

REPORT

**on “Modern Challenges for SAIs Capacity Building” by Mr H. Asadov, the
Chairman of the Chamber of Accounts of Republic of Azerbaijan,**

**in the 3rd session of IV EUROSAI/ARABOSAI held in Baku
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**Topic: Accurate definition of the boundaries of external state
financial audit is one of the main factors affecting the quality of the
measures of control**

Dear participants of the Conference!

In spite of some revival, observed in development of the World economy last years, the tempo of growth in the World economy is still weak and high risks and uncertainty still remains over it, that is why necessity for organization of control over the use of public resources is becoming more important. Economic and efficient use of the funds, full achievement of expected results turn into main goals in this case and, in their turn, particularly increase the importance of state financial control.

Internal and external audit are main means of control over the use of state funds, which regardless the status of the institutions that fulfil the function of controlling, the forms and the methods applied, serve to one goal – provision of effective use of existing resources. According to the standards accepted in the international practice, internal audit is a process of control organized, carried out and developed by the authorized decision makers who adopt decisions to reveal irregularities or shortcomings timely within the entity. This control finally serves for provision of accuracy of financial reports and operations, as well as achieving goals set for the entity in compliance with the requirements of legislation. External financial audit mainly aims at determination of legality and accuracy of financial management and reports, at determination of effectiveness and efficiency of

activity and at provision of transparency and accountability. These very factors considerably extend its scope of activity compared to internal control.

Notwithstanding that importance and principles of financial control aimed at provision of effective use of budgetary funds, mandate of institution performing external audit and its place in public management and other problems are widely covered in Lima and Mexico Declarations of INTOSAI, specific and important role of Supreme Audit Institutions (SAI), fulfilling public external financial control in state financial management system, was emphasized in the Resolution adopted in the 66th session of General Assembly of the United Nations. Alongside with underlining important role of SAIs in increasing effectiveness, accountability and transparency in state management the UN, through this document, declared that achieving national and international goals and priorities is possible only through them and it called supreme authorities of the member states to apply those principles on to national institutional structures.

Since those appeals take state financial control to a new level more correct and accurate determination of organizational forms, satisfying the nature of public financial control, stipulates clearer establishment of the places of the components (external and internal) of this control in state management and their correlation. Lack of the abovementioned clarity brings to functioning of many institutions having same function and authority in the sphere of financial control, as well as to weakening of the connection among them, to delay in application of modern and effective forms and methods of control, to emerging of difficulties in establishment of unique financial control policy which, in its turn, has considerably negative influence on effective organization of financial management in general. The fact that those two components do not repeat each-other, use of the results of internal audit in external financial audit makes it fuller and more effective, as well as establishing favourable conditions for effective use of existing resources in the process of control make precise determination of boundaries between these two components and processes inevitably necessary, to our opinion.

Precise determination of boundaries and its provision in the process of control, first of all, require accurate definition of the functions of control on both levels. In this case it should be taken into consideration that internal control is an act of ‘checking, inspection’ by its nature, whereas external audit, being a supreme audit, directly controls activity of the state institutions related to funds management, results of realized economic policy and the conceptions of strategic development, as well as execution of wide scale programs and projects.

Corresponding institution, fulfilling internal control, does not only establish state financial policy, but also provides its current realization. The entity, fulfilling external state financial control, does not take direct participation in preparation of financial policy. It mostly evaluates efficiency and effectiveness of the implemented policy and turns into leading link of the system of state financial control.

External audit has more extensive function of control. It also covers wide-scale sphere of activity. However, if internal audit is mainly carried out related with budget funds, the subject of the supreme external audit is budget funds, state property and assets, other varieties of public resources, as well as extra budgetary funds. In addition, while providing the parliament with objective and full reports about efficient and effective use of public funds through joint application of financial inspection and audit, development of effective financial management and correct organization of governing activity SAIs incorporate parliament and administrative control.

Activity related to evaluation of effectiveness of executed economic policy and to definition of the directions of strategic development guarantees prevalence of external state financial control over internal one. When internal control mainly deals with activity of institutions and officers related to formation and use of state resources, the subject matter of external control is firstly evaluation of productivity of activity of internal control system.

Today, when demands and needs change so rapidly, one of the distinctive features of SAIs is their performance as an effective tool against corruption.

Taking into consideration that provision of accountability and transparency are important means in struggle against corruption the mentioned UN Resolution underlines possibility to achieve this goal through strengthening of SAIs.

To our opinion all these points determine the main aspects of the boundaries between external and internal financial control. Naturally, clarification of the boundaries is the first step on the way to solution of the problem; however provision of those boundaries carries much importance. That is why the factors affecting the boundary line between internal and external control activities, particularly those which do not depend on the level of functional and organizational activity of SAIs should be seriously considered. Those factors are mainly related to political decisions which determine legal frames of SAIs activity and are conditioned by main economic and social goals of the government. Even though in some cases the mandates and authorities of SAIs are reflected in the national Constitution in accordance with INTOSAI recommendations, the frames of those powers fixed in here, are of political character. From this point of view the abovementioned boundaries are fixed more explicitly by corresponding laws and other normative-legal acts helping to prevent crossing and repeating of the actions on internal and external control mechanisms through accurate and full development of those acts, and finally to achieve mutual complementarity between them.

Strengthening of Institutional potentiality of SAIs, regulation of their internal activity and awareness affect full and effective fulfilment by SAIs of their mandates and authorities. That emphasizes more effective and purposeful use of the potentiality existing within INTOSAI community.

We think that it is necessary to increase the efforts of SAIs in several directions related with effective organization of internal activity in accordance with the appeals of the mentioned UN Resolution. However if the Constitution and the laws have the purpose to determine relations, general boundaries and rules between the stakeholders and SAIs, instructions and the national audit standards, developed

in line with ISSAIs, should help SAIs to achieve the goals set within the frames of those boundaries and relations.

As SAI is one of the main links of public control, awareness of the state institutions and the public about the mandate, the functions and the authorities of this institution, as well as about its current activity, does not only serve for provision of transparency and accountability, but also plays an important role in determination of the boundaries between internal and external control. Raising awareness has great importance in conducting audits ensuring timely follow-ups related with audit results, as well.

Dear conference participants!

We would like to mention some points regarding regulation of those issues in our country. The powers of the Chamber of Accounts, the state supreme financial control institution of the Republic of Azerbaijan, have been fixed in the Constitution in accordance with the requirements of Lima Declaration and the special laws regulating the work of the Chamber were adopted.

Generally there are some normative-legal acts on force in the country which manage state financial control system in the republic, including Tax and Customs Codes, laws “On the Chamber of Accounts of Republic of Azerbaijan”, “On the Budget System” and “On Internal Audit”. The power and the functions of the institutions, managing internal and external audit, are fixed in the mentioned acts to some extent, but still it is necessary to overcome some challenges related to precise determination and provision of the boundaries.

To eliminate gaps in solution of these problems, to guarantee performance under mutual cooperation with other institutions of state control, to develop business cooperation with them the Chamber of Accounts, as leading link in the system of state financial control, signed agreements of cooperation on its own initiative with several leading institutions, including Ministries of Finance and Taxes and State Foundation for Social Protection. Those agreements clarify to some extend the process of determination of boundaries in the system of external and internal financial control.

An important step was made in our country for provision of effective and complex solution of the issues related to improvement of the system of state financial control, to strengthen financial discipline, to provide transparency and accountability when using public funds in the country and “National Activity Plan on Promoting Open Government” by the President of the Republic of Azerbaijan was approved as an expression of political interest in solution of those issues. Accurate directions of activity on specification of the power of the institutions, implementing state financial control and development of a draft law about financial control for provision of an improved legal framework on financial control have been mentioned under priority issues in the Activity Plan. The Chamber of Accounts, implementing supreme state financial control, has been mentioned here as a coordinating and a responsible institution.

Improvement of legal framework as one of subcomponents on capacity building of the Chamber of Accounts is planned within the frameworks of CAPSAP project, carried out in our country to achieve the set goals in accordance with World practice and audit standards. Implementation of this subcomponent will provide clarification of the powers of the institutions, carrying out state financial control, and preparation of draft law covering the issues of financial control.

We believe that the measures to be taken will give irreplaceable input in solution of the abovementioned problem.

Thank you for your attention.