



Efficient control over public spending - myth or reality?

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Auditing as an instrument of financial control

Establishing and improving financial control over the spending of public resources has always been a challenging task. Various countries have tried different methods and systems to impose control in this sector. Complete and close control cannot be exercised without an appropriate regulatory and legal framework. Despite all efforts, there are always going to be tendencies to abuse financial resources, no matter how effective the control. The provision and establishment of appropriate control mechanisms should be the goal of every policy stakeholder.

One of the mechanisms for exercising control over the spending of financial resources is the auditing or verification of financial records. Basically, there are three types of auditing: auditing of financial statements, compliance auditing and operational auditing. The most commonly used type of auditing is the auditing of financial statements. This type of auditing tries to answer the following questions: if financial statements have been prepared in a fair and objective manner, if there have been any frauds within the organization, and if any illegal acts have been committed.¹

Public auditing in Bosnia and Herzegovina and the Republic of Srpska - the current practice

Like elsewhere, it is possible to distinguish between the work of supreme audit institutions and commercial auditing companies in BiH. Supreme audit institutions are generally in charge

of auditing the public sector, although their capacities tend to be somewhat limited. On the other hand, commercial auditing companies are profit-based organizations, whose services are seldom required, primarily due to lack of legal requirement for revision, but also for the reason of costs. Both these types of auditors have general responsibility toward stakeholders of financial statements. Stakeholders represent all parties that might be interested in the financial statements of a particular institution, such as owners, customers, authorities, suppliers, employees, etc. In the case of a public institution, general public is also considered as stakeholders.

The state audit institutions in Bosnia and Herzegovina follow the constitutional architecture of the country. Accordingly, there are principally three supreme audit institutions (SAIs), each having jurisdiction over an area as specified by law.

These are:

- Audit Office for the Institutions of the Federation BiH
- The Supreme Office for the Republic of Srpska Public Sector Auditing
- Audit Office of the Institutions of BiH

These institutions should be considered as the backbone of the integrity system of the country. However, there may be a number of drawbacks to their being the sole controllers of public expenditure. Their budgets are rather limited and they can also fall under the influence of the institution subject to financial inspection.

¹ Principles of auditing: an international perspective, Rick Hayes, Arnold Shilder, p. 43.

Is control really exercised?

Each year the Supreme Office for the Republic of Srpska Public Sector Auditing adopts a plan which specifies which institutions will be subject to financial control. Certain public institutions that have budgets of over several million BAM have only been inspected once in the last several years, while others have not been controlled at all.² Another unpleasant fact is that institutions such as state hospitals, general jurisdiction courts and district courts have only been audited once or twice in the last several years. Even worse, municipal budgets have been controlled at the most twice in the last ten years.

- The budget of the largest municipality in the Republic of Srpska is around 140 million BAM. However, it has only been examined twice in the last 10 years.
- The budget of the majority of district courts has been examined only once in the last several years

pany Web-sites or elsewhere. Typical examples of this are the Banking Agency of Republika Srpska and the Republic of Srpska Securities Commission. The opinion of an independent auditor on the financial records of the latter can be downloaded from its website, although it is impossible to get any information that is more specific, such as budget execution reports or other similar reports.

The Supreme Office for the Republic of Srpska Public Sector Auditing carried out 48 audits for the financial year 2010, covering 35 on-budget entities, 4 funds managed by the Republic of Srpska Investment-Development Bank, 2 off-budget entities, as well as 7 municipalities. In terms of the total money involved, the percentage of audited on-budget entities for that year was 58%, while 42% of them were unaudited, which is not alarming in itself. The pie chart on the next page projects a clear picture, in money terms, of the extent of on-budget institutions that were subject to auditing. The chart also gives an overview of the opinions given to specific institutions.

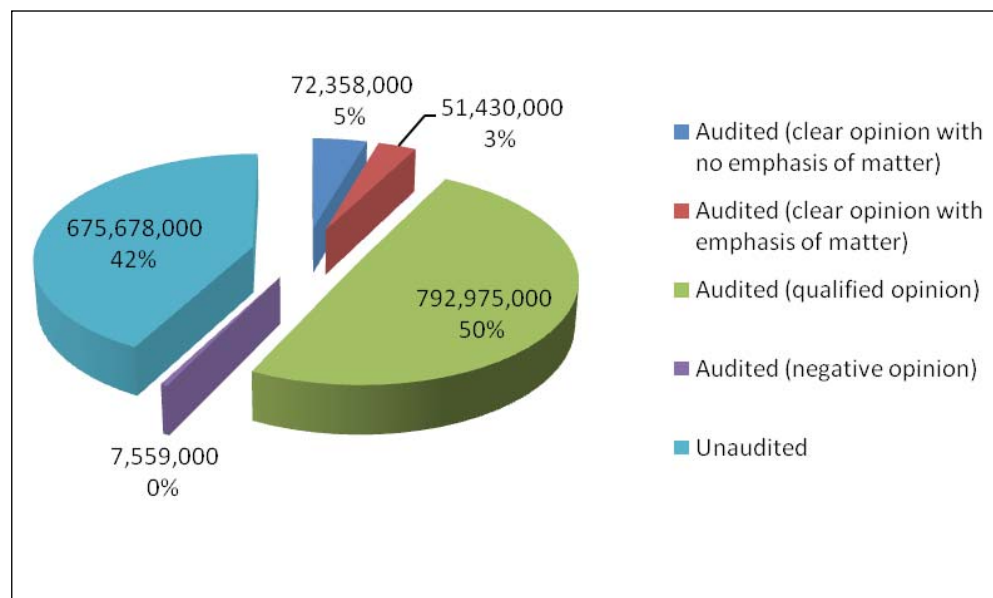
² Audit report of the Republic of Srpska SAI on the consolidated accounts of the Republic of Srpska budget.

Public disclosure - the issue of transparency

Even when an institution has been audited, the general public is rarely acquainted with it, since auditing reports are not found on com-

Where does the problem lie?

A significant proportion of municipalities, public companies and self-financed institutions managing public funds remain unaudited and thus





beyond control. The reason for this is found in the fact that the RS Supreme Audit Institution is limited in its human and financial resources, which makes it difficult for it to control all on-budget and off-budget funds. On-budget entities are easier to control, since all of them receive funding from a single account; on the other hand, public companies are self-financed through the provision of their usually monopolistic services. It is symptomatic that over the past several years, most of the corruption cases reported occurred in institutions that are seldom audited or controlled.

The media in the Republic of Srpska continuously report about cases of money misappropriation. According to a scandal recently uncovered by a newspaper, a doctor has allegedly embezzled around 200,000 BAM. An investigation is most likely going to be launched, but one may just as well ask a very simple question: how many similar cases are not uncovered by the media? How many cases of misappropriation and fraud go unrevealed?

Unfortunately, the institutional capability of the country for tackling the most serious cases of money abuse is very limited. Apart from this, other mechanisms of control over public spending are non-existent or ineffective. Consequently, increased chances to spend public resources in a non-transparent and uncontrolled way leave more room for irregular activities. Furthermore, even when cases of money abuse and misappropriation are revealed, the reaction of the competent authorities is either lukewarm or non-existent.

What can be done?

At this moment, the practice regarding the audit requirement as well as the public disclosure of audit reports is limited and highly unspecified. Different institutions act differently regarding the auditing of their financial statements. Some institutions and public companies are required by law to get their accounts audited by private auditing contractors. However, the majority of them are not required to do so. There are also

positive examples of institutions that have adopted internal books of rules specifying this requirement. These institutions have engaged private auditing companies to carry out the verification of their financial records in the past. However, there are cases of companies which have done so, but whose reports have not been made publicly available. This is certainly something that deserves special attention and that can and should be regulated in line with the most appropriate policy option.

The best way to overcome the problem as stated above is to impose an audit requirement on public interest entities and to make audit reports publicly available. The involvement of the private sector may be a solution. Nonetheless, contracting auditing to the private sector in an effort to impose stricter control over the expenditure of public money would have its pros and cons. The private sector is definitely more productive and efficient, but one has to keep in mind that it operates on a commercial basis. Probably the most effective solution would be a combination of private and public auditing. The adoption of such a scheme is not likely to eradicate corruption and misuse in the realm of public spending, but it will certainly increase the accountability of public institutions.



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A "Policy Development Fellowship Program" has been launched by the Open Society Fund BiH in early 2004 with the aim to improve BiH policy research and dialogue and to contribute to the development of a sound policy-making culture based on informative and empirically grounded policy options. The program provides an opportunity for selected fellows to collaborate with the Open Society Fund in conducting policy research and writing a policy study with the support of mentors and trainers during the whole process. Eighty one fellowships have been granted since the starting of the Program. All policy studies are available at www.soros.org.ba