How to reform the Accounting Chamber of Ukraine in Supreme Audit Institution

Annotation: The problem of transformation of the Accounting Chamber of Ukraine from the independent public organ of financial control in independent supreme audit institution is analyzed. The article forms the picture of ways and methods of such transformation. The activity of the Accounting Chamber is considered on position of legitimacy existent legal framework of which the author considers legitimate as far as it takes into account balance the public and private interests protected of inseparable rights for one subjects (at firmness rights others) and duties and plenary powers of state and public institutes called to provide realization of these rights as well. The author appeals to the criteria of legitimacy of public accountant institutions on the basis of international experience which is generalized and recommended by the International Standards for Supreme Audit Institution (ISSAI) as guidelines in the field of public finances that allows to avoid or substantially to reduce the level of excessive politicization of the audit work at least. The analysis of the perspectives for dimension upgrading of the Accounting Chamber is conducted. Attention is accent on the practical mechanism of further legal formalization of the state financial management system. Taking into account his own international experience, the author recommends ways and methods of implementation of the system of international standards, strengthening of independence of the Accounting Chamber, extension of the competency with regard to audit of public finances. The suggestions to improve the mechanisms of cooperation with Parliament, politics and audit procedures are introduced. The conceptual suggestions to the new release of Law of Ukraine about the Accounting Chamber taking into account expansion of its constitutional capacity, including audit of the financial, budgetary statements and audit of local budgets are formulated as well.

Keywords: Account Chamber of Ukraine, financial and budgetary statements, independent external audit, the International Standards for Supreme Audit Institution (ISSAI), legitimacy.

During the seventeen years since its establishment, the Accounting Chamber of Ukraine was held as an independent state external financial control institution with a special constitutional competence [1, C. 39-42]. The authority and achievements of the institution are recognized at national and international levels. The Accounting Chamber has gained some experience of carrying out institutional audits in accordance with international accounting standards, in particular with regard to the projects funded by the World Bank in Ukraine, and during the performance of functions of the OSCE independent external auditor in 2009-2012. As I have contributed a lot to the above, I beg to ask a tricky question. Has the Accounting Chamber really managed to become a legitimate instrument for the external, unbiased and reasonable assessment of the system of management of the state (public) funds system at the present stage of state building? What does the Accounting Chamber need to update its own audit practice?

The problem of improving the external audit system, particularly in Ukraine, and the status and powers of the Accounting Chamber, have been sufficiently considered by scholars and practitioners, in particular, M.T. Bilukha [2], I.K. Drozd [3], V.H. Melnychuk [4], V.F. Pihotsky...
A certain narrowness of views of scholars and practitioners is contributed by the imperfect terminology, which is widely used for the characterization of the Accounting Chamber in the national modern literature and legal framework. It is often defined as “Supreme Audit Institution”. The term comes from an incorrect translation from English of the name of the International Organization of Supreme Audit Institutions – INTOSAI, the member of which the Accounting Chamber is.

Therefore, the aim of the article is to develop theoretical and practical ideas of experts, subjects of legislative initiative, authorities and civil society with regard to the necessity of development of the Accounting Chamber's powers in the context of its actual transformation from an independent state financial control body into an independent supreme audit institution.

The answer to the questions set requires more than just describing the major functional powers of the Accounting Chamber, which are usually viewed through the applicable Ukrainian law. In the philosophical and legal aspects, the modern legal framework of the Accounting Chamber may be considered as a legitimate measure of how it takes into account the balance of public (social form of organization) and private (taxpayers) interests by mutual coordination of protection of inalienable rights of some subjects (without violation of other) with duties and powers of state and public institutions in terms of providing and implementing of such rights. As V.F. Pihotskyy rightly notes, «an effective financial control over the management of public funds is an important factor in strengthening public confidence in government, an instrument to consolidate government and society in order to achieve the common goal - welfare of citizens and stability of the government. Obviously, such control will have the confidence of citizens only when it is objective and independent on those executive authorities that administer public funds» [5, P. 184-190].

Such assessment requires turning to current self-organizing mechanisms of the legal reality inseparably from economic, political and socio-cultural aspects of the country. First of all, these are social (public) request of taxpayers for the objective independent information on the use of public funds and proposals to improve the efficiency of their use in the current social and political situation in the country. Actually, the fact that the Accounting Chamber does not really control or carry out the audit of operations with land and assents of state (including state property), local budgets, public companies or enterprises partly owned by state, foreign exchange reserves of the National Bank of Ukraine is unfair from the perspective of taxpayers. Lack of financial accounting authority (audit of compliance), efficiency audit or administrative activities audit leads to the practical application in
control measures of the methodology and procedures which represents a kind of hybrid of the former Soviet state control with elements of financial audit and thesis defense. If we consider the concept of legitimacy by Max Weber [10, C. 157-272], that is, as confidence and acceptance of the governmental institution by the society, such an approach is rightly doubtful, both in terms of control objects, that see here primarily a focus on exposing violations in the use of funds, and society, which is not interested in the fact of control, but in the specific recommendations on obtaining a particular social effect/result of committed expenditures.

It’s impossible to practically ensure the balance of such interests without functioning of the Accounting Chamber the as a supreme independent external audit institution, which operates on the basis of International Standards of Supreme Audit Institutions (ISSAI), which basing on the best international years-long practice considered the basic criteria of legitimacy that are necessary for the operation of independent audit of a public finance authority and provide a possibility to avoid or at least significantly reduce unnecessary politicization of the work of such institutions. Although, of course, these criteria do not qualify for exhaustiveness.

The criteria (measures) of legitimacy of such an institution on the basis of international experience are summarized and defined in the following standards [11]:

Level 1 (Fundamental principles) - ISSAI 1 “The Lima Declaration of Guidelines on Auditing Precepts”, which aims to call for independence of public finance auditing. “The Supreme Audit Institution” (SAI), which does not comply with this condition, cannot qualify for this status. The objectives of the Declaration are considered as achieved only under the condition of legislative consolidation of such independence. This document is of great importance for all INTOSAI Supreme Audit Member-Institutions, regardless of the region to which they belong, their level of development, place in the system of governance and form of organization. Being clear and accurate, it provides a comprehensive list of goals of public finance auditing and all related issues. The rule of law and democracy are the main prerequisites of independent public finance auditing which represent the foundation of the Lima Declaration. The ideas represented in the Declaration belong to the eternal determining principles that have remained valid for many years, since their adoption in October 1977.

Further, the Prerequisites for the Functioning of SAI are detailed on the Level 3 – Fundamental Auditing Principles (ISSAI 100 – 400) and on the Level 4 – General Auditing Guidelines (ISSAI 1000-5699).

Today, the tasks of the Accounting Chamber established by the current law do not provide for the full compliance even with the first Level that is all requirements of the Lima Declaration. Thus, the provisions of the Law of Ukraine “On the Accounting Chamber” [12] do not correspond to particular Articles 22 and 23 of the Declaration, stating the powers of a Supreme Auditing Institution on the control of equipment for electronic data processing and enterprises with state capital shares. Thus, there is a need of legitimation (recognition by social subjects of the importance of social and political reality, as a whole and in its individual forms and components [10, P. 157-272]) of status of the Accounting Chamber on the basis of INTOSAI International Standards.

The Accounting Chamber as the **Supreme Audit Institution** should act to provide **independent professional recommendations** regarding management and use of all public resources. The contribution to the new legal reality which is currently in the process of self-organization is **responsibility** for management decisions, **transparency** of cash flows and assets and **development** of economy and society.

As rightly noted by I.Y. Chumakova, the Accounting Chamber “needs to get rid of its status of a supervisory authority, increase the audit ability and change the scale and nature of its control and analytical measures” [9, P. 123].

And this is not about theoretical opposition of the terms “financial control” and “audit”. We believe that the agenda has to include the cognitive and normative interpretation of the quality of new Law on Accounting Chamber, which should indicate the basic principles of audit, obligatory for execution in the state (public) sector. Parliament should annually be presented an independent auditor's report on the consolidated financial reporting on the implementation of the consolidated budget for the fiscal year, and Government or the Ministry of Finance should receive auditor's reports on the annual financial and budget reporting of every key spending unit and local government (first of all – on the Oblast level). Efficiency and compliance audits should be carried out according to the accepted standards, which are based on ISSAI. These are standards adopted by the International Organization of Supreme Audit Institutions (INTOSAI), the member of which the Accounting Chamber has been since 1998.

The guarantees of constant quality control of audit should be ensured by the appropriate audit management system quality standard, which is also a requirement of INTOSAI standards. In such conditions the society will be able to obtain the specific socio-economic impact of audit activity in the form of improvement of examined institutions and positive changes after the regular
audit recommendations. Relations between state auditors and the audited objects acquire the character of partnership.

We should separately focus on the issue of accountability of local budgets. Paragraph 5.1 of Annex 2 to the State Program on Prevention and Combating Corruption for 2011-2015, approved by the Resolution No. 1240 of Cabinet of Ministers of Ukraine dated 28.11.2011, [13] provides for improvement of independent external audit in terms of monitoring the use of local budgets by adopting an appropriate law. In addition, one of the main directions of development of public financial management system is empowerment of the Accounting Chamber as an independent state audit institution in terms of monitoring the receipt and use of local budget funds.

 Particularly, the Unit “Objectives and Measures” of section X “Development of independent external audit” of the Resolution No. 774-r of Cabinet of Ministers of Ukraine “On the strategy of public finance management development” dated 01.08.2013 [14] provides for the development and adoption of a new wording of the Law on the Accounting Chamber in order to clarify the status of the Accounting Chamber as the supreme institution of the external audit of public finances, and the expansion of its powers in terms of monitoring the revenue side of the state budget, receipt and use of local budget funds, maintenance and utilization of public property, audit of public enterprises and implementation of account audit, internal control and annual financial reporting systems and budget reporting of key spending units.

According to the author, the large-scale modernization of the Accounting Chamber and its entry into the status of Supreme Audit Institution should be done through the gradual achievement of the long term objectives (year after year, for three to five years) in accordance with the Development Strategy of the Accounting Chamber. With the support of the Accounting Chamber Management during 2012-2013 the author with two colleagues have been trained and certified internationally as agents/mediators on implementation of financial audit standards under the Initiative for Development program (IDI) (a non-profit organization established within the framework of INTOSAI, providing assistance in strengthening independence, improving performance and professionalism to developing countries).

Due to the IDI program, a pool of ISSAI implementation agents and a community of practitioners were created at the international level. Participation in the IDI program allows any supreme audit institution to implement the ISSAI standards on its own practical level. Of course, such a serious matter requires a multilateral discourse and a formal decision of the Accounting Chamber Board.

The Accounting Chamber of Ukraine, on the basis of its own national needs, has the opportunity to use the global developments of IDI (eg. assessment of its own needs through iCATs
It is very important that the Accounting Chamber and stakeholders (especially the Parliament, the Government, the Ministry of Finance of Ukraine) before the formation of such a strategy should jointly review the implementation of ISSAI standards in general.

The fact is that without understanding of the whole system of standards, and the relationships that exist between the standards at different levels, it’s impossible to get a true understanding of their logic and requirements. For example, it is impossible to implement the requirements of the ISSAI 30 audit Code of Ethics, without providing these requirements not only at institutional level but also at the level of each individual audit.

The Accounting Chamber of Ukraine has a potential possibility to try to use its own resources to implement ISSAI of 3 or 4 levels simultaneously with the process of improving of its own legislative framework. Level 4 ISSAI is very important for each particular audit. However, it is impossible to implement Level 2 without a corresponding correlation with the requirements of Level 4.

That is why, it is very important for the Accounting Chamber to choose an integrated approach, rather than segment implementing of standards, for the implementation of ISSAI.

However, the integrated approach does not mean that the Accounting Chamber has to implement all the ISSAI standards at the same time. The implementation strategy, which requires simultaneous work with different ISSAI levels, can be implemented gradually, basing on the requirements of the Accounting Chamber and accessible resources.

: Of course, the implementation of ISSAI should systematically cover the change management process in operation of the Accounting Chamber regarding

- improving its institutional capacity, that is, the powers, regulatory support and the environment in which it operates;
- increasing the organizational capacity of the Accounting Chamber - systems, processes, procedures and resources necessary for practical implementation of ISSAI;
- increasing the professional capacity of the Accounting Chamber staff to implement ISSAI both among management and its employees.

IDI recommends implementation of the ISSAI international standards by the Supreme Audit Institutions in four stages:

Stage 1. Assessment of the need of ISSAI implementation, which includes:
- Understanding of the ISSAI requirements;
- Assessment of Supreme Audit Institution powers, environment in which it operates and expectations of stakeholders and resources;
- Comparison of the ISSAI requirements with the current practice of the audit institution.

Stage 2. Adoption of the ISSAI implementation strategy considering SWOT analysis based on the comparison:

- deciding on the level of ISSAI implementation, to which reference will be made – Level 3 or 4;
- developing the ISSAI implementation strategy at Level 2 and on the chosen level of audit basing on the SWOT analysis;
- developing the Action Plan for fulfillment of the ISSAI implementation Strategy with the timing and terms of activities and resources.

Stage 3. Implementation of ISSAI standards: introducing amendments to the management system and monitoring of ISSAI standards implementation.

Stage 4. Assessment of the implementation of ISSAI standards and the experience gained and performing certain measures on its basis.

The life cycle of the project of implementation of ISSAI international standards by supreme audit institutions involves the following phases:

Phase 1. Project initiation.
Phase 2. Project planning.
Phase 3. Project implementation.
Phase 4. Monitoring of project activities.
Phase 5. Project closing and evaluation of the implementation.

The first thing to do for the effective launch of the project of ISSAI international standards implementation in the Accounting Chamber is to take the following practical measures:

1. Compare the current state of standardization of audit according to ISSAI international standards (iCAT preparation).
2. Make a SWOT-analysis of the strengths and weaknesses of the Accounting Chamber, its opportunities and risks).
3. Identify the priority areas of development of the Accounting Chamber.
4. Prepare a strategy for the implementation of ISSAI international standards for the Accounting Chamber.
5. Develop and adopt an Action Plan with a list of measures, responsible persons and deadlines.

The success of implementation of ISSAI international audit standards will depend on the existing qualified staff, resources, clear understanding of potential of the audit institution and the environment in which it operates.
Human resources of the Accounting Chamber in cooperation with all relevant public authorities are able to do this work in the national interest of Ukraine. Of course, that will require organization of continuing education and training system. It will be useful to involve experts from international organizations to improve the working process, developing audit guidelines, acceptable for the competence of the Accounting Chamber, broad public discussion and training.

A direct reform should take place primarily by improving the process of planning of audit work in the Accounting Chamber. The successful realization of the strategy of ISSAI audit standards implementation involves determination in annual plans of the institution not only the list of “control measures”, but the results that have to be achieved through the provided recommendations, and the amount of activity to be performed, schedule, resources, working time and budget. Necessary budgetary allocations for such work shall be determined on the calculated audit burden. Since the results of work of the Accounting Chamber should be in a causal connection with the improvements achieved by the audited entities that are amenable to purely financial dimension, meet the established criteria and evaluation methodology and be recognized both by the board of the institution and objects of audit, it is advisable to introduce a system of indicators of planned tasks performance. The time for auditing should be not less than 75 per cent of working time, audit costs - not more than 70 per cent of the institution budget, and independently verified financial implications of audit activities implemented by international practice set at 10 UAH for each UAH spent on maintenance of the Accounting Chamber. This approach will ensure efficient use of resources, allocated for the financing of the Accounting Chamber operations.

As already noted, the second important factor in the strategic reform of the Accounting Chamber should be the optimization and development of its human resources. The Accounting Chamber should be provided by experts with adequate skills and qualifications, and its employees should be able to regularly improve qualification and acquire practical experience.

Auditors are motivated by a guarantee of their promotion, healthy and safe working conditions and a system of incentives. An example from the international experience can be a system where wages of the auditor is doubled in 10 years of constant qualified work on the same position (on condition of receiving a positive annual evaluation), which contributes to the consolidation of highly trained personnel. An optimal ratio of managers and employees should be achieved, and staff should be equipped with the middle and highest qualification managers. It is necessary to introduce annual mandatory staff training on the issues of audit methodology (on average, at least 55 hours per year for each manager). The staff qualification should be constantly enhanced through participation in parallel, international, coordinated audits and audits of international organizations.
It is relevant to introduce the electronic audit document management (Team Mate or other) for archiving and preserving audit documentation, supervision, resource planning and accounting of labor costs and working time for the planning and document management, monitoring the implementation of audit recommendations. The use of IDEA or ACL software has to find a decent place for the analysis of financial performance, development and implementation of instructions on how to use them on a regular basis. IT software of high quality will create conditions for improving the efficiency of audit institution.

Finally, the third component of the strategic plan of development of the Accounting Chamber should be strengthening of cooperation with international organizations and audit institutions of other countries, revision of the system of communication with the society and public institutions, improvement of internal relationships within the Accounting Chamber itself. It is necessary to provide regular contacts with objects of audit, review of information policy of the Accounting Chamber as a part of society and its relations with the Parliament and politicians on the basis of tasks and functions of the institution in accordance with the new law «On the Accounting Chamber».

Transparency and mutual support between managers and staff of the Accounting Chamber is very important. The agenda includes the creation of its own publication and satirical humorous TV program (such as “Fitil” or “Pidrakhui” on the First National TV Channel), regular information about the results of work of the Accounting Chamber in the highest-rated television news releases. Cooperation of the Accounting Chamber with the most popular Web-based resources is also necessary: inclusion of electronic links to the Accounting Chamber on news sites, placement of video clips. On condition of increasing participation of the Chairman of the Accounting Chamber and its Board members in the work of parliamentary committees, meetings of the Government and the National Anti-Corruption Committee, the society, the Parliament, the Budget Committee of the Verkhovna Rada of Ukraine and the Parliament Subcommittee on Accounting Chamber will have high degree of confidence in the Accounting Chamber as a professional, independent and not politicized authority which is a significant part of society.

It would be useful to conduct an external evaluation of activity of the Accounting Chamber by a Supreme Audit institution of another country (for example, the UK Audit Office), as it took place in Poland and the Russian Federation.

But a crucial component of the new legal reality for the Accounting Chamber should become a direct development and implementation of national audit standards of public finances harmonized with ISSAI and the best international practice, as it provided by the strategy of development of public finance management system (Order No. 774-r of the Cabinet of Ministers of Ukraine dated 01.08.2013). This is also emphasized in the Resolution No. 04-14/10-1920 of the
Committee of the Verkhovna Rada of Ukraine on budget issues dated 5 September 2013 “On the Report of the Accounting Chamber in 2012”, according to which the Accounting Chamber is recommended to provide the Budget Committee of the Verkhovna Rada of Ukraine with proposals for the new Law of Ukraine “On the Accounting Chamber” subject to the provisions of the Concept of development of public finance management system, approved by the Order No. 633-r [16] of the Cabinet of Ministers of Ukraine dated 03.09.2012 and international standards of financial control. These documents constitute the regulatory framework not only for reforming of the Accounting Chamber, but also for the modernization of the accounting system and financial reporting in the public sector and implementation of international public sector accounting standards (IPSAS). A practical mechanism of further legal formalization of the system of public finance management will necessarily require providing an independent (external) confirmation of reliability of operation of the system by the Accounting Chamber in accordance with ISSAI international standards, particularly the relevant audit opinion. For example, in the UN system the financial statements, which are based on the requirements of IPSAS, are published together with the audit report or audit opinion [17].

Independent (external) confirmation or audit of financial statements of public sector subjects in Ukraine hasn’t been held yet by any supervisory authority. However, the Ministry of Finance, as the main body in the system of central executive authorities on development and implementation of fiscal policy, including through assessment of conformity of reporting of key spending units to the parameters established by the Law on the State Budget of Ukraine, should know the actual picture of state (public) funds and be sure of its reliability. Thus, the relevance of this issue has currently increased and acquired the conceptual implementation in the context of practical implementation of measures of the Strategy of development of public finance management system.

Of course, there are both supporters and opponents of this process. Without getting into debate, I can state that the audit of the financial and budget reporting is a generally accepted international practice which meets the needs of the state and society. The auditors, which together with the author of this article have participated in the OSCE financial audit for the past four years, the professionals who regularly perform similar work for the World Bank, a number of colleagues from the Accounting Chamber, the Ministry of Finance and the leading higher research and educational institutions have worked out a number of conceptual and practical ideas on ways to implement them in the legal framework. Alternatively, the changes and additions to some legislative acts could be predicted, namely: part three of Article 14 of the Law of Ukraine “On Accounting and Financial Reporting in Ukraine” [18] and to supplement part four of Article 58 of the Budget Code of Ukraine with paragraph: “Key spending units are required to submit the annual
financial and budgetary reporting to the central authority, that ensures the formation of the state financial policy, together with the audit opinion of the Accounting Chamber on this reporting.”

I believe that a similar provision can be also added to the order No. 44 [19] of Ministry of Finance of Ukraine dated 24.01.2012 on the issue of financial and budgetary reporting. Such a step would bring the audit methodology into accordance with the ISSAI standards and would significantly help the Government and the Ministry of Finance to obtain unbiased and reliable information on the financial performance of key spending units.

Especially since such an experience was already gained by the audit team of the Accounting Chamber during the OSCE audit in 2009-2013. The work of the Accounting Chamber auditors was highly assessed by the Secretary General and other prominent members of the OSCE Audit Committee, some of whom are authors or co-authors of the ISSAI standards. Particularly, the main objective of the external OSCE audit was to provide an independent assessment of the financial and economic activity through the provision of an audit opinion on the consolidated annual financial reporting of the OSCE. The audit was directed at discovering if the financial reporting of the OSCE is truthful and faithfully reflects the results of financial activity and financial position of the international organization at the end of the year, if the assets and liabilities are fully accounted and properly reflected in financial reporting. The objectives of the audit also included discovering if all the transactions were carried out in accordance with certain rules and procedures of the OSCE and if economy, productivity and effectiveness of activity of divisions in projects and programs of the OSCE have been achieved. The assessment of financial management, accounting and reporting was carried out proceeding from the requirements (criteria) prescribed in financial rules of the OSCE, Consolidated budget of the OSCE, United Nations System Accounting Standards (UNSAS, since 2011– International Public Sector Accounting Standard) and International Financial Reporting Standards (IFRS) [20].

To successfully implement the tasks defined in the Strategy of development of the public finance management system, The Accounting Chamber Board must take their own strategic decision on the final goal - implementation of ISSAI international audit standards in the operation of the Accounting Chamber. Taking into account the practice of the Accounting Chamber, it is advisable to create a Strategic Initiatives group, which would focus on the development of the new law “On the Accounting Chamber” and making proposals to the managers on the development of the concept of a new edition of Auditing Standards. It would be desirable also to organize a public discussion concerning the ways of implementing of ISSAI standards into the operation of the Accounting Chamber with professional organizations (the Association of Chartered Certified Accountants (ACCA), the Ukrainian Association of Certified Accountants and Auditors (УАСБА), Federation of Professional Accountants and Auditors of Ukraine (full-fledged member of IFAC))
and scholars (in particular, scholars from Taras Shevchenko National University, Research Institute of the Ministry of Finance) and practitioners (representatives of the Audit Chamber of Ukraine, Ministry of Finance of Ukraine, State Treasury Service of Ukraine, Ministry of Revenues and Duties etc.).

The new version of the Law of Ukraine "On the Accounting Chamber" should take into account future expansion of the competence of the Accounting Chamber by introducing audit of financial and budgetary reporting of key spending units, audit of local budgets. At the same time other legislative acts of Ukraine require changes and additions on normalization of procedure for submission of financial and budgetary reporting by key spending units together with audit opinions of the Accounting Chamber.

References


