedures for procurement and the accordance with Sida Procurement Guidelines and also the scope and content of agreements with suppliers
- The filing system and its reliability regarding accounting and project materials

**Visits and Reporting**

The auditor shall visit XXX and XXX. The auditor shall also study relevant material and meet Sida-staff at Sida-Stockholm and Sida-XXX.

The report shall not exceed 30 pages, be written in English and submitted to Sida in two printed copies and one digital, within three weeks after the last visit.

A copy shall be sent to (lotta.sando)@sida.se (focal point for audit).

The autor shall make recommendations to address any weaknesses identified. The recommendations should be presented in priority with a suggested timing for implementing.

**Organisation, Time schedule and Budget**

It is estimated that the audit will be performed by XXX by XXX, XXX with support from XXX and XXX. A total of XXX hours should be allocated altogether.

Budget – see contract – will not exceed SEK XXX out of which SEK XXX for fees and SEK XXX for reimbursables and reserve time.

# Appendix 3

## Example of terms of reference for systems-based audits

### **Terms of reference**

Systems-based audit of XX

#### **Background**

Sida is facing growing demands in respect of efficiency and performance reports in its programmes of development cooperation. Within the framework of its responsibility to exercise controls, Sida has the assignment of following up that development cooperation funds are used efficiently for intended purposes, regardless of how the funds are channelled. Sida's basic approach in respect of ownership of contributions has the effect that the partner in cooperation is responsible for implementation. This has the consequence that partners in cooperation also have the responsibility for exercising controls of operations in their administration.

To enable Sida to follow up whether the frame organisations are able to fulfil their contractual obligations vis-à-vis Sida, Sida has decided to make regular systems-based audits of the organisations with which Sida has framework agreements on grants from the popular movement appropriation.

Important documents for Sida in its assessment of the activities of frame organisations are their documentation in the form of annual accounts, operational plans, applications etc. A systems-based audit has the aim of analysing whether the organisations' internal management and control systems guarantee the quality and accuracy of this documentation and, at an overall level, of evaluating whether the organisations have appropriate systems and routines for steering their organisations towards operational goals and contributing to the fulfilment of the goals of Swedish development cooperation. The ambition is to achieve better quality in applications and the follow-up of performance, greater efficiency in the organisations, and better cooperation between the organisations and Sida.

Sida and XX have agreed to make a systems-based audit of the XX in 200X.

#### **1 System-based audit and capacity study**

Earlier Sida has made so-called capacity studies of the frame organisations. The borderline between a capacity study and a systems-based audit can be difficult to draw and overlapping in some areas is inevitable.

In general it can be said that:

- Capacity studies have a broad and overall focus and examine goal fulfilment, planning administration, and resources for determining the quality of the development cooperation activities pursued by the organisation.
- System- based audits have a narrower and more penetrating focus and analyse how the organisation works (instead of with what) by examining routines and systems in the organisation that guarantee reliability in its work and its reports.

## **2 Aim**

The aim of a system-based audit is

- to examine the reliability and relevance of the systems for operational and financial controls that exist in XX;
- to determine, on the basis of the examination, whether the documentation that is received by Sida under current agreements reflects the real situation and can therefore be considered to function as reliable data for Sida in the administrative process;
- to give XX basic information for its future work with change.

## **3 The assignment**

The system-based audit shall include the entire organisational chain in XX, i.e. the home organisation and its activities in the field. Cooperation with XX shall also be included in the audit. The assignment therefore includes visits to XX???

The assignment includes a survey in which routines and systems for operational management and control, and for financial management purposes are to be documented and analysed. In addition to this, the consultant shall submit recommendations in respect of improvements to operational management and control at XX. The consultant can, after obtaining the agreement of Sida, also include or exclude certain aspects in order to guarantee a feasible and qualitative study.

### **3.1 Survey and documentation**

#### *3.1.1 Management and control of activities*

In the survey of systems and routines for the management and control of activities, the following shall be documented:

- XX's mandate
- Organisation and ways of working
- Selection of partners in cooperation
- Operational planning
- Goals
- Assessment of contributions
- Follow-up of contributions
- Reports on deviations
- Evaluation
- Feedback
- Decision-making procedures

### *3.1.2 Financial management*

In the survey of systems and routines for financial management and control, the following shall be documented:

- Agreements and follow-up of contractual obligations
- Authorisations
- Transfers of funds and bank and cash holdings
- Budgeting
- Audits in all parts of the organisation, quality of audit certificates
- Project management systems and chart of accounts
- Promotion of good administration, transparency in the administration of funds, and counteraction of corruption.

### *3.1.3 Other aspects which Sida and XX wish to have described*

- XX's systems and routines for procurements
- The view of XX's auditor on the audit of framework grants from Sida.

## **3.2 Analysis and assessment**

Analysis and assessment of the surveyed aspects with regard to reliability and relevance and a general assessment of XX's reports to Sida and communication in its own organisation. The analysis shall also include XX's organisational structure and the dimensioning of this structure in relation to its functions and duties.

## **3.3 Recommendations**

The assignment shall result in recommendations and an action plan in respect of the above-mentioned points. The focus of the systems-based audit is XX's organisational structure, and its systems and routines for fulfilling its contractual obligations vis-à-vis Sida. In addition to this, the consultant is free to include recommendations that can be considered to be of relevance for promoting the aim of the systems-based audit.

The autor shall make recommendations to address any weaknesses identified. The recommendations should be presented in priority with a suggested timing for implementing.

## **4 Performance of the assignment**

The person responsible for the assignment shall be a consultant who is approved by XX and whose services have been procured by Sida. The consultant shall have the support of contact persons at XX and Sida.

## **5 Method**

The assignment shall be performed through studies of available documentation, first and foremost at XX and Sida, and relevant documentation at XX's partners, and also with the aid of interviews of personnel at XX, XX's auditor and Sida. All other matters relating to the definition of methods for the implementation of the assignment are the responsibility of the consultant.

## **6 Time schedule**

The objective is that work shall begin no later than 200X-XX-XX and that the final report shall be submitted to Sida no later than 200X-XX-XX.

## **7 Contacts with Sida and reports**

### **7.1 Contacts with Sida**

In order to ensure that the report constitutes a good basis for improvement to the greatest extent possible, the following contacts shall take place with XX and Sida:

- when the first survey of available material has been made, the scope of the systems-based audit shall be discussed with XX and Sida in order to determine what is reasonable within the given time frame and where the focus should lie;
- before the final report is submitted, a draft report shall be presented at a seminar for XX and Sida.

### **7.2 Reporting routines**

The assignment shall be presented in a written report and submitted to Sida in electronic form. With the aim of making it possible to comment on any factual errors and misunderstandings, a preliminary draft final report shall be submitted to XX and Sida no later than 200X-XX-XX. The final report shall be submitted to Sida no later than two week after Sida and XX have submitted their comments and points of view. The report should result in clear recommendations that are prioritised in order of importance. The recommendations should also include an indication of the latest time by which they should have been implemented.

### **7.3 Format and disposition of the final report**

The disposition of the final report shall mainly follow the terms of reference, point 3. It shall be written in Swedish and not exceed 50 pages, excluding appendices. The final report shall also be summarised in English, not exceeding 10 pages.

The report shall be written in XX. With the aim of simplifying corrections and printing, Sida shall also have access to the report in electronic form. One copy should be sent to (lotta.sando)@Sida.se (focal point for auditing questions).

### **7.4 Presentation/debriefing**

As part of the assignment, the consultant shall make two presentations of the final results.

- For the joint working group of representatives of XX and Sida<sup>13</sup>
- In the form of a half-day seminar for XX's employees and for Sida

## **8 Other aspects**

At the request of XX or Sida, the consultant shall make himself available for discussions of recommendations and conclusions.

For Sida's human resource development purposes, it shall be possible for personnel from Sida to participate in the work of the audit, including participating in visits.

Personnel from XX shall be given the opportunity to participate in the consultant's field visits and his visits to XX.

<sup>13</sup> The working group consists of the persons at XX and Sida who have worked together on the systems-based audit (terms of reference, field visits, contacts etc).

## **9 Specification of requirements**

- 1) Tenderers shall specify the leader of the assignment
- 2) Tenderers shall specify the level of knowledge that is offered in Swedish and English in speech and writing and in other languages for the personnel/sub-consultants allocated to the assignment.
- 3) Tenderers shall specify the total cost of the assignment, in the form of an hourly fee for each category of personnel, reimbursable expenses and any other costs. All types of costs shall be given in SEK, excluding VAT.
- 4) Tenderers shall submit a time schedule for the assignment.

## **10 Requests**

- It should be possible to conclude a contract that enters into force not later than 200X-XX-XX.
- It should be possible to start the assignment no later than 200X-XX-XX.

# Appendix 4

## Example of terms of reference for capacity studies

### Terms of reference for a capacity study of XX

#### 1 Introduction

The Swedish International Development Cooperation Agency (Sida) is responsible for Swedish bilateral development cooperation. Sida is also responsible for most of Swedish cooperation with countries in Africa, Asia, Latin America and Europe. The overall goals of Swedish development cooperation are to contribute to reducing poverty, increasing democratisation and sustainable development in the partner countries (see Sida's website: [www.Sida.se](http://www.Sida.se)).

Sida's Division for Humanitarian Assistance (SEKA/HUM) administers Swedish humanitarian assistance. This activity is pursued on the basis of the vision of making it possible for poor and vulnerable people to live in peace and to regain and maintain control over their lives. SEKA's operations are permeated by the following points of departure:

- that poor and vulnerable people can make their voices heard through cooperation and organisation, and that their fundamental rights and privileges must be taken into consideration and protected. Humanitarian and development contributions shall supplement and develop the knowledge and resources available locally,
- that the engagement and work of Swedish and international organisations play an important role in humanitarian and development cooperation,
- that the popular movement and democratic foundation of the Swedish adult education tradition are important components in the development and consolidation of local organisations in the partner countries. This is a step in the process of strengthening a vibrant civil society and human rights,
- that a conflict perspective must be applied by the organisations that plan contributions and that the contributions should have the ambition of preventing or solving conflicts.

The basic policy documents for Sida's humanitarian work include Sida's strategy for conflict management and peace building, humanitarian assistance with a child rights' perspective and developmental humanitarian assistance.

## **2 Background to the capacity study**

Sida is facing growing demands in respect of efficiency and performance reports in its programmes of development cooperation. Within the framework of its responsibility to exercise control, Sida has the assignment of following up that development cooperation funds are used efficiently for intended purposes, regardless of how the funds are channelled. Sida's basic approach in respect of ownership of contributions has the effect that the partner in cooperation is responsible for implementation. This has the consequence that partners in cooperation also have the responsibility for exercising control of operations in their administration.

SEKA/HUM's cooperation with Swedish NGOs is based to a great extent on trust, which requires follow-up for effective controls and to gain the confidence and trust of the general public. SEKA/HUM places an emphasis on following up the activities of the organisations and their ways of running programmes of support. The ambition is to achieve better quality in applications and in the follow-up of performance, greater efficiency in the organisations, and better cooperation between the organisations and Sida.

### **2.1 Description of the organisation to be studied**

The description of the organisation to be studied can include, for example:

- Organisation structure including any offices abroad
- How the organisation is run
- The aim of its operations

## **3 Aim of the study**

The aim is to study the quality of XX's development cooperation activities. The capacity study will analyse the organisation's work by examining and analysing routines and systems in the organisation that are intended to ensure reliability in its work and reports. The borderline between a capacity study and a systems-based audit can be difficult to draw, and overlapping in some areas is inevitable. In general it can be said that:

- Capacity studies have a broad and overall focus and examine goal fulfilment, planning administration, and resources for determining the quality of the development cooperation activities pursued by the organisation.
- Systems-based audits have a narrower and more penetrating focus and analyse how the organisation works (instead of with what) by examining routines and systems in the organisation that ensure reliability in its work and its reports.

The main goal of the study is to facilitate Sida's future assessment of XX as a channel for humanitarian and development-oriented support.

The study is also intended to function as a tool for XX's own future organisational development.

## **4 The assignment**

The main focus of the study will consist of an analysis of the organisation's internal management and control systems (both formal and informal) in order to see whether they can guarantee quality and accuracy in all parts of its operations and, at an overall level, to evaluate whether the organisation has appropriate systems, proficiency, capacity and routines to direct its activities towards stipulated operational goals and contribute to the fulfilment of the goals of Swedish development cooperation.

Furthermore, the consultants shall analyse XX's implementing capacity. The study shall cover the entire organisational chain in both Sweden and the field. The assignment shall be based on a survey of documentation in all parts of the organisation, its management and controls, its analyses and methods, and shall result in recommendations.

#### **4.1 Survey and documentation**

##### *Organisational structure*

- Description and analysis of
  - the purpose of forming the organisation
  - number of employees, members, organisational base etc
  - analysis of organisational development at XX

##### *Management and control of operations*

- Systems and routines for, and documentation of:
  - the mandate and role of the organisation's board
  - decision-making
  - delegation system
  - visions, goals, plan of operations and policies
  - operational planning
  - measurement of results, evaluation
  - follow-up, controls of contributions
  - initiation of new projects/expansion of existing activities
  - phasing out of projects
  - cooperation with other organisations
  - organisational networks (local, international, formal and informal networks)
  - reports on deviations from plans
  - feedback
  - institutional learning.

##### *Financial management*

- Systems and routines for, and documentation of:
  - agreements and follow-up of contractual obligations
  - transfers of funds and bank and cash holdings (for example routines for exchange rate differences)
  - budgeting
  - promotion of good administration, transparency in the administration of funds and counteraction of corruption
  - audits in all parts of the organisation.

##### *Other aspects which Sida wishes to have described*

- Systems and routines for, and documentation of:
  - procurements
  - safekeeping of important and valuable documents
  - registration and archives
  - personnel policy
  - recruitment and selection procedures

- forms of employment, employment rules, pay systems
- human resource development
- security solutions for personnel in the field.

#### **4.2 Method**

The assignment shall be performed through studies and analyses of available documentation. Moreover, interviews shall be held with personnel at the organisation being studied and personnel involved at Sida, as well as auditors concerned. In the field, partners in cooperation, for example XX, shall be interviewed. All other matters relating to the definition of methods for the implementation of the assignment are the responsibility of the consultant.

#### **4.3 Analysis and assessment**

In the light of the information acquired, the study shall analyse and assess the aspects that have been surveyed in respect of reliability and relevance, and a general assessment of XX's reports to Sida and communication, controls and delegation in its own organisation. The analysis shall also include XX's organisational structure and the dimensioning of this structure in relation to its functions and duties.

### **5 Recommendations**

The assignment shall result in clear recommendations in order of priority and ought also include an indication of the latest time by which they should have been implemented.

### **6 Performance of the assignment**

The person responsible for the assignment shall be a consultant whose services have been procured by Sida. The consultant shall have the support of contact persons at XX and Sida.

#### **6.1 Time schedule**

With the aim of making it possible for any factual errors and misunderstandings to be commented on, a draft version of the final report shall be submitted to Sida no later than 200X-XX-XX. The final report shall be presented to Sida no later than 200X-XX-XX.

### **7 Report**

A written report shall be made on the assignment. The report shall also be submitted to Sida in electronic form. One copy should be sent to (lotta.sando)@Sida.se (focal point for auditing questions).

#### **7.1 Format and disposition of the final report**

The disposition of the final report shall mainly follow the terms of reference (see sections: Aim and the assignment). It shall be written in Swedish and not exceed 70 pages, excluding appendices. The final report shall also contain a summary in English (of approximately 35 pages excluding appendices).

#### **7.2 Presentation**

As part of the assignment, the consultant shall make a presentation of the final results to personnel concerned at Sida and personnel concerned at XX and its board. The presentation shall be made at Sida in Stockholm.

At the request of XX or Sida, the consultant shall make himself available for discussions on recommendations and conclusions.

## **8. Requests**

8.1 It should be possible to conclude a contract that enters into force not later than 200X-XX-XX.

## **9. Other aspects**

For reasons of Sida's human resource development it shall be possible for Sida personnel to participate in the work as observers, and to accompany the consultant(s) on visits in Sweden and in the field.

# Appendix 5

## Example of terms of reference in cases where corruption is suspected

The examples provided below are intended to function as a form of support when terms of reference shall be produced. Examples are provided of areas in which corruption is common, as well as suggestions for the type of audit and actions that can be included in an audit. Standard texts are also provided that you can copy into your terms of reference. The examples complement the general template of the items that should be included in terms of reference in appendix 1.

### **1 Background**

The background can normally be formulated in a similar way for all audits, regardless of their purpose. However, in special cases of suspicions of improprieties, it can be important not to disclose the specific suspicions in the terms of reference. Instead the terms of reference should be formulated as a general financial audit.

### **2 Aim and scope of the audit**

In cases of suspicion of corruption, you should make an integrated assessment of the risks based on your general knowledge of the programme or organisation. In order to determine the scope of the audit, it is important to specify the period of time that shall be included in the audit and whether there are specific, well defined areas that should be covered by the audit.

#### **Overall questions**

1. The audit has the aim of determining whether improprieties have occurred in respect of....
2. The audit shall examine the accounts of the programme for the years (specify years).
3. Examine that the agreement between Sida and the organisation is being followed.
4. Examine that the internal controls for the programme are satisfactory.
5. Examine that the rules in Sida's general conditions are being followed.
6. Examine the routines for procurements and the organisation and personnel in the purchasing department.

Depending on the results of your risk assessment, the areas that shall be the subject of a special examination are then decided.

One often-used expression is: *special attention shall be given to the following aspects.*

Some of most common areas where improprieties occur in accounting are listed below, together with the examinations that should be made to identify possible errors.

### **Cash or bank**

It is not uncommon that improprieties occur through shortcomings in the accounting and controls of cash and bank holdings. In many countries cash payments are much more common than they are in Sweden. The risk of improprieties occurring increases when large amounts of cash are handled. It is not uncommon that money is stolen from the cash in hand or taken from bank accounts. This is then concealed by various types accounting transactions, which can be sophisticated to a greater or lesser degree.

### **Cash and bank – points that should be examined**

1. Examine all vouchers in order to ascertain whether there are any transactions that lack real supporting documents.
2. Make a reconciliation of all bank accounts against the bank statements and against the accounts.
3. Request a statement of commitments and deposits from the bank in order to confirm the bank statements of the programme or organisation.
4. Examine the transactions on the bank accounts in the general ledger and note any unusual transactions.
5. Check the receipts and payment journal. Note and check any unusual transactions.
6. Check the liquid resources by tracing movements in the accounts to statements from the bank.
7. Compare deposit slips with the cash book (or equivalent) in respect of dates, persons making the deposits, amounts and the accounts the deposits refer to.
8. Investigate abnormal delays in deposits of any checks or items of value.
9. Check that cash books have been tallied correctly.
10. Document the number sequence of payment orders used during a certain period of time.
11. Check that payments made refer to goods and services that have been ordered and supplied.
12. Check that all receipts and payments have been approved.
13. Check that no double payments have been made, for example of suppliers' invoices or wages.
14. Check which persons who have had access to the organisation's cash holdings, cheques, revenue receipts, power of attorney, passwords and the like.

### **Bookkeeping/accounting**

Improprieties in connection with an organisation's bookkeeping/accounting can be of different types. With the aid of incorrect bookkeep-

ing, attempts can be made to conceal that funds or assets have been incorrectly appropriated from the organisation, or that funds have been used for expenditure for illicit purposes. If Sida, for example, has approved that a certain amount may be used for the purchase of books and the money is used instead to purchase petrol, the transaction is nonetheless recorded as the purchase of books.

### **Bookkeeping/accounting – points that should be examined**

1. Examine all vouchers (or make a spot-check of xx%) in order to check that it is possible to verify the transactions in the accounts against receipts or other forms of supporting documents.
2. Check that the transactions in the accounts have actually taken place. Check, for example, goods and services that have been ordered (according to purchase orders etc) against suppliers' invoices.
3. Make a reconciliation of all bank accounts against the bank statements and the accounts.
4. Check that vouchers have only been recorded once in the accounts.
5. Check that only business events relating to the business have been recorded in the accounts.
6. Check that the voucher number series is unbroken.
7. Check amounts recorded in the accounts against amounts shown on suppliers' invoices.
8. Check that all vouchers are certified/authorised for payment by persons authorised to do so.
9. Check "abnormal" amounts on each account.

### Questions:

- How is it possible to check that everything has been recorded in the accounts?
- Are there routines to ensure that items recorded in the accounts cannot be erased or made illegible?
- Is there an instruction for the filing of documents and is it followed? Is it kept up-to-date?

### **Procurements**

Procurement is a risk area where corruption is concerned. There are several ways to swindle an organisation. An organisation can, for example, receive an invoice for the delivery of three articles, but in fact only two articles are delivered. The procurement rules are not followed since the organisation does not use the cheapest supplier. The person responsible for purchasing can inform a supplier about the offers made by other suppliers and this supplier can then submit the lowest offer. It is often impossible to detect these types of improprieties through individual audit steps. What is necessary here is an in-depth analysis of all the routines and the proficiency of the persons responsible for purchasing.

### **Procurements – points that should be examined**

1. If there are written routines for procurement: check that these have been approved by Sida or that they follow Sida's procurement rules.
2. Check that procurements have been made in accordance with written routines for procurement (Who has the right to make decisions, up to what amount?)

3. Check, by making a review of procurements, that the procurement rules are being followed and that all decisions are made in accordance with the rules.
4. Check how the person responsible for procurement has been given this responsibility and the suitability of the experience and qualifications of this person.
5. Check that the person making the decision has acted within his authority (powers).
6. Check how the estimate of the value of the procurement has been made. (In the calculation of the value of the procurement, the value of all products and services are to be included, for example service costs, training costs etc. In the calculation of the value of the procurement, options given and any possible prolongation of the agreements shall also be included.)
7. Check that the procurement has been advertised.
8. How are the requirements that shall be made of the supplier determined?
9. How do direct procurements take place, are price comparisons made?
10. Check goods and services in respect of quality and quantity, against both delivery notes and orders.
11. Check how many similar goods/services have been purchased from the same supplier by obtaining information from the accounts.
12. Check the tender documents, how many tenders were invited.
13. Check the purpose of the procurement and the scope of the goods and services that shall be procured against underlying documentation.
14. Check that only those tenders received during the tender period were examined.
15. Check who was present when the tenders were opened. (Tenders shall be opened on an occasion when at least two members of the unit making the tender are present. The tenders shall be entered on a specification that shall be certified by those participating.)
16. Check that the reasons for accepting the tender have been based on the underlying documentation.
17. Check that the agreement contains information on:
  - Date, designation of the tender, name of supplier
  - Description of the assignment, scope, quality etc
  - Description of the resources that shall be made available and the name(s) of the person(s) who shall perform the work (services).
  - The amount that shall be paid and the ways in which reports and follow-up shall be made,
  - Prolongation of the agreement, disputes and penalties, options and secrecy, indemnity insurance and force majeure.

### **Payments**

Making payments to unauthorised persons is a way of misappropriating money from an organisation. The most common method is to present an improper document (double invoice, false invoice etc).

### **Payments – points to examine**

1. Examine all vouchers in order to ascertain whether there are any transactions that lack real supporting documents.

2. Make a reconciliation of all bank accounts against the bank statements and against the accounts.
3. Request a statement of commitments and deposits from the bank in order to confirm the bank statements of the programme or organisation.
4. Examine the transactions of the bank accounts in the general ledger and note any unusual transactions.
5. Check that payments have been recorded in the correct accounts.
6. Check that the payments account has been tallied correctly.
7. Check that payment orders have been signed by a person authorised to do so, and examine the signature on the payment orders.
8. Check that the persons authorised to use the bank account have not exceeded approved limits.
9. Check the number sequence of payment orders used during a certain period of time.
10. Check suppliers' invoices against the payments book.
11. Check orders for goods and services (on purchasing orders etc) against suppliers' invoices.
12. Check the documentation for goods or services received with suppliers' invoices.
13. Check that payments have only been made for approved purposes.
14. Check payments book with payment orders in respect of dates, recipients, amounts etc.
15. Assess the reasonableness and business concept in respect of the goods purchased and their quantities.
16. Check that payments have been recorded in the accounts as payments.
17. Check payments in the payments book against supporting documents.

Questions:

- How are payment transactions protected against being changed before and during transfer to the bank?
- Are there special checks of the approval of large payments?

**Advances**

Advances are a common way of misappropriating funds from an organisation. Advances are often common in activities run by organisations. To enable staff to travel, they need an advance. Where purchases are considered, it is essential that, if goods are to be delivered, a large part of the purchase price, or the entire purchase price, must be paid in advance. The most common misuse of advances is that they are never paid back or accounted for. In order to avoid misuse or abuse, it is extremely important to have definite rules for payments of advances, for the period of time an advance may remain unaccounted for, and that there is a good system for follow-up to ensure that the rules are followed. If cases of misuse or abuse arise, there are shortcomings in one or more of the above-mentioned points.

**Advances – points that should be examined**

1. Examine all advances in order to verify whether there are advances that have exceeded stipulated time limits.

2. Examine advances given against the rules for size of advances.
3. Examine that the accounts for travel advances corresponds to the organisation's rules and that the accounts contain all the documents that verify that advances have been used for their intended purposes.
4. Examine that the organisation has a separate ledger for advances and that the total amount corresponds to the amount recorded in the general ledger. Note and document unusual transactions.
5. Check that advances paid out have been recorded on the correct account.
6. Check that requests for advances have been verified by the person(s) authorised to do so.

#### **Allowances and other forms of remuneration**

These types of payments often act as an important addition to normal wages. Therefore, these payments can be misused/abused. Common ways of obtaining extra payments can be to:

- State on the travel claim that one has been away for more days than has actually been the case.
- Invent a journey that has not been made.
- The travel claim contains expenses that have not been incurred, for example that, according to an attached invoice, a business class ticket has been purchased but in actual fact this ticket has been exchanged for a ticket in economy class.
- The travel claim contains items without supporting documents.

In order to deal with these types of improprieties, a detailed examination must be made of vouchers and other supporting documents.

#### **Allowances, wages and other forms of remuneration**

##### **– points that should be examined**

1. Make an analysis of all advances. Check whether there are any advances that are older than approved time limits and that advances that have been paid do not exceed the maximum amount.
2. Check recorded advances by ensuring that all receipts are included and are correct.
3. Check that journeys made have been approved and verified by the person(s) responsible.
4. Check the purpose of the journey and whether this seems reasonable in view of the activities of the organisation.
5. Check that no unauthorised person, for example relatives or friends, have accompanied the member of staff on the journey. An examination can be made of train tickets, air tickets, and hotel bills.
6. Check that allowances have been calculated correctly.
7. Check that payment has been made for the correct number of days.
8. Check that no compensation has been given for private expenses.
9. If written instructions exist, check that these have been followed, for example that air tickets/hotels/other forms of transport are not of a more exclusive type than is permitted (for example business class), and that the journey has been booked at the correct travel agent.
10. Check, for example, that the employee has not exchanged an expensive air ticket for two cheaper tickets.

11. Advances in respect of purchases are checked by ensuring that purchased goods physically exist, and are recorded in fixed asset registers or similar.
12. Check that purchases have been made in accordance with the organisation's procurement rules.

#### **Salaries and wages**

1. Check wage payments against underlying agreements.
2. Check that only employees receive wages.
3. Check that employees only receive one wage payment each month.
4. Check who sets wage levels.
5. Is the wage reasonable in comparison with other employees in similar positions?
6. Examine what other benefits are received by employees – are they reasonable?
7. For hourly paid employees, check that number of hours paid for against the number of hours worked.

#### **Employment/appointments**

Giving preferential treatment to relatives and friends is not uncommon in connection with new appointments. However, it can be difficult to show that the wrong person has been employed without making an analysis of the routines used in the employment procedure. In addition, an evaluation must be made of the candidates who applied for the position. It is only when this has been done that it can be determined whether the right person has been given the job.

#### **Employment/appointments**

1. Are there guidelines for the employment procedure?
2. Are there documented requirements respect of experience and qualifications that apply to the post that is being examined?
3. How are the qualifications considered necessary for the post determined?
4. How was the post advertised?
5. Have all applications received for the post been registered and filed in an acceptable manner?
6. Is there a summary of all applicants and the method used for the selection process?
7. How many applicants were called for interviews and can these persons have been ranked as those who were apparently the most highly qualified?
8. Is the new employee in possession of the qualifications that were considered necessary?
9. Has the new employee been given a wage and other conditions that correspond to the advertised conditions?

### **3 Expected results of the audit**

You are welcome to define what you wish to gain from the audit. This minimises the risk that the firm of auditors and Sida have different conceptions on the scope of the audit. Read more in appendix 1 in the section on Auditor's report and Audit reports.

## **Methods, audit team and time schedule**

### *Methods*

If there is any uncertainty as to how the audit shall be performed, it is a good idea to define the methodology that shall be used for the performance of the assignment.

### *Example*

If double payment of invoices is suspected, all payments shall be examined against the original documents. All deviations shall be reported. Alternatively, only invoices exceeding a certain amount shall be examined.

### *Audit team*

If you have any special request in respect of the person who shall perform the audit, this should be stated.

### *Time schedule*

In connection with suspicions of corruption it is important that the special audit is made as soon as possible in order to avoid a situation in which accounting records disappear or are corrected. It is therefore important that a time schedule is laid down for the performance of the audit.

## **5 Reports**

As a rule, reports shall be made orally to Sida locally and to the management of the organisation or programme that has been audited. If it seems that the suspicions of corruption are confirmed, it may be necessary to make a departure from the rule of reporting to the auditee. A written report should always be submitted to Sida two to three weeks after the completion of the audit. The final report should be submitted to Sida two weeks after Sida has provided its points of view on the preliminary report. One copy of the report should be sent to (lotta.sando)@Sida.se (focal point for auditing questions).

# Appendix 6a

## Example of terms of reference for a local procurement of a framework agreement for audit services (embassy)

### **Terms of reference for framework agreement for Local Audit Services**

#### **1 Background**

##### **1.1 Information about Sida**

Sida is the Swedish government agency for bilateral international development co-operation. The Parliament and Government decide on the development co-operation budget, the countries with which Sweden shall have programmes of development co-operation, and the focus of co-operation.

The long-term objective of the Swedish development co-operation is to help create conditions that will enable the poor to improve their lives.

Sida supports activities in almost 120 countries, including the partner countries in Central and Eastern Europe. Most of the resources are allocated to the twenty or so countries with which Sida has extensive, long-term programmes of co-operation, and XX is one of these. Sida also supports regional development co-operation.

The general orientation of co-operation is laid down in country and regional strategies and the financial framework and the focus of the programme are determined in overall development co-operation agreements, usually covering 3-5 years, between Sweden and the partner government or intergovernmental organisation. The Swedish government is usually represented by Sida. For each particular project or programme, the parties conclude a Specific Agreement, spelling out the details.

For more information, please see Sida's homepage: [www.Sida.se](http://www.Sida.se)

##### **1.2 Information about Sida's work in XX**

Sida supports development programmes and projects in several sectors in XX including X, X, X and X sectors. In each sector, Sida supports a number of development co-operation projects and programmes. Partners are Government, civil society and the private sector. Sida also provides general budget support to the Government of X. The total volume of the bilateral collaboration for 20XX is SEK XXX 000 000 (MUSD XX). Indicative volumes for 20XX and 20XX are SEK XXX 000 000 (MUSD XX) per year.

Sida has delegated the task of implementing the country programme to the Embassy of Sweden in XX.

For details about Sida's development co-operation programme in XX, please see [www.Sida.se](http://www.Sida.se) and [www.swedenabroad.se](http://www.swedenabroad.se).

### **1.3 Audit of projects and programmes**

Normally, the responsibility to have operations audited rests with the partner organisation. In most project and programme agreements it is stated that the project/programme shall be audited annually. An external, independent and qualified auditor shall carry out the audit.

In addition to the audits agreed upon with partner organisations, Sida also has the right to commission special audits, for which Sida will be the contracting party. The mandatory task to perform regular audits of projects and programmes has several functions. It is there to ascertain that funding provided by the Swedish Government is spent in an appropriate manner, and in line with agreed plans. Another important aspect is that audit is a means to identify and counteract corruption. To Sida, this is of great importance.

In connection with the preparation of possible support to institutions and organisations, Sida might also commission organisational audits. Such assessments form important parts of the assessment and give guidance to the design of the collaboration.

For the last two years, the Embassy/Sida in XX has had a framework agreement with a local audit company, which has provided audit services to Sida in XX. The contract is expiring, hence the need to enter into a new contract on audit services for the Embassy in XX for the period XXXX-XXXX.

Or

In order to support the Embassy in XX in undertaking the special audits, the Embassy has decided to procure the services of a local audit firm for rendering audit services on demand.

For each audit separate Terms of Reference will be presented and agreed in accordance with the specific requirements within the particular project or programme.

### **1.4 Number and type of audits to be undertaken**

It is difficult to estimate the total number of audits to be undertaken annually under the call-off agreement, but it is expected that it will be in total X to X per year. Audits could vary in length and complexity, and may occasionally involve travel within XX and in the region. The work to be performed by the auditing firm will include other tasks than traditional financial auditing of projects and programmes, e.g. procurement audit, management audit, performance audit, capacity and systems audit etc. This is further described below under "Scope of Work". It should be noted that the call-off agreement will not include any guarantees of volume of services to be required/ provided.

### **1.5 Time schedule**

The Embassy of Sweden envisages a framework agreement with one company for two years. If the performance of the services is satisfactory, the agreement may be extended twice, for a period of twelve months for each extension.

It is estimated that an agreement can enter into force in X 20XX.

## 2 Objectives

The objectives of the audit services are:

- (1) to assist the Embassy in undertaking relevant audits of projects and programmes in a timely and professional manner in order to safeguard the use of Swedish Government funding, prevent corruption and ensure an efficient implementation of projects and programmes; and
- (2) to assist the Embassy in building internal capacity relating to audit activities.

## 3 Scope of work

### 3.1 Duties of the auditor

#### *A. Audits commissioned by the Embassy*

The Auditor shall be prepared to and have the capacity to carry out the following main types of audits:

- a) *Financial Audits* in order to examine the quality of internal controls and assess whether the accounts are true and fair, and thus, that the financial accounts provide a correct picture of the partner organisation's work. For individual projects, this may include examination of project or programme specific expenditures and financial reports submitted by the partner organisation.
- b) *Management Audits* in order to examine the quality of the administration of the partner organisation (internal controls, systems for budgeting and accounting, how results are followed up, etc).
- c) *Performance Audits* (Value for Money Audit) in order to examine how well the partner organisation has achieved its goals (goal fulfillment), the relationship between resources used and results (cost efficiency), or how well the results contribute to the impact the organisation wishes to achieve (appropriateness).
- d) *Capacity Studies* in order to examine the partner organisation's capacity with regard to goal fulfilment, planning, administration, resources etc with a view to determine the quality of the activities pursued by the organisation (covering e.g. staffing, internal controls, routines, etc).
- e) *Compliance Audits* in order to examine whether the partner organisation or project implementer follows legislation, rules, agreements etc.
- f) *Preventive Audits* (Pre-Award Survey) in order to examine whether the (potential) partner organisation's stability, structure, management capacity and manning, financing and control functions etc are such that the planned activity can be expected to be successfully pursued and that granted funds will be utilised in an accountable and transparent manner.

For certain projects or programmes, a combination of some of the above audits may be required.

In conducting audits initiated by the Embassy the Auditor shall apply internationally recognized standards.

It may be noted that in XX there is an ongoing effort to harmonise and co-ordinate support provided by external partners. The arrangements for co-ordination will take different forms depending on the project/programme to be supported. Sweden may take on the role as Lead Donor for particular projects/programmes and, in such cases; the financial audit would cover not only funds provided by Sweden but also by other co-operating partners.

### *B. Internal capacity building and support*

Whereas the Embassy may initiate certain audits, it does also receive a number of audit reports from its development co-operation partners. With respect to such audit reports, the scope of work will include assisting Embassy staff in assessing reports, assistance in drawing conclusions from audit reports and determining actions to be taken. The Auditor may be requested to provide training and advice on audits for Embassy staff. Advisory services in the design of Terms of Reference for audits may also be included.

### **3.2 Audit proceedings**

Proof arising from audit proceedings of deliberate misuse of funds or of misuse caused by neglect or irresponsibility must be reported and accompanied by proper evidence in order to facilitate the taking of any legal action necessary. In addition, recommendations shall be made as to how to secure future operations.

In cases where misuse and poor accounting can be attributed to system failures, inadequate training, poor definitions of routines, lack of qualified personnel and the like, the audit proceedings shall contribute to rectifying the situation through the Auditor's recommendations. In such cases, the Auditor shall report in such a manner so as to allow responsible audit personnel to understand where and why mistakes have been made, and to learn how better to control, follow-up and account for use of goods and funds. The audit report shall also make recommendations as to how these problems can be counteracted.

## **4 Reporting and documentation**

Subsequent to every audit, reports in English shall be submitted to the Embassy of Sweden and to the auditee unless special circumstances require otherwise. The report shall include an executive summary, which should be self-explanatory and self-contained and should include a summary of findings, conclusions and recommendations.

Three copies of the draft report shall be submitted to the Embassy within 15 days after the audit has been carried out. Within two weeks of receiving comments on the draft report, a final version of the report shall be submitted in three copies to the Embassy and, unless otherwise agreed, to the concerned organisation. In addition, the report shall be submitted in electronic format to the Embassy.

The auditor shall present the major findings of the report in a meeting with the Embassy, and, if so agreed, with the concerned organisation.

At the end of the framework agreement the auditor shall provide a final report to the Embassy summarising the major general findings from the various audits undertaken, as well as summarise training, advice and other support provided to the Embassy. This is to give the Embassy an overview of common features.

## **5 Profile of the consultant and staffing requirements**

### **5.1 Compulsory**

In order to be able to carry out the different types of audits relevant manning has to be made in accordance with the specific ToR for each assignment. Concerning financial audits the tenderer must appoint an authorized public accountant in accordance with international standards. The staff proposed by the tenderer as Senior Consultants for the specific audits must possess relevant degrees or equivalent theoretical and

practical qualifications in relation to experience of assignments within the field of auditing. The Junior/Assistant Consultants can be less experienced.

All the staff proposed must have good knowledge of written and spoken English and XX, level 1–2 according to Sida's language level definitions.

The Invitation to Tender gives more specific information on the requirements for the consulting firm as well as for the consultants.

# Appendix 6b

## Example of tender documents (embassy)

Sida recommends that the tenderer, as soon as possible after receipt of this invitation, take note of the requirements in this contract document.

Some of the requested documentation must be obtained from designated authorities, which can result in a certain time for handling. Questions giving rise to clarifications and/or additional information should be submitted at the beginning of the time given for submission of tenders enabling the Embassy to hand over additional information in good time and before the final date for receipt of tenders.

### **Invitation to tender for framework agreement for local audit services**

You are hereby invited to tender for an assignment according to the enclosed Terms of Reference (ToR), appendix 1, Draft Contract, appendix 2a and General Conditions, appendix 2b.

[Name]  
Head of Development Cooperation  
Embassy of Sweden

#### **Appendices**

Appendix 1	Terms of Reference (ToR)
Appendix 2	Draft Framework Agreement
Appendix 3	Sida's general conditions for framework agreements, 2002
Appendix 4	Solemn declaration (form)
Appendix 5	Figures for liquidity ratio and solvency ratio (form)
Appendix 6	CV (form)
Appendix 7	Previous performed assignment (form)
Appendix 8	Language Level Definition
Appendix 9	List of Consultants (form)
Appendix 10	Price Basket

## Administrative conditions

Contracting entity	Embassy of Sweden, XX
Postal address	PO Box
Contact person 1	XX Phone no: + E-mail: X.X@foreign.ministry.se
Contact person 2	Fax: + YY Phone no: + E-mail: Y.Y@foreign.ministry.se
Closing date for receipt of tender	20XX-XX-XX
Final date for validity of tender	20XX-XX-XX
Address and mark	The tender must be sealed and addressed to the contracting entity. The envelope must be clearly marked as stated below: TENDER Local Audit Services Ref. no 20XX-XXXXX Embassy of Sweden –
Tenders submitted by fax	Not allowed.
Tenders submitted by e-mail	Not allowed.
Procurement procedure	Simplified
CPV-codes	74121000, 74121210, 74120000, 74121200, 74140000

## General tendering conditions

1. The tender must be submitted in writing and be signed by an authorized representative of the company or equivalent.
2. The formation of consortium or joint venture is allowed. In such case the tenderer must submit either,

a tender signed by all partners of the consortium or joint venture and a draft of a consortium or joint venture agreement providing for joint and several liability with reference to the contract including the nomination of the lead firm of the consortium or joint venture,

or

a tender signed by the lead firm and a copy of a consortium or joint venture agreement, signed by all participating parties, providing for joint and several liability with reference to the contract including the nomination of the lead firm of the consortium or joint venture.

3. The tender and all enclosed documents must be produced in English<sup>14</sup> and contain all information and documentation set out in this contract document.
4. The complete tender must be submitted in duplicate – one original and one copy. All appendices should be listed in the tender and be marked with the name of the tenderer and Embassy's reference number.

<sup>14</sup> Documents originally written in another language than English must be translated to English. The translation of official documents such as certificates etc. must be certified.

5. The tender must contain information of the tenderer's type of organisation, VAT registration number, contact person, telephone, e-mail and postal address.
6. The tender should not be hardbound, fastened together or glued. Loose sheets in an ordinary file or folder are sufficient.
7. The tender will be opened and listed on the second day after the closing date for receipt of tender in the presence of at least two officials appointed by Sida.
8. The regulations in the Act (1992:1528) on Public Procurement (LOU) apply to this procurement. LOU is accessible at [www.nou.se](http://www.nou.se).
9. It is a fundamental principle for procurements carried out in accordance with LOU that all tenderers must be treated equally. As a consequence the possibility to elucidate or amend the information already submitted in a tender is very limited. It is therefore of utmost importance that the tender contains all the information and documents requested.

### **The procurement process**

Before evaluating the tenders the contracting entity shall examine whether the tenderers fulfill the requirements imposed upon the suppliers. These requirements are addressed in section 4, 5 and 6.

If the tenderer fulfils the requirements and is regarded as qualified the tender will be evaluated. The evaluation criteria and method are described in section 8.

### **Check-up of the tender**

Firstly a check-up is made to verify that the tender is received in due time, signed and containing the requested documents. A tender not fulfilling these requirements may be rejected.

### **Check-up of the tenderer**

Secondly a check-up is made to verify that the tenderer has fulfilled the specified requirements below. As a confirmation that the requirements are fulfilled the tenderer must submit in the tender the information and documentation requested. A tenderer not fulfilling the requirements may be rejected.

### **Legal status**

The tenderer must be a legal entity<sup>15</sup> or an individual established as a registered company<sup>16</sup>. The following requirements must be fulfilled.

The tenderer must have fulfilled the required legal obligations regarding registration, social security contributions and other legal charges in the tenderer's home country.

The tenderer and individuals representing the tenderer must not have been found guilty of crime related to the exercise of his profession. A supplier subject to the circumstances according to Chapter 1, 17 § The Act on Public Procurement<sup>17</sup>, will be excluded from taking part in the procurement.

A tenderer registered according to a) and b) below must submit the following documents:

<sup>15</sup> A legal entity refers to a limited or private company (corporation), a limited partnership, a trading company, an economic or non-profit association or foundation.

<sup>16</sup> A registered company refers to a physical person established as a registered company.

<sup>17</sup> The Act on Public procurement 1:17 (<http://www.nou.se/loueng.html>)

- a) a certificate of registration (copy) issued by a competent authority showing the tenderer is registered by a national Registrars of Companies or a Trade Association
- b) certificate (not older than six months) showing that the tenderer, is registered for declaration and payment of value added tax or a similar sales tax in accordance with the tenderer's national legislation, has declared preliminary taxes for staff and employee contributions, and is free from debts regarding taxes and social security contributions.
- c) a solemn declaration (affirmation of truth), appendix 4, must be signed by a authorized signatory, showing that the persons having influence over the company's activities have not been found guilty of offences or committed serious offences in business dealings.

If a consortium or a joint venture submits a tender or if a sub-consultant is included in the tender, each individual partner or sub-consultant must provide the required information and documentation.

### **Financial position**

The tenderer must have a solid financial and economic base. The tenderer's latest approved annual accounts must contain figures showing a liquidity ratio<sup>18</sup> not less than 1 and a solvency ratio<sup>19</sup> not less than 15%. The basis of the calculation must be the figures accounted for in the latest year of activity.

In case lower figures than required are shown, or there is a lack of figures, the tenderer may still be regarded as qualified if the tenderer, in his tender, can present an explanation showing the tenderer is in a corresponding position of financial and economic stability, for instance a guarantee issued by the parent company.

The tenderer must, in appendix 5, confirm and submit to the tender, the following:

- a) confirm that the above mentioned requirements for figures are fulfilled and
- b) if not, provide the required explanation,
- c) confirm that the latest annual accounts (not older than two years) are approved by the auditors;

The tenderer shall upon request submit the latest approved (not older than two years) annual accounts.

If a consortium or a joint venture submits a tender, each individual partner must provide the required information or documentation. However, it is not mandatory for sub-consultants to provide the information or documentation.

### **The tenderer's technical capacity and capability**

Thirdly an assessment of the tenderer's technical capacity and capability is performed.

<sup>18</sup> Liquidity = short term payment ability Calculations: Current assets/Short term liabilities

<sup>19</sup> Solvency = long term payment ability Calculations: Share holders equity + (0,7 x Untaxed reserves)/Total assets

## **Capacity and capability (consultant firm)**

The tenderer must be an authorized public accounting firm or a firm providing authorized public accountants in accordance with international audit standards.

The tenderer (the firm) must have documented resources, knowledge and experience to perform assignment/s within the requested area/s of competence/s.

The tenderer must have extensive experience of auditing foreign funded development co-operation projects in XX, i.e. at least two major assignments.

The specification/description below may include all members of a consortium or sub-consultants. The assessment of the tenderer's technical capacity and capability shall include the combined experience.

The tenderer must:

- a) confirm that requirements specified above are fulfilled and present a specification of the assignments the tenderer refers to. A specification must consist of:
  - scope of work
  - start date and completion date
  - name of client
  - number of staff months provided by the tenderer
- b) present a brief description of the tenderer (facts about the company, competence and capacity, market position, plans for development);
- c) confirmed the resources necessary for the performance of the Framework Agreement will be at the Tenders disposal.

## **Personnel for the performance of the services**

Tenderers may offer two different levels of consultants: Level 1 and Level 2. These two levels are described below.

The tenderer shall supply at least one (1) consultant (individual) for each Level.

The tenderer may offer a maximum of five (5) consultants (individuals) per level. If a tenderer offers more than five consultants (individuals), only the first five (5) listed will be considered.

A consultant (individual) may not be part of more than one tender related to this procurement.

### **Level 1 – Senior Consultant**

The person(s) responsible for the performance of each specific audit assignment shall be Senior Consultant(s) and have a very high level of competence within his/her area. The Senior consultant(s) shall be able to work as a team-leader. A very high level of competence is defined as the consultant (individual) meeting all of the requirements below:

- Shall have at least seven years relevant working experience as a Senior Consultant for assignments with relevance to the Auditing Sector.
- Shall have a degree from a college/university with relevance for performing assignments in the Auditing Sector or alternatively equivalent substantiated knowledge acquired through fifteen years of working experience.

- Shall have been responsible for and/or carried out at least five assignments in the last five years with relevance to auditing donor funded projects or programmes in development cooperation. The total contract period of these five assignments shall be at least 3 months, and the person shall have been responsible for at least two of the assignments. At least two of the five have to be in XX.
- Shall have very good knowledge of English (written and spoken) at least as per Language Level 2, Full Professional Proficiency in Appendix 8, Language Level Definition.

#### **Level 2 – Junior/Assistant Consultant**

Shall have a good level of competence within his/her area and be able to work independently. A good level of competence is defined as the consultant (individual) meeting all of the requirements below:

- Shall have at least three years working experience of assignments with relevance for performing assignments in the Auditing Sector.
- Shall have a degree from a college/university with relevance for performing assignments in the Auditing Sector.
- Shall have participated in at least three assignments during the last five years within the Auditing Sector. At least two of the three have to be in XX.
- Shall have very good knowledge of English (written and spoken) and at least as per Language Level 2, Full Professional Proficiency in Appendix 8, Language Level Definition.

#### **Documents that shall be enclosed (for item 6.2.1 and 6.2.2) with the tender**

- a) Information stating which persons the tenderer intends to use to carry out the assignments. The persons shall be introduced in an enclosed Curriculum Vitae (CV) set out according to Appendix 6 Template for CV and contain name, theoretical competence, experience and assignments carried out that show that the requirements regarding Consultant Level 1 and 2 have been met. The presentation of the assignments carried out shall also detail the type of assignments that have been carried out, showing experience in relation to the sector (Auditing). The CV shall also show which consultant level the person belongs to.
- b) A brief description of two assignments per person that meet the requirements of the consultant level in question. The assignments shall have been performed within the Auditing Sector. The descriptions shall normally be confirmed in writing by the relevant employers (Appendix 7 shall be used as a template).
- c) List of consultants (individuals) offered by the tenderer (Appendix 9, List of Consultants shall be used as a template).

#### **The tender**

The ToR specifies the fundamental and the specific requirements for the implementation of the assignment as well as the objectives of the programme or the project.

The tenderer shall draw up a tender based on the given prerequisites. The tender must fulfill the requirements stated below.

## **Confirmation of requirements**

The tender must contain a confirmation that the requirements for the implementation of the assignment specified in the ToR are fulfilled. The tenderer's proposal based on the requirements in p. 7.2 up to 7.6 will be assessed in accordance with the evaluation criteria and method stated below.

## **Implementation and method**

Based on the requirements, in the ToR, the tender must present the methodology the tenderer intends to use for carrying out assignment and in particular specify how the method will comply with the requested objectives.

The following criteria will be assessed:

- the understanding of the services – the proposal should show that the tenderer has a good grasp of the services and its role and task (2 p);
- the proposal should show that the tenderer has experience and knowledge of this type of services (2p);
- how the tenderer describes the tenderer's methods used to carry out the different types of audits, studies and investigations (2p);
- how the tenderer describes the tenderer's approach and method to combat corruption (2p);
- the tenderer's experiences in carrying out training activities and methods used (2p);

The methodology should show, in a clear and transparent way, whether:

- Funds for projects and programmes under Sweden's development co-operation agreements with Zambia or under the Embassy's agreements within Regional Development Cooperation have been utilised efficiently;
- Funds have been utilised in accordance with the agreements as well as the regulation in force.

## **Organization of the services**

The tenderer must specify the organizational set up for the performance of the services.

The following criteria will be assessed:

- the organization should be designed to secure that personnel with adequate qualifications and experience are designated for the services (2p);
- the interface between the client and the Consultants should, on the Consultants side, consist of as few contact persons as possible and the distribution of responsibilities should be as clear and transparent as possible (2p);
- the organization should be clear, transparent and well suited to the purpose and objectives of the services (2p);

## **Availability**

The tenderer must state the time needed for preparation before a specific audit service under the Framework Agreement can be commenced (14p).

The tenderer must confirm that less complicated advise can be given by telephone or e-mail within two days.

The tenderer must state the time the concerned personnel requires to be available to start a short-term<sup>20</sup> assignment and a long-term<sup>21</sup> assignment, after request or ToR has been received. The tender must state one of the intervals specified below for both short- and long-term assignments (percentage according to principles for evaluation, section 8:2):

<b>Short-term assignments</b>	<b>Long-term assignments</b>
a) 1–2 days (100%)	a) 1 week (100%)
b) 3–4 days (80%)	b) 2 weeks (80%)
c) 5–9 days (60%)	c) 3–4 weeks (60%)
d) 10–14 days (40%)	d) 5–6 weeks (40%)
e) More (0%)	e) More (0%)

### **Qualifications and competence**

The tender must include information on qualifications and competence of the proposed personnel, see p. 6.2.1 and 6.2.2. The information will be evaluated and compared to the following requests.

In addition to p. 6.2.1 and 6.2.2 the proposed Senior Consultant and Junior/Assistant Consultant should:

- a) have extensive professional experience from auditing in general
- b) have extensive experience in auditing in a wide variety of donor-funded projects or programmes,
- c) have extensive experience in accounting and financial management rules, procedures and practices in XX,
- d) be acquainted with polices for procurement applied by the different sectors of Government in XX,
- e) have experience of issues related to identifying and combating corruption and
- f) have experience in carrying out training activities.

### **Fees and costs**

The tender must specify the fee/hour for each category (level) of proposed personnel in the tender (max five persons per level).

All fees and costs must be stated in USD exclusive of VAT and must include all other taxes and levies. The Embassy will accept invoices in US Dollars, payable at the exchange rate at the day of payment.

The financial evaluation will be performed based on the total hourly fee according to the enclosed form “Price Basket”, appendix 10. Please note that the tenderer shall not fill in the form as it is enclosed for information only.

### **Commercial conditions and contract**

The tenderer must, in the tender, confirm acceptance of the enclosed draft contract including the Standard Conditions. However, the tenderer may comment on the wording of the contract but any proposed alteration must not alter the significance of the contract in a substantial way.

### **Tender evaluation**

A tenderer who fulfils the requirements set out in section 4, 5 and 6 will be considered qualified as a potential supplier. A qualified supplier’s tender will be further assessed to test whether the qualifications of the services are fulfilled.

<sup>20</sup> Short term assignment = up to one month

<sup>21</sup> Long-term assignment = more than one months and up to six months

## Principles of evaluation

The contract will be awarded to the tenderer who makes the economically most advantageous tender with regard to the following evaluation criteria.

Technical Evaluation	Evaluation Criteria	Max. Points
	1 Method, organization and availability	
	– Adequacy of the proposed method	10
	– Adequacy of the proposed organization	6
	– Availability	14
	2. The combined (as per p. 7.5.1) competence and experience of proposed staff for the performance of the services	50
	– Senior Consultant	20
	– Junior Consultant/Assistant Consultant	
	Total points	100

## Method of evaluation

The number of points to be given under each of the technical evaluation criteria. For example, a criterion of max. 20 p. considered as "Good" will receive $0,8 \times 20 = 16$ points.	Not addressed <sup>22</sup> or	0%
	Poor	40%
	Not fully acceptable <sup>23</sup>	60%
	Satisfactory <sup>24</sup>	80%
	Good <sup>25</sup>	100%
	Very Good <sup>26</sup>	
Required minimum technical score	A Technical proposal must obtain a minimum of 60 points as a condition for further evaluation	

To conclude the evaluation the technical score and the total price (fee) are converted to a Comparison value. The winning tender has the lowest Comparison value. The Comparison value is an adjustment of the price based on the following formula:

Comparison value = Offered price x (1+Percentage increase).

Percentage increase = (Maximum technical score – Actual technical score)/Maximum technical score x Adjustment factor;

The Adjustment factor indicates the weight the technical score has in relation to the price. Normally the factor is between 0,5 and 4.

In this case the adjustment factor is 1,75.

<sup>22</sup> The criterion is not addressed in the tender or not sufficient

<sup>23</sup> Sufficient in some aspects but not as a whole

<sup>24</sup> Sufficient but lacks substantial advantages or has uneven quality

<sup>25</sup> Adequate and well suited to the purpose

<sup>26</sup> Gives added value and shows high quality on the whole

### **Example**

The adjustment factor in this example is 2,5.

Tender A:

Price 480 000, Technical score 90.

Tender B:

Price 400 000, Technical score 75.

Evaluation Tender A:

Percentage increase =  $(100-90)/100 \times 2,5$ ; Percentage increase = 0,25

Comparison value =  $480\,000 \times (1+0,25)$ ; Comparison value = 600 000.

Evaluation Tender B:

Percentage increase =  $(100-75)/100 \times 2,5$ ; Percentage increase = 0,625

Comparison value =  $400\,000 \times (1+0,625)$ ; Comparison value = 650 000.

The winning tender is A since it has the lowest Comparison value.

## **Contract**

### **The Framework agreement(s)**

Framework agreement will be signed with two tenderers if possible of which one will be first ranked. The first ranked tenderer will normally be awarded the assignments but in case of conflict of interest with the current assignment the second ranked tenderer will be awarded the assignment.

### **Validity of the contract**

It is the Embassy's objective to conclude the Framework Agreement(s) to apply from X 20XX remaining in force until the end of X 20XX (i.e. a period of two years. If the framework agreements are concluded later the framework agreement period will be two years from the day it enters into force).

The contract period is 24 months with the option to extend the period with 24 months (see ToR and Draft Contract).

### **Openness and confidentiality**

Confidentiality covers information in a procurement matter until an award decision has been taken or the procurement is completed in other ways.

If a tenderer is of the opinion that information given in a tender should be covered by confidentiality, the tenderer should state in the tender which information is concerned and specify the damage that publicity of the information would entail for the tenderer. The Embassy will, however, perform an independent assessment in the matter.

## **Contract documents**

### **Questions and answers**

All questions regarding the contract documents must be presented in writing by the tenderer – preferably by e-mail – to [X.X@foreign.ministry.se](mailto:X.X@foreign.ministry.se) 20XX-XX-XX at the latest.

A summary of relevant questions and answers will be published on <http://www.Sida.se>

**Clarification of Tender**

Clarifications or additional information requested for by the Embassy must be presented in writing and addressed to the contact person stated in this Contract Document.

**Notification of Awarded Contract/Concluding of the Procurement**

As soon as Sida has made a decision regarding contract award, all tenderers will be notified in writing (by e-mail) and informed about the reasons for the decision.

The agreement between the Embassy and the tenderer(s) awarded framework agreement(s) will be signed as a procurement contract. An awarded tenderer shall be ready to sign the framework agreement as soon as possible and not later than ten days after the decision of contract award has been taken.

The message regarding contract award does not mean that a binding contract between Sida and the tenderer is established. A legally binding contract is not established until both parties have signed the contract.

# Appendix 7

## Examples of terms of reference for consultancy audits

### **Terms of reference for auditing 20xx of consultancy firms appointed by sida**

#### **Background**

A large proportion of the appropriations at Sida's disposal are handled, to a greater or lesser extent, by others: partner countries, consultancy firms, non-governmental organisations, etc. Sida shall make sure these funds are managed satisfactorily from a control point of view. This control is exercised in part by following up the goal fulfilment of development cooperation, and in part through the follow-up of financial contributions. For the cooperation to be carried out on a basis of trust, it is essential for Sida to be certain, on the best basis possible, that the audits of the partner country and consultant meet the requirements of sound accounting practice and that there is good internal control.

Cooperation between Sida and the consultants is regulated by agreements, which are mostly based on Sida's "Standard Conditions for Short and Long term Consulting Services, 2002". The agreements also have other content depending on the type of activity.

Sida lays down annual plans for control audits for a number of consultancy firms. The selection is made based on suggestions from the sector departments concerned and the criteria of importance and risk. (The departments also have consultancy audits carried out on their own initiative.)

#### **Aim**

The audit shall verify that the development cooperation funds, internal control, accounting and invoicing of services carried out by the consultancy firm are managed in accordance with agreements entered into and sound accounting practice.

#### **The assignment**

The assignment covers auditing and assessment of Sida's cooperation with the named consultants, and shall cover the following points:

1. the consultant's accounting with regard to the requirements for sound accounting practice
2. the consultant's system for internal control
3. the consultant's application of the agreement with regard to staff costs and related compensation according to the existing agreement

4. the consultant's systems and routines for accounting and invoicing of the time spent on Sida-financed contributions
5. the consultant's application of the agreement with regard to the basis of other costs charged to Sida
6. the consultant's budgeting and financial follow-up of the contribution within the Sida-financed project and adaptation to Sida's requirement for budgeting and accounting methods

and where applicable

7. bigger, individual procurement cases with regard to sound procurement practice and government procurement regulations. For these tasks, the audit shall appoint procurement expertise, and consult with Sida's divisions for legal and procurement matters for a definition of the assignment in this part

*Where the consultant has been audited before, at Sida's request, the audit shall also cover the results of the measures that the consultant was recommended to take after the previous audit.*

#### **Working plan and timetable**

The work shall be undertaken primarily in the consultants' offices in Sweden. The assignment shall be carried out during X-X 20XX and reported by X 20XX at the latest.

Each assignment can be expected to take max two person weeks.

#### **Reporting**

Each assignment shall be reported on according to these terms of reference, as a separate section of a report. This shall be presented to Sida in two copies and by an electronic medium.

#### **Payment**

Payment will be made according to Sida's normal routines for invoice payments after the assignment has been completed and the report approved by Sida.

# Appendix 8

## Example of a section on auditing in the agreement templates

The extract below has been taken from Sida's agreement templates for agreements with foreign organisations. There are corresponding texts in agreement templates for universities, contract-financed technical cooperation etc.

### **Foreign partners – 3c, agreement on research cooperation with organisations**

#### *Article 9 Audit*

[The ORG] is responsible for that the project/programme is audited annually. The audit shall be carried out by an external, independent and qualified auditor. The audit shall be carried out in accordance with international standards issued by International Organisation of Supreme Audit Institutions (INTOSAI) or International Federation of Accounts (IFAC). The terms of reference for the audit and the selection of auditor shall be approved by Sida. The cost for the audit shall be paid by [the ORG] and shall be a part of the budget.

The Audit Report shall express an opinion whether the submitted Annual Financial Report is correct and gives a true and fair view of the activities of the project/programme and whether the execution has complied with the rules and conditions governing the use of funds as expressed or referred to in this Agreement.

The auditor shall submit an Audit Memorandum or a Management Letter, which shall contain the audit findings made during the audit process. The audit memorandum/management letter shall state which measures have been taken as a result of previous audit reports/audit memorandums/management letters and whether measures taken have been adequate to deal with reported shortcomings.

If requested by Sida the audit shall also cover the progress report of the project/programme.

[The ORG] shall present the Audit Report and the Audit Memorandum/Management Letter to Sida as soon as it has been received from the auditor; and no later than [state date]. A management response shall be produced by the implementing agency and submitted to the auditor and to Sida within three weeks.

[The ORG] shall co-operate with and assist Sida in the performance of any additional audits, follow-ups and financial studies that Sida may request.

**Comments:**

The auditor's report must normally be finished and delivered to Sida within 3–4 (max 5) months after the end of the financial year (or other agreed period). The date must be stated in the agreement.

Audits must be carried out in accordance with international standards. So far as the public sector is concerned, INTOSAI (International Organisation of Supreme Audit Institutions) issues rules. In the private sector, IFAC (International Federation of Accountants) issues ISAs (International Standards of Auditing). The auditor's report must state which standard is being used. National standards that accord in all material particulars with the aforementioned international standards may be accepted.

Sida's Guidelines for Planning, Reporting and Audit ([www.Sida.se/partnerpoint](http://www.Sida.se/partnerpoint)) and DAC Good Practice Paper no. 5 on Financial Reporting & Auditing together with Technical Guidance Notes nos. 6–9, provide good guidance on the choice of auditor, wording of the Terms of Reference, etc.

Audits, as a minimum, include scrutiny of the accounts. They may also, if so agreed, contain checks on internal control systems, management efficiency, reliability of progress reports, proposals for improvements as seen against identified shortcomings, etc. This is usually included in a Management Letter/Audit Memorandum.

It is important to recognise that the job of audit normally does not include looking for any signs of fraud or corruption. American audit firms do not undertake such tasks at all because they do not want to risk becoming liable for any undetected cases. Special measures must therefore be undertaken in accordance with Sida's anti-corruption rules if there is suspicion of e.g. corruption. Special audits and investigations can then be commissioned from the auditors or other consultants.

Right from the preparatory phase of the Contribution, the system and routines for internal control must be scrutinised and evaluated.

If Sida is already analysing whether operations-oriented progress reports correspond with reality, this does not need to be covered by the audit report. In the preparatory phase ("insatsberedning") Sida shall plan how, and when, such checks are to be made and in what context.

In cases where a Supreme Audit Institution (SAI), i.e. the national audit office, is expected to audit development cooperation funds, Sida must – in the course of the project preparation phase – make an assessment of the capacity of the SAI to perform the services requested. If its skills are found to be insufficient, Sida shall give consideration to alternative arrangements, to be agreed between the parties and stated in the Agreement.

It is important to note that an SAI often does not do auditing at the level required for an individual project. Even if this were the case or it were to be accepted as an exceptional case, it is necessary to ensure that the auditor's report can be delivered within the timescales stated above (max 5 months) for an audit by an SAI to be acceptable.

The draft Terms of Reference (ToR) for auditors is usually agreed during project preparation. They should include a description of the project, define the implementing agency, the accounting methods being used, the reporting requirement, the scope of the audit, the coverage of the management letter and, where applicable, the required qualifications of the auditor (for a specimen See DAC Technical guidelines Note 7)

As laid down in a recent (name and web reference to be inserted!) policy agreement between OECD/DAC members on good practice in

development cooperation, donors should accept the audit arrangements of partner countries where these are considered to be of acceptable quality. Where project financial reports reflect all sources of funds, the audit report should normally fulfil the requirements of all donors. A single audit report meeting the needs of both government and donors thus constitutes good practice. (For further reading, see DAC Technical guidance note 9)

Findings from the audit of the financial reports or material issues raised in the management letter/audit memorandum will normally be project specific. As project accounting and internal control systems are usually applicable to the entire executing agency or government, these findings may also provide useful information on broader systemic issues at the institutional level. Project audit findings may therefore make it easier for the government – with donor support as appropriate – to address these systemic issues.

# Appendix 9

## Sida's framework agreements with firms of auditors

The text below is an extract from Sida's framework agreement for audit services. All framework agreements are available in their entirety on Sida's intranet, iNSIDE. Go in under the heading Supporting Functions/Law & Procurement/Procurement & Contracts/5. Framework Agreements/Sida's own Framework Agreements. Then click on Framework Agreements for Financial, Forensic and Performance Audits. Alternatively, go to the Support Functions/Audit at Sida/Framework Agreements.

### **§ 1 Framework agreement**

The embassies also have the right to call off from this framework agreement. When calling off, embassies shall be treated in the same way as Sida.

### **§ 2 Sida's General Conditions for framework agreements**

Sida's General Conditions for Framework Agreements, 2002, (hereinafter General Conditions) shall be applicable, Appendix A.

If the consultant is carrying out any part of the assignment outside Sweden, the following provisions from Sida's Standard Conditions for Short and Long-Term Consulting Services, 2002, shall apply in addition to the General Conditions for Framework Agreements.

### **§ 3 Services and staff**

The consultant undertakes, after Sida's call-off, to carry out the services specified below.

*Area 4.1 Financial audit:* examines that the accounting is correct through substantive testing and examination of internal controls. *Management audit:* examines the management's administration (systems for internal control, how budgeting and accounting work are carried out, result follow-up and risk analyses) as well as observance of the rules (*compliance audit*). This area also covers auditing of suspected corruption.

*Area 4.2 Forensic audit:* an analysis of security-related threats, e.g., fraud, embezzlement, money laundering, information theft and electronic monetary transactions. Forensic audits should serve as basic data for disputes.

*Area 4.3 Performance audit:* examines how well the organisation has met its goals, the relationship between the resources used and the results. Ca-

capacity study: examines the organisation's ability to meet goals, planning, administration, resources, etc. The aim is to determine the quality of the activity carried out by the organisation. The focus is broad and general.

*System audit:* examines how the organisation works by auditing routines and systems within the organisation that should guarantee the reliability of work and reporting. The focus is narrower and goes into greater depth.

#### **§ 4 Call-off**

For short assignments (less than five days) and e-mail inquiries, the call-off can be through the application of the conditions in the framework agreements. In these cases and based on the contents of the framework agreements, Sida shall choose the consultant that best meets the requirements of the authority calling off.

If Sida decides to call off through a renewed competitive tender, the call-off shall be preceded by a call-off inquiry by Sida to find out which consultant can offer Sida the best adapted solution.

*The following applies to call-off inquiries:*

1. The call-off inquiry shall be put to all consultants with agreements in the area concerned. Some assignments may, due to problems of definition between areas, be judged to fall within more than one area. In these cases, the call-off inquiry may be put to those consultants with agreements within the relevant areas. The call-off inquiry shall include written terms of reference specifying the background, aim, contents, timetable, reporting form and other information important to the assignment.  
  
Sida shall specify the criteria that will be used as a basis for awarding the assignment. These criteria shall be covered by the criteria that formed the basis of Sida's choice of consultant. Sida decides which of these criteria are relevant to the specific call-off. It is recommended that inquiries are made via e-mail.
2. Sida shall specify a reasonable deadline for a reply to the call-off. This deadline shall be set with regard to the complexity of the contract object and the time needed to submit a reply to the call-off.
3. The call-off replies shall be in writing. It is recommended that the call-off replies are via e-mail.
4. The assignment shall be awarded to the consultant that gives Sida the best reply to the call-off based on the criteria specified in the call-off inquiry.
5. After entering a contract, Sida shall inform the consultant that has taken part in the renewed competitive tender of the decision that has been made.

#### **§ 5 Reporting**

If embassies or departments and/or units at Sida other than EVU/ Ekonomi call off assignments from this Framework Agreement, before the start of the assignment, the consultant shall inform EVU/ Ekonomi that an assignment has been called off and the content/scope of the assignment. In connection with the final report being sent to the orderer, one copy shall also be sent to EVU/ Ekonomi. This information shall be sent to Lotta Sandö or person put in her place by Sida. The information shall be sent by e-mail to [lotta.sando@Sida.se](mailto:lotta.sando@Sida.se).

# Appendix 10

## Terms of reference for Sida's framework agreements for audit services

The extract below is from Sida's terms of reference when the framework agreement for audit services was procured. The document is available in its entirety on Sida's intranet, iNSIDE. Go to the Supporting Functions/Audit at Sida/Framework Agreements where there is a direct link to the framework agreement.

### **4. Assignment**

Audits can refer to contributions/projects as well as implementing consultants and organisations in Sweden and in the partner countries. Audits can be made of international organisations or of consultants/organisations in countries other than Sida's partner countries. This means that it shall be possible for the tenderer to also offer audits abroad and/or to channel services that are covered by the framework agreement.

Auditing assignments may refer to one or more types of audit. The procurement is divided into three auditing areas:

1. *Financial audit*: examines that the accounting is correct through substantive testing and examination of internal controls. Management audit: examines the management's administration (systems for internal control, how budgeting and accounting work are carried out, results follow-up and risk analyses) as well as observance of the rules (compliance audit). This area also covers auditing of suspected corruption.
2. *Forensic audit*: an analysis of security-related threats, e.g., fraud, embezzlement, money laundering, information theft and electronic monetary transactions. Forensic audits should serve as basic data for disputes.
3. *Performance audit*: examines how well the organisation has met its goals, the relationship between the resources used and the results. Capacity study: examines the organisation's ability to meet goals, planning, administration, resources, etc. The aim is to determine the quality of the activity carried out by the organisation. The focus is broad and general. System audit: examines how the organisation works by auditing routines and systems within the organisation that should guarantee the reliability of work and reporting. The focus is narrower and goes into greater depth.

Organisation also means administration by a partner country.

An auditing assignment can refer to a preparatory audit ahead of planned cooperation and continuous auditing during ongoing cooperation to follow up audits carried out previously or as a final audit after completed work (e.g., a project).

During the current agreement period, Sida may also require education contributions within the area of auditing. This is also covered by this procurement.

Assignments can cover audits of budget support, sector programme support and project support, and, in exceptional cases, there can be separate procurement.

Assignments can be initiated as part of Sida's planned follow-up or for a particular reason. The assignments are normally carried out independently, but can in some cases be carried out in co-operation with an auditing firm appointed by another donor or partner, or with the partner country's Supreme Audit Institution. However, this does not mean that the requirement for independence is set aside.

Auditing assignments shall observe sound accounting practice, sound auditing practice and/or sound practice in the area.

Evaluations of a general nature are not covered by this procurement.

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*Halving poverty by 2015 is one of the greatest challenges of our time, requiring cooperation and sustainability. The partner countries are responsible for their own development. Sida provides resources and develops knowledge and expertise, making the world a richer place.*



**Sida**

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