

EITI Assurance Data and Quality Review

Final Draft Report

Prepared for the World Bank

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1 Executive Summary

Introduction

CIPFA was asked to review the EITI rules in relation to the quality and reliability of data gathered for EITI reconciliations, and to make recommendations for improvement of the directives, processes and key outputs.

The main focus of the review was in connection with Requirements 12 and 13 that call for company and government reports to be based on accounts audited to “international standards”.

Six country cases were examined to inform this review.

Professional View

There is a substantial lack of clarity in the current set of EITI directives. Based on our review of EITI implementation, this impacts on the achievement of EITI requirements.

There is considerable diversity of practice in the implementation of EITI in different countries. While some variation is necessary to reflect differences between countries, the lack of clear distinction between different levels of assurance is unlikely to promote or encourage improvement.

While allowing a degree of flexibility in the interpretation of the EITI directives is reasonable, this should reflect an understanding of the degree of independent assurance to be taken from the reconciliation process.

Detailed drafting of specific EITI directives is needed. However, this can only be pursued when the EITI Board (or appropriate working group) concludes on what type of assurance is required by Criteria 2 and 3.

Recommendations:

The EITI Board, secretariat or working group should

- clarify inconsistencies and other lack of clarity in the EITI Criteria
- Redraft EITI guidance to reflect the improved criteria, and to provide a consistent basis for assessing the achievement of compliance
- Develop a ‘target’ model for EITI assurance to inform assessment of partial achievement of independent assurance
- Encourage greater achievement of the target model through “country led” and “reconciler based” approaches

2 CIPFA's Brief

- 2.1 CIPFA received this brief to provide advice on how to improve quality assurance of data disclosed through EITI reports. This work was commissioned by the World Bank (through its Sustainable Energy Gas Oil and Mining unit – SEGOM) whose members participate actively in the EITI Strategy Working Group.
- 2.2 The issue was defined as follows:

“Concerns have been raised that the EITI Rules, even after the 2011 revisions, do not adequately ensure consistently high quality and reliable EITI data. The predominance of reconciliations in countries with weak accounting and audit practices is challenging. Most countries may need to consider audits in the absence of (government) audited data. EITI requirements 12 and 13 have proven to be particularly problematic, and constitute one of the most common barriers to compliance. In addition, it represents a high risk for the EITI brand if not addressed properly in the short term.”
- 2.3 The objective of the assignment is to produce a professional view of the current operation and concrete suggestions on practical and viable ways to increase assurance of EITI quality of data and reports. CIPFA was asked to provide a professional view on how to adjust the current EITI system and existing practices dealing with quality assurance and data/report viability, specifically how to improve:
 - the body of directives (criteria, requirements and guidance);
 - the set of processes (MSG assessment, TORs for Reconcilers, TORs for Validators); and
 - key outputs (EITI templates and reports).
- 2.4 CIPFA was asked to examine the relevant practices in six EITI countries:
 - Central African Republic
 - Liberia
 - Mongolia
 - Niger
 - Nigeria
 - Norway.

3 CIPFA's approach to the brief

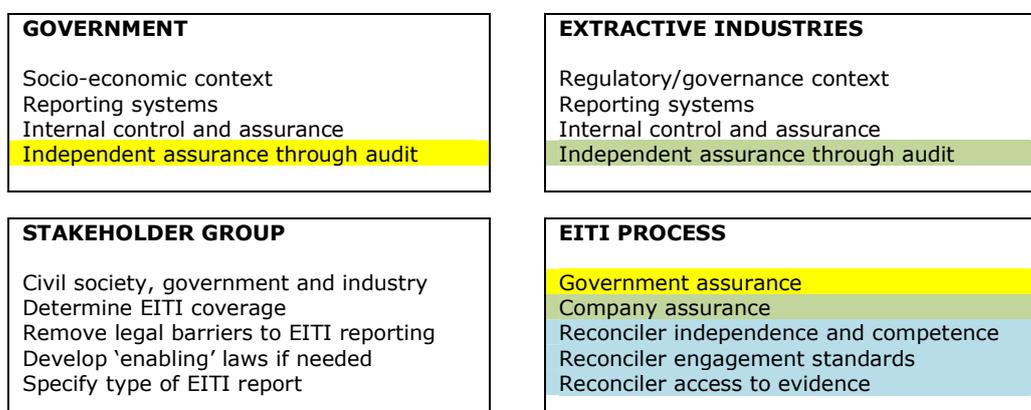
- 3.1 The CIPFA team's approach to the brief involved a number of steps, including
- Understanding the EITI framework and processes;
 - Distinguishing between aspects of EITI which relate to independent assurance, and aspects which contribute to transparency and improvement by other means;
 - Developing a CIPFA view of a target model for effective operation of independent assurance in the EITI reconciliation process;
 - Assessing risks to the operation of EITI, paying specific attention to issues relating to quality assurance of EITI data;
 - Reviewing the operation of EITI in some countries by reference to validation reports, reconciliation reports and other documents;
 - Developing preliminary views on how EITI might be improved, and making a presentation on these to the EITI Strategy Working Group
 - Testing the preliminary views against feedback from the EITI Strategy Working Group, EITI secretariat, World Bank, and other stakeholders;
 - Re-expressing the preliminary views in line with that feedback; and
 - Setting out more developed recommendations on how the EITI Board could improve or clarify quality assurance of EITI data
- 3.2 In line with the Terms of Reference, the CIPFA team gained an understanding of the EITI process through a combination of desk review and discussion with key stakeholders in EITI, including
- Discussion of the operation of EITI and the application of EITI principles, rules and guidance with World Bank employees, members of the EITI secretariat, and firms involved in the preparation of Validation Reports and EITI Reconciliation Reports.
 - Review of EITI formal pronouncements on the EITI website and in the April 2011 and November 2011 EITI Rules
 - Review of reports and EITI papers on 6 compliant countries selected by the World Bank, supplemented with review of publicly available material on some other countries.
- 3.3 At an early stage, the CIPFA team determined that audit terminology used in the EITI criteria and requirements is not consistent with usage by audit professionals using international standards, and most of the 'audit' reports attached to reconciliations begin by explaining that no audit has been carried out. While there is no strict need for EITI to maintain consistency with auditing standard setters, CIPFA reviewers were alerted to possible confusion that might arise from variant terminology.

- 3.4 While the CIPFA team sought to understand the entire EITI process, for the purpose of developing recommendations on issues relating to quality assurance of EITI data attention was focussed on those aspects of EITI relating to independent audit and assurance. An overview of the EITI governance and assurance environment is provided in section 4 (Modelling the EITI governance and assurance environment), and this also sets out how various activities and institutions contribute to independent assurance.
- 3.5 CIPFA recognises that EITI is seeking to achieve transparency and improvements to institutions, governance and systems which discourage or eliminate corruption and other practices which can become associated with the extractive industries. Independent audit and assurance is not a principal objective of EITI, but strongly supports the EITI process through its role as an indicator of the credibility of the EITI reconciliation reports. It also provides motivation for country improvement through those EITI criteria and requirements which are expressed in terms of independent audit and assurance outcomes.
- 3.6 CIPFA observations on the operation of EITI in practice are set out in section 5. Before we reviewed the sample country documentation we were aware that in many countries the components of independent assurance set out in the EITI requirements were not in place, even for some countries deemed compliant by the EITI Board. To inform our review of the sample countries we therefore developed a view of a 'target model' of independent assurance that might provide a systematic basis for assessing whether alternative approaches might be considered to provide an appropriate level of independent assurance or other reason for allowing countries to be deemed EITI compliant.
- 3.7 The 'target model' of independent assurance also informed development of CIPFA suggestions to improve EITI assurance in section 6. These are expressed slightly differently to the suggestions in the Henley presentation, having regard to comments made by members of the EITI Strategy Working Group and other discussion since that meeting.

4 Understanding the EITI assurance environment

- 4.1 To inform our work on data quality and assurance, the CIPFA team reviewed the governance, assurance and reporting environment in which the EITI process operates. In doing this we considered key components relating to government, extractive industries, stakeholder groups and the EITI process. We were keen to model the process in a way that applied to all countries, while recognising that some components of governance or assurance may exist partially, may not exist at all or may not operate effectively.
- 4.2 Even in the “ideal” situation where all aspects of governance, assurance and reporting are operating effectively, the assurance processes will still have limitations. 100% assurance is probably impossible to achieve, and if it were possible it would be extremely expensive.
- 4.3 We were also conscious that some important aspects of EITI reporting and reconciliation are more difficult to verify than straightforward cash payments to government. Non-monetary transfers (transfers of extracted produce in kind) may not be visible in accounting records, and their valuation may depend on volatile market prices and the timing of sales and conversion to cash. Flows or transfers going to third parties beyond companies and governments are also intrinsically more difficult to capture and reconcile than those within the normal boundaries.
- 4.4 A diagram setting out our view of the wider EITI environment is provided in Appendix B. Figure 1 below is a simplified diagram which has been coloured to show how the sources of independent assurance might fit together in an EITI reconciliation. The EITI process combines the work of the reconciler with the assurance provided through the audits of government and companies. The stakeholder group informs the development of the EITI process but is not in itself a provider of independent assurance.

Figure 1: Independent Assurance Aspects



- 4.5 The un-shaded areas in the Government and Extractive Industries boxes reflect aspects of the government socio-economic and administrative context (including political and legal systems, accounting, control and governance), and the extractive industries socio-economic and regulatory context (including systems, accounting, control and governance). The effectiveness with which these contextual measures are implemented in governments and companies has an impact on data quality. The most effective approaches to improving data quality and related reporting are through sound governance systems, including effective accounting and good internal control.
- 4.6 No matter how good systems of governance, internal control and internal assurance are, they do not directly provide independent assurance which must, by definition, be independent. These factors do however impact on the risk assessments which inform the work of independent auditors and reconcilers.
- 4.7 The CIPFA team have considered the risk factors associated with the components listed in figure 1 and set these out in a matrix at Appendix B. Addressing these risk factors falls outside the Terms of Reference for this report. Appendix B therefore only sketches potential mitigations for these, generally in terms of improvement over the medium to long term through targeted capacity development.

5 Observations on the operation of EITI in practice

- 5.1 The focus of this work has been on the components of assurance and governance used in the EITI assessment process to determine the sufficiency of transparency achieved. The main observation is that there is a diversity of practice which could undermine the credibility of the EITI brand.
- 5.2 Risks can be associated with the governance and assurance model but their importance varies, with some being fully addressed by existing EITI processes and some being minor and unlikely to prove problematic in practice. The main risk factors and some of their mitigations are outlined in Appendix B.
- 5.3 Some risks relate specifically to the EITI assessment process, some relate to public sector governance and financial management and some relate to private sector governance and financial management. Risks relating to public and private sector governance issues generally involve long term capacity development solutions that are outside the EITI's immediate scope to solve (though donors attention can be drawn to them). Good examples of such measures are: improving government revenue management systems, training public sector audits in financial audit and enforcing company audit requirements.
- 5.4 The focus of CIPFA's work in this area has been on the risks to the achievement of independent assurance, including:
 - Risks relating to interpretation of EITI pronouncements
 - Risks arising from non-compliance with assurance requirements in EITI rules
 - Risks arising from compliance with EITI rules which are at the less stringent end of the 'target' model (for example attestation).
- 5.5 EITI compliance can mean different things in different countries. EITI reports offer different degrees of reporting, assurance and transparency in different countries.
- 5.6 Support to the EITI process from government audit varies considerably; as does support from company audit, though to a lesser degree.
- 5.7 Below we pick out some key aspects of the diversity we have encountered from the case studies of the six countries we have examined in detail.

Key Features of EITI implementation in different countries

5.8 **Table: 1 Key Features and assurance outcomes of EITI Implementation in different countries.**

Country	Features	Assurance Outcomes
Central African Republic	Artisanal and few large companies comprise sector; General Inspection procedures underpin government audit; smaller companies higher risk; regional norms for reconciler standards. Progression towards greater resolution of un-reconciled differences.	Potential gaps in independent assurance, mitigated by disclosure of gaps
Liberia	Wide range of forestry, mining and agricultural sectors; demands high on reconciler; lack of some government information; unresolved discrepancies; evidential deficiency.	Gaps in independent assurance, mitigated by additional work by reconciler and disclosure of remaining gaps
Mongolia	Minerals, coal and oil. No mention of SAI audit in report. Some companies omitted. Scope of work review.	Potential gaps in independent assurance, mitigated by extensive work by reconciler and disclosure of remaining gaps. No reference to government assurance which is not referred to in the reconciler Terms of Reference.
Niger	Mining with oil recently added; Cour des Comptes provides specific no objection statement; Smaller companies higher risk; Full independence of collator's role queried; Use of local reconcilers.	Potential gaps in independent assurance, mitigated by additional work by reconciler and disclosure of remaining gaps.
Nigeria	High revenues from oil and gas industry; Signature bonus disputes. Substantial reconciler report; no definitive register of licence holders produced by government; Complex revenue flows to government; Incomplete company participation. Capacity building required for Government revenue service, and Accountant General Department.	Potential gaps in independent assurance, mitigated by extensive work by reconciler and disclosure of remaining gaps.
Norway	High proportion of GDP in extractive industries; Complete audit coverage of industry and government; highly regulated companies.	Independent assurance provided for all components of the reconciliation

Appendix D provides further coverage of the sampled countries.

Conclusions

5.9 There is considerable diversity of practice in the implementation of EITI reconciliations and reporting in different countries. While some degree of variation is necessary to reflect the different circumstances in each country, the lack of clear distinction between different levels of assurance may not drive improvement.

6 CIPFA suggestions to improve EITI assurance

6.1 In line with the Terms of Reference this report concentrates on approaches through which improvement might be achievable in a shorter timescale through adjustment of the EITI process.

6.2 The CIPFA team identified approaches to improving EITI assurance, as follows:

- **Clarifying** inconsistent or confusing terminology and explanations, mainly in **the EITI Criteria and Requirements**
- **Structural redrafting of the EITI guidance** so that the guidance at pages 14-30 of the 2011 Rules is consistent with the 'headline' Requirements at page 13. In particular, partial achievement of a requirement should be distinguished from full achievement.
- **Reframing guidance** relating to partial achievement of requirements to reflect the process the EITI Board could use to determine that the overall country achievement is sufficient.
- **Developing and agreeing a 'target' model** for EITI assurance, to inform the assessment of compliance with EITI assurance requirements where countries are not able to fully satisfy the headline requirements.
- Achievement of the 'target' model using '**country led' approaches**
- Achievement of the 'target' model through '**reconciler based' approaches**

6.3 In addition, linked to the clearer distinction between full and partial achievement of EITI requirements, the EITI Board would need to take a view on whether a failure to fully achieve EITI assurance Requirements was acceptable in the short, medium or long-term. We would expect this to depend on the specific type of non-achievement. The EITI Board could also consider whether to publicly signal different levels of assurance through 'scoring'. We understand that the Board is more generally considering 'scoring' different levels of EITI achievement of its requirements.

Assumption underlying the CIPFA review and analysis

6.4 The CIPFA review of papers and guidance was conducted on the basis of a view of the apparent intentions behind the EITI process, informed by our initial reading of the Principles, Criteria and Requirements and discussions with World Bank and EITI staff. A key aspect of this was that while EITI reconciliations were clearly not audits, the Criterion 3 reference to 'auditing standards' being applied to the reconciliation process was taken to indicate that they were independent assurance engagements which were somewhat similar to audits. In particular, reconcilers would be expected to have regard to the reliability of reconciliation data and not

take this at face value. In order to do this, the reconciler would need to obtain evidence themselves, or obtain information from independent third parties such as auditors.

Clarifying the EITI Criteria and Requirements

- 6.5 A review of the drafting of the 2011 EITI Rules, including the EITI Principles, Criteria and Requirements is attached at Appendix C.
- 6.6 A key observation is that the EITI Criteria make reference to audit and auditing standards. As explained at Appendix A, the terminology, practice and cultural context of audit varies considerably, and it is correspondingly difficult to formulate pronouncements in relation to audit which will be understood by all.
- 6.7 Against this background, Criterion 2 on the audit of revenue and payments is difficult to understand. It can be interpreted as setting out an ideal set of requirements that might be very difficult for many countries to achieve. However, it can also be interpreted with a narrow scope that may sometimes provide little support to the EITI reconciliation. It would be helpful to redraft the requirement. In order to do this, EITI would need to decide what it intended by the Criterion, and some redrafting of related Requirements would be necessary to obtain consistency.
- 6.8 In addition, Criterion 3 on the EITI reconciliation process refers to international auditing standards in a confusing way. This is because the EITI reconciliation is not a type of engagement to which the body of international standards relating to audit applies (that is, when using the term 'audit' as defined within those international standards). This seems inconsistent and has caused confusion in practice. We suggest that it would be appropriate to reframe this criterion in terms of international standards on independent assurance.
- 6.9 This could be linked to further guidance on the types of EITI reconciliation engagement in terms of the specific standards which can be applied to this work. We note that International Standard on Related Services (ISRS) 4400 was the main standard applied in the reconciliation reports reviewed by the CIPFA team.

Structural redrafting of the EITI guidance

- 6.10 A review of the drafting of the 2011 EITI Rules, including the EITI Principles, Criteria and Requirements is attached at Appendix C.
- 6.11 The CIPFA team found that the guidance on different EITI Requirements was very varied: the function of the guidance varied significantly, and in some cases the guidance might be considered to significantly modify or undermine the achievement of the headline Requirement.
- 6.12 The overall effect is that the Requirements do not function as the basis of a standard as that term is normally used in the accounting and auditing context. Instead, they might be seen as the basis for a framework for improvement, where compliance with the framework is principally assessed on the basis of 'best endeavours' and improvement plans rather than concrete achievements.

- 6.13 We would emphasise that this is a valid approach, and we understand that it is vital for EITI to promote improvement. We also recognise that even where the requirements are only partially satisfied (and in particular where unexpected discrepancies are being discovered and investigated) the EITI process can drive significant improvement.
- 6.14 We consider that it is confusing that the EITI Rules begin by setting out Criteria and Requirements, before providing further guidance which dilutes both the criteria and the requirements. In our view it would be clearer and more transparent if either
- The headline Requirements were reframed to reflect the extent to which they are contingent or aspirational; OR
 - The guidance attached to individual requirements was redrafted so that it principally provided guidance on how the requirement might be satisfied in practice, and any guidance provided on partial achievement of requirements clearly distinguished partial from full achievement.

In line with the underlying assumption explained at 6.4, CIPFA initially pursued the second approach.

Re-framing guidance

- 6.15 If the second redrafting approach at 6.14 was taken, then many of the countries currently deemed compliant would fail to achieve the revised requirements, only partially achieving some of the 'headline' requirements. This could be a particular problem in respect of audit of government accounts as required under Requirement 13. The Board would need to decide whether to
- revoke the compliant status of each country
 - to allow compliance for a transitional period; or
 - consider whether there was an acceptable basis for maintaining compliant status
- 6.16 If the Board took the third of these approaches, there would need to be guidance on the rationale on the basis of which countries could be deemed compliant. This would replace and reframe guidance including Requirement 13 a) iv which currently allows the Stakeholder group to deem the Requirement to be satisfied. New guidance would ideally be based on a view of the strengths, weaknesses and risks of the overall EITI procedure having regard to the strength of assurance and full compliance in respect of other requirements.

Developing and agreeing a 'target' model

- 6.17 The underlying EITI approach of reconciliation is very powerful, especially where disaggregated figures are directly agreed by Reconcilers and are made publicly available. Much of the benefit of the EITI reconciliation could in theory be obtained in the absence of the ideal scenario of high quality accounts, high quality EITI templates and full formal audit. However, this would only work if it were possible to be reasonably confident that the figures provided by government and by companies for reconciliation were truly independent and sufficiently complete.

6.18 The main threats to independence and completeness of data which would undermine reconciliation are

- collusive fraud resulting in co-ordinated omission or misstatement of data in company and government information
- dependency of one data provider on the other due to lack of accounting capacity and/or budget constraints

We mention these specifically because they are in effect the 'blind spot' which is not covered by a reconciliation based process, even in countries where the general ethical and governance environment and institutional capability are well regarded.

6.19 Having said this, we can see scope for achieving a substantial part of the benefit of EITI from the performance of a satisfactory reconciliation by an independent reconciler, supported by less than the 'ideal' assurances in respect of company or government audit. For example, where Requirement 13 in respect of government audit is not fully satisfied, the 'target' model might rely upon:

Full reconciliation with no discrepancies by a competent independent reconciler
Full audit of <i>company</i> templates by competent, independent auditors
Some alternative assurance or procedure which impacts against concerns about the risks of collusive fraud or dependency of one data provider on another

6.20 This 'target' EITI model would not provide a specific formal level of assurance. But neither would a full EITI reconciliation under most circumstances. One way of thinking about the 'target' model would be that it equates to the standard or 'ideal' EITI model with additional risks in case there are issues with fraud or dependency. It would be important that the reconciler had regard to any evidence that these risks might materialise, and highlighted any concerns they had.

6.21 Furthermore, in order for the 'target' model to be credible, it is vital that the other parts of the EITI assurance work effectively. If government audit is missing, then this would ideally be balanced by full audit assurance in respect of all material payments by companies. It is also vital that the EITI reconciliation process itself is carried out effectively, by an independent and competent reconciler that is able to gather evidence and resolve discrepancies through appropriate access to documents and people.

6.22 We should stress that the 'target' model proposed is not a standardised assurance product. It might also be considered a framing device for evaluation of current EITI compliance, whereby different EITI countries can be seen as operating more or less closely to the ideal model.

6.23 The target model might also be considered to inform progress toward full compliance, allowing countries to prioritise in a way which achieved the full requirement in respect of one strand of assurance, together with an acceptable alternative approach in respect of another.

- 6.24 We would note that in general, CIPFA would have some concerns if the target model were taken to equate to the 'full' model implied by the EITI Requirements. However, it could provide a credible and clear alternative for countries to work with in the absence of the ideal.

'Country led' approaches

- 6.25 Where the normal assurance for government or companies is not available, it is worth exploring whether there are alternative approaches which achieve a sufficiently similar result. This may be easier to implement and less costly where the approach can be modified through work done by similar parties to the normal EITI model.
- 6.26 This might involve a greater focus on the EITI figures, particularly where there are gaps in the overall financial reporting of government, or gaps in the coverage of government auditors, or gaps in company audit or reporting.
- 6.27 It might also involve assurance from parties other than the relevant auditor. It may also be worth considering if 'assurance gaps' can be compensated for by additional measures designed to enhance governance or control.
- 6.28 Possible country led approaches to obtaining EITI assurance include
- alternative assurance provided by the normal assurers. For example, government or private sector auditors could provide assurances on an EITI template even in the absence of accounts audited to an international standard.
 - auditors could provide a credibility check or a high level review rather than an audit. This only would only work if the right sort of information is available to check or review for credibility. It might be an approach which can be used to supplement Cours des Comptes and other approaches to state audit that confirm compliance with budget law, where these are effective, but which do not focus on full audit of financial statements, or involve any data testing.
 - assurance provision by internal audit or government inspectorates which are not formally independent. Under administrations based on former English and French colonial and Soviet regimes there may be 'internal' assurers who could provide this. In some cases there may be sufficient safeguards for this to be a long term solution. In other cases it may be acceptable as a short term measure.
 - assurance provision by public sector auditors who do not satisfy the independence requirements of INTOSAI, having regard to the possible risks from government influence.

These could in some cases result in something very close to the effect of full achievement of the relevant EITI Requirement.

- 6.29 Other possible modifications to existing EITI include

- reliance on Cours des Comptes and other approaches to state audit where these do not focus on financial statements or on EITI revenues: these may provide assurance on the systems of control or governance for government generally
 - systems/governance based solutions: one approach would be to accept strong systems of control or governance as a substitute for audit verification. We would not expect this to apply to companies.
 - attestation or representation by responsible persons: similar to the above, some comfort might be drawn from representations by senior officials or government ministers.
- 6.30 These approaches are rather different from those at 6.26, in that they are providing something other than assurance through verification procedures. The 'attestation' approach is currently referred to in Requirement 13, and the Validator's Report for Mauritania suggested that EITI should consider redrafting the requirement so that it could be allowed as a permanent or full achievement of Requirement 13. While we can see that these approaches have merit, they do not provide independent assurance and we consider that they should be distinguished from approaches which do.
- 6.31 Officially endorsed departures from the existing EITI process carry a number of risks, particularly where they make a qualitative change by replacing assurance with governance, control or attestation. However, they could be credible on a transitional basis or in the longer term if the difference from 'full' EITI compliance was signalled.

'Reconciler based' approaches

- 6.32 An alternative approach would be for the EITI reconciler to carry out additional work, to fill in gaps in independent assurance. This would differ from some of the 'country led' approaches, in that it would generally seek to obtain very similar assurances to those provided by full achievement of the relevant EITI Requirements. It would however focus mainly on EITI figures rather than government and company accounts.
- 6.33 The work would be mainly done by the EITI Reconciler firm, and would involve substantive evidence gathering and review of the type normally associated with audit.
- 6.34 If there were gaps in both government and company information, this approach would involve direct testing of both sets of information.
- 6.35 Even so, this work has limitations, which are similar to those attached to audit:
- The work would not provide 100% assurance (it might provide reasonable assurance and an 'opinion' in line with audit, or limited assurance and a correspondingly limited opinion, or a report of findings).
 - Nor would it be proof against fraud, particularly collusive fraud. Especially in countries with weak governance and systems.
 - In countries with very weak institutional capacity, even a reconciler based approach might fail to obtain the required assurance.

- Non-monetary flows and hard currency payments would still present verification issues.

6.36 Reconciler based approaches could also be used to extend the EITI process beyond the current requirements. For some EITI flows, it would be possible to incorporate tests on the completeness and correctness of revenue flows.

6.37 Reconciler based approaches would have both costs and benefits:

Costs

- There would be significant additional costs.
- For countries with very diverse flows, multiple sectors and many companies the costs could be very large.
- However, many Reconcilers already do extensive testing in order to achieve reconciliation.

Benefits

- Gaps in both government and company assurance can be addressed (as long as the systems, data quality and access to information are sufficient for the reconciler to carry out the work).
- It may be possible for EITI reports to have an 'opinion' which clearly signposts the overall outcome (although sometimes this opinion may need to be 'adverse' or 'disclaimed').
- Even where the Reconciler reports on their findings from agreed upon procedures, these findings may be clearer because of the increased evidence available to the Reconciler.

In summary the reconciler based approach could provide assurance which is in line with full achievement of the headline EITI requirements, but would add significant extra costs.

Approaches to different varieties of compliance

6.38 As noted at 6.3 and 6.13, if EITI makes a clear distinction between full and partial achievement of requirements, it will be necessary to take a view on what to do in cases where countries which are compliant under the 2011 would only partially satisfy requirements under new EITI Rules. One approach would be to immediately revoke their compliant status, or to require full compliance with the new rules within a specified timescale.

6.39 The EITI Board might consider that certain of the approaches which allowed under the current rules to be acceptable in the short, medium or long-term, even though they fall short of the full requirements. Under these circumstances we suggest that EITI should distinguish these lesser achievements from full compliance.

6.40 We understand that the Board is more generally considering 'scoring' different levels of EITI achievement of its requirements, generally. While we have not considered how this would apply to requirements which relate to matters other than independent assurance, we expect that these two approaches could be aligned.

Alternative views of EITI assurance requirements

6.41 As described at 6.4, CIPFA's review of papers and guidance was conducted on the basis that Criterion 3 implied that the reconciliation was part of an

overall assurance process, and that the reconciler would need to satisfy themselves that the information provided for reconciliation was basically reliable, having regard to the audit assurances on company accounts information and on government reporting required to satisfy EITI Criterion 2 and the headline text for Requirements 12 and 13.

- 6.42 In CIPFA's view, this is the most straightforward interpretation, but as discussed at Appendix C, Criterion 3 is confusingly drafted and it would be difficult to see how it could be interpreted literally. There are other ways in which Criterion 3 can be interpreted.
- 6.42 One alternative approach would be to consider the EITI reconciliation work to be a *specifically focussed assurance*, where the reconciler would need to satisfy themselves of the reliability of reconciliation data only inasmuch as this is specified in the reconciler Terms of Reference. In some EITI countries the Terms of Reference require the reconciler to obtain evidence that both government and company audit assurances have been delivered, and this will generally have the effect of converting a specific assurance requirement into an overall assurance requirement.
- 6.43 Another approach would be not to view the EITI reconciliation process as an assurance process at all. Given the confused drafting of Criterion 3 this may be a legitimate interpretation. However, we are not sure how different the work of the reconciler would be from specifically focussed assurance, given the requirement that the reconciler must provide an opinion.

Effect of the alternative view on CIPFA findings and proposals

- 6.44 While the CIPFA team carried out its review using the interpretation set out at 6.4, much of the analysis in this and earlier chapters would be unaffected if the interpretation at 6.42 was adopted. Specifically
- The Criteria and Requirements are unclear, and redrafting them would be beneficial
 - The diversity of practice in the implementation of EITI reporting, coupled with a lack of clear distinction between different levels of assurance may not drive improvement
 - The CIPFA 'target model' would provide a benchmark against which the achievement of independent assurance could be assessed.
 - Achievement of the target model could be progressed either using local institutions or through reconciler based approaches
- 6.45 In CIPFA's view, the EITI report would also need to transparently set out the extent to which it partially or fully achieved the headline text of the current EITI Requirements, which may go slightly beyond current reporting in some cases. For example, the parameters of the reconciler's work should be clearly explained, including any matters which the reconciler is *not required to consider*.

Drafting improvements

- 6.46 In line with our analysis, which reflects both CIPFA's underlying assumption at 6.4 and the discussion of the alternative view above, we

now provide more concrete suggestions on how EITI directives might be redrafted and the implications for other aspects of the EITI process. The exact form of such drafting would depend significantly on the redrafting and interpretation of Criterion 3.

Drafting implications for the EITI Criteria

6.47 Criterion 3 would be clearer and would better reflect the reality of the EITI process if it were redrafted so that it does not imply that the reconciliation should be conducted in accordance with international auditing standards. For example

- the reference to international auditing standards could be deleted;
- the Criterion could refer to *international assurance standards*; or
- the reference to standards could be directed at the inputs to the reconciliation, which in line with Criterion 2 are already required to be subject to audit.

6.48 In addition, agreement would need to be reached on how Criterion 3 is expected to be interpreted, and in particular whether it is intended to require *overall assurance* rather than a *specific focussed assurance*.

6.49 Criterion 2 is also extremely unclear. It would be beneficial if this was more clearly drafted. It may however, be less urgent – especially if the EITI requirements supporting Criterion 2 are redrafted more clearly.

Drafting implications for the EITI Requirements

6.50 In general, the EITI Requirements would be easier to understand if they were restructured so that

- the headline text clearly states the requirement which needs to be satisfied in order to achieve compliance;
- the supporting text provides further explanation, and may describe different levels of achievement, but does not include guidance on how the requirement may be deemed to be satisfied in cases where the headline text is not achievable.

6.51 It is difficult to provide more specific redrafting suggestions until the drafting and interpretation of Criterion 3 is settled. A possible approach using Requirement 13 as an example is set out on the next page.

REQUIREMENT 13 The government is required to ensure that government reports are subject to adequate assurance procedures, and that any gaps in independent assurance are transparently disclosed.

1. It is required that Government acknowledges responsibility for the accuracy of the information in the EITI templates, which must be signed off by senior government officials or ministers.
2. It is recommended that the government assurance process relies as much as possible on existing procedures and institutions, and on international standards.
3. The requirement for government assurance will be fully satisfied, and no additional disclosures will be required if:
 - Government EITI templates are audited by a Supreme Audit Institution or other independent auditor; AND
 - Government accounts which include the EITI revenues in the template are audited by a Supreme Audit Institution or other independent auditor; AND
 - Standards used for audit are based on INTOSAI International Standards for Supreme Audit Institutions (ISSAIs), or IAASB International Standards on Auditing (ISAs).
4. Disclosures in the reconciler's report will be required if
 - Either Government EITI templates or relevant Government accounts are not audited; this might include circumstances where government audits focus only on compliance with budget law
 - Assurance similar to independent audit is provided by parties who are not independent – this might include assurance by internal audit or from the work of inspectors or auditors who are not sufficiently independent to satisfy the independence requirements of ISSAIs 1 and 10.
 - Standards used for audit or other assurance are not based on ISSAIs or ISAs. (It may however be possible to use local standards if these are of sufficient quality)
5. The disclosures at paragraph 4 above allow an assurance process to be used which is not in line with the full requirements at 3. However, they do not provide sufficient support for the situation where the only assurance provided is attestation by senior officials or ministers in line with paragraph 1 above – this can only be accepted if the target model of assurance is obtained for Requirement 12.

[the requirements could rank various levels of assurance achievement in line with other EITI scoring proposals, with attestation lowest, full audit highest]

6. The full range of disclosures outlined at 4 above will not be required if this requirement is augmented with assurance from Requirement 12, in line with the EITI target model for successful reconciliation. That is, Requirement 12 is fully satisfied in respect of all material company information, and the reconciler's report provides a clear statement that the reconciler is not aware of any evidence that the information provided for reconciliation is incomplete. Under these circumstances, the reconciler's

report must disclose that the principal audit assurances for the reconciliation are provided through the audit of company information.

- 6.52 We would note that this is not a proposed redraft, but provides an example of how the wording of requirements might be restructured, including
- how partial achievement of the objective of the requirement might be handled;
 - a specific view of insufficient achievement; and
 - an indication of how both insufficient and partial achievement could be handled using the target model

Implications for EITI reporting

- 6.53 Specific suggestions relating to EITI reporting would need to reflect the drafting and interpretation of Criterion 3, and any consequential amendments to requirements which affect the EITI reconciler report, especially in respect of Requirements 12 and 13.
- 6.54 To provide transparent reporting on the overall EITI process, the reconciler's report should explain the basis of EITI compliance inasmuch as this affects the reconciler's report. This would describe any partial achievement of Requirements 12 and 13, including any aspects which the reconciler is not required to report upon – for example if the government figures were deemed to be assured purely through Supreme Audit Institution procedures which did not focus on or test relevant EITI data.

Implications for EITI process

- 6.55 The terms of reference for reconcilers need to set out the work of the reconciler and in line with 6.54 above
- Should set out the basis of how the reconciliation process satisfies the relevant requirements
 - Should require the reconciler to explain this in the reconciler's report
 - Should require the reconciler to make any other disclosures in line with the redrafted requirements.
- 6.56 Terms of reference for validators would need to reflect both the revised requirements and their implications for the reconciler's report.
- 6.57 MSG assessment processes would need to reflect the revised requirements.

7 Recommendations

7.1 In the light of our analysis in Chapters 3 to 5, and the suggested approaches for improvement outlined in Chapter 6, CIPFA would recommend that the EITI Board:

- **Clarify the EITI Criteria and Requirements**
 - The Board should decide what the meaning of Criterion 2 should be and redraft the criterion to explain this clearly.
 - Amendments should be made to Criterion 3 so that references to standards are consistent
- **Redraft EITI guidance to be consistent with Requirements**
 - The requirements and guidance at pages 13-30 of the 2011 Rules should be redrafted so that the supporting material at pages 14-30 supports and is consistent with the 'headline' Requirements at page 13. Partial achievement of requirements should be distinguished from full achievement.
 - CIPFA has paid particular attention to matters relating to independent assurance, but it may be appropriate to carry out other clarification and improvement.
- **Decide approach for handling partial achievement of the redrafted Requirements**
 - Inasmuch as this related to independent assurance, we suggest that EITI might frame this in terms of a target model
- **Develop and agree a 'target' model for EITI assurance.**
 - CIPFA has mainly considered the case where the reconciliation is carried out effectively, one of the audit requirements is achieved in full, while another audit requirement is replaced by an alternative assurance or procedure. The EITI Board might adopt this approach, or allow further modification, which would involve a further degree of risk.
- **Determine Board views and produce guidance on 'country led' approaches**
 - Examples of alternative assurances and procedures which might be acceptable in the context of the target model are provided in Chapter 6. Guidance would also be needed on how to distinguish more and less risky alternatives. This assessment of risk could also feed in to a 'score' which reflected the extent of achievement of independent assurance requirements.
- **Determine Board views and produce guidance on 'reconciler based' approaches**
 - The extent to which Reconciler based approaches need to function as a 'fall-back' may depend on the line which the EITI Board takes on partial achievement.
 - Some countries with large extractive industry revenues may see advantages in using 'reconciler based' approaches, particularly if they use them as a basis to go beyond EITI requirements
- **Reframe guidance and explain approach to partial achievement of requirements**
 - Partial achievement of requirements should be distinguished from full achievement.

If this process is to inform the next revision of the EITI rules in time for the 2013 EITI Conference, it will need to be planned to match key decision points against intervening working group and EITI Board meetings.

Appendix A

Notes on Terminology

Problems with the word 'audit' and its cultural context

Glossary of IAASB and INTOSAI acronyms and types of standard

Notes on the use of terms in this report

Problems with the word 'audit' and its cultural context

The word 'audit' is used differently in different countries and by different accountants and its meaning changes over time

- audit sits in law and in professions differently in different countries, even across Europe
- audit has a specific meaning in international standards for statutory audits of companies
- it has a slightly different meaning for international standards for the public sector
- most countries distinguish between accounting standards and auditing standards (whatever these refer to)
- BUT some countries deal with accounting and audit together, and may include auditing in accounting standards/guidance
- some countries use the term 'accountant' to mean auditor/assurer
- professional accountancy bodies can be audit-only, can exclude audit, or cover a wide range
- government audit in some countries is more related to law than to accountancy
- whereas in France the role of the Cour des Comptes has widened from a focus on fiscal regularity, this is not always the case in Francophone Africa
- roles and relationships of internal and external audit vary, especially in government, as do other control, inspection and assurance activities.

Glossary of IAASB and INTOSAI acronyms and types of standard

IFAC – the International Federation of Accountants. IFAC is a member body for professional accountancy organisations, many of whom are principally focussed on the statutory audit of companies

IAASB -The International Auditing and Assurance Standards Board IAASB is and IFAC board which operates as an independent standard-setting body that sets international standards for auditing, quality control, review, other assurance, and related services

ISAs - International Standards on Auditing are professional standards for the independent audit of historical financial information, by which is mainly meant the audit of financial statements of companies or other entities.

ISQC1 – International Standard on Quality Control 1. This standard sets out requirements for quality control of audits at the level of the firm or other organisation carrying out audit.

ISAEs – International Standards on Assurance Engagements. An assurance engagement is a more general type of engagement than audit and covers wider categories of information than financial statements. There are two types of assurance engagement: a reasonable assurance engagement and a limited assurance engagement. ISAE 3000 is used for some EITI reconciliation engagements

ISRSs – International Standards on Related Services These comprise 'agreed-upon procedures' and compilations. ISRS 4400 on agreed upon procedures is used for some EITI reconciliation engagements

INTOSAI – the International Organisation of Supreme Audit Institutions. INTOSAI operates as an umbrella organisation for the external government audit community

ISSAIs International Standards of Supreme Audit Institutions. These are standards developed by INTOSAI covering various aspects of the quality, performance and independence of public sector audit. Particularly important ISSAIs for the purpose of the EITI include

ISSAI 1 The Lima Declaration, which includes material on

- Independence
- Relationship to Parliament, government and the administration
- Powers of Supreme Audit Institutions
- Audit methods, audit staff
- Reporting

ISSAI 10 Mexico Declaration on SAI Independence

ISSAIs 1000-2999. Financial Auditing Guidelines, which provide guidance on the application of ISAs to the financial audits of government. Each ISSAI is in the form of a Practice Note plus the relevant ISA.

Notes on the use of terms in this report

Audit is generally used to refer to the independent or external audit of financial statements, except where it specifically refers to

- wider or differently focused audit carried out by public sector auditors, which may focus on budget compliance, regularity, or the achievement of value-for-money
- audit of specific figures in financial statements
- assurance on specific figures in financial statements provided by auditors who have audited the financial statements (although technically this is assurance rather than audit)
- internal audit

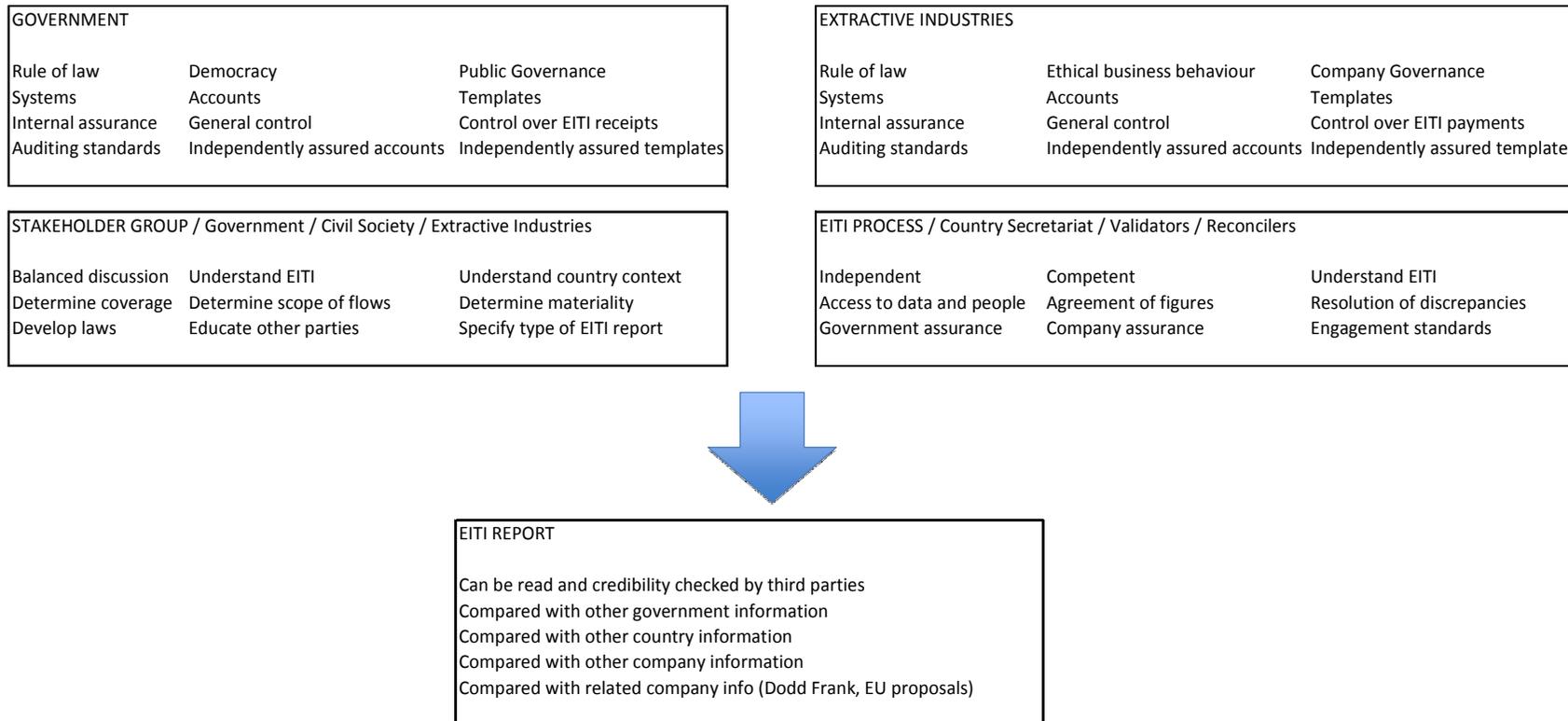
Assurance is used to refer to independent assurance and other assurance. Assurance is characterised as a verification process based on evidence. Representations or attestations by management or other persons charged with governance will not normally provide evidence in their own right for this purpose. We have tried not to include governance and control in 'assurance', although the term is used by some in this way.

Independent Assurance is a more general concept than audit, and includes engagements which provide similar levels of assurance to audit ('reasonable assurance'), lower levels of assurance ('limited assurance') and other engagements which may or may not give rise to a predetermined level of assurance.

Internal Assurance is not a standard term, but we have used it to bring together the various forms of assurance which are not independent in the sense used by IAASB. In Anglophone and some other countries these are formulated as internal audit, while slightly different approaches may be used in some Francophone and former Soviet regimes. In Francophone Africa the role of Inspectorate Generale and its equivalents may be similar to internal audit, or may be more akin to a Supreme Audit Institution, although it may not be able to satisfy ISSAIs on SAI independence.

We would note that the term 'independent' is also used differently by different professional bodies and this can cause confusion. The IAASB refers to 'independent audit' in contrast to 'internal audit' and characterises effective internal audit as 'objective'. The Institute of Internal Auditors takes a different approach, and defines internal audit as an independent, objective assurance and consulting activity.

THE EITI ASSURANCE ENVIRONMENT



RISK FACTORS AFFECTING EITI ASSURANCE

Risk	Sector affected	Potential Mitigation Approaches
<p>Socio-Economic Rule of law, democratic values, public and company governance and ethical business behaviour can be placed under stress due to civil unrest, man-made or natural disasters, war, poverty and endemic corruption.</p>	Government and Extractive Industries	Mostly beyond EITI mainstream but include national and local economic development and major donor initiatives.
<p>Public Financial Management Poor and inadequate development of PFM systems, accounting (accounts not finalised), Internal Assurance and Control mechanisms weak, dysfunctional or corrupted (Internal Audit, Controllers, Experts Comptables or Inspection regimes).</p>	Government	Capacity Development to strengthen PFM using for example PEFA analysis or in line with the model set out in the CIPFA publication "Public Financial Management: a Whole System Approach" and more recently, "Fixing the Foundations". Capacity Development to strengthen revenue and accounting functions (especially where raised by reconcilers in their recommendations). Full adoption of International Public Sector Accounting Standards. Internal Assurance mechanisms upgraded.
<p>Private Financial Management Risks Corporate governance, accounting, internal control and assurance maybe poorly developed, especially for smaller companies.</p>	Extractive Industries	Donor private sector development (around World Bank ROSC A&A) and wider economic development creating demand for better corporate behaviour. EITI pressure in localised areas.
<p>Government reporting capacity Government systems may not be able to produce template information in a timely, efficient and effective manner. Government systems may aggregate EITI information without an adequate audit trail.</p>	Government	EITI specific (primarily reconcilers) improvement possible but better if part of wider capacity development improvements.

<p>Company EITI reporting Companies may decide not to participate; company systems may not be able to produce template information readily in a timely fashion. Company systems may aggregate EITI information without an adequate audit trail.</p>	<p>Extractive Industries</p>	<p>EITI specific (primarily reconcilers) improvement possible but better if part of wider capacity development improvements.</p>
<p>Government Audit and EITI Audit SAI or other appointed auditors of government may:</p> <ul style="list-style-type: none"> • be incapable of auditing government accounts due to independence, training and resource issues; • not focus on financial statements; • not conduct audit in accordance with appropriate standards (ISSAIs or adequate local standards); • not provide a view on EITI templates. 	<p>Government and EITI Process (country secretariats, validators, reconcilers)</p>	<p>INTOSAI capacity development (potentially IDI), professionalisation and country led initiatives.</p>
<p>Company Audit Company audit may not be well developed. Smaller operators may not be subject to audit. Audit may not be a regulated profession in country. Auditors may not be member of an IFAC member professional body. Auditors may not use International Standards on Auditing or adequate local standards for public audit work.</p>	<p>Extractive Industries</p>	<p>Donor private sector initiatives (around World Bank ROSC A&A). Develop EITI guidance with regard to smaller operators. Development of appropriate professional regulation. EITI participants to review implications of lack of compliance with standards on case by case basis.</p>
<p>Company EITI audit specific Company auditors may not provide a view on EITI templates thus undermining assurance and independence from company templates.</p>	<p>Extractive Industries and EITI process (country secretariats, validators, reconcilers)</p>	<p>EITI participants to push for country led changes and if not feasible assess the risk in the local context.</p>

<p>Threats to independence Civil society participation may be ineffective, Government involvement may be inappropriate, Local firms involved in reconciliation maybe too small to avoid conflicts of interest. EITI secretariat may become over engaged and directive.</p>	<p>Stakeholder Group (Government, Civil Society and Extractive industries) EITI process (country secretariats, validators, reconcilers)</p>	<p>Country led changes and improvements to the terms of reference for reconcilers.</p>
<p>Poor understanding of EITI Stakeholders may have difficulty understanding the application of standards to EITI reporting, and the respective roles of auditing and accounting standards. Validators may draw conclusions that meet the letter but not the spirit of EITI guidance. Some reconcilers may have difficulties understanding the application of standards to EITI reporting. Stakeholders may develop alternative or temporary measures which are not fully aligned with EITI objectives.</p>	<p>Stakeholder Group (Government, Civil Society and Extractive industries) EITI process (country secretariats, validators, reconcilers). EITI Secretariat.</p>	<p>Clarify EITI principles, inform (educate) stakeholders and validators, standardise guidance, inform all of options and what is allowable in principle and provide guidance.</p>
<p>Specification of EITI work Stakeholders may not consider all issues relevant to determining the company coverage, scope of flows and nature of EITI work. Consideration of materiality may not be sufficient and barriers to implementation may not be addressed in TORs.</p>	<p>Stakeholder Group (Government, Civil Society and Extractive industries)</p>	<p>Address any threats to understanding or independence through improved EITI guidance.</p>

<p>Reconciler and validator competence Reconcilers and validators may have insufficient understanding of assurance and extractive industry issues. If audit is not a regulated profession and or local professional bodies are not IFAC members (or robust enough) it may be unrealistic to apply IAASB standards.</p>	<p>EITI process (country secretariats, validators, reconcilers).</p>	<p>Review risks. Build capacity through IFAC PAODC and near country partnerships. Appoint reconcilers and validators with assurance expertise available to them.</p>
<p>EITI report process Reconcilers may face limitations on the scope of their work, such as access to people (especially in government) and data. Reconcilers may not be able to agree figures or resolve discrepancies due to inadequate disaggregation or other deficiencies.</p>	<p>EITI process (country secretariats, validators, reconcilers).</p>	<p>Country led changes, scope limitation, report of findings, scope limitation.</p>
<p>Usefulness of the EITI report An unreliable EITI report clouds transparency. The utility of an EITI report is reduced if other government or company information is unavailable for comparison. Insufficient disaggregation may reduce or cloud transparency; too much disaggregated information may result in information overload unless tools to aid analysis are provided.</p>	<p>Government. Extractive Industries. Stakeholder Group (Government, Civil Society and Extractive industries) EITI process (country secretariats, validators, reconcilers). EITI Secretariat.</p>	<p>Report should be read and credibility checked by third parties (compared with: other government, other country, other company and related company, information). All previous points apply to this risk. Disaggregation maybe partially addressed though electronic tagging of data and similar measures.</p>

Appendix C

Comments on the drafting EITI Principles, Criteria and Requirements

Overall Comment

The EITI Rules are helpful and constructive, and should serve to drive improvement. However some redrafting seems necessary and other clarification may be desirable.

Principles

The EITI Board may wish to consider whether data quality or independent assurance should be directly referenced in the Principles.

Criteria

Criterion 2 on the audit of payments and revenues is written too concisely to be interpreted unambiguously, and we cannot build up a clear view of the intention of the criterion. The effect of the current drafting may be to produce requirements which are too strong or, paradoxically, too weak. There is also little scope to form a balanced view where strong assurance from one source may compensate for weaker assurance from another source.

Criterion 3 on EITI reconciliation is not clear and it is difficult to see how it could be satisfied if interpreted literally. The EITI reconciliation is not an audit as that term is used in the international auditing standards to which it refers. The Requirements relating to this criterion provide no clarification or guidance

- On the use of standards by the Reconciler;
- in respect of the independence or competence of the Reconciler.

We are also not sure what the criterion intends by the term 'administrator'.

Requirements

There are some cases where the drafting of guidance is unclear or may be inaccurate.

Guidance on materiality attached to Requirement 9 establishes a tension between different types of materiality which may significantly increase the cost of EITI reconciliation, without providing any guidance on how this should be resolved.

More generally, the status of guidance attached to requirements is not clear. While the 'headline requirements' on page 13 are supported by additional text on pages 14 to 30

- some supporting text provides specific guidance on how the requirement should be achieved, and might be considered part of the requirement
- some text describes process steps to be taken before the requirement is achieved, but does not equate to achieving the requirement.
- Some text seems to equate achievement with stakeholder perceptions of achievement.
- Some supporting text seems to override the headline requirement

This lack of clarity is compounded by the fact that Validators are given guidance on some requirements which allows a 'best endeavours' approach to achieving improvement, or allows for acceptance based on 'action plans' rather than actually achieving the requirements as set out on page 13.

Scope and limitations of this drafting review

The drafting comments in this Appendix are made on the Principles, Criteria and Requirements as set out in the November 2011 document *EITI Rules, 2011 Edition*.

While the comments focus on the drafting in that document, they also have regard to issues which may arise in practice from the application of the Rules, based on CIPFA's review of validation and reconciler reports for the sample of 6 countries specified for this assignment, and other countries including Azerbaijan and Mauritania where review was carried out on some publicly available papers.

CIPFA recognises that the validation and reconciler reports reviewed will have mainly been developed in the context of earlier versions of the EITI Rules. The November 2011 Rules seem to be clearer and to represent an improvement over the previous edition. It is possible that some of the risks identified in this review might not materialise when the 2011 Rules are used, especially where the EITI approval processes are supplemented by knowledgeable review of the EITI Validation and Reconciler reports by the EITI secretariat and the EITI Board.

We would also note that CIPFA's views on issues which have arisen in practice may reflect discussions by stakeholders and validators who do not speak English as a first language and in some cases may reflect English translations of reports initially drafted in other languages. There is therefore a risk that issues identified in documents written in English may not reflect the facts as intended by the non-English drafters or stakeholders. We have endeavoured to manage this risk in various ways: two of the team members specialise in international work; another team member is familiar with translation issues addressed by IFAC standard setters and the particular initiatives undertaken in the Clarity redrafting of International Standards on Auditing; the team also included a capable French speaker.

Notes on EITI Principles

We have no drafting observations to make on the EITI Principles, which seem to provide helpful information on

- beliefs underlying the EITI project
- aspirations of the EITI project
- scope of the EITI project
- practicalities and limitations of EITI
- the need for countries to retain ownership and sovereignty
- the need for engagement of stakeholders outside both government and the extractive industry

The EITI Principles do not necessarily link directly and systematically to the Criteria and Requirements.

In particular, the Principles focus on transparency, accountability and related reporting.

There are no explicit references to data quality, or to independent audit or assurance.

This may be because these are deemed to be included within transparency and accountability. Alternatively it may reflect an early view on the strength of the reconciliation process, which might be seen as reducing the need for audit or other independent assurance.

The CIPFA team has no strong views on this matter, and indeed, it may be more appropriate to introduce assurance considerations in the Criteria, which is the current approach.

Notes on EITI Criteria

The Criteria generally

The Criteria seem to take forward the Principles in a manner which generally supports a robust and flexible EITI process which fosters improvement and recognises achievements in improved reporting, data quality as evidenced through independent assurance, stakeholder engagement, and other improvements.

Unlike the Principles, two of the six Criteria specifically mention the need for independent assurance which they suggest should be achieved through independent audit, and they also suggest that international auditing standards should be applied.

The criteria are however expressed very compactly, which may result in

- a lack of clarity in criterion 2. The word 'audit' can be interpreted in a variety of ways; there is a tension between the way the word is understood by the general public and more specialist interpretations by audit and assurance professionals;
- problems in interpreting criterion 3, which refers to international auditing standards while using different language to that used in international standards, and applying the term to a process which would not be considered to be independent audit when using the terminology of international standards.

Criterion 2

Where such audits do not already exist, payments and revenues are the subject of a credible, independent audit, applying international auditing standards

This criterion seems to be talking about audits as if audit were a process that applies to specific figures (payments and revenues). However, it is more usual for audit engagements to be carried out on the financial statements of a single entity (or consolidated financial statements of a group entity controlled by a parent entity). Without additional work the audit may not provide specific assurance on particular figures in the financial statements.

Also, except inasmuch as it refers to 'audits' in the plural, the criterion may not engage with the practical implications of the fact that the revenues may sit in the financial statements or the accounting records of several government departments or agencies, and the corresponding payments sit in the financial statements and/or records of a potentially large number of companies.

What we believe the Criterion endeavours to encompass is that

- Government revenues relating to extractive industries should be subject to adequate audit assurance processes
- Extractive Industry Company payments to government should be subject to adequate audit assurance processes

This may be a clearer formulation, but 'adequate audit assurance processes' still needs further clarification. We can envisage an idealised formulation of this, but if this is used as the basis for requirements they may be more onerous than EITI would wish.

In the ideal, the audit assurance for government revenues should be backed by

- the audit of relevant government accounts (otherwise there is a greater risk that revenues received but not included in EITI templates would not be detected)
- specific assurance on EITI revenues or other measures which relate the audited accounts to the EITI templates
- audit by an auditor such as the Supreme Audit Institution for the country
- audit performed in accordance with local standards drawn up by reference to International Standards of Supreme Audit Institutions (ISSAIs) or through direct application of ISSAIs or of ISAs.
- standards compliance to specifically include achievement of auditor independence requirements of ISSAIs 1 and 10.

To frame a criterion and related requirements which are less than this ideal, the EITI Board would need to consider whether it is content to allow risks relating to the independence of the SAI, whether different (or no) standards might be applied, and whether to allow the scope of audit to be restricted to the financial statements, or to be restricted to the EITI templates.

The Board would also need to consider whether, in the interests of driving improvement, it is content to allow gaps in independent government audit assurance to be filled on a more or less temporary basis by measures which **do not provide independent assurance**, or which represent plans **or promises to provide independent assurance at a later date**.

The Board's view on this would ideally drive the drafting of requirements, which currently allow independent assurance requirements to be formally satisfied by measures which do not provide independent assurance.

It is important that if the EITI Board allows approaches which are not based on current achievement of independent assurance; these should not be represented as reflecting independent assurance.

Similar points apply to the adequacy of audit assurance on Extractive Industry Company payments to government, which would ideally be underpinned by

- the audit of relevant company accounts
- specific assurance on EITI payments or other measures to relate the audited accounts to the EITI templates
- audit by a competent independent auditor
- audit in accordance with ISAs or comparable local standards.

Criterion 3

Payments and revenues are reconciled by a credible, independent administrator, applying international auditing standards and with publication of the administrator's opinion regarding that reconciliation including discrepancies, should any be identified.

Meaning of 'Administrator'

Criterion 3 refers to the reconciliation by a credible administrator, applying international auditing standards, and to the publication of an opinion.

We are not sure what the criterion intends by the term 'administrator'. This may be a term which is more meaningful in other languages than UK English or under legal or regulatory arrangements other than those with which we are familiar. We presume that the intention of the term is to refer to a competent and independent person or firm without specifically requiring them to be an audit or assurance professional.

Although the term may be unclear we have seen no indications that it is causing confusion or difficulties in application.

References to audit and 'international auditing standards'

The criterion refers to 'international auditing standards'. We would note that

- The main international standards for auditing are set by the International Auditing and Assurance Standards Board (IAASB).
- Their auditing standards are International Standards on Auditing (ISAs), which primarily focus on financial statements
- ISAs **do not apply** to engagements like EITI reconciliation reports as they appear to be being carried out
- in general, the reconcilers do not claim to be following ISAs, and in many cases they specifically explain that their work is not an audit
- the majority of the engagements seem to be being carried out as agreed upon procedures engagements in accordance with International Standard on Related Services (ISRS) 4400
- other engagements have been reported as being carried out in accordance with ISAs, or with International Standard on Assurance Engagements (ISAE) 3000, or have not referred to the standards used

In the light of the above we considered that it is potentially very confusing to represent EITI reconciliation work as being generally conducted in accordance with 'international auditing standards'.

We have identified at least one case where the **civil society stakeholders were very concerned that this criterion was not satisfied**, and may not have been convinced by the Validator's explanation that the criterion was not meant to be literally complied with. (Azerbaijan Validation Report page 20, in discussion of Indicator 12). In the same section of the report, the fact that the EITI reconciliation process was not an 'audit' was used to justify a lower standard of evidence for company payments (i.e. audited financial statements without any supporting work on templates). **We were not confident that the logic of this is in accordance with the intention or spirit of EITI.** We would note that the

Validator did express concern over the lack of clarity in Indicator 12. It may be also be that this decision could have been justified in other ways.

Use of other standards and references to an 'opinion'

While other international standards can potentially be applied to EITI reconciliation, some may be difficult to apply in all cases, while others may not provide an 'opinion' in the way in which that term is used in the relevant international standards.

We note that some Reconcilers have applied ISAE 3000, *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*. It may seem strange to apply this standard to EITI Reports which should very definitely be constructed from historical financial information. However, we can see that EITI reports are not the same as the historical information envisaged by IAASB for the purpose of audits and reviews, that is, financial statements relating to a single reporting entity or a consolidated financial statement of a group of entities under common control.

We note that ISAE 3000 is relatively similar to audit, and that engagements can be conducted to provide 'reasonable assurance' in the same way as audit, giving rise to a positive 'opinion' in the assurance professional's report. ISAE 3000 engagements can also be formulated in terms of 'limited assurance' which is less than 'reasonable assurance', and where a successful report mainly notes that no matters have come to the attention of the assurance professional which suggest that the information is materially incorrect.

We can see some challenges in applying ISAE 3000 to EITI reconciliations without carrying out a lot of testing on government and company systems and records. The ISAE 3000 report that we saw contained caveats that may have the effect of rendering it more like an agreed upon procedures engagement.

The majority of reconcilers seem to be applying ISRS 4400, *Engagements to Perform Agreed-Upon Procedures Regarding Financial Information*, and in practice most of the other reports were presented in a similar manner to agreed-upon-procedures work. The reporting under ISRS 4400 primarily provides an account of how the assurance professional has performed procedures specified by the client responsible for the engagement, together with factual reporting on findings. No 'opinion' is provided – the report is primarily focussed on providing the client with information they can use to form their own views. The effect of this can be to make it quite difficult to read some of the Reconciler's reports where performance by governments and companies has been patchy. One of the reconcilers we spoke to suggested that it might be better to develop a standard which was based on ISRS 4400, but where the form of the report on findings was more tailored to the needs of readers of EITI reconciliation reports.

While we did not consider there were major problems in the reporting for the six sample countries, we agree that it should be possible to improve the form of reporting, and it would be worth considering how to do this by reference to available standards when carrying out necessary improvements to the drafting of Criterion 3 and related requirements.

Notes on EITI Requirements

Requirements generally

- some supporting text seems to provide specific guidance on how the requirement should be achieved, and might be considered part of the requirement
- some text describes process steps which might be taken before the requirement is achieved, but does not equate to achieving the requirement.
- Some text seems to equate achievement with stakeholder perceptions of achievement.
- Some supporting text seems to override the headline requirement

Some of the requirements are articulated using vocabulary such as 'should' which can give rise to confusion when translated into some languages.

Some of the requirements are articulated in terms of 'ensuring' which can in some cases be impossible to achieve. (Perhaps in recognition of this, the guidance is generally framed in terms of 'taking steps to ensure').

Requirement 9

Materiality is an area where the guidance is not clear. Furthermore, our discussions with reconcilers indicate that this is the area where more and better guidance would be particularly helpful.

We would note that in financial reporting and auditing/assurance contexts various different definitions of materiality are used, and that separate consideration is given to materiality relating to triggers for recognition in reports, separate disclosure in reports, and acceptable levels of possible error.

Several EITI Requirements include references to materiality, materiality thresholds, material flows and individually material payments or revenues, but the different uses are not all clearly distinguished.

Requirement 9b describes what is meant by a revenue stream being material, using wording which may be modelled on definitions used in audit and financial reporting. It is however a more specific description and does not read easily against other uses of the term 'material' and discussion of 'materiality thresholds'.

Requirement 9d encourages Stakeholders to consider the size of EITI flows having regarded to the overall financial context, but at the same time asks them to consider flows in terms of institutions or regions receiving them. While this is logically consistent and may be important for some aspects of transparency, it may have the effect of multiplying some of the EITI reconciliation workload by a factor proportional to the number of regions or institutions involved. No guidance is provided on how the benefit of additional transparency should be balanced against possibly very considerable extra cost.

Materiality also figures in some determinations of the companies which should be included in the EITI process, and in some countries we note that all companies and persons in the extractive industries are included in the reconciliation. This can cause problems, especially for small scale operations or persons who might not normally prepare accounts of any kind, and for whom requirements for audit or

EITI templates might be considered disproportionate. The effect in several countries has been to increase the level of unilateral reporting and of EITI templates not supported by company audit.

Requirement 10

Appointment of Reconcilers is perhaps an area where more substantial guidance is necessary, but it might not be appropriate to include this in the EITI Rules; it may be that such guidance exists outside of the EITI Rules.

Requirement 11

The headline requirement is that governments should 'ensure' adequate participation in EITI reporting. However, supporting text c) is framed in terms of reasonable steps, rather than achieving the requirement.

This approach is not unreasonable, but it does not equate to satisfying the requirement.

General comment on Requirement 12

The headline requirement is that the government ensure that company reports (which we assume means reports based on EITI templates) are based on accounts audited to international standards.

The supporting text in a) i-v sets out a list of 'reasonable steps', rather than explaining what it means to achieve the requirement. These steps might be misread as reflecting achievement of the objective. We know that some Validators have suggested that step a) v should be sufficient and e.g. recommended that Mauritania be deemed compliant on this basis.

Specific issues with Requirement 12, content of supporting text a) vi

Furthermore, the supporting text at a) vi allows for the headline requirement to be suspended if the stakeholder group is content that the problem is being addressed. The specific proposal is that there is a time bound action plan, which at least suggests that the suspension of the requirement is temporary, but if this is the intention it would be better if this were made explicit.

It is worth pointing out that supporting text at b) sets out a model whereby companies provide both audited accounts and additional assurance from auditors on the 'company reports' (which we assume means EITI templates). This is an excellent starting position, and the Requirement would be improved if this were represented as the default position, while noting that other approaches with similar effects are used in some countries.

Drafting error relating to Requirement 12, content of supporting text a) vi

The supporting text at a) vi seems to be misdrafted, conflating auditing standards with reporting standards, as follows

*vi. where **figures submitted for reconciliation are not to audited standards**, the multi-stakeholder group is content with the agreed way of addressing this, for example, by developing a time-bound action plan for ensuring*

*that company reports are based **on audited accounts to international standards.***

'Figures' cannot be 'to audited standards'. They can be part of accounts prepared in accordance with accounting / financial reporting standards. Or they can be subject to audit which is carried out in accordance with auditing standards. This may be particularly confusing for countries which do not distinguish between a body of auditing standards and separate accounting standards.

A more accurate draft would be as follows:

*vi. where figures submitted for reconciliation are not **audited in accordance with international** standards, the multi-stakeholder group is content with the agreed way of addressing this, for example, by developing a time-bound action plan for ensuring that company reports are based on accounts **which have been audited in accordance with** international standards.*

We know that this is an area where stakeholders and validators may have been confused: while accounting standards are a relevant issue for stakeholder groups to consider, they may have done so for the wrong reasons. We have also noted instances where the basis for measuring the figures (which is an accounting matter) has been represented in the Terms of Reference as relating to auditing standards.

Having said this, despite apparent confusion in this area, it is not clear that there has been any adverse effect on the validation process.

Other comments on Requirement 12

While not drafting issues, we would note that there may be some confusion about how this standard is applied to small (especially non-company) operators, who may not produce accounts or submit them for audit. Also to circumstances where not all companies provide audit certificates. The EITI process seems to have an element of proportionality built in to the principles but it is not clear how this is explicated in the rules.

Requirement 13

Similar comments apply as apply to Requirement 12. The overall requirement is a strong one, and 13 b) mentions the possibility of SAI certification of EITI templates provided by government. Doing this in addition to government audit of accounts would be the ideal. In the absence of government audit of accounts this may be a practical expedient.

However, section a) reads as if it were scene setting for non-achievement of the objective. Text at a iv) provides for the MSG perception that the situation is satisfactory (e.g. because there is an action plan) and we know that some countries Validation reports have suggested that a iii) should be sufficient to represent achievement of the objective. Whereas we would see it as a starting point.

Requirement 17

The reconciler must ensure that the EITI Report is comprehensive, identifies all discrepancies, where possible explains those discrepancies, and where necessary makes recommendations for remedial actions to be taken.

This requirement is not supported by any additional guidance.

As expressed the first aspect of this requirement may be unachievable, and we have certainly noted cases where the Reconcilers make it clear that it is not achieved in literal terms.

The reconcilers appear to have addressed a reasonable interpretation of the requirement, by

- Taking reasonable steps to construct a comprehensive Reconciliation which satisfies the reporting requirements set out in their Terms of Reference;
- Having regard to the fact that achieving reconciliation with all discrepancies resolved provides some assurance in connection with completeness; furthermore, in some cases where discrepancies cannot be resolved, it may be possible to gain assurance that the error or omission relates to a sum which is not greater than the discrepancy.
- EITHER Taking some steps when reviewing the data from which could in principle identify omissions, but explaining that their work cannot identify all omissions; OR Explaining that their work cannot identify omissions if those omissions affect both company and government templates.
- Identifying all discrepancies in the information provided to them.
- Resolving all discrepancies where they have access to relevant data or persons, or can achieve reconciliation with the assistance of the EITI secretariat
- Where possible, resolving any remaining discrepancies.
- Drawing attention to problems identified during the reconciliation process and making recommendations as to how these could be addressed.

It would be helpful if this Requirement was drafted in line with the redrafting of Criterion 3.

Appendix D: Summary of EITI Assurance Outcomes for Sample Countries

Country	Industry Characteristics	Audit of Government Accounts and EITI Templates	Audit of Company Accounts and EITI Templates	Reconciliation effectiveness	Reconciler Standards Used
Central African Republic	Mining sector with small number of industrial miners in exploration phase. Artisanal mining currently prevails. Many cash payments poorly recorded in manual ledgers if at all.	Reliance on internal control and inspection procedures.	Many small artisanal mining companies not audited. Larger companies audited by a member of the Ordre des Experts Comptables agréés (ONECA) in compliance with OHADA accounting chart principles.	First reconciler report showed major un-reconciled differences (co-operation problems not resolved). Second report more successful but still had shortfalls (3% in 2009).	"Regional norms" and EITI procedures.
Liberia	EITI covers Agriculture (Rubber and Palm Oil), Forestry, Mining (includes Diamonds, Iron, Gold) £72 million EITI revenues No materiality. All transactions to be covered.	Auditor General committed to use ISSAI standards. Arrangements for audit of government EITI templates in place. However, did not materialise because relevant Ministries did not provide required	Legal requirement in place for audits of EITI companies above a certain size. Linkage between accounts and EITI templates. However, audited company information far from complete.	The unresolved discrepancy <i>from submitters</i> assessed as not material. A material but nevertheless relatively small proportion by value of company figures was unresolved mainly due to lack	No standards declared in Reconciler report. Work done and style of Report of Findings appeared to be Agreed Upon Procedures plus very substantial additional work by the Reconciler to resolve

	119 companies identified, plus aggregated government figures for pit sawyers and for small scale miners. Most of revenue from about 20 companies.	evidence.	Essentially no returns from non-company operators. <i>The reconciler demonstrated significant capacity to pursue information and resolve discrepancies.</i>	of company side information from some companies and non-company small operators.	discrepancies in the face of lack of government or company information.
Mongolia	Minerals, coal, oil. Mining industry accounts for 55 percent of industrial output and generates 33 percent of government revenues. Not clear if this encompasses oil. 360 companies registered with the tax office, many are small operators. 101 companies included in 2009 reconciliation.	Mongolian NAO reckoned capable, but not clear how closely their work is aligned with the EITI figures. Validator concerns due to Donations not being recognised in reports which would be looked at by MNAO. No references to MNAO work in the Reconciler's report.	ISA audits required by law, but only evidenced for 31 companies. Observations made on non-compliance with IFRS, but not clear how relevant all of these are to the EITI flows.	6 companies not covered because omitted from govt info used to plan the work. Scope of EITI work requires review to reflect material flows including: Sales of Government Bonds, sub-contractor payments Donations to non-government bodies not reconcilable and need to be excluded from reconciliation requirement. Very significant work required to	(Hart Nurse + Ulan Bator Audit Corporation LLC) Agreed upon procedures.

				achieve reconciliation within required tolerance.	
Niger	Primarily mining but recently oil added. Sharp fall in revenues in 2009 (419 million USD to 143 million USD) and fewer companies reporting (63 down to 39).	Cour des Comptes (CNC), comprising sworn senior magistrates, reports, on the formal budget law compliance of the Government financial statements. CNC issued a 'no objection' statement on the Government EITI data.	Major companies have their annual accounts audited by international auditors and follow OHADA (Organisation for the Harmonisation of Business Law in Africa) West African Accounting Standards.	EITI Secretariat used as Collator, and Validator report hints at independence risk. Representative MSG considered process effective.	Reconciliation not an audit. Signed as "Expert comptable, Commissaire aux comptes." Claim to have followed procedures as defined by IFAC and IASB (norms ISA)
Nigeria	Substantial revenues (financial flows to government total USD 60,364.5 million); Payments in kind; Complex industry situation, including: taxation, signature bonuses (in dispute between government and companies), royalties; three	Government audit carried out according to Nigerian Audit Standards in accordance with the requirements of the Institute of Chartered Accountants of Nigeria (ICAN) which were deemed consonant with international standards.	NEITI Act makes it an offence for any company to misrepresent any record. A legal requirement for international standards exists. ICAN has a compliance role. Reconciler requested letter of representation from company auditors to confirm	Yes at 5% materiality. Several unresolved areas for further consideration and recommendations for public sector bodies to receive capacity development.	International Standard on Related Services applicable to agreed upon procedures.

	companies non-participating; some weak government systems identified.		compliance.		
Norway	Substantial revenues (265,957.2 million Norwegian Kroner in 2010); Straightforward tax and state shares of cash flows form oil and gas production	State Oil receipts to the Central Bank. The Auditor General uses international standards under Norwegian law.	Validator judgement that international standards used (all major companies involved). Request for companies to attach audit reports as part of reporting material.	Reconciliation successful.	ISRS 4400 Engagements to perform agreed upon procedures regarding Financial Information