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THE ROLE OF INTERNAL CONTROL SYSTEMS AND ACCOUNTABILITY IN THE EFFECTIVE MANAGEMENT OF STATE TARGETED FUNDS

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ABSTRACT----------
This article examines the role of internal control systems and accountability mechanisms in enhancing the effective management of state targeted funds in Uzbekistan. Drawing on international practices, it highlights institutional gaps, governance challenges, and the need for integrated, performance-based oversight. The study offers strategic recommendations to improve transparency, efficiency, and fiscal responsibility in the administration of earmarked public resources.

KEYWORDS: *State Targeted Funds, Internal Control, Accountability, Public Financial Management, Fiscal Governance.*----------

INTRODUCTION

In the architecture of modern public financial management (PFM), state targeted funds represent a strategic instrument for financing priority development objectives in critical sectors such as education, healthcare, infrastructure, innovation, and environmental sustainability. Unlike general budget expenditures, these funds are often earmarked for specific policy goals and are governed by distinct allocation and spending rules. In Uzbekistan, as in many developing and transition economies, such funds have proliferated over the past two decades in response to evolving public service delivery needs and sectoral development priorities. However, the increased financial significance of these funds has not always been accompanied by a corresponding enhancement in oversight, transparency, and operational efficiency.

As the scale and complexity of targeted funds grow, so too do the risks of resource misallocation, duplication of efforts, low absorptive capacity, and weak developmental impact. One of the most persistent institutional challenges in this regard is the lack of integrated and systematic internal control mechanisms, as well as underdeveloped frameworks of accountability both upward (to central government or parliament) and downward (to citizens and beneficiaries). These weaknesses not only compromise the achievement of fund objectives but also erode public trust and fiscal discipline. In this context, internal control systems and accountability structures are not mere administrative tools but rather core components of governance architecture that enable a results-oriented, transparent, and responsive public sector.

The concept of internal control refers to an organization's structure, policies, and procedures that are designed to ensure operational efficiency, compliance with laws and regulations, protection of assets, and the reliability of financial and non-financial reporting. In the public sector, these systems serve as a first line of defense against corruption, fraud, and inefficiency. Meanwhile, accountability encompasses the obligation of public officials to provide information, explain decisions, and be answerable for the use of public resources. A lack of accountability mechanisms whether through performance reports, public hearings, or citizen audits creates a vacuum in which funds may be diverted, poorly implemented, or wasted without consequence.

Global experiences underscore the importance of strengthening both internal control and accountability in the governance of state targeted funds. For instance, the Swedish National Financial Management Authority has established internal control guidelines mandating performance-based assessments for all extra-budgetary funds. Similarly, in South Korea, the Board of Audit and Inspection (BAI) maintains an independent oversight mandate for all special-purpose funds, including the authority to impose administrative sanctions. In OECD countries,

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targeted funds are often subject to integrated control systems that connect expenditure tracking, performance auditing, and citizen feedback. These models illustrate how systemic internal control and institutionalized accountability can significantly improve the fiscal and developmental outcomes of public funds.

LITERATURE REVIEW

The governance of state targeted funds occupies a critical niche in public financial management (PFM) literature, particularly in the intersection between expenditure efficiency, internal control systems, and accountability mechanisms.

The foundational framework for internal control is most comprehensively articulated in the COSO Internal Control–Integrated Framework (1992; updated 2013), which defines internal control as a process designed to provide reasonable assurance regarding the achievement of operational, reporting, and compliance objectives [1]. The COSO model outlines five interrelated components: control environment, risk assessment, control activities, information and communication, and monitoring. These elements have since been adopted and adapted globally in both private and public sectors, with various countries customizing them to the specific needs of government financial operations. In the public sector, the INTOSAI Guidelines for Internal Control Standards for the Public Sector (ISSAI 9100–9400) complement the COSO model by emphasizing principles such as transparency, legality, and stewardship of public funds [2].

Empirical literature also underscores the operational value of internal control systems in preventing resource leakages and enhancing fiscal discipline. A study by Ferreira and Otley [3] demonstrated that weak internal control systems correlate with high levels of financial misreporting and project failure, particularly in environments where extra-budgetary funds lack integrated audit trails. Similarly, Diamond [4], in his comparative analysis of African and Southeast Asian countries, found that poorly coordinated internal control mechanisms contribute to the duplication of expenditures and delays in public service delivery.

In the case of state targeted funds, which operate outside conventional budget channels and are often governed by sectoral agencies or special committees, the risk of governance asymmetries is significantly higher. Andrews [5] refers to this as the "institutional gap," where funds are legally recognized but procedurally isolated from broader accountability frameworks. According to OECD (2018), special-purpose funds must be treated with the same rigor and transparency as general budgetary allocations, including ex-ante controls, ex-post audits, and performance evaluations [6].

The literature on accountability further enriches the discussion by framing the role of public officials not only as agents of technical compliance but as stewards of public trust. Bovens (2007) defines accountability as "a social relationship in which an actor feels an obligation to explain and justify conduct to a forum" [7]. This perspective is particularly relevant in the management of state targeted funds, where the end-users citizens often have limited visibility into how funds are allocated, spent, and evaluated.

Ostanaqulov A [8] argues that accountability has evolved from procedural compliance to performance-based governance, with emphasis on outputs, outcomes, and societal impact. In this context, the use of citizen report cards, participatory audits, and public expenditure tracking surveys (PETS) has gained traction as a means to close the feedback loop between government agencies and constituents.

Moreover, contemporary scholarship links accountability directly to digital governance and open data initiatives. Cangiano et al. [10] stress that integrating internal controls with digital PFM systems (e.g., e-procurement, e-budgeting, and e-reporting) not only improves timeliness and accuracy but also enables real-time tracking and citizen engagement. The World Bank's PEFA assessments further reinforce that countries with robust internal control and accountability frameworks demonstrate higher scores in expenditure efficiency, fiscal transparency, and trust in institutions [11].

ANALYSIS AND RESULTS

The analysis of internal control and accountability mechanisms in the governance of state targeted funds requires a multidimensional diagnostic approach. Unlike general budget expenditures, targeted funds often operate through

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specialized channels, administered by sectoral agencies or extrabudgetary entities with varying degrees of integration into national public financial management (PFM) systems. This structural complexity creates unique governance challenges, such as fragmentation of oversight, duplication of functions, and blurred lines of accountability.

Table 1. Forecast of the Consolidated Budget for 2025 and Projections for 2026–2027, *(Trillion UZS)*

№	Indicators	2025 Forecast	2026 Projection	2027 Projection
I	**Consolidated Budget Revenues**	431.1	496.8	565.4
1	State budget revenues*	308.9	354.1	406.4
2	Revenues of state targeted funds*	66.2	81.8	94.1
3	Receipts to the Uzbekistan Reconstruction and Development Fund	22.2	24.5	26.2
4	Receipts to off-budget funds of budgetary organizations	33.8	36.5	38.6
II	**Consolidated Budget Expenditures**	480.3	547.4	619.1
1	State budget expenditures*	290.4	339.3	390.8
2	Expenditures of state targeted funds	116.9	129.4	143.2
3	Use of funds from the Uzbekistan Reconstruction and Development Fund	20.3	21.5	22.9
4	Use of off-budget funds of budgetary organizations	33.8	36.5	38.6
5	Expenditures on state programs financed by external debt	18.8	20.8	23.7
III	Transfers to state targeted funds	54.4	52.1	53.5
IV	Transfers to the state budget	10.5	10.4	10.4
V	Consolidated budget balance (surplus +, deficit -)	-49.2	-55.2	-63.7
VI	Balance of state budget and targeted funds (surplus +, deficit -)	-32.7	-33.2	-33.8
VII	Public debt repayment	46.8	50.0	58.3

Source: imv.uz

The forecasted figures for Uzbekistan's consolidated budget from 2025 to 2027 underscore the increasing significance of state targeted funds in the country's fiscal landscape. Revenues of targeted funds are projected to grow from 66.2 trillion UZS in 2025 to 94.1 trillion UZS by 2027, accounting for nearly 17% of consolidated budget revenues by the end of the period. This growth trajectory is paralleled by a rise in their expenditures from 116.9 trillion UZS in 2025 to 143.2 trillion UZS in 2027 highlighting their expanding role in delivering public services and development programs.

However, the data also reveal several structural and governance-related concerns that necessitate the strengthening of internal control systems and accountability frameworks:

First, the growing fiscal footprint of targeted funds increases the risk of resource mismanagement, particularly in the absence of integrated audit mechanisms. Given that expenditures from these funds are not always subject to the same ex-ante and ex-post scrutiny as the core state budget, the likelihood of inefficiencies, duplication, or opaque allocation rises. This calls for the institutionalization of standardized internal control procedures such as risk-based audits, real-time expenditure tracking, and harmonized reporting systems across all state targeted funds.

Second, the budget table reveals consistent negative balances (deficits) for both the consolidated budget and the combined balance of the state budget and targeted funds. For example, the consolidated budget deficit is expected to widen from -49.2 trillion UZS in 2025 to -63.7 trillion UZS in 2027, while the joint deficit of the state budget and targeted funds remains persistently above -30 trillion UZS annually. These structural deficits emphasize the need for performance-based budgeting and accountability mechanisms that not only track spending but also assess cost-effectiveness and outcome achievement particularly within targeted funds that finance strategic sectors like infrastructure, innovation, and human capital.

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Third, the simultaneous increase in transfers to and from targeted funds and the state budget over 50 trillion UZS in annual transfers illustrates complex interdependencies that are vulnerable to fragmentation and misalignment in the absence of a unified control framework. To ensure effective financial governance, Uzbekistan should adopt an integrated control environment based on the COSO framework, with clear roles for internal audit units, centralized oversight bodies (e.g., the Supreme Audit Institution), and line ministries.

Table 2. Comparative internal control frameworks for state targeted funds

Country	Institutional Arrangement	Control Instruments Used	Level of Integration with National PFM
Finland	Internal audit units within each ministry; coordinated by National Audit Office	Risk-based audit planning, financial compliance tools, IT audit modules	Fully integrated with performance budgeting and Treasury data
South Korea	Centralized oversight by Board of Audit and Inspection (BAI)	Real-time monitoring tools, audit dashboards, citizen reporting systems	Centralized control linked to e-Government platforms
Uzbekistan	Fragmented internal audit units under separate fund administrators	Manual reporting systems, limited control procedures	Weak integration with budget, audit, and procurement systems

Source: Developed by the author

This comparative table illustrates the divergence between well-established internal control systems and Uzbekistan's fragmented, under-coordinated structure. In Finland and South Korea, internal control is embedded within the national fiscal infrastructure, allowing for real-time expenditure monitoring, performance risk assessments, and synchronized reporting. In contrast, Uzbekistan's internal audit systems for targeted funds often function independently from central PFM tools, leading to inefficiencies, duplicated reporting, and weakened accountability. Reform priorities must therefore include institutional unification of audit functions, application of digital control instruments, and enhanced connectivity between fund administrators and the Treasury.

Table 3. Accountability and transparency practices in the oversight of targeted funds

Country	Public Reporting Requirements	Parliamentary Oversight Mechanism	Citizen Engagement Tools
Canada	Mandatory fund-level reports linked to outcomes	Audit reports reviewed by Parliamentary Budget Officer	Online portals, public dashboards, participatory consultations
Chile	Annual audit statements with legal compliance review	Special congressional commission on public spending	Audit progress trackers and citizen complaints mechanisms
Uzbekistan	Limited narrative reporting; focus on financial inputs	Budget committee reviews limited to overall fund envelopes	Minimal; occasional publication of aggregate reports

Source: Developed by the author

The accountability mechanisms in Canada and Chile reflect a deliberate effort to link financial transparency with institutional and citizen oversight. Parliamentary involvement extends beyond passive review to active scrutiny, with structured hearings and follow-up mechanisms. In Uzbekistan, however, reporting on targeted funds is often limited to aggregated financial input data, with little emphasis on outcome-based accountability or citizen participation. There is a critical need to introduce fund-specific performance reports, institutionalize ex-post hearings in the legislature, and develop user-friendly digital interfaces for public oversight.

RECOMMENDATIONS

To ensure the effective and accountable management of state targeted funds in Uzbekistan, a comprehensive reform strategy must focus on institutional integration, standardization of internal control mechanisms, and the deep embedding of accountability practices into public financial governance. First and foremost, internal control

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systems must be unified across all targeted funds under a national framework coordinated by the Ministry of Economy and Finance or the Supreme Audit Institution. This requires the adoption of a single set of internal control standards—aligned with international frameworks such as COSO and ISSAIapplicable to all public entities managing earmarked resources. Such harmonization will eliminate duplication, ensure consistency in audit planning, and allow the state to shift from reactive, compliance-based monitoring to proactive, risk-informed control.

Simultaneously, Uzbekistan should adopt a model of performance-based accountability that links financial resource use with measurable outputs and policy outcomes. This demands a shift away from input-focused reporting towards integrated financial and non-financial disclosures, in which each targeted fund publishes annual performance reports validated by internal audit units and parliamentary oversight bodies. These reports should clearly articulate how fund expenditures contribute to sectoral strategies and national development goals, allowing both the legislature and the public to hold administrators accountable for efficiency, effectiveness, and equity. Mechanisms for downward accountability such as public dashboards, participatory audit processes, and grievance redress systems must be institutionalized to enable citizen engagement and reinforce transparency.

Moreover, the deployment of digital infrastructure is imperative to support integrated control and accountability. A unified e-platform for state targeted funds connected to Treasury systems, e-procurement databases, and audit management tools should enable real-time monitoring, automated anomaly detection, and cross-fund comparison of performance indicators. Drawing from models implemented in countries like South Korea and Chile, Uzbekistan can leverage digital tools to improve compliance, reduce manual reporting burdens, and create an auditable trail that enhances fiscal credibility.

Finally, to close the accountability loop, it is essential to strengthen the legal enforceability of audit findings and internal control recommendations. This includes establishing formal timelines for corrective action, empowering parliamentary audit committees with investigative powers, and linking audit outcomes to managerial performance assessments. Without a structured enforcement regime, even the most advanced control systems risk becoming ceremonial rather than corrective.

CONCLUSION

In conclusion, the governance of state targeted funds in Uzbekistan stands at a critical juncture. As their strategic importance and fiscal magnitude grow, so too does the need for institutional rigor. The future of effective fund management lies in the construction of a fully integrated control and accountability architecture—one that not only protects public resources from mismanagement but also ensures that every so‘m spent delivers measurable public value. Transitioning to this model is not merely a technical upgrade; it is a foundational reform that will determine the credibility, efficiency, and legitimacy of Uzbekistan’s fiscal statecraft in the decades to come.

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