

THE ISSUES OF THE INTERDEPENDENCE OF PERFORMANCE AUDIT AND FINANCIAL CONTROL IN THE PUBLIC SECTOR

Varduhi Tananyan

Armenian State University of Economics, Ph.D. student

tananyanvarduhi.2000@gmail.com

<https://orcid.org/0009-0007-8882-829X>

Abstract: Traditionally, the functions of financial control in public sector organizations have been targeted at the formation of budgets and, accordingly, the execution of expenditures. However, in recent decades, performance budgeting has been implemented in international practice, which has followed not only the expenditure of financial resources, but also the results expected from them in the public sector. The article discusses the possibilities of integrating the functions of financial control and performance audit in the public sector. In particular, it is proposed to introduce a key performance indicator monitoring system into the traditional financial control toolkit.

Keywords: financial control, performance audit, key performance indicators, financial control ecosystem

JEL codes: M40, M41

Research aims: to comment on the weaknesses and strengths of traditional financial control in the public sector and based on this, to present recommendations for improving the financial control toolkit.

Research novelty: It is proposed the use of KPIs for improvement in the financial control toolkit of public sector, whereby monitoring of financial discipline accompanied by assessments of the target cost - effectiveness of financial resources.

Introduction

Participants of public services and the non-profit sector regularly evaluate their activities in terms of the mission, goals and objectives for which they were created. In international practice, from this perspective, performance audit is of particular importance, which is widely used in public sector organizations (Dal Mas, F., Massaro, M., Lombardi, R., Garlatti, A., 2019).

Performance audit is an independent, impartial and credible study, that reveals the extent to which public initiatives are relevant and timely, the extent to which certain systems, operations, programs, activities or organizations operate in accordance with the principles of economy, purpose and cost effectiveness, and whether there is room for improvement or not (Funnell, W., 2015).

The principles of economy, purpose and cost effectiveness of performance auditing can be defined as follows:

- ✓ The principle of economy means minimizing the cost of resources. The resources used should be available at the right time, in the right quantity and quality, as well as at the best price.
- ✓ The principle of cost-effectiveness means getting the most out of the resources available. This refers to the relationship between the resources used and the results, in terms of quantity, quality and time.

- ✓ Purposeful effectiveness is related to the implementation of the set goals and achieving the intended result.

Thus, the main purpose of performance audit is to constructively promote effective management in terms of economy, achievement of objectives and costs, which will be considered also by financial control in public sector (Hay, D., Cordery, C., 2018).

Research results

Performance audit contributes to increasing the level of accountability and ensuring transparency. By promoting accountability, it helps those with management and supervisory powers to improve the results of their organizations (Ahonen, P. and Koljonen, J., 2020). This is done by analyzing whether the decisions of legislative and executive bodies are developed and implemented effectively, in terms of purpose and cost, and whether citizens and taxpayers are provided with the best combination of price and quality (Schillemans, T., van Twist, M., van der Steen, M. and de Jong, I., 2018).

Performance audit does not question the objectives and decisions of the legislator, but analyzes whether any gaps in laws, legal acts or any shortcomings in their implementation hinder the achievement of certain objectives (Zhang, J., X. and Rich, K., T., 2016). The focus of performance audit is on those areas where it is possible to create the greatest value for citizens and those areas that have the greatest potential for improvement (Furqan, A.C., Wardhani, R., Martani, D. and Setyaningrum, D., 2020).

Performance audit creates constructive incentives for responsible parties to take appropriate steps. It preserves

transparency by providing parliament, taxpayers, other funding sources, recipients of state policies and the media with in-depth information on various government actions and the final results obtained from them (Gustavson, M., Sundström, A., 2018). Thus, performance audit directly contributes to providing useful information to taxpayers, while serving as a basis for improvements (Gustavson, M., Sundström, A., 2018).

Although clear legislative standards apply in the case of financial control, this is not typical of performance audit. Therefore, due to the purpose of the latter, it is extremely important to choose reliable and impartial criteria (Heald, D., 2018). Consequently, we emphasize the importance of using progress KPIs in financial control, integrating it with performance audit (see Figure 1). In the case performance audit aimed at solving any problem, the starting point is the identified deviations or suspicions about their existence. However, the main goal is, of course, not to identify deviations (deviation from KPI and its consequences), but to identify the causes of their occurrence.

Financial controllers are obliged to manage resource expenditure risks in the public sector, in particular, addressing incorrect or incomplete conclusions, the provision of unbalanced or non-value-added information for users, etc (Yang, L., 2020). As a rule, performance audit focuses on the control of the management systems and their functions and procedures of various organizations, agencies and programs financed from the state budget in the public sector, as well as non-profit organizations.

When conducting a performance audit, the review criteria are set by the auditors on a case-by-case basis, while in the case of a

financial audit, the relevant criteria are established by legislation or industry regulations (Licht, J., 2019).

Similarly, performance audit reports are prepared with a specific approach, according to the given case, while financial audit reports are mainly prepared in a standardized format.

Performance audit, unlike financial audit, based more on the assumption of precedent. Each individual performance audit ultimately creates added value, which cannot be said about financial audit (Loozekoot, A. and Dijkstra, G., 2017). If financial audit reveals accountability errors, then performance audit considers issues more from the perspectives of economy, efficiency and effectiveness, bringing the ability to create new value to the activity management process (Torres, L., Yetano, A., Pina, V., 2019).

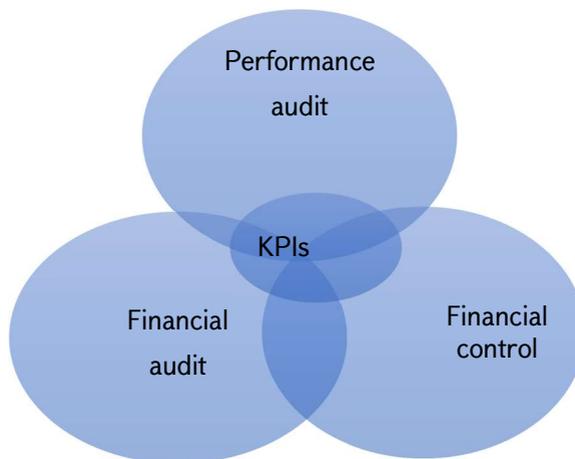


Figure 1. The ecosystem of financial control in auditing framework⁵

⁵ Created by the author.

Traditionally, financial control in the public sector has focused on revenue collection and, accordingly, keeping financial discipline in the implementation of expenditures (see Table 1). In this case, the qualitative characteristics of the expenditure of financial resources are relegated to the background.

Therefore, when advanced KPIs become applicable in the financial control toolkit, the purposefulness of the resources spent and the actual return on the results will be taken into account in the control process, along with financial discipline keeping.

Table 1. Consolidated budget of RA (mln. drams)

Items	2020	2021	2022	2023
Revenues and transfers, total	1 608 728	1 743 865	2 132 864	2 455 140
Expenditures, total	1 924 899	2 061 941	2 322 360	2 638 353
Deficit (-)	-316 171	-318 074	-189 496	-183 213

Source: *Statistical Year Book Armenia, 2024, p. 463*

Conclusion

In the public sector, financial control has traditionally been associated with financial audit, with the aim of assessing the consistency of financial resources formation and expenditures. However, performance budgeting, which is currently actively used in international practice, also requires not only monitoring of financial flows in the public sector, but also performance assessments arising from implemented monetary expenditures. In

such a case, it becomes necessary to strengthen the relationship between performance audit and financial control, based on evolution KPIs. The use of KPIs in the financial control system allows assessing the cost-effectiveness of monetary resources according to their purpose and the actual results formed.

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**ՀԱՆՐԱՅԻՆ ՈԼՈՐՏՈՒՄ ԿԱՏԱՐՈՂԱԿԱՆԻ ԱՌԻԴՏԻ ԵՎ
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ՓՈԽԱՌՆՉՈՒԹՅԱՆ ՀԻՄՆԱԽՆԴԻՐՆԵՐԸ**

Վարդուի Թանանյան

Հայաստանի պետական տնտեսագիտական համալսարան
ասպիրանտ

Բանալի բառեր - ֆինանսական վերահսկողություն, կատարողականի աուդիտ, կատարողականի ցուցիչներ, ֆինանսական վերահսկողության էկոհամակարգ, առաջընթացի առանցքային ցուցիչներ

Հանրային ծառայությունների և ոչ առևտրային ոլորտ սուբյեկտները պարբերաբար գնահատում են իրենց գործունեությունը՝ այն առաքելության, նպատակների և խնդիրների առումով, որոնց համար իրենք ստեղծված են: Միջազգային պրակտիկայում, այս տեսանկյունից, առանձնակի կարևորվում է կատարողականի աուդիտը, որը լայնորեն կիրառվում է հանրային ոլորտի կազմակերպություններում:

Կատարողականի աուդիտն անկախ և անկողմնակալ ուսումնասիրություն է, որտեղ բացահայտվում են, թե որքանով են հանրային նախաձեռնությունները տեղին և ժամանակին, թե որքանով են որոշակի համակարգեր, գործառնություններ, ծրագրեր, միջոցառումներ կամ կազմակերպություններ գործում տնտեսման, նպատակային և ծախսային արդյունավետության սկզբունքներին համահունչ, և արդյոք կա բարելավման հնարավորություն, թե՛ ոչ:

Հոդվածում քննարկվում են ֆինանսական վերահսկողության և կատարողականի աուդիտի ինտեգրման հնարավորությունները, որոնց իրականացման պարագայում հանրային հատվածի կազմակերպությունների գործունեության վերահսկողությունը ստանում է նոր որակ: Մասնավորապես, առաջարկվում է ֆինանսական վերահսկողության համակարգում սահմանված ստանդարտներին զուգահեռ՝ կիրառել առաջընթացի առանցքային ցուցիչներ, որով կնարձրանա ֆինանսական ռեսուրսների ծախսահատույցի վերահսկողության արդյունավետությունը:

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