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## Improvement of public financial control in the context of ensuring financial security of the state

**Abstract.** Increasing threats to financial security are one of the major economic problems in Ukraine in terms of accelerated globalisation of the world economy against the background of overcoming the global financial crisis. It is required to improve public financial control (PFC) to provide an effective response to real threats in the financial sector. The article summarises the shortcomings inherent in the public financial control at the current stage of its development. The authors of the article have determined factors affecting the state of public financial control in Ukraine and defined areas for improvement of public financial control in the context of the financial security of the state.

The authors have proved that the key areas to enhance PFC in the context of the financial security of the state are the improvement of the existing legal framework, the development of domestic standards by taking into account international standards and the EU standards aimed at complying the domestic standards in the field of PFC with international standards of the financial control and the EU requirements, legal separation of powers of the public control bodies with regard to control measures undertaken in the financial sector, improvement of organisational and methodological implementation of relatively new forms of control including the audit of efficiency, improvement of information and communication in terms of PFC staff development, strengthening the preventive function of PFC, i.e. its shift to the prevention of fiscal violations.

**Keywords:** Public Financial Control; Financial Security of the State; Internal public Financial Control; External Independent Financial Control; Managers of Budgetary Funds

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### Удосконалення державного фінансового контролю в контексті забезпечення фінансової безпеки держави

#### Анотація

Однією з найважливіших економічних проблем в Україні в умовах прискореної глобалізації світового господарства на фоні процесів подолання світової фінансової кризи є зростання загроз фінансовій безпеці держави. Забезпечення ефективної протидії реальним загрозам у фінансовій сфері потребує удосконалення державного фінансового контролю. У статті узагальнено недоліки, що притаманні державному фінансовому контролю на сучасному етапі його розвитку; визначено фактори, що впливають на стан розвитку державного фінансового контролю в Україні та запропоновано напрями удосконалення державного фінансового контролю в контексті забезпечення фінансової безпеки держави.

**Ключові слова:** державний фінансовий контроль; фінансова безпека держави; державний внутрішній фінансовий контроль; зовнішній незалежний фінансовий контроль; розпорядники бюджетних коштів.

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**Усовершенствование государственного финансового контроля  
в контексте обеспечения финансовой безопасности государства**

**Аннотация**

Одной из важнейших экономических проблем в Украине в условиях ускоренной глобализации мирового хозяйства на фоне процессов преодоления мирового финансового кризиса является рост угроз финансовой безопасности государства. Обеспечение эффективного противодействия реальным угрозам в финансовой сфере нуждается в усовершенствовании государственного финансового контроля. В статье обобщены недостатки, которые присущи государственному финансовому контролю на современном этапе его развития; определены факторы, которые влияют на состояние развития государственного финансового контроля в Украине, а также предложены направления усовершенствования государственного финансового контроля в контексте обеспечения финансовой безопасности государства.

**Ключевые слова:** государственный финансовый контроль; финансовая безопасность государства; государственный внутренний финансовый контроль; внешний независимый финансовый контроль; распорядители бюджетных средств.

**1. Introduction**

The peculiarity of the current stage of the economy development of Ukraine is its integration into the world economic and legal space in difficult conditions of overcoming the financial crisis. In this connection, the further development of the economy will apparently take place under quite rigid constraints of public financial resources. The latter affects the growth of threats relating primarily to financial security.

Improvement of public financial control (PFC) is one of the priorities of the economic policy of the state in order to minimise threats relating to financial security. As it is stated in recent legal documents regarding the ways to overcome the consequences of the crisis and the fight against corruption, an important role in this process is given to the main function of public financial management, which is public financial control, which must ensure legitimate and effective formation, distribution and use of public financial resources, especially those accumulated in the budgetary system and create a transparent and effective system of state management of financial resources aimed at improving the welfare of Ukrainian citizens [1-2].

Moreover, it should be noted that Ukraine seeks to acquire the status of candidate for accession to the European Union and keeps the course to the comprehensive integration in political, legal and economic space of the European Community. This is confirmed by the conclusion of the Association Agreement with the EU in 2014, and the development of the Strategy of Sustainable Development «Ukraine-2020» [3-4].

In addition to other conditions, immediate improvement of public financial management, especially by reforming the PFC system through its harmonisation with EU standards, and strengthening the institutional role of the Ministry of Finance of Ukraine as the main authority that develops both the financial policy in general and the policy in the field of PFC in particular, as well as ensures its implementation in the system of central executive bodies.

In Ukraine, the reform of the PFC system has already lasted over 20 years. Yet, the beginning of the year 2005, when the concept of public internal financial control for the period until 2017 was introduced, should be considered to be its official starting point [5]. Thus, the PFC reform in Ukraine is first of all based on the reform of public internal financial control (PIFC), a type of control from various executive bodies, ministries, organisations and institutions using budgetary funds and being in charge for the implementation of budgets at all levels, based on the responsibility of the head of the relevant state body.

The latter is due to the fact that the public internal financial control concept was developed by the European

Commission in the late 1990s and is now used to guide and support countries seeking to develop modern systems of the public financial control. The uniqueness of this concept consists in using the PIFC abbreviation (which was first proposed by Robert de Koning in the article published in November 1999) and determining different components of the public internal financial control, such as internal control, internal audit and their harmonisation with international standards at the central level [6].

As for the current standing of the PFC in Ukraine, it should be noted that values peculiar to the specified constituent of the national control system have been formed, namely:

- transparency of control powers related to the use of budgetary funds;
- improvement of financial discipline when using budgetary funds;
- consistent and full implementation of the principle of the targeted use of budgetary funds;
- increasing control over the preservation of assets by budgetary institutions;
- achievement of the quality of the control function;
- standardisation as the basis of harmonised procedures relevant to public financial control over various bodies of the public sector.

However, the support of the developed values formed in recent years is based on their correspondence to the EU requirements and standards which demand constant improvement of PFC.

So, despite the fact that in domestic and foreign economic literature a lot of researches are devoted to the study of the theory and practice of PFC, there are still many uncertainties and controversial issues, such as:

- there is no consensus on the nature of the PFC, its aim and subject, as well as the capture of this notion in the legislation;
- there is no clear understanding of the essence and components of PFC, conceptual foundations of its structure;
- the experience of developed countries of the that having similar political systems to that in Ukraine regarding the construction of PFC in terms of public financial security context is understudied, etc.

All this causes a need to study existing deficiencies of PFC at the present stage of its development, systemizing and analysing the influence of factors on the development of PFC in Ukraine and elaboration of ways to improve PFC in the context of public financial security as a basis for sustainable development of the country and guaranteed execution of social obligations to citizens.

## 2. Brief Literature Review

Fundamental works by foreign authors such as, R. Adams, A. Arens, A. Vysser, R. Konyng and J. Mozer [7-11], are dedicated to disclosure of the theory and practice of organisation and functioning of PFC.

Among the important researches regarding PFC in the context of public financial security, we can identify works by the following foreign and domestic scientists: O. Baranovskyi, I. Basantsov, L. Dikan, O. Dyshkant, H. Dmytrenko, I. Ivanova, L. Ivashova, S. Kulpinskyi, A. Liubenko, Ye. Mnykh, V. Symonenko, Y. Chumakova, N. Shevchenko, O. Shevchuk and others [12-29]. Upon that, there is no concept of the SFC development in Ukraine, and the ways to improve SFC have no sufficient scientific justification.

## 3. Purpose

The article aims to study ways to improve SFC in the context of public financial security through summarising existing imperfections which are inherent in PFC at the present stage of its development and to analyse the factors impacting the development of the PFC in Ukraine

## 4. Results

Before defining the most effective measures that will help to quickly bring the domestic system of PFC to its European prototype in the light of the course chosen by Ukraine towards European integration, it is useful to understand the extent of the problems existing in this area today. To do this, it is essential to determine which obstacles exist at the current stage of the PFC development in Ukraine. Thus, there is a number of ideas in the specialised literature to identify imperfections of PFC at the present stage of its development. Yet the common view on the matter is not observed [13-16; 21; 26; 29].

In Table 1, the disadvantages relating to the public financial control in Ukraine at the present stage of its development are summarised.

According the data in Table 1, it is appropriate to identify factors affecting PFC under the current conditions of modernisation of public financial management in Ukraine to ensure, above all, an appropriate level of financial security of the state. An analysis of trends corresponding to the relevant factors of development will make it possible to timely detect changes in the efficiency of PFC depending on the quality of

public regulation and conditions for the functioning of supervisory financial authorities.

It should be noted that the authors of the present research, based on the analysis of the works by the domestic and foreign scientists, have singled out factors that affect PFC. It is advisable to divide all such factors into external and internal ones, taking into account the position of supervisory bodies. The level of effectiveness of PFC itself depends on the sufficient provision of conditions for the functioning of PFC bodies. In our view, it is appropriate to designate the following factors as external ones: legal, methodological, coordinative, economic and informational. The internal factors are technological, qualificative and organisational ones.

Various factors have an impact on the implementation of PFC, but the most important one is the imperfection of the legislation with regard to the regulation of the control bodies' functioning. I. Basantsov emphasises the existence of more than 170 legislative acts in Ukraine, which in some way regulate supervisory activities [13]. However, this diversity leads only to confusion and complication of relations between supervisory authorities and does not provide the comprehensiveness of control. Even the Law of Ukraine «On the Main Principles of the Public Financial Control in Ukraine» (hereinafter - the Law) is unable to solve the abovementioned problems [30]. The problem is that the Law is aimed only at the State Financial Inspection (which is now the State Audit Service of Ukraine [31]), (the specialised PFC body which provides centralised governmental control in the system of the executive branch of power, while the Accounting Chamber of Ukraine, the external body of PFC that carries out the external parliamentary control in the system of legislative branch of power, is ignored in the specified legal document.

Also, a lack of independence of regulatory bodies and a lack of autonomy in their decision-making, especially at the regional level and their controllability by branches of government, whose activities are audited by them, should be viewed as shortcomings of the legislation in the area of PFC.

Other factors impacting the effectiveness of control are methodological factors. Until recently, control in our country has been carried out in the form and by methods that do not meet European requirements, namely in the form of audits

Tab. 1: The disadvantages inherent in state financial control of Ukraine at the present stage of its development

Disadvantages	Author						
	H. Dmytrenko [16]	A. Khmelkov [26]	O. Dyshkant [15]	I. Basantsov [13]	O. Shevchuk [29]	Ye. Mnykh [21]	L. Dikan [14]
1. Imperfection of the legal system	+	+	+	+	+	+	+
2. Imperfection of the PFC system	+	+	+	+	+	+	+
3. Weakness of the previous and current control		+	+	+	+	+	+
4. Absence of a united database		+	+	+	+	+	
5. Imperfection of methods and forms of control	+	+	+	+	+	+	
6. Inappropriate material incentives to control public bodies	+						
7. Overloading of controllers	+						
8. Increased level of staff turnover	+						
9. Excessive costs		+					
10. Limited access for the public		+				+	
11. Inability to encompass all objects of control		+					
12. Low standard of internal control and internal audit		+		+	+	+	+
13. Lack of independence				+	+		
14. Imperfection of the responsibility of managers of budget funds				+			+
15. Inadequate level of interaction with law enforcement and judicial authorities				+			
16. Imperfection of personnel training				+	+		

Source: Compiled by the authors based on: [13-16; 21; 26; 29]



and inspections. In developed European countries, progressive forms of PFC are audit, or more precisely, the public audit (the audit of public finances), internal audit in the system of public bodies and inspection. First of all, it concerns the implementation and development of public internal financial control.

It should be noted that the basis for the reforming the PFC system in Ukraine, which is characterised by the centralised system of control over the financial resources of the state, is decentralisation of the organisational structure of PFC. In this regard, the main efforts in the implementation of reforms are exactly imposed on the reorganisation and restructuring of the PFC bodies, the implementation of new forms of the control and the development of methodological support related to modern forms of PFC, such as public financial audit and inspection by the State Audit Service of Ukraine (formerly - the State Financial Inspection), internal audit in the system of governmental bodies (financial audit, compliance audit and performance audit) and inspection.

In addition to the above, it is also important to stress the weak implementation of modern information technologies in the practice of controllers. Moreover, there is no common concept of the PFC system reflecting a unified theoretical and methodological basis and principles of control. Also, it is possible to consider directions in order to carry out control and to prevent violations as methodological shortcomings. Ye. Mnykh is of the same view, considering it necessary to increase the value of preventive control during implementation of control activities [21].

In addition to methodological factors, coordinating factors play an important role in the formation and development of the PFC in Ukraine. I. Basantsov believes that there are many regulatory bodies in the domestic PFC system, yet there is no clear system of coordination of actions between the relevant authorities to maintain their effective and efficient operation. Upon the availability of a large number of control entities, significant chains of public finance areas remain uncontrollable. This adversely affects the level of financial security and increases the existing threats. Also, the Accounting Chamber of Ukraine is the highest body of the public financial control in Ukraine. However, the authority to coordinate actions and set up an extensive regional system of the control has not been assigned. Today, clear interaction between supervisory authorities and law enforcement and judicial bodies in order to achieve the maximum impact on compensation of damages caused to the state and bring the guilty persons to responsibility remains unestablished [13]. Also, Ye. Mnykh pays attention to the imperfection of the Ukrainian legislation and a significant number of amendments to the Constitution of Ukraine, which promotes disorders and complicates the work of controllers. In

addition, a large number of terms are missing in the legislation, and it is not possible to interpret them in a common manner [22]. According to O. Dyskant, the lack of a unified system of control bodies and coordination of their actions is the most significant drawback of the modern financial control system, especially in the context of financial security of the state [15].

As for the economic factors of PFC, it should be noted that their content appears to be inefficient because the costs exceed the results of such control. Thus, the analysis of the current state of control in the public sector shows that the domestic system of PFC is not effective because it does not fully perform its tasks and functions in the form of separate elements, rather than as a single system. It only partially takes into account the basic principles of the system of control which is in force in European countries. As a consequence, there is still an extremely low level of financial discipline in the budget sector and the number of violations in the budget funds is growing from year to year in Ukraine [33]. The latter is also extremely unfavourable for the financial security of the country.

In relation to the latter group of factors of external influence on the information factors, it should be noted that there is absence of proper information base and insufficient openness of the results of control for the public. In fact, to increase the efficiency and operational ability of control, it is essential to create a unified database. In Ukraine, it is problematic for controllers to obtain information if accounting is automated. For example, a controlling authority in the Netherlands is granted unlimited rights to access information related to the object of control. I. Stefaniuk says that the regulatory authorities within the Dutch system of financial control are entrusted with the task to ensure credibility of the government and transparency of public bodies. Also, they are entrusted with public access to the results of the monitoring of the activities of the public sector, which is not observed in the Ukrainian PFC system [25].

Thus, internal factors have no less important impacts on the standing and development of PFC in the context of ensuring financial security of the state than external factors. Internal factors are technological, organisational and qualitative factors.

Technological factors show the insufficient use of modern information technologies in the controllers' work, and the lack of modern programs and technologies in the controllers' work significantly increases the risk of non-detection of violations.

Qualification factors are the low level of target personnel training, imperfect instructional materials, inadequacy and inefficiency of personnel training aimed at financial control, namely failure to acquire an adequate practical experience and the lack of effective methods.

Tab. 2: Approach to the improvement of public financial control

Approach	Key components of the approach
System approach	Improvement of the system of public financial control
	Development of a regulatory framework of the subjects' activity under PFC
	Introduction of foreign experience with regard to national peculiarities
	Introduction of a comprehensive approach to solving problems relating to PFC
Functional approach	Professional improvement
	Use of information technologies
	Creation of a unified control database
Managerial approach	Introduction and development of internal control and audit
Organisational approach	Interaction between control bodies and public bodies
	Publicity of control
	Scientific research in the field of PFC
	Development of a training system for controlling bodies
Methodological approach	Introduction of controllers' ethical principles
	Development of prior control methodology
	Introduction of new control methods

Source: Compiled by the authors based on [14; 16-18; 20-22; 24; 26; 29]

Organisational factors represent fragmentation of interests of subjects and objects of control; rating assessment of control bodies according to the amount of funds reimbursed to the state is incorrect. It is possible to prevent violations due to tactical and strategic planning and staff motivation within controlling bodies. According to Ye. Mnykh, persecution by the government, ordered inspections and lobbying significantly reduces staff motivation and therefore efficiency of control [19].

However, there are many opinions expressed by domestic scientists, including L. Dikan, H. Dmytrenko, I. Ivanova, L. M. Ivashova, A. Liubenko, Ye. Mnykh, I. Stefaniuk, A. Khmelkov and O. Shevchuk, regarding the correction of the mentioned shortcomings of PFC [14; 16-18; 20-22; 24; 26; 29]. The authors' generalised approach regarding the improvement of PFC is presented in Table 2.

Currently, it is important to implement all the measures mentioned in Table 2. Nevertheless, according to the authors, the priority is to improve the PFC system in general, the legal framework of activities of the subjects of control, control methods and the use of modern information technologies in controllers' work.

In our view, creating an appropriate legislative framework is an important step to improve control. Ukraine's domestic legislation provides definitions neither for the concept of public financial control, nor for the whole system of PFC. Such a situation is viewed to have a very negative impact on the improvement of PFC in the context financial security of the state.

Imperfect methods and forms of PFC reduce its effectiveness and the failure to use new and more advanced methods and forms, e.g. audit of efficiency, leaves controllers powerless, while the objects control may use the latest technologies and modern methods of management. Identification of violations and punishment of the perpetrators does not reduce the number of future violations. Therefore, one needs to strengthen the role of previous and current control executed by the Ministry of Finance of Ukraine and the State Treasury of Ukraine. Also, it is necessary to assign the current control in the government to internal controllers. However, despite the fact that internal control in the government reduces the number of violations, there is no mechanism of interaction between the internal control and the external control within the executive bodies. Today, it is necessary to increase the effectiveness of audit and to implement advanced methods and forms of SFC in the practice of controllers such as monitoring, internal audit and controlling, as well as economic and mathematical methods and techniques of financial analysis.

An effective system of PFC is impossible without creating a unified information base, which would contain systematised information on the results of inspections of all objects under control concerning all existing regulatory authorities. Such a system should simplify the exchange of information between supervisory authorities to avoid duplication of audits and to enable risk assessment based on the study of the results of previous inspections. The creation of a unified database will provide an opportunity to obtain information not only by regulatory authorities, but also by the public. Public information about inspections will increase public trust to the government and managers of budget funds. Also, it will enhance the level of financial security.

The next step to improve control is to develop specialised computer software. The use of such software will minimise controllers' time required to identify risk factors, analyse the causes of violations and assess the effectiveness of institutions. Also, the application of the relevant software in public financial control will make it possible to control the majority of objects at a time and to use continuous methods for most operations during inspections. Since most control objects use specialized accounting programs, accounting data may not even be entered in the program by controllers, but transferred to them.

Public financial control is carried out by controllers, which is why the result depends on their skills. It is therefore

advisable to establish a unified system of training. Such a system should be aimed at developing professional skills. The high level of qualification should be confirmed by an appropriate certificate, a document prove the controller's right to carry out the relevant activities. The training body should also ensure access to appropriate literature, check methodology, develop ways to improve control, research and introduce international experience in the domestic practice of controllers.

An important role in enhancing the effectiveness of public financial control to ensure an adequate level of financial security in Ukraine and minimise the corresponding threats belongs to the organisation of public controllers' work. Today, an excessive number of controllers reduces the effectiveness of control undermined by customized inspections, inadequate staff motivation and the ineffective system of assessment of supervisory departments. It is possible to solve such problems by developing an effective system of assessment of departments that would take into account not only the control measures or the amount of money returned to the budget, but also indicators such as the ratio of the amount of funds returned to the budget to control measures undertaken to provide the relevant activities, or the ratio of detected violations to the number of internal government auditors involved, etc.

The implementation of the above mentioned measures will bring PFC to a new level that will open a possibility for economic growth of our country and bring the domestic PFC system to the systems of PFC in developed countries.

The above measures aimed at improving PFC can be realised only through appropriate legislation, as well as amendments to already existing regulations through the implementation of international standards and best European practices [34-37].

Today, significant steps are already being made towards approximation of the PFC in our country to the models of PFC system operating in the EU.

In terms of the implementation of legislation related to PFC, Ukraine has adopted a number of key legal instruments: the Concept of Public Internal Financial Control until 2017 (2005), the Budget Code (2010), the Law of Ukraine «On the Main Principles of Public Financial Control in Ukraine», the Concept and the Strategy for Public Finance Management (2012 and 2013 respectively), the Law of Ukraine «On the Accounting Chamber of Ukraine» (2015) and a large number of legal documents concerning internal control and internal audit in the government [5; 32; 30; 1; 2; 38; 39-42].

## 5. Conclusions

The authors of the article have substantiated that, along with significant achievements in the field of the SFC, there is still a number of shortcomings that need to be addressed, considering the influence of external and internal factors over the development of PFC.

The authors have proved that the key areas to enhance the public financial control in the context of the financial security of the state are the improvement of the existing legal framework (including the adoption of the Concept and the Strategy for the PFC Development and the Law of Ukraine «On Public Financial Control»), the development of domestic standards by taking into account international standards and the EU standards aimed at complying the domestic standards in the field of PFC with international standards of the financial control and the EU requirements, legal separation of powers of the public control bodies with regard to control measures undertaken in the financial sector, improvement of organisational and methodological implementation of relatively new forms of control including the audit of efficiency, improvement of information and communication in terms of PFC staff development, strengthening the preventive function of PFC, i.e. its shift to the prevention of fiscal violations.

In this regard, it is appropriate to take into account the best practices of developed countries and global trends in the field of PFC as a starting position for further development of the PFC in Ukraine.

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