



Validation Report

Reference Number: PVR-232
Project Number: 35144
Loan Number: 2127(SF)
December 2012

Indonesia: State Audit Reform Sector Development Program

Independent Evaluation Department

Asian Development Bank

ABBREVIATIONS

ADB	– Asian Development Bank
BAPPENAS	– Badan Perencanaan dan Pembangunan Nasional (National Development Planning Agency)
BAWASDA	– Badan Pengawasan Daerah (Regional Inspectorate)
BPK	– Badan Pemeriksa Keuangan (Supreme Audit Board)
BPKP	– Badan Pengawasan Keuangan dan Pembangunan (Financial Supervisory and Development Board)
PCR	– project completion report
PIU	– project implementation unit
RRP	– report and recommendation of the President
SDR	– special drawing right
TA	– technical assistance

NOTE

In this report, “\$” refers to US dollars.

Key Words

adb, asian development bank, audit institutions, civil society, government efficiency, ied, independent evaluation department, indonesia, investor confidence, legal framework, pcr, project completion report, poverty reduction, psm, public sector management, state audit reform, systems, validation

The guidelines formally adopted by the Independent Evaluation Department (IED) on avoiding conflict of interest in its independent evaluations were observed in the preparation of this report. To the knowledge of IED management, there were no conflicts of interest of the persons preparing, reviewing, or approving this report.

In preparing any evaluation report, or by making any designation of or reference to a particular territory or geographic area in this document, IED does not intend to make any judgments as to the legal or other status of any territory or area.

PROJECT BASIC DATA

Project Number:	35144	PCR Circulation Date:	Oct 2011	
Loan Number:	2127(SF)	PCR Validation Date:	Dec 2012	
Project Name:	State Audit Reform Sector Development Program (Project Loan)			
Country:	Indonesia		Approved (\$ million)	Actual (\$ million)
Sector:	Public Sector Management	Total Project Costs:	42.730	31.174 ^a
ADB Financing:	ADF: \$25.001 million	Loan: (SDR equivalent)	25.001 16.680	22.171 ^a 14.420
	OCR: 0.000	Borrower:	12.728	4.960
		Beneficiaries:	0.000	0.000
		Others:	0.000	0.000
Cofinanciers:	Government of the Netherlands	Total Cofinancing: ^b	5.001	4.445
Approval Date:	13 Dec 2004	Effectiveness Date:	13 Mar 2005	17 Dec 2004
Signing Date:	16 Dec 2004	Closing Date:	30 Jun 2010	01 Jul 2011 ^c
Project Officers:	R. Budiman J.M. Lacombe F. Ahmed	Location:	Indonesia Resident Mission Indonesia Resident Mission Indonesia Resident Mission	
Validator:	B. Graham, Senior Evaluation Specialist, IED1	Peer Reviewer:	R. Vasudevan, Evaluation Specialist, IED1	
Quality Reviewer:	R. Sabirova, Evaluation Specialist, IED1	Director:	W. Kolkma, IED1	

ADB = Asian Development Bank, ADF = Asian Development Fund, IED1 = Independent Evaluation Department (Division 1), OCR = ordinary capital resources, PCR = project completion report, SDR = special drawing rights, SF = special funds.

^a At the time of PCR preparation, the loan account was still open. Actual loan disbursements at loan closing amounted to \$22.171 million compared with the PCR's \$21.769 million. Thus, actual total project costs amounted to \$31.576 million instead of \$31.174 million as shown in the PCR.

^b This excludes the Government of the Netherlands' technical assistance (TA) estimated at \$5 million at appraisal. Actual TA disbursements amounted to \$4.2 million.

^c As reflected in the Loan Financial Information System. This was shown as 31 December 2010 in the PCR.

I. PROJECT DESCRIPTION

A. Rationale

1. An effective public audit function was essential for good governance in Indonesia.¹ While Indonesia had institutional arrangements for public sector audit since the early 1940s, the transparency, accountability, and overall performance of the audit sector suffered from unclear legal and regulatory frameworks, weak oversight, inadequate capacity, low public awareness, and inefficient resource allocation.² Decentralization added further complexity and challenges to

¹ ADB. 2004. *Report and Recommendation of the President to the Board of Directors: Proposed Loans to the Republic of Indonesia for the State Audit Reform Sector Development Program*. Manila.

² The Supreme Audit Board (Badan Pemeriksa Keuangan [BPK]) is the external auditor and Supreme Audit Institution. Central government internal audit function is carried out by inspectorate generals within each ministry and the Financial Supervisory and Development Board (Badan Pengawasan Keuangan dan Pembangunan [BPKP]), which reports to the President. The regional inspectorates (*Badan Pengawasan Daerah* [BAWASDAs])

the situation. The State Audit Reform Sector Development Program aimed to address these impediments through a package of policy interventions, adjustment measures, and investments. The program comprised two parts: (i) an investment component financed through a project loan, a cofinancing grant from the Government of the Netherlands and contributions from the Indonesian central and regional governments; and (ii) a program component financed through a two-tranche program loan.³ This validation reviews the project loan.

B. Expected Impacts

2. The sector development program aimed to achieve the overarching goal of enhancing governance and the efficiency, economy, and effectiveness of public sector audit function, through strengthened central and regional audit institutions operating to internationally accepted standards. Additional expected benefits and impacts (social, economic, and technical) included: (i) reduced poverty, (ii) better integration of audit institutions, (iii) increased interaction between the audit sector and civil society, (iv) improved government efficiency, (v) improved investor confidence, and (vi) improvements in audit systems and practices. Table 1 provides a summary of the overarching goal and objectives of the program and the program- and project-specific objectives and components (report and recommendation of the President [RRP], Appendix 4: Program Framework, and paras. 89–91).

3. Performance indicators and targets for the program goal, as stated in the RRP program framework, were participating central and regional government institutions meet benchmarks on operational capability and minimum service standards. Monitoring mechanisms were to include (i) government budget and service delivery data; (ii) national, regional, and/or local budget and socioeconomic surveys; (iii) International Corruption Assessment Report (Transparency International); and (iv) investment climate assessments.

C. Objectives or Expected Outcomes

4. The overarching program objectives were as follows: (i) an improved policy and legal framework for state audit institutions, (ii) a strengthened and efficiently aligned operating framework for external and internal audit, (iii) enhanced accountability and oversight of the audit function at all levels of government, and (iv) increased public awareness of the benefits of audit and what it can deliver. Project-specific objectives were to (i) enhance the capability of the audit institutions by building upon past support and by introducing techniques and approaches that will allow the institutions to meet their immediate mandates by operating effectively and efficiently, and incorporating international best practices; (ii) build a strong external auditor able to effectively operate at the national level; (iii) enhance the capability of the internal audit function and institutions; (iv) enhance the oversight capability of central and regional parliaments; and (v) increase the public awareness of the audit function (RRP, loan summary on pages ii and iv). Table 1 summarizes the program goal and objectives.

are the regional government internal audit agencies. In 2001, amendments to the Indonesian Constitution significantly expanded the BPK's mandate, to cover both the central and local government levels.

³ This validation only covers the PCR for the project loan, (2127-INO) and not the accompanying program loan (2126-INO). PCR for the program component has also been prepared, (footnote 9).

Table 1: Overarching Goal and Objectives, and Program/Project Objectives and Components of the State Audit Reform Sector Development Program

<p>Program Goal:</p> <p>Enhance governance and the efficiency, economy, and effectiveness of public sector audit function, through strengthened central and regional audit institutions operating to internationally accepted standards</p>	
<p>Program Objectives:</p> <ul style="list-style-type: none"> (i) An improved policy and legal framework for state audit institutions (ii) A strengthened and efficiently aligned operating framework for external and internal audit (iii) Enhanced accountability and oversight of the audit function at all levels of government (iv) Increased public awareness of the benefits of audit and what it can deliver 	
<p>Program Loan (2126)</p> <p>Objectives:</p> <ul style="list-style-type: none"> (i) Improve the policy and legal framework for state audit institutions (ii) Strengthen external and internal audit functions by providing adequate resources to institutions in line with their legal mandate (iii) Put in the policy measures to enhance accountability and oversight of the audit function at all levels of government (iv) Put in strategies to increase public awareness of the benefits of a well functioning state audit system and what it can deliver <p>Components:</p> <ul style="list-style-type: none"> (i) Rationalization of the policy, legal, and regulatory framework for state audit institutions (ii) Alignment and provision of resources to enable audit institutions to fulfill their mandate (iii) Enhanced oversight on audit recommendations and of the audit function at the central and regional level (iv) Enhanced transparency and public awareness of the state audit function at the central and regional level 	<p>Project Loan (2127)</p> <p>Objectives:</p> <ul style="list-style-type: none"> (i) Enhance the capability of the audit institutions by building upon past support and by introducing techniques and approaches that will allow the institutions to meet their immediate mandates by operating effectively and efficiently, and incorporating international best practices (ii) Build a strong external auditor able to effectively operate at the national level (iii) Enhance the capability of the internal audit function and institutions (iv) Enhance the oversight capability of central and regional parliaments (v) Increase the public awareness of the audit function <p>Components:</p> <ul style="list-style-type: none"> (i) Establishment of sector development project management in the form of an Investment Loan Monitoring Unit in the National Development Planning Agency (BAPPENAS) to be the executing agency for the investment component (ii) Introduction of new systems and practices for effective external audit (iii) Institutional enhancement and repositioning through new regulatory structures and practices for effective internal audit covering, as applicable, inspectorate generals, regional inspectorates (BAWASDAs), and the Financial Supervisory and Development Board (BPKP) (iv) Assistance to a professional formal education and nonformal certification program for internal auditors (v) Introduction of new practices for parliamentary oversight of public sector audit

BAPPENAS = Badan Perencanaan dan Pembangunan Nasional (National Development Planning Agency), BAWASDA = Badan Pengawasan Daerah (Regional Inspectorate), BPKP = Badan Pengawasan Keuangan dan Pembangunan (Financial Supervisory and Development Board).

Source: Report and Recommendation of the President, Loan and Program Summary, paras. 26, 27, 34, and 59.

D. Components and Outputs

5. The five project components (listed in Table 1) were to produce key outputs. These included: (i) new systems and practices for effective external audit (Supreme Audit Board [BPK]) and internal audit (Regional Inspectorate [BAWASDA] and inspector generals) (ii) new systems and practices for the Financial Supervisory and Development Board (BPKP) to fulfill its new mandate, (iii) establishing professional education program for internal auditors (Inspector General Department of Education), (iv) new practices for Parliament (House of Representatives [Dewan Perwakilan Rakyat]) and regional parliament (Dewan Perwakilan Rakyat Daerah) oversight of Supreme Audit Board (BPK) audit reports, and (v) public awareness of the public sector audit function established.

E. Provision of Inputs

6. Planned activities and sub-activities fell into five broad input areas: (i) introduce new systems and practices for effective external audit (BPK); (ii) introduce new systems and practices for effective internal audit (BAWASDA and inspectorate generals); (iii) introduce new systems and practices for the Financial Supervisory and Development Board (BPKP) to fulfill its new mandate; (iv) establish a formal and nonformal education program for internal auditors; and (v) prepare the Institutional Development Plan for parliament and regional parliament secretariats. The project loan of SDR16,680,000 (about \$25 million) was to be supplemented by \$10 million in cofinancing from the Government of the Netherlands, comprising \$5 million in technical assistance (TA) and a \$5 million grant. Major cost components were (i) consultants, workshops, and counterpart staff (\$18.5 million); (ii) training and overseas tours (\$11.0 million); (iii) information technology equipment (\$4.7 million); (iv) scholarships (\$4.5 million); and (v) recurrent maintenance (\$1.5 million).

F. Implementation Arrangements

7. The planned project duration was 5 years, with targeted completion by 31 December 2009. The National Development Planning Agency (BAPPENAS) was the executing agency and coordinated the work of component implementing units through an Investment Loan Monitoring Unit. The greatest perceived risks were low government commitment to reform, weak ownership of the policy package, insufficient consultation with the government, and overly complex and ambitious policy conditionalities. Safeguards taken to mitigate these risks included (i) wide consultation on the policy framework (including during early stages) to secure political commitment at the central and regional levels; (ii) concentration on a few core reforms; (iii) involvement of a wide range of the government counterparts; and (iv) linkage of policy actions and project interventions. Covenants included implementation and coordination arrangements and reporting requirements. Consultants engaged through the Technical Assistance Support for the Implementation of the State Audit Reform Investment Project⁴ supported monitoring of project activities, output delivery, quality assurance, and assisted the Investment Loan Monitoring Unit secretariat and project implementation units (PIU) with project management.

⁴ ADB. 2004. *Technical Assistance Support for the Implementation of the State Audit Reform Investment Project* Manila (TA 4474-INO).

II. EVALUATION OF PERFORMANCE AND RATINGS

A. Relevance of Design and Formulation

8. The project completion report (PCR) rated the project *relevant*, based on its alignment with and support for the government's intention to reform and improve public audit function. Public audit reform was a clearly articulated priority of the government prior to and during the project, and it remains a priority even now. Strengthening audit capacity and function was a stated goal in the medium-term development plans for 2000–2004⁵ and 2004–2009⁶ and continues to be a focus area in the current National Medium-Term Development Plan, 2010–2014 and in the National Long-Term Development Plan, 2005–2025. The Asian Development Bank (ADB) country strategies for Indonesia, including the 2003–2005 strategy,⁷ identified public audit reform as a national priority to be supported by ADB. This validation assessed the project design as relevant, with respect to the inputs, activities, implementation arrangements, and outputs leading to achievement of the intended outcomes and impacts. The project design was also appropriate in that it was the first major effort to support system-wide audit improvement, complementing earlier and ongoing efforts (including those supported by other development partners), which mainly focused on strengthening individual audit entities. The overall assessment of *relevant* is validated.

B. Effectiveness in Achieving Outcomes

9. The PCR rated the project *effective*, based on the achievement of the majority of outputs and outcomes.⁸ Some disruptions were met in a few components and activities, which is to be expected given the broad scope of the project and the large number of organizations and activities involved. It is important to point out that whereas the project component of the program, which this validation reviews, appeared effective in achieving most of its outcomes, the program component failed to deliver on some of its key outputs and outcomes,⁹ which had a dampening effect on the achievement of the intended overarching outcomes of the program. The accompanying program loan was rated *partly successful*, largely due to the failure to reorganize the BPKP and establish an independent internal auditor certification program. This validation concurs with the PCR on the general effectiveness of the project in achieving its specific outcomes.

C. Efficiency of Resource Use in Achieving Outputs and Outcomes

10. The PCR rated the project *efficient*, as the majority of outputs and outcomes were achieved within agreed costs and without significant disruptions. There were some delays, including a 6-month delay in commencement,¹¹ some unforeseen mid-course delays,¹² and a 6-month extension of the closing date.¹³ Moreover, a sizeable portion (12%) of the loan budget

⁵ Government of Indonesia. 2003. *National Development Program (Propenas) 2000–2004*. Jakarta.

⁶ Government of Indonesia. 2004. *The National Medium-Term Development Plan (RPJMN) 2004–2009*. Jakarta.

⁷ ADB. 2002. *Country Strategy and Program: Indonesia, 2003–2005*. Manila.

⁸ While para. 51 indicates that “most” of the outputs and outcomes were achieved, para. 58 states that “all” outputs and outcomes were achieved; this is an internal inconsistency in the PCR.

⁹ ADB. 2010. *Completion Report: State Audit Reform Sector Development Program in Indonesia*. Manila (Loan 2126-INO).

¹¹ The PCR stated reasons for this as insufficient commitment, ownership and understanding of some stakeholders; the late release of budget allocations to PIUs; and difficulties faced in the capacity building program.

¹² For example, the development of an Institutional Development Plan for BPKP was delayed due to the enactment by the government of a new regulation which introduced new and complex functions for the organization.

¹³ To accommodate a delay in the issuance of Government Regulation No. 60/2008, which delineated and clarified responsibility between external and internal audit functions.

was undisbursed and ultimately canceled.¹⁴ The PCR (Lessons, paras. 49–51) also pointed to other implementation challenges such as annual delays in budget allocation, too many PIUs at the central and regional level, coordination challenges, and complications in the block grant administration. Altogether, project indicators suggest that efficiency in resource use in achieving outputs and outcomes was satisfactory; this validation concurs with the PCR rating of *efficient*.

D. Preliminary Assessment of Sustainability

11. The PCR gave a preliminary rating for sustainability of *likely*, basing this on four main considerations: (i) the development of audit-related human resources through formal and informal education is expected to continue; (ii) BPKP has conducted workshops, training, and diagnostic assessments for local governments to support the implementation of the Government Internal Control System; (iii) several universities participating in the project scholarship program continue to promote and implement the program; and (iv) BAWASDAs are expected to allocate funds for continued capacity development for their auditors. The PCR did not discuss the rationale for recommended follow-up actions to enhance the likelihood of sustainability,¹⁵ nor did it mention other, arguably more important, determinants of sustainability, such as (i) continued political commitment to and prioritization of state audit reforms (with adequate resource allocation), (ii) effective enforcement of new audit policies and laws, and (iii) strengthening of public awareness and demand for better accountability. Moreover, the PCR pointed to some potential sustainability challenges.¹⁶ Furthermore, the failure of the program's program component to deliver on such key outcomes as the reorganization of the BPKP and the establishment of an independent internal auditor certification program, may consequently curtail the sustainability of project achievements. While there are clear downside risks to sustainability, this validation agrees that the four capacity-sustaining processes cited by the PCR should help to sustain some momentum gained during the project. Moreover, there is sufficient evidence that state audit reforms continue to be prioritized.¹⁷ Thus, on balance, this validation cautiously concurs with the preliminary assessment of *likely to be sustainable*.

E. Impact

12. The PCR did not explicitly rate impact, but described project-level impacts as positive and significant. Impacts on staff capacity, systems, procedures, nonformal training programs, and the regulatory framework were clear. The project helped to cement the BPK's role as the supreme audit institution. This much can be confirmed from ADB and other sources.¹⁸ Nevertheless, some caveats require attention. As mentioned earlier, the overarching program goal (enhance governance and the efficiency, economy, and effectiveness of public sector audit function) was to be jointly achieved by the program and project components. While effectiveness has improved, efficiency and economy impacts appear to have been limited. Moreover, the PCR provides no discussion on whether the expected impacts of reduced poverty, improved investor confidence, and increased interaction with civil society were achieved. The PCR does not directly link its discussion on impact to the original performance

¹⁴ The PCR does not provide clear explanation on the reasons for this cancellation and budget underrun (PCR guidelines require explanation for significant overruns or underruns). Moreover, the PCR section on disbursements fails to assess whether the appraisal disbursement schedule was realistic and/or whether any delays were encountered.

¹⁵ ADB. 2009. Project Completion Report. *Project Administration Instructions*. PAI 6.07A. Manila.

¹⁶ For example, in para. 36 it points to the fact that consultants, instead of counterpart staff, produced analyses reports on audit findings and recommendations for parliament committees.

¹⁷ For example, as reflected in the Indonesia National Medium-Term Development Plan 2010–2014.

¹⁸ For example, the 2007 Indonesia Public Expenditure and Financial Accountability Assessment mentions ongoing improvements in some audit capacity areas.

indicators and monitoring mechanisms identified in the program framework. While impact at the project level can be validated as having been *significant*, achievement of the higher-level program goal was less clear.

III. OTHER PERFORMANCE ASSESSMENTS

A. Performance of the Borrower and Executing Agency

13. The PCR rated the performance of the borrower as *satisfactory*, based on its provision of adequate counterpart funds and timely responses to requests for approval. The PCR also gave a *satisfactory* rating to the executing agency, based on its strong ownership and timely submission of required reports. Despite some delays and disruptions, the borrower and executing agency generally fulfilled their agreed-to responsibilities in a satisfactory manner. This validation concurs with *satisfactory* ratings.

B. Performance of the Asian Development Bank

14. The PCR rates ADB's performance as *satisfactory*, citing close working relationships and ongoing dialogue between ADB staff and counterparts throughout the project. The project commencement delay was attributed to ADB's initial unwillingness to make adjustments to suit the needs of the PIUs, but the project was brought back on track through better coordination and communication. This validation rates ADB's overall performance as *satisfactory*.

C. Others

15. The project had no direct or indirect involuntary resettlement, and did not negatively affect indigenous peoples. It did not require an initial environmental examination or environmental impact assessment under Indonesian laws and regulations.

IV. OVERALL ASSESSMENT, LESSONS, AND RECOMMENDATIONS

A. Overall Assessment and Ratings

16. This validation endorses the PCR's overall rating of *successful* (Table 2). The project was aligned with Indonesia's needs and its design was generally appropriate. Despite some delays and challenges, the project achieved the majority of its intended outputs and outcomes. Some of the momentum and outcomes achieved from the project are likely to be sustained. Impact at the project level was significant, although higher level impacts are less clear. Altogether, the project achieved its aims.

Table 2: Overall Ratings

Criteria	PCR	IED Review	Comments
Relevance	Relevant	Relevant	
Effectiveness in achieving outcome	Effective	Effective	
Efficiency in achieving outcome and outputs	Efficient	Efficient	
Preliminary assessment of sustainability	Likely to be sustainable	Likely to be sustainable	

Criteria	PCR	IED Review	Comments
Overall assessment	Successful	Successful	
Borrower and executing agency	Satisfactory	Satisfactory	
Performance of ADB	Satisfactory	Satisfactory	
Impact	Not rated	Significant	Clear project-level impact achieved (para. 12).
Quality of PCR		Satisfactory	Refer to para. 20.

ADB = Asian Development Bank, IED = Independent Evaluation Department, PCR = project completion report.

Note: From May 2012, IED views the PCR's rating terminology of "partly" or "less" as equivalent to "less than" and uses this terminology for its own rating categories to improve clarity.

Source: ADB Independent Evaluation Department.

B. Lessons

17. The PCR identified important lessons, with which this validation concurs. Continued efforts to strengthen the Indonesian audit sector should benefit from such lessons.

C. Recommendations for Follow-Up

18. This validation agrees with the recommendations put forward in the PCR, especially the general recommendation to continue reforms to improve public expenditure management in Indonesia. While this specific project delivered some notable results and impact, there remains significant room for further strengthening across the state audit system.. The project loan achieved notable progress in this area, introducing new curriculum and programs and providing scholarships, among other achievements. Capacity development for internal auditors will remain a critical need and continued support from ADB in this area is important.

V. OTHER CONSIDERATIONS AND FOLLOW-UP

A. Monitoring and Evaluation Design, Implementation, and Utilization

19. The RRP had set out monitoring and evaluation responsibilities and mechanisms, including a project management monitoring system that was to collect information to facilitate assessments of project impacts and effectiveness. Moreover, the program framework had also identified a wide range of indicators by which project performance was to be measured, such as government budget and service delivery data, investment climate assessments, audit coverage indicators, corruption assessment reports, and results of the public surveys. By all indications, monitoring and reporting activities took place as planned. The PCR as well as other project documentation provided some indicators on which partial assessments of impact can be made. Nonetheless, limited baseline data were provided, inhibiting a more robust assessment of project achievements.

B. Comments on Project Completion Report Quality

20. The overall quality of the PCR is rated *satisfactory*.

C. Data Sources for Validation

21. Primary references included ADB RRP, ADB PCR, executing agency PCR, loan review reports, the project administration memorandum, and ADB country strategies. Secondary

references included the 2007 Indonesia Public Expenditure and Financial Accountability report, World Bank governance ratings and reports, Global Integrity Report for Indonesia 2010, and other relevant assessments and analyses on Indonesia.

D. Recommendation for Independent Evaluation Department Follow-Up

22. Despite some of the quality limitations of the PCR, this validation generally concurs with the overall PCR ratings and assessments. No project performance evaluation is hereby recommended.