AUDITING, ACCOUNTABILITY AND ANTICORRUPTION:
MULTILATERAL LENDING TO LEGISLATIVE BUDGET OVERSIGHT
AND EXTERNAL AUDITING OF PUBLIC FINANCES IN LATIN AMERICA

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INTRODUCTION: IMPROVING GOVERNANCE AND CURBING CORRUPTION IN PUBLIC FINANCE

Reforming budgetary institutions is a critical task for emerging economies seeking to strengthen economic governance, enhance government accountability and curb corruption in public finances. There is heightened recognition that rule of law in public finance management requires reinforcing those institutions tasked with overseeing government, especially in presidential systems. There is indeed heightened awareness of the weaknesses of the mechanisms of government oversight in presidential systems and the consequent need to enhance the institutions of ‘horizontal accountability’ (O’Donnell 1994, 1998, 1999; Mainwaring and Welna 2003). A central thrust of current efforts at reforming the state resides in the building of robust institutional checks and balances within the state, so that the state can self-restraint itself (Schedler 1999).

As a result, the governance of the budget and the mechanisms of integrity in public finance are the subject of renewed scrutiny. It is increasingly recognised that the quality of the public budgeting is a critical determinant of good government. Mitigating the risks of excessive executive discretion in economic policymaking necessarily requires reinforcing the countervailing mechanisms of government accountability in public finance management. Consequently, the role of legislatures and the contribution of supreme audit institutions are being reassessed, putting the reform of governmental financial management in the broader political economy context of executive-legislative relations in the budget process. There is heightened awareness on the role of parliaments in the budget process and their responsibility in ensuring government accountability (Santiso forthcoming; Schick 2002, 1998; 1990; Wehner 2004, 2002; OECD 2001b; Manning and Stepenhurst 2002; Krafchik and Wehner 1998; Petrei 1998.)

Legislative budget oversight by critical legislatures and external auditing of public accounts by capable supreme audit institutions represent key institutions of accountability in public finance management, whose full potential is yet to be realised. The effectiveness of budget oversight institutions remains inhibited by capacity constraints and structural factors, both internal and external to legislative organisation. Institutional arrangements and political economy considerations largely explain why parliaments and external audit agencies have not yet exploited the full scope of their budgetary powers. The general trend is for legislatures to take a more active role in the budget process. However, legislatures have to demonstrate that they are able to take an active and responsible role in the budget process while ensuring fiscal discipline. The challenge facing Latin American legislatures is to strengthen the institutional arrangements fostering fiscally responsible interventions.

While there exists some controversy surrounding the concept of accountability and the linkages between its ‘vertical’ and ‘horizontal’ dimensions (Mainwaring and Welna 2003), ‘horizontal accountability’ is hereby defined as: ‘The existence of state agencies that are legally enabled and empowered, and factually willing and able, to take actions that span from routine oversight to criminal sanctions or impeachment in relation to actions or omissions by other agents or agencies of the state that may be qualified as unlawful’ (O’Donnell 1999:38). Horizontal accountability deals exclusively with those actions that ‘are undertaken by a state agency with the explicit purpose of preventing, canceling, redressing, and/or punishing actions (or eventually non-actions) by other state agencies that are deemed unlawful, whether on the grounds of encroachment or of corruption’ (O’Donnell 2003:35.)

The governance of the budget can be defined as encompassing the interest, incentives, individuals and institutions governing the formulation, approval, execution and oversight of the budget and shaping fiscal outcomes.
Current arrangements for budget oversight and public finance accountability remain largely inadequate in Latin America. Nevertheless, the emergence of situations of divided government, such as in Mexico, creates new confining conditions for governing the budget in presidential systems. Parliaments are progressively reasserting their prerogatives in the budget process (Schick 2002, 1990; Santiso nd, forthcoming). In the course of the 1990s, there has been a general move towards a second wave of reform strategies to enhance public budgeting and public finance management in emerging economies. Traditional approaches have tended to focus on improving efficiency and effectiveness within the executive branch, targeting finance ministries, tax authorities and central banks and introducing integrated governmental financial management systems. In recent years, however, greater attention has been directed at strengthening the institutions of public finance management beyond the executive and improving the mechanisms of oversight and accountability. This second stage of reform in public finance management is partly the result of new findings on the determinants of the quality of economic policy and the need to balance executive discretion and government accountability in public budgeting. This has led to a renewed interest in the credibility and integrity of public finance systems and the contribution of legislative budget institutions to budget accountability (Haggard and McCubbins 2001).³

The international financial institutions (IFIs) have a fiduciary and a developmental interest in improving accountability in public finance management. Mitigating fiduciary risk in policy-based lending and direct-budget support necessarily requires strong, credible and reliable budget management systems in recipient countries (Santiso 2004d). The multilateral development banks provide significant support to strengthen the institutions of public finance governance in emerging economies in the broader context of the second-generation institutional reforms being sought (Santiso 2004c, 2003a; Burki and Perry 1998.) Since the early 1990s the World Bank, the IDB and the United States government have assisted Latin America countries to modernise their financial administration through the establishment of integrated financial management systems (Dorotinsky and Matsuda 2002). In the course of the 1990s, Argentina, Bolivia, El Salvador, Honduras, Guatemala, Nicaragua and Venezuela have benefited from technical assistance loans and grants to enhance their governmental financial management systems.

This chapter reviews multilateral lending to the institutions of budget oversight and public finance accountability in Latin America, focusing on the case of the IDB. The IDB lending and technical assistance to legislative budget institutions and external audit agencies is part of its broader efforts to enhance financial management in the public sector of its borrowing countries. It is thus aimed both at reinforcing public governmental financial management and ensuring that the resources it provides are used efficiently. Nevertheless, the essay argues that the second stage of economic reform requires devising new approaches to strengthen the institutions of public finance governance. It involves addressing the political economy determinants of governance reform and institutional development. In particular, ensuring greater oversight and integrity in public finance requires enhancing the functional linkages between the institutions participating in the budgetary process and the national system of control.

The chapter is divided in four substantive sections. The first section provides an overview of the conceptual foundations of the contemporary debate on parliament’s role in budget policymaking and oversight. The second section reviews recent developments in the approaches of the IFIs to budget management and public finance accountability in emerging economies. The third section focuses on the patterns of IDB lending to national parliaments and supreme audit institutions and parliaments in Latin America. The final section offers some concluding remarks on how this assistance could be improved. It is argued that there exists unexplored potential to enhance the effectiveness of multilateral lending to budget oversight institutions. Beyond increasing technical capacity and enhancing operational efficiency, second-stage reforms entail strengthening the

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³ Supreme audit institutions (Supreme audit institutions) are also referred to as general accounting offices, general auditor’s office or national audit offices. The term supreme audit institution will be used hereafter to refer to those institutions tasked with the external audit of government programs and public accounts.
incentives of budgetary institutions to effectively oversee governmental financial management. This includes, in particular, securing the political independence and financial autonomy of supreme audit institutions and promoting more efficacious links between supreme audit institutions and parliamentary public accounts committees. More fundamentally, it requires improving legislative capacities for independent budget analysis and legislators’ political incentives to hold government to account.

STRENGTHENING LEGISLATIVE OVERSIGHT AND REFORMING BUDGETARY INSTITUTIONS

Understanding the governance of the budget

Despite significant progress in recent years, we continue to lack a robust theory of the budget process in emerging economies. While the seminal work by Aaron Wildavsky (1964, 1992) and Allen Schick (1995, 2002) provides us with invaluable insights into the politics of the budget process in developed countries, the political economy of public budgeting in developing countries is only beginning to be closely scrutinised.

Adequately understanding the political economy of the budget process is critical to grasp the institutional determinants of economic policymaking and public budgeting and design feasible fiscal reforms seeking sustainable impact results (Cox and McCubbins 2001; OECD 2003; Santiso 2004b). Research by Alberto Alesina et al (1999) and Enesesto Stein et al (1998) has increased our understanding of the influence budgetary institutions on fiscal outcomes in Latin American emerging economies. Similarly, Lisa Baldez and John Carey (2001) demonstrate that budgetary restraint and fiscal discipline in Chile is largely attributable to the institutional arrangements of budget policymaking. Similarly, David Samuels (2002) and Jeffrey Weldon (2002) underscore the negative impact legislative politics has on dysfunctional fiscal policy and budgetary process in Brazil and Mexico, respectively.

However, there continues to be great controversy as to what the most appropriate role of parliaments ought to be in public budgeting. Prevailing orthodoxy posits that excessive legislative prerogatives in public budgeting tend to lead to fiscal disequilibria, greater budget deficits and public debt; overspending and under-taxation are likely results (Alesina 1999; Stein 1998). It warns against the dysfunctional fiscal effects of unrestrained legislative budgetary powers and consequently favours the insulation of economic policymaking within the executive branch. It thus argues that ‘hierarchical’ budget systems that ‘concentrate power in the finance minister, vis-à-vis other ministers, and in the executive vis-à-vis congress’ (Stein 1998:3) provide stronger procedural incentives for promoting fiscal prudence. Such views, which have influenced economic policies in Latin America in the 1990s, counsel giving greater independence to the institutions of economic governance, in particular central banks, tax authorities and regulatory agencies. The 2000 Law of Fiscal Responsibility adopted in Brazil constitutes a more recent attempt at establishing numerical and procedural budget constraints.

Nonetheless, there are important risks associated with hierarchical budgetary arrangements. In presidential systems of government these arrangements tend to reinforce executive powers and allow for excessive executive discretion in public budgeting. Often, unconstrained executives misuse their constitutional authority and delegated powers, left largely unchecked by amenable parliaments. Unfettered executive discretion, reflected for instance in the extensive use of executive decrees to re-allocate budget appropriations, hampers external scrutiny and hinders political accountability. It not only weakens the mechanisms of democratic accountability, but also tends to render public finances vulnerable to corruption and capture. Finding the most adequate balance between executive and legislative prerogatives in budget policymaking is a critical challenge for emerging economies struggling to consolidate their democratic institutions. Ultimately, the governance of the budget reflects a delicate balance between executive power and legislative oversight.
Echoing George Tsebelis’ rational choice theory on ‘veto points’ and ‘nested games’ in public policymaking (Tsebelis 2002, 2000, 1995), political economy analyses of fiscal policymaking focus underscore the accountability functions of parliaments and supreme audit institutions in the budget process, acting as ‘accountability points’ in economic policy (Morgenstern and Nacif 2002; Mainwaring and Welna 2003.) This new strand of comparative research revisits traditional assumptions on the contribution of national parliaments to economic policymaking and public budgeting in presidential systems. It challenges or, at least, amends the prevailing view of executive-legislative relations in Latin America, which has tended to emphasise the reactive role of assemblies and the proactive role of presidents (Cox and Morgenstern 2002.)

Latin American governance is indeed emblematic of the predominance of the executive in economic policy and the uses, misuses and abuses of executive discretion in public finance management. Nevertheless, even in symptomatic cases of ‘delegative democracy’ (O’Donnell 1994), legislatures play an important role in economic policy and public budgeting, often greater than originally thought. For example, Argentine legislators have had more influence on fiscal policymaking (Jones 2001) and taxation reform (Eaton 2002) that it was originally assumed. The oversight functions of the Argentine legislature, while still weak, are gradually being strengthened (Morgenstern and Manzetti 2003.) Similarly, Carlos Santiso and Arturo García Belgrano (2004) detect increased legislative activism in Peru since the restoration of democracy in 2001, although its impact in fiscal outcomes is still difficult to ascertain. However, the Latin American paradox remains that, while endowed with limited budgetary powers, legislatures in the region fail to effectively use those that they do have. Argelina Figueiredo (2003:172) demonstrates that the 1988 Brazilian Constitution ‘provides an extensive array of oversight mechanisms and an adequate legal apparatus to sanction government […] These favourable institutional conditions, however, are not sufficient for effective oversight. Congress’s legal ability to take on oversight initiatives is much greater than its capacity to achieve actual results.’

The greatest challenge of legislative budgeting remains to strengthen democratic accountability while ensuring fiscal discipline. Legislatures have a key role in the governance of the budget: they authorise the executive to raise revenue and manage public expenditures. They help ensure government accountability in the management public finances, by approving budget allocations, overseeing budget execution and controlling budget performance. Indeed, enhancing legislative scrutiny of the budget is increasingly considered as a means to strengthen government accountability and curb corruption (OECD 2001). In emerging economies, however, the role of parliaments in budgeting remains subdued and is often dysfunctional, partly as a result of executive dominance, but also because of legislatures’ own deficiencies.

Legislative budgetary institutions, such as standing committees, legislative budget offices and supreme audit institutions have largely been neglected in the first stage of economic reform and financial administration modernisation. They nevertheless perform critical accountability functions. Legislatures constitute central agencies of state self-restraint and external accountability in public finance management. They help enforcing the accountability cycle of public budgeting:

• **Ex ante accountability**, ensuring that budget allocations adequately reflect policy priorities;
• **Concurrent accountability**, overseeing the execution of the budget by the executive; and
• **Ex post accountability**, holding government to account for performance and results.

In practice, however, legislatures often fail to adequately and responsibly use their budgetary powers and perform their accountability functions. What then explains this disjuncture between the potential contribution of legislatures to public budgeting and their actual role?

**Legislative budget authority**

Strengthening legislative budget oversight would undoubtedly contribute to re-equilibrate executive-legislative relations in public finance management in presidential systems of government characterised by weakly institutionalised mechanisms of accountability. Legislative budgeting can be defined by the scope of budget authority and the effectiveness of budget oversight. It is a recent
development in Latin America: the first budget formally approved by the Argentinean legislature was that of 1990. In Latin America as elsewhere in the developing world, there exists an important gap between the formal powers and actual role of parliaments in public budgeting. The legal framework for legislative budgeting only partly explains the actual performance of legislatures in the budget process. Parliament’s role in budget oversight remains inhibited by structural factors related both to the internal organization of parliamentary work and the broader external context of executive-legislative relations. It is thus contingent on both capacities and incentives.

Four sets of variables are particularly determinant to assess the contribution of parliaments to budget policymaking and oversight:

- Whether parliament is legally empowered to intervene in budgeting,
- Whether it is endowed with the required technical capacities,
- Whether it possesses the necessary political will, and
- Whether the governance environment is conducive.

In Latin America, legislative budgetary powers, as defined in the constitution, the organic budget law and parliaments’ internal rules, are severely limited by the prerogatives of the executive in the budget process. Constitutional provisions endow presidents with uncommon powers in public budgeting, both in absolute and relative terms, although important variations between countries. Assessing the budgetary powers of the executive in 23 presidential systems, Mathew Shugart and Stephan Haggard (2001) find that in seven of them presidents enjoy exclusive power over spending legislation and legislatures confront severe constraints on amending presidential proposals. Legislative budgetary powers are nevertheless along the different phases of the budget cycle, i.e. formulation, adoption, execution, and control. Table 1 captures the main constitutional restrictions on the budgetary powers of ten Latin America countries.
Table 1: Constitutional Restrictions on Legislative Budget Authority in Latin America

<table>
<thead>
<tr>
<th>Country</th>
<th>Argentina</th>
<th>Bolivia</th>
<th>Brazil</th>
<th>Chile</th>
<th>Colombia</th>
<th>Costa Rica</th>
<th>Ecuador</th>
<th>Peru</th>
<th>Uruguay</th>
<th>Venezuela</th>
</tr>
</thead>
</table>

- Only the President can propose the budget
  -Yes Article 100.6
  -Yes Article 147
  -Yes Article 61(1)II (b)
  -Yes Article 64
  -Yes Article 346
  -Yes Article 178
  -Yes Article 258
  -Yes Article 78
  -Yes Article 215
  -Yes Article 313

- Congress cannot increase the budget for any items or create new budgetary categories
  -No
  -Yes with loophole Article 166
  -Yes with loophole Article 64
  -Yes Article 351
  -No
  -No
  -Yes Article 79
  -Yes Article 215
  -No

- If no new budget is passed, current budget remains in effect
  -Yes Implicit
  -No
  -No
  -No
  -Yes Implicit
  -No
  -No
  -Yes Implicit
  -Yes Article 313
  -Yes Article 147
  -Yes Article 64
  -Yes Article 348
  -Yes Article 258
  -Yes Article 80
  -No
  -No

Budget formulation The executive has a predominant role in the formulation of the budget and the drafting of the budget bill presented to parliament for review and adoption. It has the exclusive right to initiate the budget process and draft the budget bill. The central budget offices of the finance ministries are responsible for coordinating the budget drafting process within the executive and overseeing its execution by spending agencies.

Budget approval Once approved by the government, the budget proposal is submitted for consideration to the legislature, which as a set period of time allocated for that task. As Table 2 shows, the time allocated to debate in the budget committee and the plenary varies between 30 days in Mexico to 120 days in Honduras. The legislature can amend the budget bill, thereby ensuring ex ante budget accountability. However, its amendment powers vary. In five of the ten cases included in Table 1, legislatures are not allowed to create or increase public spending, except as it pertains to their own budget. Furthermore, if the budget is not approved by the set deadline, the current budget remains in effect in only four cases (Argentina, Costa Rica, Uruguay and Venezuela). In five other cases (Bolivia, Chile, Colombia, Ecuador, Peru), the executive’s proposal automatically becomes law, usually by legislative decree. These clauses give the executive extraordinary leverage over the legislature, as legislative inaction does not preclude the executive proposal from being adopted. They de facto neutralise legislative obstruction and significantly diminish the leverage of legislatures in the budget bargaining process, as legislatures have no veto power over the executive’s budget proposal. While they help avoid deadlock over the budget, these provisions create a set of incentives that is not conducive to effective scrutiny and oversight.

Table 2: Review of the Budget in Latin America

<table>
<thead>
<tr>
<th>Country</th>
<th>Parliamentary structure</th>
<th>Budget approval authority</th>
<th>Number of days allocated for reviewing budget proposal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina</td>
<td>Bicameral</td>
<td>Both chambers</td>
<td>n.a.</td>
</tr>
<tr>
<td>Bolivia</td>
<td>Bicameral</td>
<td>Both chambers</td>
<td>60</td>
</tr>
<tr>
<td>Brazil</td>
<td>Bicameral</td>
<td>Both chambers</td>
<td>100</td>
</tr>
<tr>
<td>Colombia</td>
<td>Bicameral</td>
<td>Both chambers</td>
<td>90</td>
</tr>
<tr>
<td>Chile</td>
<td>Bicameral</td>
<td>Both chambers</td>
<td>60</td>
</tr>
<tr>
<td>Paraguay</td>
<td>Bicameral</td>
<td>Both chambers</td>
<td>90</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td>Bicameral</td>
<td>Both chambers</td>
<td>Max 90</td>
</tr>
<tr>
<td>Uruguay</td>
<td>Bicameral</td>
<td>Both chambers</td>
<td>90</td>
</tr>
<tr>
<td>Venezuela</td>
<td>Bicameral</td>
<td>Both chambers</td>
<td>n.a.</td>
</tr>
<tr>
<td>Mexico</td>
<td>Bicameral</td>
<td>Chamber of Deputies</td>
<td>30</td>
</tr>
<tr>
<td>Costa Rica</td>
<td>Unicameral</td>
<td>Legislative Assembly</td>
<td>90</td>
</tr>
<tr>
<td>Ecuador</td>
<td>Unicameral</td>
<td>National Congress</td>
<td>90</td>
</tr>
<tr>
<td>El Salvador</td>
<td>Unicameral</td>
<td>Legislative Assembly</td>
<td>90</td>
</tr>
<tr>
<td>Guatemala</td>
<td>Unicameral</td>
<td>Congress of the Republic</td>
<td>120</td>
</tr>
<tr>
<td>Honduras</td>
<td>Unicameral</td>
<td>National Congress</td>
<td>105-120</td>
</tr>
<tr>
<td>Nicaragua</td>
<td>Unicameral</td>
<td>National Assembly</td>
<td>n.a.</td>
</tr>
<tr>
<td>Panama</td>
<td>Unicameral</td>
<td>Legislative Assembly</td>
<td>90</td>
</tr>
<tr>
<td>Peru</td>
<td>Unicameral</td>
<td>Congress of the Republic</td>
<td>90</td>
</tr>
</tbody>
</table>


Budget oversight Constitutions give parliaments an important in the oversight of the execution of the budget, the scrutiny of budget re-allocations, and the review of public accounts. In practice, however, legislative oversight of budget execution is still embryonic, undermining its contribution to concurrent budget accountability. Legislatures exercise only a limited monitoring of the government’s compliance with formal budgetary rules and procedures as set in the budget law. They even more ill-equipped to monitor the performance of public spending and enforce results-based budgeting.
Nevertheless, parliaments possess a potentially powerful instrument to control budget execution and enforce ex post accountability: the annual certification of public accounts. Parliamentary public accounts committees (PACs) play a critical role in that regard. They inform their opinions with the audited report on public accounts prepared by the supreme audit institutions. Parliaments subsequently consider public accounts committees’ opinions in plenary and decide whether to discharge government. In Latin America, institutional arrangements for supreme audit institutions very along three broad models: as advisory bodies to parliaments to parliament, such as in Argentina; autonomous state agencies, such as in Chile; or independent institutions with quasi-judicial powers, such as in Brazil. Whether nominally linked to parliaments or not, supreme audit institutions provide critical support to parliaments’ oversight functions. Henceforth, the quality of institutional linkages between public accounts committees and supreme audit institutions is a key determinant of the effectiveness of legislative budget oversight. Ex post accountability is nevertheless constrained by the timing and sequencing of legislative scrutiny. There are important time lags and inconsistencies that adversely affect the accountability cycle of the budget process. For example, the review of public accounts and the evaluation of the auditor general’s report often take place at a time that does not always allow them to adequately feed-back into the budget process.

**Legislative budget oversight**

The effectiveness of legislative budget oversight is greatly conditioned by the quality of the budget process itself and the governance of its execution. Research on budget transparency reveals the gap between the quality of the legal framework for public budgeting and adherence to it (IBP 2003.) According to the survey data reproduced in Tables 3 and 4, while the quality of the legal framework for public budgeting in Argentina, Brazil, Chile, Mexico and Peru is generally sound, perceptions of budget transparency are poor. It is interesting to note that legislative oversight and external auditing are perceived as particularly deficient.

### Table 3: Budget Transparency in Latin America (Aggregate Index)

<table>
<thead>
<tr>
<th>Country</th>
<th>Assessment of Legal Framework</th>
<th>Perceptions Index</th>
<th>Average Index (un-weighted)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Out of 1000 points</td>
<td>1 to 10</td>
<td>1 to 10</td>
</tr>
<tr>
<td>Argentina</td>
<td>700</td>
<td>7.0</td>
<td>5.1</td>
</tr>
<tr>
<td>Brazil</td>
<td>636</td>
<td>6.4</td>
<td>5.1</td>
</tr>
<tr>
<td>Chile</td>
<td>733</td>
<td>7.3</td>
<td>5.9</td>
</tr>
<tr>
<td>Mexico</td>
<td>507</td>
<td>5.1</td>
<td>5.0</td>
</tr>
<tr>
<td>Peru</td>
<td>598</td>
<td>6.0</td>
<td>3.7</td>
</tr>
</tbody>
</table>

Source: IBP 2003:5. Notes: The legal framework score is on a scale of 0 to 1000. The index of perceptions is an average on a scale of 1 to 10, of not transparent to transparent.

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4 Many countries do not formally possess public accounts committees as such. These committees can either be sub-committees of budget or finance standing committees or their functions can be performed by budget or finance standing committees.
Table 4: Budget Transparency in Latin America (Disaggregate Index)

<table>
<thead>
<tr>
<th>Phases of the budget</th>
<th>Most transparent</th>
<th>Least transparent</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Chile</td>
<td>Mexico</td>
</tr>
<tr>
<td>Formulation</td>
<td>3.36</td>
<td>2.67</td>
</tr>
<tr>
<td>Approval</td>
<td>2.80</td>
<td>2.79</td>
</tr>
<tr>
<td>Execution</td>
<td>3.16</td>
<td>2.71</td>
</tr>
<tr>
<td>Oversight and auditing</td>
<td>3.07</td>
<td>2.31</td>
</tr>
<tr>
<td>Economic Information</td>
<td>3.53</td>
<td>3.15</td>
</tr>
</tbody>
</table>

A number of structural issues do constrain legislative budget oversight. First, the rigidity and inertia of the budget itself tends to limits the scope for exercising legislative budget powers. In Brazil, 90 percent of the budget is rigid, as a result of constitutionally mandated expenditures, earmarking of tax revenues and mandatory expenditures. Hence, the type of public spending on which parliament could potentially have the greatest influence, capital expenditure, represents only a small fraction of public expenditures, albeit of strategic importance for building ad hoc political coalitions, as in the case of Brazilian system for executing budget appropriations (OECD 2003). Second, the gap between the approved and executed budgets further hinders legislative oversight. Optimistic assumptions on revenues, weak execution capacity of sector ministries and ad hoc changes in appropriations partly explain this gap.

The resulting instability of budgetary institutions and fiscal rules hampers the consolidation of credible budget processes with predictable procedures and enduring structures. Capacity constraints and skewed incentives further hamper effective budget oversight. Factors explaining constraining legislative budget oversight in emerging economies can be regrouped in two broad categories: one consisting of factors internal to legislative organisation; and another one consisting of external factors linked to the governance context in which Latin American legislatures operate.

A first set of constraining factors is internal to the legislatures, related to deficiencies in the structures and processes of legislative budgeting. They essentially relate to organisation, resources and capacity. Three legislative budget institutions are particularly important.

- **Legislative committees** The organisation of legislative committee work tends to lack the kind of institutionalisation that would allow specialised committees to effectively contribute to the budgetary process. The division of responsibilities between the different committees dealing with different facets of public finance (taxation, budgeting, oversight and control) remains unconsolidated. In bicameral systems, joint legislative budget committees are not permanent structures, although this is starting to change. These shortcomings are particularly detrimental to budgetary work, given its increasing complexity and technical specificity. Furthermore, the internal composition of committees, which is proportional to that of parliaments, tends to lessen the incentives for legislative oversight of government, as parliaments tend to be dominated by the same party as government (Messick 2002). Legislative committees are most often chaired by the legislative majority, which sets their agendas and work-plans. In contrast, in parliamentary systems, the opposition often chairs public accounts committees. Reforms are gradually being introduced,
such as in Chile in 2003 where the Special Joint Budget Committee became a permanent legislative committee.

- **Legislative technical advisory capacity** is largely inadequate to allow legislatures to effectively engage in the increasingly complex budget process. Budget and public accounts committees are assigned only a limited number of permanent technical advisers. In fact, most of the advisory work is carried out by the political advisers of the legislators sitting in the budget and public accounts committees. As a result, technical input in the budget review process lacks the technical substantiation required for impartial evaluation. The absence of a tenure-track parliamentary staff in many Latin American countries is accentuated by the weaknesses of civil services. Parliaments can only rely on the limited research and advisory services that are available to them through incipient legislative research offices and ill-equipped parliamentary libraries. Such resources exist or have been recently established in Brazil, Chile, Colombia and Peru.

- **Legislative budget research capacity** remains insufficient for effective legislative budget oversight. Latin American legislatures have not yet developed the technocratic institutions necessary for ensuring the financial and administrative accountability of the presidency and executive agencies. Budget and public accounts committees rely almost exclusively on the information that government agencies provide, which significantly constrains their ability to carry out independent budget reviews and adequately oversee budget execution. While financial constraints partly explain the deficiencies in budget research capacity, there also exist political reasons explaining why parliaments have generally not purposefully sought to build these capacities. Timely access to budget information is strategic in the sense that the opposition has the greatest incentives for independent budget analysis. This is gradually changing, however, as the contribution of legislative budget offices is increasingly acknowledged. Although not as powerful as the US Congressional Budget Office (USCBO), legislative budget offices are gradually emerging or being strengthened, such as in Venezuela since 1997 or Mexico since 1998. It is indeed noticeable that a main impediment to legislative budgeting often resides in parliaments’ incapacity to engage with the budget process, rather than the restraints put on their budgetary powers. Nevertheless, one needs to be mindful that the establishment of a legislative budget office does not per se guarantee independent budget analysis. Impartiality and non-partisanship must characterise the work of this office for it to be credible and effective. This requires broad-based, multiparty commitment (Anderson 2004). 5

A second set of factors are external to the legislature, linked to the formal and informal rules shaping executive-legislative relations, the presidential nature of the political system, the over-reliance of executive decree authority, skewed electoral incentives, and a fragmented political party system.

- **Legislative oversight and external auditing** Supreme audit institutions provide critical information and advisory services to parliaments, directly or indirectly (Dye and Stapenhurst 1998.) The availability of timely and reliable information on budget performance is key to the effectiveness of legislative oversight. Improving the functional linkages between Public accounts committees and supreme audit institutions is thus critical to anchor accountability in public finance and budget management. In turn, securing the political independence of supreme audit institutions, which have been significantly undermined by executive interference and political meddling, is critical to guarantee effective external auditing of government finances (INTOSAI 2001.) Issues such as criteria guiding the nomination and removal of auditor generals and the length of their term in office, as well as the procedures regulating recruitment, promotion and dismissal of professional staff are critical determinants of the effective independence of supreme audit institutions. Predictable financial resources are also a necessary, yet not sufficient for institutionalising supreme audit institutions and insulating them from political interference. Most Latin American countries are now seeking to strengthen their external auditing functions, with the support of IFIs (Santiso forthcoming). Indeed, important reforms have been introduced in recent years.

5 I am grateful to Barry Anderson for this insight.
• Economic governance and budgetary decision-making Beyond the constrains imposed by the institutional frameworks for legislative budgeting, the presidential nature of political systems, coupled with an over-reliance on executive decrees have been particularly detrimental to the strengthening of the institutions of government accountability in public budgeting. The use of executive decrees in public budgeting is impressive both in absolute and relative terms in countries such as Argentina, Brazil or Peru. The frequent and early recourse to executive decrees to re-allocate budget appropriations not only undermines the legislative oversight, but also weakens the credibility of the budget as an instrument of economic governance and strategic planning (Santiso forthcoming). In practice, parliaments exercise little oversight on presidential decrees.

• Political governance and legislative budgeting Legislative behaviour and executive-legislative relations in public budgeting are necessarily intermediated by political parties and electoral rules. Stein et al. (1998) have uncovered a statistically significant relationship between electoral systems and fiscal performance. Electoral systems characterised by a large degree of proportionality (i.e. large district magnitude) and political fragmentation (i.e. number of effective parties represented in parliament) tend to have larger governments, larger deficits and a more procyclical response to the business cycle. Similarly, Torsten Persson and Guido Tabellini (1999) show that large deficits and debts have been more common in countries with proportional rather than majoritarian electoral systems, coalition governments and frequent government turnover and lenient rather than stringent government budget processes. Furthermore, the fragmentation and volatility of political party systems has been detrimental to the effective exercise of legislative budget oversight, significantly shortening the time horizons of individual legislators. In many countries in the region, parties lack the sort of internal coherence, cohesion and discipline that would allow them to act purposefully and consistently within parliament.

• Political opposition and government accountability The behaviour of members of parliament is itself shaped by the incentives to which they respond. Executive-legislative relations are necessarily intermediated by political parties and electoral rules, as there is a possibility of control dilution when the ruling party or coalition holds a disciplined majority position in parliament. Recent research on the politics of budgeting in Brazil (Mainwaring and Welna 2003; Morgenstern and Manzetti 2003; Figueiredo 2002, 2003) shows that participation by the legislative branch in the budget process can only be understood when the political parties and electoral rules are taken into account. As the executive dominates the budget process and controls budget execution, partisan participation in the budget process depends on the parties’ relations with the executive (Pereira and Mueller 2002). Indeed, presidential systems marked by fused executive and legislative majorities tend to have inoperative systems for enforcing government accountability (Messick 2002; Manning and Stapenhurst 2002).

The political economy of the budget process reveals that political and technical aspects interact in determining the effectiveness of legislative budget oversight along the different phases of the budget cycle. Parliaments do possess important budgetary powers. However, they seldom use them effectively or responsibly. While capacity constraints partly explain why parliaments do not exercise their budgetary powers effectively, governance constraints explain why they sometimes do not exercise them responsibly. Henceforth, parliaments’ ability to establish their credibility as institutions of economic governance is thus contingent on the strengthening their technical and advisory capacities to perform its budget functions, and the existence of an enabling governance environment that allows these to be exercised effectively and responsibly. The question of strategy then becomes whether legislative capacity should be build first, or should it emerge as a result of increased legislative activism.

Sound public finance management and accountability requires finding an adequate balance between executive and legislative prerogatives in the different phases of the budget. It may be argued that, while executive dominance in public expenditure management is more likely to ensure fiscal prudence, legislative oversight is critical to provide effective checks and balances and enforce accountability in the formulation, execution and control of the budget. The key challenge of legislative budgeting in Latin American presidential systems is to retain the advantages of strong
executive authority required to ensure fiscal discipline while providing the institutional checks and balances that guarantee effective accountability.

**IDB APPROACH TO BUDGET OVERSIGHT AND PUBLIC FINANCE ACCOUNTABILITY**

The IFIs recognise that strengthening of public finance accountability is a critical institutional reform required to consolidate second-generation economic reforms (Kuczynski and Williamson 2003; Santiso 2004c, 2003a.) In the first stage of reform in public budgeting, the Washington consensus policy prescriptions favoured a predominant role for the executive and the insulation of economic policymaking. However, the abuse of executive discretion by autocratic presidents misusing the prerogatives of executive decree authority and the delegation of legislative authority have often led to the neutralisation of accountability mechanisms, restrictions on the role of parliaments in the budget process and the capture of oversight institutions (Santiso 2001a, 2001b).

**Governance institutions and public finance management**

There is heightened awareness that the quality of a country’s governance system is a key determinant of the ability to pursue sustainable economic and social development. The push to confront governance challenges in developing countries has largely originated in the urgent need to tackle the structural causes of embedded corruption. It is now well established that corruption has corrosive effects on both economic management and aid effectiveness.

Undeniably, the introduction of the governance agenda has led the IFIs to broaden the scope of their interventions (Santiso 2004a, 2001b, 2000). In 1996, the International Monetary Fund (IMF) was urged by its governors to ‘promote good governance in all its aspects, including by ensuring the rule of law, improving the efficiency and accountability in the public sector, and tackling corruption, as essential elements of a framework within which economies can prosper’ (IMF 1996:327.) The 11-point Declaration on Partnership for Sustainable Global Growth adopted in September 1996 added an explicit mandate to promote good governance and combat corruption by strengthening transparency, accountability, and integrity in public finance management. The IMF’s role in governance has since then expanded considerably, integrating concerns over transparency, accountability and predictability of fiscal policy (IMF 1997 and 2001; Op de Beke 2002; Abed and Gupta 2002.) The IMF nevertheless focuses on those economic aspects of governance that could have a significant macroeconomic impact and those that affect the implementation of economic reforms, in particular the transparency of government accounts, the effectiveness of public resource management, and the stability of the regulatory environment for private sector activity.

In the mid-1990s, the World Bank began supporting programs to strengthen accountability institutions, such as the rule of law, judicial systems, public finance management systems, and parliamentary oversight mechanisms (World Bank 2000.) It adopted, in 1997, an anticorruption strategy and guidelines to orient its involvement in governance issues in November 2000 (World Bank 1997 and 2000). Between 1996 and 2000, it has undertaken over 600 governance-related programs and initiatives in 95 countries. Between 1987 and 1998, it carried out 169 civil service reform programs in 80 countries. In Latin America, according to recent estimates, it has undertaken 126 core public sector reform projects between 1982 and 2002, totalling US$12 billion (Fuhr and Krause 2003). A majority of these projects, usually policy-based loans with a marked emphasis on fiscal reform, have a strong focus on public budgeting and government financial management.

Governance is a difficult concept for the multilateral development banks that do not want to be seen as political and thus adopt a doctrine of political neutrality (Santiso 2001b, 2004a.) One of the most contentious issues relates to the interface between economic and political aspects of governance. It encompasses the form of the political regime, the process by which authority is exercised in the management of a country’s economic and social resources for development, and the capacity of governments to design, formulate and implement policies and discharge functions. While the World Bank recognises that governance is intrinsically a political concept, it is careful to
underline that its engagement through lending, technical assistance and policy advice is confined to its economic dimensions. It underscores that the nature of the political system falls outside the purview of its mandate enshrined in its Articles of Agreement. According to the standard World Bank definition, the concept of governance captures ‘the manner in which power is exercised in the management of a country’s economic and social resources for development’ (World Bank 1992:1).

Henceforth, ensuring sound management of public finances, efficacious oversight of the budget process and effective accountability of the government is an integral dimension of good governance.

The IDB’s approach to the reform of the state and the modernisation of the public sector, while similar to that of the World Bank, is generally less reluctant to engage in politically sensitive areas. The IDB has broader political goals enshrined in the expansion of its mandate in 1994, which now includes the consolidation of democracy as one of its corporate objectives. The IDB’s policy on the modernisation of the state was first articulated in 1996. It was updated in July 2003 to integrate concerns over the political economy of institutional development, in particular party systems, electoral rules and executive-legislative relations (IDB 2003). It recognises that politics matter for development and that, consequently, its lending and technical assistance should more actively address political economy considerations (Payne 2002.) However, there remains an important gap between policy pronouncements and lending operations.

**Diagnosing public finance accountability**

The IFIs have significantly upgraded their diagnosis instruments to assess the quality of public budgeting and the robustness of the mechanisms of accountability in government finances. The main channels through which the IMF promotes good governance are surveillance, lending and technical assistance. In terms of surveillance, the IMF has actively sought to promote standards and codes of good practice thorough its Article IV consultations in fiscal matters. Since the late 1990s, prompted by the fall-out of the Asian financial crisis, the IMF has acknowledged the importance of transparency in monetary and financial policy management, adopting a *Code of Good Practices on Fiscal Transparency* in 2001. A country’s observance of these standards is regularly assessed in the *Reports on the Observance of Standards and Codes* (ROSCs,) 264 have been completed for 80 countries at the end of June 2002, 193 of which have been published.

These diagnosis instruments complement those of the World Bank assessing the quality of public finance processes and structures. While the IMF addresses issues related to revenue policies and tax structures, multilateral development banks tend to confine themselves to expenditure policies and budgetary processes. The IDB not developed its own diagnosis instruments and relies instead on those produced by the World Bank, or undertakes them jointly. *Public Expenditure Reviews* (PERs) analyse a country’s fiscal position and expenditure policies, evaluate the robustness of its public expenditure management systems and the efficiency and efficacy of its resource allocation. They may also examine institutional arrangements for public expenditure management, civil service reform, and revenue policy and administration (World Bank 2001a). Recommendations of the PERs are used to develop loan conditionalities, either through project loans or policy-based loans. The World Bank carries out, on average, 20 to 25 PERs. The *Public Expenditure Tracking Survey* (PETS) undertaken jointly by the World Bank and the IMF in highly indebted poor countries (HIPCs) assesses the capacity of countries to track spending. From a 36-question questionnaire, 15 core performance indicators are identified, providing a general picture of the quality of public expenditure management systems. The HIPC expenditure tracking assessment has been applied in 24 HIPCs over the period 2000-2002. The results showed that these countries generally have low capacity to track spending.

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6 The Fund has identified twelve key areas, which include accounting, auditing, anticorruption, banking supervision, corporate governance, fiscal transparency, monetary policy and financial policy transparency.

7 For an overview of the World Bank’s public expenditure work, see: http://www1.worldbank.org/publicsector/pe/index.cfm
The *Country Financial Accountability Assessment* (CFAA) is another important, yet more recent, diagnostic tool that provides information on the state of public financial management systems (World Bank 2003.) It is intended to give the World Bank a sound knowledge of the country’s public finance management system, as a basis for broadly assessing the likelihood that lent funds will be appropriately managed. Similarly, the *Country Procurement Assessment Reviews* (CPARs) examine public procurement institutions and practices in borrower countries. The CFAA evaluates quality of public budgeting as an integrated whole, including budget development, budget execution and monitoring, external fiscal reporting and transparency, internal and external auditing, and legislative scrutiny of budget execution. The governance and institutional aspects of budget management are core dimensions of CFAAs. Information obtained from the CFAA supports the preparation of an integrated fiduciary assessment. The results of this assessment inform the preparation of the World Bank’s *Country Assistance Strategy* (CAS), particularly the sections dealing with the size of the support program, the sectors to be supported, selection of lending instruments, and approaches to risk management.8

Institutional and Governance Reviews (IGRs), while not necessarily focusing on public finance management systems, assess the quality of governance systems and political institutions and evaluate the quality of accountability, policymaking, and service-delivery institutions. IGRs have only been recently designed and were first piloted in 1999-2000.9 They have been conducted in Argentina, Armenia, Bangladesh, Bolivia, Eastern Caribbean States, Indonesia, Nigeria and Peru. They often focus on the institutions of economic governance and are thus complementary to CFAA. In fact, they are indispensable to adequately capture the political economy of economic development and the institutional dimensions of public finance management and accountability: ‘The IGR relates to the CFAA in its diagnosis of the shortcomings of formal public finance management systems that are due to inadequate capacity, incentives, or signals’ (World Bank 2003:2-3.) Indeed, a noticeable trend in the refinement of these diagnosis instruments is the gradual convergence between the economic approach to public finance management and the political economy approach to public finance accountability. Increasingly, and reflecting the recognition of the governance dimensions of public finance management, the World Bank undertakes *Public Expenditure and Institutional Reviews* (PEIRs), such as for Turkey or Croatia in 2001 (World Bank 2001b, 2001c.)

There exists other diagnosis instruments, such as for example, the Asian Development Bank’s Diagnostic Study of Accounting and Auditing, the European Commission’s ex ante assessments of country financial management, and the United Nations Development Program’s Country Assessment in Accountability and Transparency. Although they possess different mandates and perform different functions, the IFIs are seeking to better coordinate and harmonize their assessment instruments along the public finance cycle, from revenue collection to expenditure management (PEFA 2003.) For example, the *Public Expenditure and Financial Accountability* (PEFA) program, a multi-donor initiative established in December 2001, aims at harmonizing international public sector standards in accounting, auditing and internal control in developing and transitional countries.10

**IDB strategy towards budget oversight institutions**

The contribution of legislative budget institutions to budget policymaking and oversight is being re-evaluated. It is being increasingly recognised that these institutions are critical to enforcing government accountability and guaranteeing integrity in public finance management, especially in presidential systems. The OECD *Best Practices for Budget Transparency* include considerations over the role of parliaments in the budget process (OECD 2001a). As such, they go a step further

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8 The CFAA is particularly important where multilateral lending is managed by the country’s own public finance management system, as in the case of adjustment lending. CFAAs also identify critical areas of weakness in the public finance management system and often lead to the design of targeted investment lending projects.

9 For further information on IGRs, see: http://www1.worldbank.org/publicsector/igrs.htm

10 See: www.pefa.org
than the IMF’s *Code of Good Practices on Fiscal Transparency*, which tends to restrict itself to the governance of the budget within the executive. This restraint is also noticeable in the assistance provided by the IFIs to transitional countries reforming their budget procedures. Furthermore, technical assistance has tended to concentrate either on the expenditure side, providing assistance to prime minister’s offices and finance ministries, or the revenue side, providing tax reform advise and strengthening the capacities of tax authorities.

Nevertheless, in recent years, multilateral development banks have broadened their support to budget policymaking and oversight institutions by lending support to national parliaments and supreme audit institutions. The role of parliaments and external auditing agencies in public budgeting, public finance accountability and corruption control figure prominently in the newly adopted strategy on the modernisation of the state of the IDB. After a first wave of reforms targeting the efficiency and effectiveness of government financial management systems within the executive, the new strategy acknowledges the critical importance of the mechanisms of transparency and external oversight of governmental financial management beyond the executive. It thus approaches public budget as a process of economic and political governance.

In its efforts to consolidate democratic governance, the IDB stresses the need to ‘strengthen the institutional capacity of the legislative branch,’ in particular by supporting programs designed to ‘strengthen technical assistance systems that will improve the quality of legislation and help ensure budgetary, monitoring and oversight functions are performed based on objective and technical criteria’ (IDB 2003:12). Furthermore, the strategy allows the IDB to provide support for increasing ‘the technical capacities and functional independence of institutions that oversee government performance, for example, the offices of the comptroller general, court of accounts, auditor general, ombudsman, public defender, public prosecutor and attorney general’ (13).

As such, parliaments and supreme audit institutions are approached as key components of the national systems of control. The IDB recognises that ‘audit and other supervisory institutions do not always have the independence, objectivity and technical capacities necessary for them to be able to oversee adherence to the rule of law’ (5). It notes that ‘the prevalence of corruption is to some degree an expression of the weakness of the rule of law, but calls attention also to the weakness of the state’s financial administration’ (5). The IDB approach emphasises the necessity to ‘strengthen the fiscal capacity of the state and improve the efficiency and transparency of expenditure management’ (18) and to implement “comprehensive financial and accounting management systems and promoting the transparency of budgetary information’ (18).

### IDB LENDING TO BUDGET OVERSIGHT AND EXTERNAL AUDITING INSTITUTIONS

#### Lending to national parliaments

Parliamentary strengthening is a relatively new area for the IDB. The IDB began providing concessional lending to strengthen national legislatures in the late 1980s, coinciding with the restoration of democracy in the region. Originally, the assistance provided was aimed at strengthening the institutionalisation of parliaments and its representation, legislative and oversight functions. Indeed, its support to national legislatures is firmly embedded in its broader support to the consolidation of democracy. Democracy promotion has indeed become a corporate objective of the IDB since 1994 with the eighth replenishment of its resources (IDB 1994, 1999.) In Latin America and the Caribbean, as Table 5 shows, the IDB has approved seven lending operations between 1994 and 2003, totalling over US$50 million (as part of parliamentary reform programs totalling over US$85 million). Including the operations currently in design or approval stages (Argentina, Costa Rica and Guatemala), total IDB multilateral lending to national parliaments amounts to almost US$60 million. The stated aim of IDB financing is to strengthen the

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The strategy focuses on four priority areas of intervention: the democratic system; the rule of law and justice reform; state, markets and society; and public management.
representative, legislative and oversight functions of parliaments. The bulk of financing is directed at ‘hardware investments,’ such as physical infrastructure development, information technology improvements, and human resources management.

### Table 5: IDB Lending to National Parliaments

<table>
<thead>
<tr>
<th>Year</th>
<th>Country</th>
<th>Title</th>
<th>Amount (in $US million)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Total IDB lending</td>
<td>Counterpart financing</td>
</tr>
<tr>
<td>2005</td>
<td>Argentina †</td>
<td>Institutional Strengthening of the Senate</td>
<td>...</td>
</tr>
<tr>
<td>2003</td>
<td>Costa Rica ‡</td>
<td>Modernization of the Legislative Assembly</td>
<td>7.48</td>
</tr>
<tr>
<td>2003</td>
<td>Peru</td>
<td>Institutional Strengthening Program for the Peruvian Congress</td>
<td>10</td>
</tr>
<tr>
<td>2002</td>
<td>Guatemala ‡</td>
<td>Modernization of the Congress of the Republic</td>
<td>14.40</td>
</tr>
<tr>
<td>2000</td>
<td>Honduras</td>
<td>Modernization of the Honduran Congress</td>
<td>3.25</td>
</tr>
<tr>
<td>2000</td>
<td>Dominican Republic</td>
<td>Program for Modernizing the National Congress and the Office of the Comptroller General</td>
<td>28 (25.55) ‡</td>
</tr>
<tr>
<td>1999</td>
<td>Colombia</td>
<td>Modernization of the Congress of Colombia</td>
<td>10</td>
</tr>
<tr>
<td>1999</td>
<td>El Salvador</td>
<td>Modernization and Strengthening of the Legislative Assembly</td>
<td>4.40</td>
</tr>
<tr>
<td>1996</td>
<td>Panama</td>
<td>Project to Modernize the Legislative Assembly</td>
<td>4.10</td>
</tr>
<tr>
<td>1994</td>
<td>Peru</td>
<td>Institutional Development for the Legislative Branch of Government</td>
<td>3.74</td>
</tr>
<tr>
<td></td>
<td>TOTAL</td>
<td>85.37</td>
<td>64.90</td>
</tr>
</tbody>
</table>

|      |      |      |      |      |
| †    | Loan operation under consideration. |
| ‡    | Loan operation in the design stage (Perfil I), 6 June 2003. |
| ‡    | Loan operation in the approval stage (Perfil II), 21 March 2002. |
| ‡    | Amount allocated to the parliament. |

Source: Based on projects approved or foreseen as of May 2004. www.iadb.org

A salient feature of IDB lending to national legislatures in the increasing focus on their role in the budgetary process, primarily by improving committee work, strategic planning and capacities for legislative research. Legislatures are central budget institutions, both in the making of budget policy (through the budget committees approving the state budget) and the oversight of budget execution (through the public accounts committee.)

- A first set of initiatives supported by the IDB aims at strengthening legislatures’ internal structures and procedures shaping the legislative process. There is a marked emphasis on those parliamentary committees involved in the budget process, either at the approval or the oversight stage (e.g. the budget and public accounts committees.) The role of Public accounts committees is indeed being re-evaluated as a core legislative budgetary institution (McGee 2002; Wehner 2003). Public accounts committees are a critical linkage between the responsibility of parliament in enforcing government accountability in public finance and the external auditing function performed by supreme audit institutions.
A second set of initiatives aims at enhancing the capacities of parliaments for independent budget analysis, contributing to the creation or strengthening of legislative research centres and budget offices advising budget and public accounts committees. IDB lending operations have been relatively successful in helping parliaments to enhance their research and advisory services. In a few instances, such as Venezuela, they have contributed to the creation of legislative budget offices, although this remains an isolated case.

The strengthening of legislative budgetary powers reflects a gradual shifting of power between the executive and the legislative branches in Latin American presidential systems. Legislatures are becoming increasingly assertive, as opposition parties make strides. Historically, legislatures have been dominated by majorities belonging to or associated with the president’s party. This is starting to change and many presidents not longer control legislative majorities. These new dynamics of executive-legislative relations have a significant impact on economic policymaking and public budgeting. Legislatures are gradually re-asserting their powers in budget oversight, partly as a result of the newfound assertiveness of parliamentary opposition. Divided government – the situation in which the president no longer controls the legislature – is becoming increasingly common throughout the region and creates new confining conditions constraining executive discretion in public budgeting. The surge of legislative activism in public budgeting in Mexico is the result of the emergence of an assertive opposition since the long-time ruling party, the Partido Revolucionario Institucional, lost its majority in parliament in 1997 (Carbonell 2002; Weldon 2002.) In Brazil, parliament has traditionally been the privileged arena for pork barrelling over budget appropriations and amendments (Samuels 2002.) Even in Argentina, a country characterised by relatively disciplined parties, public budgeting has been the subject of more conflict and bargaining than previously though (Eaton 2002; Jones 2001).

The case of Mexico is illustrative. Since 1997, Mexico has undertaken a series of institutional reforms specifically aimed at strengthening the role of parliament in budget policymaking and oversight (Solares Mendiola 2004). The technical capacities for independent budget were significantly enhanced with the establishment in 1998 of the well-staffed and funded Centre for the Study of Public Finances (Centro de Estudios en Finanzas Públicas, CEFP) in the lower chamber of parliament. The Mexican parliament’s general research capacities were already relatively important by that time, with the Research and Analysis Services (Servicio de Investigación y Análisis, SIA) of the parliamentary library and the Institute for Legislative Research of the upper chamber of parliament (Instituto de Investigaciones Legislativas del Senado de la República, IILSEN) created in 1985 to provide general technical advise to the Senate. Henceforth, parliament is now better equipped to perform its budgetary responsibilities. It is indeed noticeable that a main impediment to legislative budgeting often resides in its incapacity to engage with the budget process, rather than the restraints put on its budgetary powers. Technical capacities are thus important considerations to take into account when assessing the effective role of legislatures in budget oversight. In 1999, after four years of negotiations, an external audit office was established specifically to assist parliament in the oversight of federal public finances and the certification of public accounts. The Auditoría Superior de la Federación (ASF) was created as an advisory body to the lower chamber of parliament, assisting the later in the review of budget execution and certification of public accounts of the federal government. In 2000, parliament also approved law on external oversight and accountability (Ley Superior de Fiscalización de la Federación). The emergence of an effective parliamentary opposition as a result of the 1997 elections, which ultimately succeeded in defeating the long-time ruling party in the general elections of 2000, thus significantly increased both the incentives and capacities for effective legislative budget oversight.

The contribution of legislative budget offices to effective budget oversight is increasingly recognised, as it allows parliaments to access independent sources of budget analysis, rather than relying on the information provided by the government. Access to budgetary information is indeed strategic in the sense that it is the parliamentary opposition that has the greatest incentives to strengthen parliament’s capacities for independent budget analysis (Messick 2002; Rubio Llorente 1993.) Capable professional staff and institutionalised technical expertise within parliament itself
are necessary conditions for legislatures to be able to exercise their budget oversight functions effectively and responsibly. The lack of professional legislative staff and the absence or weaknesses of advisory services to parliamentary committees are major hindrances to effective legislative budgeting. Members of parliaments, including those sitting in the budget and public accounts committees, do have their own political advisors. However, standing parliamentary committees lack the necessary research and advisory capacity and permanent advisors with the required technical expertise and institutional memory. This, too, is starting to change. Although not as powerful as the US CBO, incipient legislative budget offices tend to gradually emerge throughout Latin America, reflecting an increasing recognition of the current weakness and, simultaneously, the potential contribution of parliaments to budget oversight. Chile, Mexico and Venezuela possess incipient legislative budget offices, while Argentina and Colombia are currently considering establishing such offices.

Understandably, the IDB is reluctant to engage in the reform of the incentive structure shaping the role of parliaments in the budget process, in particular the quality of the legislative process, the role of political parties and parliamentary groups, executive-legislative relations and electoral rules. These are indeed very complex and sensitive areas, which do not lend themselves to quick fixes and transposed institutional solutions. They require a solid understanding of the interests and incentives shaping the behaviour of individuals in institutional contexts. The IDB, which is owned by borrowing governments and staffed by high-quality policymakers from the region, is well placed to understand these dynamics. Yet, lending operations tend to confine themselves to the inner working of parliaments, rather than approach public budgeting as an integral process. As a result, loan operations often fail to generate the systemic impact they potentially could have on the quality of the budget process and parliament’s role in budget oversight.

More fundamentally, it is increasingly recognised that the nature of the political regime and the quality of the political party system are key variables. In particular, ‘opposition parties have the greatest incentive to oversee government’ (Messick 2002:2) and ensuring effective oversight of government financial management. Indeed, in many parliamentary systems, such as the United Kingdom, a representative of the main opposition party chairs the Public accounts committees. Ultimately, the degree of cohesion and discipline of political parties determines, to a great extent, the effectiveness of the institutions of accountability and the quality of executive-legislative relations. Understandably, these are extremely difficult questions and highly contentious areas of engagement for the IFIs.

A critical challenge for strengthening legislative budget oversight is that only the parliamentary opposition, when it exists, has a interest and incentives in enhancing parliament’s capacities for effective budget oversight, and consequently for creating or strengthening capacities for independent budget review and oversight. As such, strengthening legislative budget institutions must necessarily by approached in the broader context of executive-legislative relations in presidential systems of government. For example, in Venezuela, an Economic and Financial Advisory Office (Oficina de Asesoría Económico y Financiera de la Asamblea Nacional, OAEF) was created in 1997 within the National Assembly, with support from the Inter-American Development Bank to enhance the technical advisory services of parliament in public finance. This new parliamentary structure was able to draw on the existing sources of legislative research and analysis, such as the Autonomous Service of Legislative Information (Servicio Autónomo de Información Legislativa, SAIL) created in 1994. Nevertheless, increasing tensions between the executive and the legislature since President Hugo Chávez took office have undermined the functioning of this office. OAEF was closed in February 2000 to be subsequently reopened in June of the same year, as part of the reactivation of the suspended loan by the IDB. In 2002-03, the office was under renewed pressure (Rojas and Zavarcé 2004). The case of Venezuela is particularly interesting, as the IDB became, willingly or not, an actor in the struggle between the executive and the legislature over budgetary powers.
Lending to supreme audit institutions

Lending to Supreme audit institutions is also a relatively new area for the IDB (Llanos 2002). In theory, Supreme audit institutions act as a core oversight mechanism to ensure that government is held to account for the manner in which it manages public finances. They are independent state institutions responsible for auditing government performance and public accounts and, in some cases, supervising the internal auditing system. While significant progress has been made in recent years to improve legal and financial compliance in government spending, much remains to be done to anchor performance auditing, as well as the effective external auditing of budget execution. In many Latin American, external auditing of budget execution and certification of public accounts remains deficient and audit reports fail to inform the budget-making process.

The multilateral development banks have only recently begun to support the auditor generals and strengthen Supreme audit institutions, albeit modestly. IDB’s support to Supreme audit institutions has generated great expectations in many countries, as it is talking place at a critical stage of the reform process and the modernisation of the state. As countries realise that sound public finance management and effective anti-corruption mechanisms require robust accountability institutions, especially in Latin America’s presidential systems, IDB’s support to Supreme audit institutions necessarily inserts itself in the broader context of the strengthening of governmental financial administration. As such, IDB lending constitutes a potent signalling mechanism that strengthens the hand of reformers. The case of Chile is particularly telling in that regard, as the US$25 million loan program agreed in 2001 has allowed the Chilean Contraloría General de la República (CGR) to pursue its institutional strengthening program and reinforce the political commitment to its reform.

Since 1993, the IDB has approved nine institutional strengthening projects to national supreme audit institutions, representing over US$50 million in the context of institutional strengthening programmes totalling about US$90 million (Table 6.) Two further lending operations are being considered for over US$ 12 million. Total IDB multilateral financing for national supreme audit institutions in the region represents almost US$65 million, as part of US$110 million institutional reform packages. There is a noticeable trend toward stepping up multilateral support to national supreme audit institutions.

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12 In some countries supreme audit institutions also act as the supervisory agency of government internal auditing. However, this essay focuses on external auditing. Nevertheless, it is to be noted that the links (or lack thereof) between internal and external auditing functions are critical (Diamond 2002.)
Table 6: IDB Lending to Supreme Audit Institutions

<table>
<thead>
<tr>
<th>Year</th>
<th>Country</th>
<th>Title</th>
<th>Amount (in US$ million)</th>
<th>Total</th>
<th>IDB lending</th>
<th>Counterpart financing</th>
<th>Disbursement period</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Peru   a</td>
<td>Modernization of the Office of the Comptroller General</td>
<td>14.50</td>
<td>10.15</td>
<td>4.35</td>
<td></td>
<td>4 years</td>
</tr>
<tr>
<td>2002</td>
<td>Brazil</td>
<td>Modernization of the Federal Court of Accounts</td>
<td>10</td>
<td>5</td>
<td>5</td>
<td></td>
<td>3 years</td>
</tr>
<tr>
<td>2002</td>
<td>Chile</td>
<td>Modernization of the Office of the Comptroller General of the Republic</td>
<td>25</td>
<td>15</td>
<td>10</td>
<td></td>
<td>4.5 years</td>
</tr>
<tr>
<td>2002</td>
<td>Nicaragua</td>
<td>Modernization Program of the General Auditing Office</td>
<td>6</td>
<td>5.40</td>
<td>0.60</td>
<td></td>
<td>4 years</td>
</tr>
<tr>
<td>2000</td>
<td>Colombia</td>
<td>Strengthening the Offices of the Comptroller General (CGR) and Auditor General of the Republic</td>
<td>42</td>
<td>23</td>
<td>19</td>
<td></td>
<td>4 years</td>
</tr>
<tr>
<td>2000</td>
<td>Dominican Republic</td>
<td>Program for Modernizing the National Congress and the Office of the Comptroller General</td>
<td>2.45 (28) b</td>
<td>2.45 c</td>
<td>5.70</td>
<td></td>
<td>3 years</td>
</tr>
<tr>
<td>2000</td>
<td>Honduras d</td>
<td>Strengthening and modernization of the Directorate for Administrative Probit</td>
<td>3</td>
<td>2.5</td>
<td>0.50</td>
<td></td>
<td>n.a.</td>
</tr>
<tr>
<td>1999</td>
<td>El Salvador</td>
<td>Modernization and Strengthening of the Accounts Tribunal</td>
<td>4</td>
<td>n.a.</td>
<td>n.a.</td>
<td></td>
<td>n.a.</td>
</tr>
<tr>
<td>1994</td>
<td>Uruguay</td>
<td>Modernization of the Accounts Tribunal</td>
<td>1.50</td>
<td>1.41</td>
<td>0.09</td>
<td></td>
<td>n.a.</td>
</tr>
<tr>
<td>1993</td>
<td>Caribbean</td>
<td>Audit Institutions of the Caribbean Countries</td>
<td>0.81</td>
<td>0.60</td>
<td>0.21</td>
<td></td>
<td>n.a.</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td></td>
<td>109.26</td>
<td>64.91</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Based on projects approved or under consideration as of May 2004. www.iadb.org

a Loan operation in the approval stage, 10 February 2004.
b Total amount allocated to the strengthening of both the national parliament and the national supreme audit institution of the Dominican Republic.
c Amount assigned to the national supreme audit institution of the Dominican Republic. As it is not possible to distinguish the share of counterpart financing, the overall amount of the programme is attributed to the IDB.
d Loan operation in the design stage (Perfil I) as of 19 July 2000. The Directorate for Administrative Probit was established in 1975 as an auxiliary institution to the supreme audit institution of Honduras, the Contraloria General de la República. Nowadays, it is an autonomous control agency with constitutional rank (article 232 of the Constitution), assisting parliament in its oversight functions. It is worth noting that Honduras in one of the few cases in the region where support to the supreme audit institution is provided by the World Bank.

Nevertheless, the relative size (in financial terms) of these operations varies across countries, both in absolute and relative terms. Therefore expectations on their impact ought to be realistic. Table 7 provides an illustration of the contribution of IDB loans to the budget of supreme audit institutions in Brazil, Chile, Colombia and Nicaragua.
<table>
<thead>
<tr>
<th>Country</th>
<th>SAI annual budget In million US$ *</th>
<th>IDB annual lending In million US$ *</th>
<th>As percentage of SAI annual budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brazil (2003)</td>
<td>242.2</td>
<td>1.6</td>
<td>0.8</td>
</tr>
<tr>
<td>Chile (2002)</td>
<td>19.0</td>
<td>3.3</td>
<td>17.4</td>
</tr>
<tr>
<td>Colombia (2003)</td>
<td>54.3</td>
<td>5.8</td>
<td>10.6</td>
</tr>
<tr>
<td>Nicaragua (2002)</td>
<td>5.2</td>
<td>1.5</td>
<td>28.8</td>
</tr>
</tbody>
</table>

*: The fluctuation of the dollar warrants caution when using it as a referent.
Source: Based on the information provided by the supreme audit institutions’ websites.

Several issues are worthwhile underlining. First, multilateral lending represents only a portion of the institution’s budget, which can nevertheless be important in some cases. While in Nicaragua IDB lending contributes to almost 30 percent of the supreme audit institution’s annual budget, in Brazil this figure barely reaches one percent. In Chile and Colombia, IDB lending represents approximately 18 and 11 percent of the institution’s annual budget, respectively. Quite expectedly, this figure tends to be higher for smaller countries. Indeed, IDB considers these projects as ‘innovative loans.’ Second, budget allocations to Supreme audit institutions have tended to increase in recent years, although their share of the national budget remains small. In the case of Brazil, the budget of the Tribunal de Contas da União (TCU) represents a mere 0.08 percent of the federal budget (TCU 2002:38.) Third, counterpart financing is often significant, such as in Brazil (50 percent), Chile (40 percent) or Colombia (45 percent). These latter two aspects reflect the increasing importance national governments attach to the strengthening of external audit functions. Hence, any assessment of the impact of these innovative projects ought to consider not only their financial size, but also their technical content and institutional focus.

In broad terms, IDB loans tend to focus on improving the administrative efficiency of Supreme audit institutions through strategic and organizational development, human resource management, capability building and training, and improvements in information technology, equipment and infrastructure. They also include provisions for improving relations with civil society. Furthermore, IDB projects have a marked focus on improving legal and financial compliance auditing functions, admittedly the core business of Supreme audit institutions. They sometimes include provisions for ‘innovative initiatives,’ in particular performance auditing, environmental auditing or auditing techniques for regulating agencies of public utilities, such as in Brazil. Furthermore, they usually concentrate their efforts on improving operational auditing of government programs, especially in the social sectors, rather than enhancing the role of Supreme audit institutions in the auditing of the national budget and the certification of public accounts by the legislature. Arguably, this latter core function of Supreme audit institutions would be naturally enhanced as a result or ‘side-effect’ of the strengthening of the supreme audit institution as a whole, albeit not automatically.

The IDB approach remains restrained by a technical bias, which inhibits addressing sensitive governance issues. Indeed, the effectiveness of external control mechanisms and legislative budget oversight in Latin America is hampered by the dysfunctional relations between the individual components of the systems of control and integrity in public finances. In general, these different components tend to act in isolation from one another. This has allowed corruption to flourish almost unrestricted in countries such as Argentina under Carlos Menem (1989-1999) or Peru under Alberto Fujimori (1990-2000), as the institutions of integrity and accountability were particularly vulnerable to capture. Ultimately, the effectiveness of national integrity systems largely depends on the strength of the synergies between their different components, inter alia government accounting systems, internal auditing mechanisms, external control institutions, administrative and criminal courts, and parliamentary oversight committees (Diamond 2002.)

Supreme audit institutions are particularly exposed to political meddling and prone to capture by partisan interests, especially in presidential systems of government. The experience of the
Peruvian *Contraloría General de la República* (CGR) between 1993 and 2000 is illustrative in that regard. A strategy for preventing such a capture resides in strengthening the functional links between the institutions of ‘horizontal accountability’ that are part of the national system of control (O’Donnell 1998; Schedler 1999). Political economy considerations are thus key to explain the effectiveness of Supreme audit institutions, conceived as integral parts of the national systems of control and corruption prevention. To be fully effective, Supreme audit institutions must enhance their functional and institutional relations with the judiciary (the administrative and criminal courts tasked with following-through the recommendations of audit reports) and the legislature (in particular the public accounts committees, responsible for holding government to account politically). Whether nominally attached to parliaments or not, supreme audit institutions functionally linked to them in the ‘chain of public finance oversight.’

The case of the support provided by the IDB to Colombia is noticeable, as it reflects an integrated effort to strengthen government accountability, public finance integrity, budgetary oversight and law enforcement. In April 2003, the IDB approved a US$14 million loan (as part of a US$20 million program) to the Office of the Attorney General, the *Procuraduría General de la Nación* (PGN,) the judicial office in charge of oversight and discipline of public agencies. This program completes a decade-long financing cycle of modernisation of agencies of oversight and law enforcement in public finance management, which included a US$23 million loan (as part of a US$42 million program) to the offices of the comptroller general, the *Contraloría General de la República* (CGR), and auditor general, the *Auditoría General de la República* (AGR) in March 2000 and a US$9.5 million loan (as part of a US$15.7 million program) to modernize the administration of justice and the prosecutor’s office, the *Fiscalía General de la Nación* (FGN) in December 1995. All three loans had significant counterpart financing, reflecting the recipient country’s commitment to the programs, which amounted to US$77.7 million in total.

Supreme audit institutions provide critical advisory services to parliaments, directly or indirectly, in the exercise of their accountability functions. However, relations between Supreme audit institutions and Public accounts committees are largely deficient, characterised, at best, by polite disregard. Loans to Supreme audit institutions tend to overlook the dysfunctional linkages between parliaments and Supreme audit institutions. While IDB lending operations to national parliaments focus on enhancing the role of parliaments in budget policymaking, their support to Supreme audit institutions tend to overlook their role in budget oversight and auditing. Only in a few instances, such as in the Dominican Republic in 2000 and El Salvador in 1999, did the IDB address the relationship between Supreme audit institutions and parliaments. In these two instances, a loan to the supreme audit institution was designed in conjunction with a larger loan for the modernisation of the legislature. In the case of the Dominican Republic, these were merged into a single loan.

It is paradoxical that IDB lending operations only reluctantly address the dysfunctional links between Public accounts committees and Supreme audit institutions, although this is gradually starting to change. As Table 8 underscores, a series of institutional factors determine the ultimate effectiveness of Supreme audit institutions, such as vested powers, supervising authority, nomination and removal procedures, scope of mandate and terms of office. These are areas in which the IDB seems reluctant to engage. This reluctance may be explained by the fact that Supreme audit institutions in Latin America are indeed characterised by their great diversity. In Argentina, for example, the *Auditor General de la Nación* (AGN) is a collegial body that acts as the technical advisory agency to parliament to ensure government accountability and budget oversight. The main opposition group in parliament nominates the president of the AGN. In other countries, such as Chile, Peru or Brazil, supreme audit institutions are nominally autonomous from both the executive and the legislature. In Brazil, the TCU is a collegial body with a long institutional history that combines functions of an administrative court. It concentrates it audit work on compliance auditing of government programs and agencies. Its main ‘client’ is thus the public administration it audits. In the Andean countries, such as Chile and Peru, Supreme audit institutions position themselves as governance institutions, independent of both the executive and the legislature.
### Table 8: Institutional Determinants of Supreme Audit Institutions’ Effectiveness

<table>
<thead>
<tr>
<th>Country</th>
<th>Ex ante control</th>
<th>Institution linked to the executive</th>
<th>Institution linked to the legislature</th>
<th>Autonomous institution</th>
<th>Quasi-judicial powers</th>
<th>Nomination procedures</th>
<th>Terms of office</th>
<th>Removal procedures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina</td>
<td>✅</td>
<td>✓</td>
<td>✓</td>
<td>Financial and functional independence</td>
<td></td>
<td>Legislature</td>
<td>8 years (renewable)</td>
<td>Legislature through a joint resolution of both houses</td>
</tr>
<tr>
<td>Bolivia</td>
<td>✅</td>
<td>✓</td>
<td>✓</td>
<td>Financial and functional independence</td>
<td></td>
<td>Executive (at proposal by the senate)</td>
<td>10 years</td>
<td>Legislature through a judgement of responsibilities by the Supreme Court</td>
</tr>
<tr>
<td>Brazil</td>
<td></td>
<td>✓</td>
<td>✓</td>
<td>Mixed: President elected by peers; 1/3 nominated by the President with Senate confirmation; and 2/3 by the Congress</td>
<td></td>
<td>Legislature through a joint resolution of both houses</td>
<td></td>
<td>Supreme Federal Tribunal</td>
</tr>
<tr>
<td>Chile</td>
<td></td>
<td>✓</td>
<td>✓</td>
<td>Designated by President subject to agreement of Senate majority</td>
<td></td>
<td>Legislature</td>
<td>Indefinite, until 75 years old</td>
<td>Chamber of Deputies carries out accusation and Senates removes</td>
</tr>
<tr>
<td>Colombia</td>
<td></td>
<td>✓</td>
<td>✓</td>
<td>Legislature, from list presented by Constitutional Court, Supreme Court and State Council</td>
<td></td>
<td>Legislature</td>
<td>4 years</td>
<td>Supreme Court, after previous accusation of national prosecuting attorney</td>
</tr>
<tr>
<td>Costa Rica</td>
<td></td>
<td>✓</td>
<td>✓</td>
<td>Financial and functional independence</td>
<td></td>
<td>Legislature</td>
<td>8 years, renewable</td>
<td>Legislature</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td></td>
<td>✓</td>
<td>✓</td>
<td>Executive</td>
<td></td>
<td></td>
<td>Indefinite</td>
<td></td>
</tr>
<tr>
<td>Ecuador</td>
<td></td>
<td></td>
<td></td>
<td>President, from list presented by Congress</td>
<td></td>
<td></td>
<td>4 years</td>
<td>Legislature, after impeachment</td>
</tr>
<tr>
<td>El Salvador</td>
<td>✅</td>
<td>✓</td>
<td>✓</td>
<td></td>
<td></td>
<td>Legislature</td>
<td>3 years, renewable</td>
<td>Legislature</td>
</tr>
<tr>
<td>Guatemala</td>
<td></td>
<td>✓</td>
<td>✓</td>
<td>Legal</td>
<td></td>
<td></td>
<td>4 years, non renewable</td>
<td>Legislature</td>
</tr>
<tr>
<td>Honduras</td>
<td></td>
<td>✓</td>
<td>✓</td>
<td>Functional and administrative independence</td>
<td></td>
<td>Legislature</td>
<td>5 years</td>
<td>Legislature</td>
</tr>
<tr>
<td>Mexico</td>
<td></td>
<td></td>
<td></td>
<td>Technical and managerial autonomy</td>
<td></td>
<td>Legislature</td>
<td>8 years</td>
<td>Legislature, also by impeachment</td>
</tr>
<tr>
<td>Nicaragua</td>
<td></td>
<td></td>
<td></td>
<td>Functional and administrative autonomy</td>
<td></td>
<td>Legislature, from list proposed by President and members of the legislative assembly</td>
<td>5 years</td>
<td>Legislature</td>
</tr>
<tr>
<td>Panama</td>
<td></td>
<td></td>
<td></td>
<td>Legislation</td>
<td></td>
<td></td>
<td>5 years, renewable</td>
<td>Supreme Court</td>
</tr>
<tr>
<td>Paraguay</td>
<td></td>
<td></td>
<td></td>
<td>Legislation</td>
<td></td>
<td></td>
<td>5 years</td>
<td>Executive, after agreement of Senate</td>
</tr>
<tr>
<td>Peru</td>
<td></td>
<td></td>
<td></td>
<td>Legislation, proposed by President</td>
<td></td>
<td></td>
<td>7 years</td>
<td>Legislature</td>
</tr>
<tr>
<td>Uruguay</td>
<td></td>
<td></td>
<td></td>
<td>Functional autonomy</td>
<td></td>
<td>Legislature</td>
<td>5 years</td>
<td>Legislature, after definite sentence of court of justice or competent court</td>
</tr>
<tr>
<td>Venezuela</td>
<td></td>
<td></td>
<td></td>
<td>Functional, administrative and organizational autonomy</td>
<td></td>
<td>Legislature, from list presented by citizen committee</td>
<td>7 years, renewable</td>
<td>Legislature, after pronouncement of Supreme Tribunal of Justice</td>
</tr>
</tbody>
</table>

Source: Based on tables 9.2 and 9.3 in Payne et al., 2002, pp.228-23.
However, IDB lending operations tend to resist confronting the broader governance context in which Supreme audit institutions operate and the incentives conditioning public finance accountability. They seldom seek to actively advocate the political independence and financial autonomy of Supreme audit institutions in an active and purposeful manner. This may be explained by the fact that IDB loans are mainly shaped by borrowing countries, which ultimately control most voting rights in the IDB. Issues such as criteria guiding the nomination and removal of auditor generals and the length of their term in office, as well as the procedures regulating recruitment, promotion and dismissal of professional staff are nevertheless critical determinants of the effective independence of supreme audit institutions. Credible appointment criteria and stability of tenure determine the extent to which auditor generals are likely to behave independently. Predictable financial resources are also a necessary, yet not sufficient for institutionalising Supreme audit institutions and insulating them from political meddling (INTOSAI 2001.)

The politicisation of the auditor general’s appointment procedure and that of the staff of Supreme audit institutions are major hindrances to the effective independence of the institution. When government controls a majority in parliament, either in parliamentary or presidential systems, nominations often reflect political bargains. Furthermore, short terms of office that coincide with that of the president tend to reduce the incentives of auditor generals to exercise any political independence they may have. Ultimately, these individual incentives motivate the institutional behaviour of supreme audit institutions. In Argentina, for example, the constitution and law on financial administration stipulate that Auditor Generals are appointed for an eight-year renewable term. However, in an effort to increase the independence of the AGN, an amendment to the constitution in 1994 established that the president of the AGN is to be chosen from the main opposition party. As a result, presidents of the AGN have changed as government majorities have. Furthermore, the extreme politicisation of the civil service has entailed high rates of staff turnover and thus has not allowed the consolidation of technical expertise and an ‘esprit de corps’ within the AGN. A highly prepared and recognized civil service, with stability of tenure and reasonable career prospects within the institution, is determinant for anchoring professionalism in external auditing of government finances.

IDB lending operations have tended to concentrate their efforts at the national or federal level. Yet, in most countries, the mechanisms of internal and external auditing of government finances are weaker at the local level than at the national level. The IDB is nevertheless starting to support sub-national supreme audit institutions in federal systems and accompany their de-concentration in unitary states. In countries that are being decentralised, such as Peru, IDB lending supports the de-concentration of the supreme audit in institution. More radically, in federal countries, the IDB is paying increasing attention to state supreme audit institutions. It is considering an impressive loan operation to state supreme audit institutions in federal Brazil, for a considerable amount of US$38 million, in the context of a US$60 million institutional strengthening programme (IDB 2004). If approved, this would represent the biggest loan operation to supreme audit institutions by the IDB. The commitment of the Brazilian government to strengthening sub-national state auditing is reflected in the relative importance of counterpart financing, representing 60 percent of the total. It demonstrates the federal government’s to anchor fiscal discipline in the public finances of Brazilian states and municipal governments in the context of the Law of Fiscal Responsibility of 2000.

In general, strengthening technical capacity per se does not necessarily improve the effectiveness of supreme audit institutions, nor has it prevented them from being captured, as in the case of Nicaragua. Securing the effective independence of supreme audit institutions is a critical determinant of their ultimate ability to hold government accountable, as underscored by the 1977 Lima declaration of principle of the International Organization of Supreme Audit Institutions (INTOSAI) and, more recently, the final report of INTOSAI task force on independent government auditing (INTOSAI 2001.) It is widely recognised that an inherent weakness of the state in developing countries resides in the frailty of the institutional mechanisms of ‘horizontal...
accountability’ anchored in those state institutions whose function is to control government and
restrain the state (Mainwaring and Welna 2003.)

CONCLUSION: THE POLITICAL ECONOMY OF PUBLIC FINANCE
ACCOUNTABILITY

The political economy of the budget process reveals that political and technical aspects
interact in determining the effectiveness of legislative budget oversight along the different phases of
the budget cycle. Parliaments do possess important budgetary powers. However, they seldom use
them effectively or responsibly. While capacity constraints partly explain why parliaments do not
exercise their budgetary powers effectively, governance constraints explain why they sometimes do
not exercise them responsibly. Henceforth, parliaments’ ability to establish their credibility as
institutions of economic governance is thus contingent both on the strengthening their technical and
advisory capacities to perform its budget functions, and the existence of an enabling governance
environment that allows these to be exercised effectively and responsibly. The question of strategy
then becomes whether legislative capacity should be build first, or should it emerge as a result of
increased legislative activism.

The core challenge remains to adequately combine increased legislative budget activism with
the furtherance of fiscal discipline. As Allen Schick aptly underscores, ‘As legislatures enhance
their budget role, one of the challenges facing budget architects will be to balance the impulse for
independence with the need to be fiscally responsible. The future of legislative-governmental
relations will be strongly influenced by the manner in which this balance is maintained’ (Schick in
Wehner 2004:14). Strengthening the capacities of legislatures to effectively engage with the budget
process and assume its budgetary responsibilities certainly helps minimizing the dysfunctional
effects of irresponsible legislative budgeting and ensuring a positive contribution of legislatures to
fiscal discipline and prudence. The weakness of legislative budget institutions results in an
inadequate access to independent budget analysis, the insufficiency of apolitical technical advice
and the unavailability of timely information on budget performance. Redressing these shortcomings
would require strengthening legislative budget offices and the contribution of general audit offices
to legislative budget oversight.

However, increasing technical capacity alone is likely to remain ineffectual as long as there
does not exist the right political incentives for them to be exercised effectively. Technical
improvements can easily be neutralized or be emasculated by adverse political economy constrains.
Henceforth, re-habilitating legislative budgeting in Latin American is a typical ‘chicken and egg’
problem: Should legislative capacity be build first or should it emerge as a result of increased
legislative activism? The study of legislative budgeting in Latin America clearly demonstrates that
capacities and incentives ought to be addressed simultaneously. The challenge of effective
legislative budgeting in Latin American presidential systems is to move from a context of trade-offs
between democratic accountability and fiscal discipline, to one of positive synergy and ‘virtuous
circle.’ Fiscal responsibility and democratic accountability are to be forged simultaneously.

This essay further underscores that that one ought to more clearly differentiate the
contribution of legislatures to budget policymaking in the different phases of the budget. While the
management of public expenditures ought firmly remain within the purview of the executive, the
role of the legislature is critical to ensure that government is held to account for the manner in
which it allocates, executes and oversees public spending. Sound economic governance requires
the effective and responsible oversight of the budget by a responsible legislature. Furthermore, by
strengthening the mechanisms of accountability in public budgeting, legislative budget oversight is
likely to enhance, over time, the credibility of the budget and provide effective restraints on
executive discretion in public expenditure management.

Ultimately, the governance of the budget reflects a delicate balance between executive power
and legislative oversight. The key challenge of legislative budgeting in Latin American presidential
systems is how to retain the advantages of strong executive authority required to ensure fiscal
discipline while providing the institutional checks and balances that guarantee effective
accountability. The efficacy of the institutions of ‘horizontal accountability,’ such as legislative oversight of the budget, critically hinges upon the quality of the mechanisms of ‘vertical accountability,’ in particular the nature of political regime and the coherence of the political party system, greatly influence (O’Donnell 1998; Schedler 1999). The effectiveness of the mechanisms of ‘horizontal accountability’ within the state ultimately depends on the effectiveness of the mechanisms of ‘vertical accountability.’ Strengthening the institutions of legislative budget oversight and the agencies of public finance integrity is undoubtedly a structural challenge for Latin American emerging economies. It is nevertheless a critical one.

Five broad conclusions can nevertheless be underscored.

• First, and although that is gradually starting to change, IDB lending to national parliaments and supreme audit institutions displays a reluctance to engage in the political economy of budget accountability and the politics of public finance integrity. The international financial institutions justify their apolitical approach arguing that technical improvements can, over time, contribute to improving governance, without being diluted in the intricacies of politics. Framing governance as a technical question has indeed allowed them to become involved in governance issues, while remaining within the boundaries of their respective mandates. However, public budgeting is political to the core: determining who controls the budget and how decisions on budget allocations are made are intrinsically political decisions affecting power relations (Schick 1995; Wildavsky 1964, 1992; Wildavsky and Caiden 2000). As a consequence, trying to separate the economic and the political facets of public budgeting is, to a large extent, artificial.

• Secondly, the quality of the functional linkages and institutional relationships between public accounts committees and supreme audit institutions is decisive to enforce government accountability (McGee 2002; SIGMA 2002). Public finance accountability is a system. As such, the effectiveness of one of its components is largely conditional on that of its other components as well as the quality of inter-institutional cooperation. The reports and recommendations of supreme audit institutions are largely ineffective if they are not acted on by other institutions part of the system of control, in particular the public administration itself (administrative accountability), the judiciary (criminal accountability) and parliament (political accountability.)

Furthermore, there exist complex intertwined institutional relations between the organisations part of the system of checks and balances in public finance management. For example, the quality of parliament’s oversight of government finances critically depends on the availability credible information and independent budget analysis provided by supreme audit institutions in a timely manner. At the same time, the effectiveness and ultimate impact of supreme audit institutions largely depends on the extent to which parliaments act upon the recommendations of their audit reports. Moreover, the consent of a qualified majority of members of parliament (often a two-thirds majority,) thus including that of the ruling party, is required for nominating auditor generals. The political bargains that are struck often undermine the political independence of the chosen candidate.

• Thirdly, a broader understanding of the governance of the budget process and the political economy of public budgeting is warranted, in the wider context of the national systems of control and integrity in public finance. Institutional arrangements and incentives structures do largely explain the ultimate effectiveness of public accounts committees and supreme audit institutions. Public accounts committees’ willingness to exercise their powers and hold government to account is determined by broader governance factors. These committees are a reflection of legislative politics and the nature of executive-legislative relations. Indeed, it could be argued that the effectiveness of the mechanisms of horizontal accountability within the state ultimately depends on the effectiveness of the mechanisms of vertical accountability, in particular electoral rules and party structures.

There thus exists unexplored potential in the support provided by multilateral development banks to Latin America’s supreme audit institutions and public accounts committees. The second stage of multilateral support to budget institutions should seek thus to strengthen the political independence and financial autonomy of supreme audit institutions, and promote more effective
links between supreme audit institutions and public accounts committees. The review of IDB loans to parliaments and supreme audit institutions often reveals the absence of such linkages in the design of these interventions. In general, IDB lending operations tend to be designed as self-contained interventions, which has the advantage of protecting them from unwarranted external interference, but which also has the disadvantage of inhibiting synergies between interventions.

- *Fourthly, the international financial institutions should endeavour to design integrated initiatives addressing the entire budget cycle and the governance of the budget process as a whole.* This would require linking efforts to modernise public financial management information systems within the executive with those aimed at enhancing the contribution of external audit agencies and legislative committees in the oversight of the execution of the budget. This would also entail integrating efforts to improve public finance management and accountability more tidily with those aimed at consolidating the rule of law, reforming civil services, strengthening legislatures and combating corruption. More fundamentally, this would necessarily require a greater degree of coordination, if not integration, between the different institutions’ approach to the strengthening of public financial management systems in emerging economies.

- *Lastly, multilateral lending aimed at strengthening budget oversight institutions need to factor in and engage with structural power dynamics.* As Kaufmann (2003:33) underscores, ‘a proper understanding of the political forces affecting policymaking and, related, the set of required institutional incentives for progress’ is necessary to understand the dynamics of budgetary reform. The IDB (2003:8-9) does indeed recognise that ‘projects that are limited to changing instrumental elements or simply strengthen technical organizational capacities, without altering the structure of incentives that affect the political will to apply them are likely in general to have a negligible impact. Thus institutional changes that condition the effectiveness of instrumental and organizational reforms need to be addressed at the same time […] It does little good to establish a financial management system without the development of a budgetary authority with the professional independence, power, and capacity to enforce it.’ Reform efforts fail not only because they are incomplete, but also because they are often designed to solve technical shortcomings when the problem lies in the institutional framework and the structure of incentives.

Increasing technical capacity and enhancing analytical capabilities through building legislative research services or improving investigation techniques in audit institutions are likely to remain ineffectual as long as there does not exist enough political space for them to be exercised effectively. Technical improvements are likely to be emasculated by adverse political dynamics and governance constraints. The key question is whether endowing oversight institutions with more technical capacity can strengthen them, or whether increased independence and assertiveness would lead these institutions to create and utilize more technical capacity.

Sound public finance management and accountability requires finding an adequate balance between executive and legislative prerogatives in the different phases of the budget. It may be argued that, while executive dominance in public expenditure management is more likely to ensure fiscal prudence, legislative oversight is critical to provide effective checks and balances and enforce accountability in the formulation, execution and control of the budget. The key challenge of legislative budgeting in Latin American presidential systems is to retain the advantages of strong executive authority required to ensure fiscal discipline while providing the institutional checks and balances that guarantee effective accountability.

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