

Organizational and Functional Aspects for Improvement of State Financial Control System in The Country

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Abstract. In this article has been researched organizational and functional changes resulting from reforms in state financial control system of Uzbekistan. In this case, main attention is focused on the process of introducing the audit function to state financial control system, its necessity, essence and content of main duties, institutional and functional, as well as legal and methodological support.

Keywords: State financial control, external audit, internal audit, financial inspection, financial audit, compliance audit, performance audit, internal control, transformation, revision, inspection, review.

1. INTRODUCTION

In recent years, fundamental reforms have been carried out in public finance management system in Uzbekistan. In this case, main attention is focused on results-oriented state financial support, strengthening financial discipline, improving accountability and independence. During these reforms, allocation of budgetary funds is increasing in terms of quantity and expanding in terms of quality. If increase in terms of quantity refers to the increase in public expenditure in recent years, on the other hand, expansion in terms of quality is associated with the increase in financing methods and mechanisms.

Meanwhile, taking into account international best practice, in our country improving the quality of financial control by increasing the addressability, efficiency and effectiveness of public expenditure, strengthening the prevention of violations of budgetary legislation and expanding remote financial control is defined as a priority task in state financial control system.

2. LITERATURE REVIEW

In theoretical view, there are different thoughts on the content and essence of state financial control, and they can be broadly divided into two large groups. State financial control is defined as ensuring "compliance with legislation" by the first group of scientists, while the second group, along with compliance, also refers to "efficiency or saving the resources" as the duty of state financial control.

In particular, as L.N. Ovsyannikov states [2], state financial control is the implementation of the right of state to legally protect its financial interests, as well as financial interests of citizens through a system of legislative, organizational, administrative and law enforcement measures. This definition mainly focuses on compliance function of state financial control.

According to other foreign researchers such as V.I. Samarukha and I.V. Derevtsova [1], state financial control is one of control forms aimed at ensuring the proper allocation of public budget in accordance with legislation on financial law, ensuring the rule of law and protection of state property, targeted and effective use of public budget, as well as identifying the cases of violations of financial discipline.

Another researcher S.E. Prokofev [3] indicates that state financial control is a set of actions and processes aimed at checking compliance of the use of public budget with financial and other relevant legislation acts by state and other bodies, as well as local self-governance bodies, legal entities and individuals, regarding the effectiveness and efficiency of the allocation of public financial and other resources.

Based on study of theoretical evidence, it is appropriate to focus state financial control on efficiency and effectiveness, along with compliance, of the use of public budget.

It should be highlighted that, within the framework of efforts carried out in this direction, internal audit services have been established in all ministries and agencies. Determining main duties and functions, rights and obligations of these internal audit services based on international best practices, training and retraining of personnel in this direction is remarked as the most essential condition for establishing a new state financial control system.

Legal basis for the implementation of state financial control in our country is regulated by Budget Code of the Republic of Uzbekistan. In particular, Chapters 26-28 of this Code are about state financial control, and Article 171 defines the list of state financial control authorities. According to this Article, state financial control bodies are Chamber of Accounts of the Republic of Uzbekistan, Ministry of Finance of the Republic of Uzbekistan and authorized bodies within its organizational structure. State financial control on revenue part of state budget and budgets of state trust funds is

carried out by state tax service authorities within the scope of established authority.

Financial control on expenditure part of budgets of the budget system is a more complicated process in comparison to revenue part. Because accomplishment of main duties and functions of the state in terms of financial perspectives are ensured through expenditure part. Taking this into account, we focus main attention on state financial control on expenditure part of budgets of the budget system.

Currently, major part of procedures regarding the implementation process of budget expenditures can be observed in foreign experiences, in which control on these procedures is known as audit. We can mention the following reasons for this:

1. Orientation of budget expenditures to efficiency requires to transfer main emphasis in financial control from "compliance" to "efficiency".
2. There is a need to assess expenditure approaches. Because expenditure turns out to be oriented to particular goals and this need is derived from assessing the opportunity of these expenditure methods to achieve the goals;
3. In order to achieve the goals, it is required that ministries and agencies have sufficient independence. It is also essential to get advantage of this independence effectively and at the same time to avoid non-targeted spending [5].

These reasons resulted in the need to conduct transformation of state financial control system to audit in our country. Therefore, with Resolution RP-3231 of the President of the Republic of Uzbekistan "On further improvement of financing mechanism of educational and medical institutions and state financial control system", dated August 21, 2017, internal audit and financial control services were established at Ministry of Public Education, Ministry of Health, Ministry of Higher and Secondary Special Education, Center for Secondary Special Vocational Education of the Ministry of Higher and Secondary Special Education, Off-Budget Pension Fund under Ministry of Finance of the Republic of Uzbekistan.[6,7,8,9]

It can be clarified that transfer of internal audit and financial control functions to internal audit services has been starting point of transformation from financial control to audit. While this Resolution was legal basis for the organization of internal audit, law of the Republic of Uzbekistan "On Chamber of Accounts of the Republic of Uzbekistan" clarified the legal basis for duties of external audit. In particular, Article 3 of the law states that Chamber of Accounts of the Republic of Uzbekistan is a supreme body of state financial control and external audit [4].

As a reasonable continuation of this transformation, Decree No. DP-6300 of the President of the Republic of Uzbekistan "On measures to further improve state financial control system", dated August 27, 2021, was adopted. According to this Decree, it was declared that financial audit, compliance audit and performance audit are to be implemented in addition to control forms and types carried out by Chamber of Accounts.

These audit methods as additional control forms and types, specified by this Decree, are forms of external audit in international experience, and they are a part of International Standards of Supreme Auditing Institutions (ISSAI) developed by International Organization of Supreme Auditing Institutions (INTOSAI) [10].

Based on this Decree, we can realize that a new stage of transformation has begun in state financial control system in our country. At this stage, major attention is focused on the development of audit. However, this does not necessarily mean to abolish or weaken financial control duties. On the contrary, it is intended to improve the scope and quality of activities of financial control bodies, especially by organizing new types of control, including development of control based on information technologies.

3. ANALYSIS AND RESULTS

Expenditure from state budget is viewed as the main object of state financial control system. Because primary aim of state financial control is to increase compliance with legislation and efficiency of allocating public budget. Therefore, analysis of the functions of current state financial control system should be carried out with analysis of information on state budget expenditure.

Changes in quantity and quality indicators of state budget expenditures was cited above, in which change in terms of quantity describes main conditions for reform of state financial control system. In particular, we believe that increase in the amount of state budget expenditures complicates compliance assessment with legislation. Because increase in expenditure is usually in line with adoption of new regulatory legislation acts, and this leads to an increase in the number and types of objects for compliance assessment.

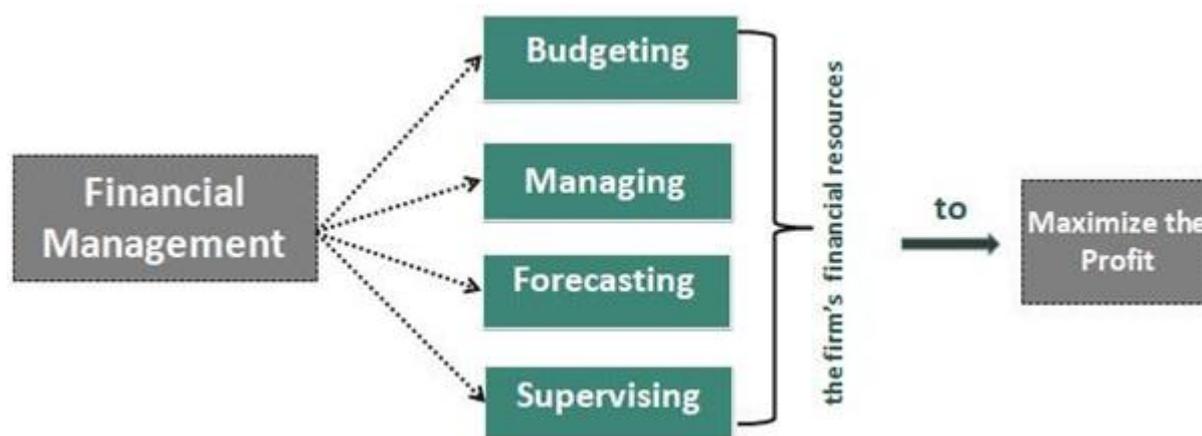


Figure 1. Financial Management structure [12]

At the same time, expansion of state budget expenditures in terms of quality through implementation of allocation methods and mechanisms creates obligation to diversify control targets, methods and directions in state financial control system. It focuses on transition from compliance to efficiency. Because compliance of allocation with legislation does not necessarily mean efficiency. In addition, expansion of allocation methods and mechanisms refers to the fact that it is essential to assess proper selection of these methods and mechanisms. In this case, key focus should be on efficiency assessment of methods applied to allocation of public budget.

Despite continuously growing pattern in state budget expenditure compared to previous year, we can see that it has been increasing at decreasing rate in recent years.

These changes are leading to changes in distribution approach of state budget expenditures, and it primarily requires institutional and functional transformation of duties of state financial control system based on internationally recognized experiences, and formation of its new outline in collaboration with audit.

To sum up, it can be noted that there is a need to transform state financial control system, and it is actually significant to conduct this transformation based on international best practice.

Coordination between financial control authorities and audit structures has a key role in further development of state financial control system. In process of transformation, duplications of functions in their activities might be inevitable since audit services also have function to conduct compliance audit regarding the compliance with legislation on financial activities similar to financial control. In turn, this might lead to the fact that financial control and audit structures perform identical type of control activity within the same organization. In such cases, it is essential to coordinate activities of control structures. But it is highly remarkable to analyze mutual collaboration among functional units of state financial control.

In international practice, financial inspection, external audit and internal audit are included in functional structure of state financial control system [11]. "Financial control" function in practice of Uzbekistan corresponds to "financial inspection" in international experience. Because compliance of financial flows with legislation is conducted through financial inspection in international experience, and main focus is on the determination of errors and shortcomings. Therefore, it is appropriate to use the term "financial inspection" for the analysis of mutual collaboration among functional units of state financial control. Along with the introduction of internal audit system, referring to the term "financial inspection" rather than financial control simplifies the application of international practice as well as analysis of practice in our country.

These duplications can be viewed in three-way form. For example, internal and external audit perform similar duties in terms of financial and compliance audits, while internal and external audit as well as financial inspection perform almost similar duties in terms of monitoring compliance with legislation. Assessment of compliance with legislation or inspection is carried out in a similar approach, but expected targets are not the same in audit and inspection. Compliance by internal audit system should initially refer to assessing the opportunities to regulate existing regulatory legislation acts. That is, in case of complications in application of relevant regulatory legislation acts and regulatory system, it is required to identify them as a result of audit engagements. Inspection activities usually do not ensure for this, and they control compliance with regulatory legislation acts.

In addition, there is an area (highlighted in red in Figure 1) that can be identified by all of these three control units, which implies possibility of detecting shortages, theft and illegal disbursement. Although such cases are the main duty of financial inspection, they can also be detected during audit engagements.

Another feature of Figure 1 is the analysis of non-duplicated functions of these three control units that are

illustrated as non-intersecting areas (highlighted in different colors). We can observe that non-intersecting areas are much larger than intersecting areas once we look at the position of each function in this Figure. It means that non-intersecting parts should be the basis of functions or main attention should be focused on performance of duties.

Main duty of external and internal audit, which does not overlap with financial inspection, is efficiency assessment. This is termed as performance audit in international practice. However, performance assessment by external and internal audit differs from each other. We can observe differences in purpose and scale. In particular, internal audit services conducts study of internal control processes, effectiveness of particular financing procedures or actual results of target indicators of particular programs within ministries and agencies while efficiency audit by external audit covers full performance assessment of ministries and agencies or their joint performance [6].

Other duties of financial inspection include control of budget allocated to legal entities (state-owned enterprises, economic entities) and individuals, fight against corruption and economic crimes.

Therefore, coordination matters regarding these functions should be carried out according to results of activity as mentioned above. At the same time, differences between audit and financial inspection activities can be illustrated as purpose, subordination and scope of activity (Table 2).

Taking these features into account, reforms of state financial control system is going on in our country. In particular, Resolution No. RP-128 of the President of the Republic of Uzbekistan "On further increasing efficiency of state budget expenditures of the Republic of Uzbekistan and improving the activities of state financial control bodies", dated February 14, 2022, was adopted.

According to this Resolution, a number of measures on qualitative development of the activities of financial inspection and internal audit services have been carried out through institutional restructuring:

1. Institutional features:

– On the basis of Department of State Financial Control within the central apparatus the Ministry of Finance of the Republic of Uzbekistan and its regional branches, State Financial Control Inspectorate with a status of a legal entity was established under the Ministry of Finance;

– Division for Working with Internal Audit Services was established within the central apparatus of the Ministry of Finance of the Republic of Uzbekistan.

2. The following measures are being carried out on qualitative development of financial control and internal audit:

– an electronic controller-inspector information system in the field of financial control is being developed by organizing a database based on integration of software complexes of state bodies;

– engagement of personnel in special training courses based on international practice is organized;

– national standards of internal audit and a manual for conducting internal audit engagements have been developed, and internal audit engagements are being conducted based on these documents;

– measures to increase the scope and quality of remote audit engagements as well as determination and prevention of risks are being conducted.

Table 1. Differences in functions of state financial control

No.	Indicators	Financial inspection	External audit	Internal audit
1.	Purpose	Determination of violations in legislation	Efficiency assessment of projects by state bodies, economic sectors and regions, and study of compliance of expenditures with legislation	Reducing the risks associated with inefficient and illegal spending by improving the efficiency of organization and improving financial discipline, in which internal audit service is established
2.	Subordination	Ministry of Finance	President and Parliament	First head of organization (ministry or agency) in which internal audit service is established

3.	Scope of activity	Organization where financial control engagement is carried out	State bodies, economic sectors and regions	Organization (ministry or agency) in which internal audit service is established
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Furthermore, within the framework of this Resolution, charter regulating the activities of State Financial Control Inspectorate under the Ministry of Finance, as well as model charter as a legal basis for organization of the activity of internal audit services, national standards of internal audit, and manual for conducting internal audit engagements have been approved.

Meanwhile, the following outstanding problems still exist in further development of state financial control system:

- absence of a system for mutual collaboration and recognition of activity results between state financial control bodies and internal audit services;
- absence of a unified integrated risk analysis system in state financial control system;
- absence of a system for qualification certification of internal audit service personnel;
- absence of a system for quality assessment of the activities of internal audit services;
- absence of "internal audit committees" in ministries and agencies;
- lack of standardization of internal control system in ministries and agencies.

4. CONCLUSIONS

In summary order to further improve efficiency of state financial control system based on elimination of outstanding problems mentioned above, the following measures are proposed:

1. Preparation and approval of a memorandum regarding cooperation on the introduction of a new system providing mutual collaboration and recognition of activity results of state financial control bodies and internal audit services.

2. The following measures should be carried out in order to launch unified integrated risk analysis system in state financial control system:

- review of existing risk analysis systems (purpose of implementation, mechanisms, procedure, results, level of applying information technologies, content of programs, level of integration (with IT systems of ministries and agencies) and modules);
- summarizing information about risk factors and algorithms;
- development of unified risk register based on summarized risk factors, classification of risks and analysis of statistics;
- development of a single database for risk analysis and organization of structural unit for the management of this database;
- development of proposals for the development of new risk factors based on integration;
- development of unified integrated risk registers and ensure its implementation by all control structures.

3. Development and implementation of certification procedure for qualification certification of internal audit personnel;

4. Development and implementation of a system for quality assessment of the activity of internal audit services based on includes internal assessment, consisting of ongoing monitoring and periodic assessment, and external assessment;

5. Development and implementation of procedure for organization of internal audit committees in order to increase independence and accountability of internal audit services of ministries and agencies;

6. Organization of systematic work on assessment and standardization of internal control based on results of internal control in ministries and agencies. In accordance with international practice, development of a manual for organization of internal control system, assuming that internal control includes operational and financial management process that ensures achievement of effectiveness, compliance with legislation and efficiency of the activities of ministries and agencies.

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