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INTRODUCTION: CONTEMPORARY ISSUES IN PUBLIC SECTOR ACCOUNTING, AUDITING AND INTERNAL CONTROLS

Brief Summary:

Countries' national statistics institutions compile public finance statistics from national sources, notably from the financial accounting and reporting systems of public institutions. Therefore, the quality of public finance statistics is strongly dependent upon the quality and reliability of public sector accounting and auditing/internal control systems. Therefore, countries want to come to the forefront in terms of both comparability and accountability by minimizing the differences in accounting systems with other states and to provide timely and accurate information to users of the financial statements.

Public sector accounting and internal control vary significantly between countries and different subsectors of government in a country. For example, some governments use cash accounting while others use accrual-based accounting. Also, the scope and content of financial statements varies across countries.

The purpose of this book series is to collect relevant information on the existing public sector accounting and auditing practices for countries and preparing a comparative analysis of the practices of these countries; and to analyze the role of the public sector accounting and auditing/internal controls in the provision of information that would assist financially sustainable policy making, and thus assess the relevance of accounting frameworks in this process.

Overview of the Book

The advancements observed in economic and social life everyday cause change in the role of the state in the economy. The deepening international relations, the removal of the borders in the transfer of goods and services, and the advancement of the international trade lay burdens on the state in any field make it impossible for the state to leave its classical activities. In countries, where the state exists at any point of the economy and implements inward-oriented policies, the knowledge needed for managing the economy and the use of this knowledge is simple. It can be seen that, in history, the public sector accounting performed by many countries has focused on preparing and implementing the budget. In this system, one cannot go beyond keeping the records of revenues and expenses in a

budget year and preparing the relevant reports. Thus, the process of passing from the cash-based accounting, which reports only the results of budget implementations, to the accrual-based public sector accounting having financial contents has accelerated in the whole world.

As a result of these events, the new approaches to the public sector accounting have been developed and these approaches have brought the new accounting systems in the public sector accounting together with them. The studies are carried out in order to develop an accounting system, which is capable of yielding results in compliance with the international standards, especially in recent years, and these studies aim to control the financial transactions, achieving reliable and accurate reports, and making effective decisions. One of the most important studies is those carried out by the Public Sector Committee, which is a sub-committee of International Federation of Accountants (IFAC) and establishes the standards for public sector accounting and reporting. To date, IFAC has published 42 accounting standards and the studies for the new standards are continuing. As it can be understood from the developments in the international area, the most important point here is the scope of public sector accounting.

Despite the broad scope and importance, publications related to public sector accounting and auditing are in a limited framework. Our study aims to make a difference by combining different aspects of public sector accounting and auditing in a single book. In this book, the importance of this subject will take into consideration, and explain and discuss the public sector accounting and auditing/internal control systems, and their weaknesses and strengths. Moreover, the information about the approaches, recording methods, and international regulations on public sector accounting and auditing/internal controls will be provided.

Overview of the Chapters:

This CSEF Volume 105 is dedicated to Contemporary Issues in Public Sector Accounting, Auditing and Internal Controls and consists of 14 chapters. Chapter 1 relates to an evaluations of the effectiveness of public sector accounting systems in Turkey. In chapter 2, the author delve into the harmonization process of the Albanian accounting standards and international accounting. The authors of Chapter 3 carry out a critical review of the role of public auditors in fraud detection. Chapter 4 is dedicated to the financial and performance information presentation in the Turkish municipalities' annual report. The author of Chapter 5 evaluates the effectiveness of financial auditing in the Turkish public health sector. In Chapter 6, the authors compare and analyse the Laws Related to Public Financial Responsibility and State Budget. In Chapter 7, the author discusses the evolving competencies and the future of the public sector auditor. The authors of Chapter 8 delve into the advantages of a tax audit. This is followed by Chapter 9 on the overpayment and undue payment operations in public sector accounting and their accounting process. In Chapter 10, the author delves into the modern approaches, recording methods, and international regulations on public sector

accounting. Chapter 11 is dedicated to a discussion on the past, present, and future of the Turkish government accounting system. The authors of Chapter 12 study Turkey's internal audit in Public Banks using the International Internal Audit Standards framework. In Chapter 13, the authors measure the effectiveness of Internal Audits in the public sector. Chapter 14, final chapter, is an evaluation of the Maturity of Governance, Risk Management and Compliance (GRC) within the Maltese public sector.

Prof Simon Grima and Dr Engin Boztepe
Editors

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CHAPTER 1

SOME EVALUATIONS OF THE EFFECTIVENESS OF PUBLIC SECTOR ACCOUNTING SYSTEM IN TURKEY

A. Kadir Işık and Emine Seda Koç

ABSTRACT

In Turkey for a long term, the public financial management system was carried out according to the provisions of the General Accounting Laws No. 1050 since this law was in force over a long period of time. This law had not been changed for long years and it became far from the needs due to developing dynamic conditions and rapidly changing economic conditions. In addition to these factors, the emergence of economic crises, the need for reform and the country's EU harmonization process increased the need for revision in this field. The Public Financial Management Project was signed with the Ministry of Finance and the World Bank in 1995 and the Public Financial Management system was renewed with the Public Financial Management and Control Law No. 5018 dated January 01, 2006.

Due to the reasons mentioned above, these changes in public financial management led to the use of the concept of public sector accounting instead of state accounting. Public sector accounting is defined as a financial system that provides data for the effective and efficient use of resources. In this accounting, the current accounting system needs to provide the necessary data. While obtaining financial data in an economy, it is necessary to obtain information about the economic situation of that country in a healthy and transparent manner also.

The main objective of this study is to address a number of problems related to the effectiveness of public sector accounting auditing and to propose solutions. For this purpose, the public sector accounting system in Turkey has been handled by giving basic information on this subject; problems arising in this context have been evaluated and suggestions for solutions have been proposed.

Keywords: Public sector economics; accounting; Turkey; Financial Accountability; Financial Policies; State Accounting

JEL Codes: H11; H83

1. INTRODUCTION

The concept and application of public accounting is an essential element in order to monitor the financial events of countries regularly. When the accounting is mentioned within the public sector economy, financial management and discipline, a system which is necessary for financial management and discipline and which should be implemented adequately is understood. In parallel with the development of enterprises and states in the world, accounting science has shown significant developments in itself. As a branch of accounting, it has always maintained its status that is needed in every field of life. Since the early days of human history, various methods of calculation and registration have been carried out. These operations emerge without the discrimination of individuals, businesses, and public institutions.

Government or the concept of government is the largest social organization that has been going on for centuries. Therefore, it is necessary for the government or similar organizations to record and follow up financial events regularly for effective management and efficient use of resources. For these reasons, when the concept of government exists and this organization is implemented, accounting practices will always be maintained and implemented.

The application and development of the concept of state accounting that emerged in the fifteenth century was realized through the kameral accounting system. In this kameral system, public accounting practices are largely budget-oriented and based on the collection and expenditure of revenues and expenditures.

Reliable, accurate, and exact identification and recording of financial data needed for public sector planning; monitoring; analysis; and reporting of these data and making them available to the executives by periods is an important issue. The healthiness of this system helps managers to make right decisions and paves the way for increased public welfare and efficient use of resources (Karaarslan, 2007, p. 1).

Economic developments in the world directly affect the accounting discipline, and the developments and changes in the activities of enterprises are mutually affected by these advancements. The importance of accounting in the public sector has become increasingly important in the government as it is in public sector. Namely accounting that is known as public accounting keeps records of transactions

of financial institutions of public institutions and reports this to existing managers. Previously, the public institutions in Turkey used to manage cash basis accounting system and this system was very incomplete in practice. For this reason, works that are started since 1990s were moved into accruals accounting system by 2004 and many arrangements have been made with the transition to this system.

In this way, a soundly functioning structure that is compatible with accounting systems has been established, and an accounting system that enables the consolidation of accounts in the public was constituted (Özelçi, 2018, p. 1).

Public accounting contributes to the determination of the results of financial transactions, formulation of budgetary practices, and management of economic activities and allows the control of many active variables such as income, expenditure, assets, and capital in an effective and efficient manner (Çetinkaya, 2004, p. 86). In addition, it serves as a system that provides the necessary data by providing financial information and responsibility in the public sector economy and presents the financial information in a transparent manner (The Governmental Accounting System in Argentina, 2019, p. 1).

The application of public accounting system is defined as the recording and analysis of financial information about the government, classification, summarizing and all processes related to these transactions (Dean, 1996, p. 266, Transferred by Çetinkaya, 2004). At this point, the determination of the components of an accounting system is important. Accordingly first is the registration of assets that are the subject of accounting transactions. The second is the decisions taken in this process. Third is the form and method of classification used in this system. Fourth, these processes should be reported and this should be done with the coding system. The fifth is the internal control system that tests the accuracy of the information received. The last one is to clearly state the application and evaluation parameters of the accounting system (Çetinkaya, 2004, p. 86).

It is claimed that classifying assets and transactions and obtaining meaningful results from them and keeping records of transactions related to the financial policies of governments by recording them is the most important function of public accounting (Topkaya, 20016, p. 56).

When public accounting is effectively implemented, not only it shows where and in what ways public resources are spent but also allows managers, who use public funds to account for where and how they use these funds, in line with their permissions. In this way, the way for efficient and effective use of resources is paved, and State Accounting and its practices are proposed as an indispensable element of financial accountability and transparency (Baldacchino et al., 2020; Duman, 2019, p. 2).

2. MAIN FRAMEWORK AND DEVELOPMENT OF PUBLIC ACCOUNTING

Public accounting is a system that reports the results by accurately determining the revenues and expenses occurring in the fiscal year on the basis of the estimation process in order to achieve its objectives like assisting the control of the

activities, their results of the government and other affiliated public institutions within the fiscal calendar year and income–expense management.

In the process of historical development of public accounting, it first emerged as a system that follows only revenues and expenses and this first system has taken its place in the literature as a classical approach. However, with the fact that the government may also have assets and various resources, receivables, debts, and the planning responsibility of these, the above definition of the actual public accounting has emerged and this system has been called as the modern approach (Giray, 1997, p. 136; Gökçen, 2003, pp. 34–35). Today, governments are also considered as advanced organisms with assets/sources and income/expenses just like individuals or businesses. Therefore, it is very important for all countries to establish a system that can monitor all these financial events.

Following up the resources and assets belonging to the general management; summarizing and reporting them in accordance with the needs of the related parties at the end of the period is another purpose of public accounting.

The determination of the costs of the services presented by the government, the establishment of a basis for efficiency analyzes; the constitution of numerical basis and data on the audits and evaluations to be performed on the success criteria of the public administrations serve as a financial instrument for management. This issue is mostly related to the modern public accounting perspective.

Another purpose of public accounting is to enable financial reports to be compared between all units within the administration by creating an accounting and reporting system that can be used by all public administrations, that is, all public institutions within the general administration (Karaarslan, 2007, p. 7).

In order to provide the necessary economic data for the public sector and other stakeholders for ensuring the planning and management of the national economy, monitoring the revenues and expenditures, which are dealt with in the budget during the fiscal year, at the beginning and at the end of the period; pursuing the resources and assets of the government units and also the budget of the management units and reporting the results of operations in accordance with needs in specific periods may be considered as other purposes of public accounting (Sermeçeli, 2010, p.5).

Public accounting also helps to make comparisons and prepare reports in a single format, by allowing for a common standard of practice in central government, local governments, and social security institutions.

These objectives can be summarized as listed below:

- Recording the financial activities of the government,
- Ensuring the transparent determination of the assets and liabilities of the government and its presentation to the relevant segments,
- Enabling the audition of performance and efficiency by comparing the activities of government and affiliated institutions with the budget implementation result,
- Providing the total cost of all the activities of the government and the services presented to public,

- Ensuring the audition of all financial events of public institutions that is carried out in accordance with the legislation in force,
- Providing the necessary data in order to determine the correct use of tax and other public revenues by taxpayers,
- Enabling the managers in public administration to make decisions easily and effectively (Atgür and Altay, 2015, p.34).

About public accounting system, classical and modern views are proposed in the literature. According to the classical view, the function of public accounting is to monitor the income–expenditure status of the state and to ensure that these income–expenses are made in accordance with the budget. From this point of view, this classical public accounting is considered as “Budget Accounting.” The scope of this approach includes only the government’s income and expenses, but the government’s debts, receivables and assets are excluded.

In the modern view, public accounting is seen as a process that can manage the society with the least amount of cost in order to enable competition and maximize productivity (Wayne, 2019, p. 1).

According to the modern view, the government that has legal entity should account for public accounting by including the government’s assets and expenses as well as its assets. In practice, public accounting is not only considered as a means of budgetary control because the government may be a debtor and a creditor depending on the activities carried out, as well as assets. For example, while the purchase of a real estate by the government is expenditure (expense) in terms of budget, the purchase of real estate in terms of the assets of the government is not an expenditure (expense) but an asset or an asset increase that will be depleted in the long term (Giray, 1997, pp. 135–138).

The development in government and need for development is mostly due to the fact that organizations and various economic union structures (such as OECD, IMF, World Bank, international financial institutions and the European Union) needed these reports for making comparisons. When these data are obtained, the process of comparing the countries with each other or the sectors within a country with each other can walk on a healthier ground (Kerimoğlu, 2002, p. 91).

The first reference in this area was published by the Organization for Economic Cooperation in Europe (later OECD) in 1952 under the name “Standardized System of National Accounts.” Subsequently, “National System of Accounts and Basis Statements” was published by the United Nations in 1953 and “National System of Accounts” was published in 1968 (Lequiller & Blades, 2006, pp. 398–402).

If different administrative units of a country use different accounting systems, auditing and analysis of accounts becomes very difficult. For example, central government and local government use different accounting systems. Similarly, these problems arise when various countries within the EU use different systems.

In the Ottoman period, the concept of budget was first adopted by the “Budget Regulation” that is adopted in 1855 and took its place in history as a budget law. Although this was the first time that the budget was accepted as an administrative

document, the implementation could not be fully realized. The final adoption of the budget right was only possible with the 1876 Constitution. In this constitution, the principle of approval of revenues and expenses, the principle of annual budget, the legality of taxes and the final account law have been adopted for the first time. However, implementation of the constitution was postponed due to various events. With the constitution, which was put into force in 1909, the budget right was started to be implemented. After this, a regulation regarding the registration system was issued with “General Accounting Laws.” With this regulation, a step has been taken into the dual registration system. This system continued until the Republican period. The 1924 Constitution adopted the law that the budget would be annually, the legality of taxes, the final account law. Also the rule that the president could not veto the budget on the principle that the state goods could not be spent off-budget was first adopted by this constitution. Based on the 1924 Constitution, the “General Accounting Laws” numbered 1050 was issued on May 26, 1927 and the persons responsible for collecting public revenues, making public expenditures, arranging final accounts and those works were also determined (Yıldırım & Çetinkaya, 1999, p. 63).

Even though there were various ideas in Turkey about creation of a common accounting and reporting standards that will include public institutions and organizations, concrete steps have not been taken to implement this (T. R. Ministry of Finance, 2002, p. 15).

3. REGULATIONS MADE BY LAW NO. 5018

Turkey’s present economic, social, and financial conditions have made it necessary to be addressed in the new financial management and control. On the other hand, as a result of the external factors that emerged in this regard, the problems listed below have arisen.

- Limiting the scope of budget and financial management,
- The increase in public expenditures other than budget,
- Weakening the relationship between the development plan and the budget,
- Inefficient use of public resources,
- Slowness of spending processes,
- Authority-responsibility imbalance in processes,
- The actors of the budget process are not given the necessary initiative,
- Failure to give necessary initiative to actors of budget process,
- The lack of principles such as accountability and fiscal transparency, which are essential elements of contemporary public financial management.

These are some of the problems and negativities that are brought on by the traditional understanding of public administration. In a modern public financial management approach, it is suggested that there should be a participatory and sharing structure, a transparent and accountable system, a structure based on strategic planning and performance (Atgür and Altay, 2015, p.34).

Therefore, there is a broad consensus that the key concepts of the new financial management system in the future will be as follows:

- Responsibility of management approach
- Efficient and effective resource usage
- Strategic Plan
- Performance Budget System
- Multi-term budget
- Accountability
- Financial Transparency
- Accrual-based Accounting
- Internal Audit and Control System
- Efficiency of Internal Audit
- Extension of External Audit

According to Article 5 of Law No. 5018, the basic principles of public finance are as follows:

- Public financial management is formed and carried out in harmony.
- Public officials are accountable.
- Fiscal policy is in line with macroeconomic, fiscal, and other social objectives and followed in this way.
- Public financial management of the Grand National Assembly of Turkey to the budget right policy is carried out properly.
- Public financial management ensures financial discipline.
- Public financial management provides a suitable basis for public choices, ensuring economic, financial, and social effectiveness together.
- Public administrations must use efficient techniques while producing goods and services.

According to the Law No. 5018, public financial management is defined as “legal and administrative systems and processes that will ensure the effective, economic and efficient use of public resources in accordance with defined standards.” The innovations in this area are presented below.

- Budgets types were reprised; in this context, the concept of added budget was abolished and the public administrations were transformed into institutions with general or special budget according to their administrative and financial autonomy and status.
- Law No. 5018 specifies how financial transactions are accounted for and reported. Funds and revolving fund operating budgets are included in the budget of the institution to which they belong and their liquidation is planned in the long term. With these applications, it is provided that the expenditures are subject to the information and control of the parliament.
- All revenues and expenditures of public institutions are included in the budget.

- Importance has been given to the relationship between development plans and budget.
- In the preparation and implementation of the budget, initiatives and flexibility have been provided to public institutions.
- The visa procedure has been abolished in the contracts and contract drafts under the authority of the Ministry of Finance.
- Recommendations have been developed for the establishment of an internal audit system to encourage specialization in auditing.
- The common accounting system is obligated in the public sector.
- The new budget classification in accordance with the GFS standards of the International Monetary Fund was enacted.
- Budgets of local administrations and social security institutions were submitted to the Grand National Assembly of Turkey.
- Public revenues (tax expenditures) that are waived due to tax exemptions, exemptions and reductions and similar practices were added to budget laws
- When these issues are summarized, it is seen that with this law a wide area of initiative is left to public institutions through budget unity, fiscal transparency, accountability, and effective use of public resources (Kesik, 2005, ss.44–46).

4. ISSUES RELATED TO PUBLIC ACCOUNTING IN TURKEY

With a regulation adopted in 1923, a bilateral accounting method was introduced. The basic rules of public accounting and budget were introduced by the General Accounting Law dated May 26, 1927 and numbered 1050. With the regulation enacted in 1928, a system named as grading journal was adopted instead of bilateral accounting adopted. With the Public Accounting General Regulation and Public Accounting Transactions Regulation which came into force on January 01, 1948, the essence of the state accounting system was put forward and the binary (victorious) system was returned.

These regulations, which were changed in time, were merged under the name of Public Accounting Regulation as of January 01, 1990 by taking into consideration the needs of the day. In order to proceed to accrual-based accounting, this regulation was abolished and the Regulation on Departments Included in General Budget and Administrations with Added Budget was put into practice by January 01, 2004.

After inurement of Law No. 5018, this regulation was also abolished and the General Budget Accounting Regulation was started to be implemented by January 01, 2006 and remained in force for one year. The “Central Public Accounting Regulation,” which was prepared following the amendments made to the Law No. 5036, entered into force on January 01, 2007 (Gear et al., 2007, pp. 13–15).

As the cash-based accounting system cannot provide sufficient data and information to the decision-making managers in making decisions and foreseeing the future, the obligation to account for the managers is not fully developed, which leads