ECONOSCITECH INTEGRATION

ISSUE 9

INTERNATIONAL SCIENTIFIC
ELECTRONIC JOURNAL

TASHKENT STATE
UNIVERSITY OF ECONOMICS

American University
of Technology
Powered by Arizona State University®

ISSN: 3060-5075

Acceptance of articles
PUBLISHED MONTHLY

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CONTACT: +998 94 3540880 https://econoscitech-integration-journal.uz 2026

THE SCIENTIFIC-POPULAR ELECTRONIC JOURNAL **"ECONOSCITECH-INTEGRATION"** HAS BEEN REGISTERED UNDER THE NUMBER C-5669651 BY THE AGENCY FOR INFORMATION AND MASS COMMUNICATIONS (AOKA) OF THE REPUBLIC OF UZBEKISTAN, EFFECTIVE FROM OCTOBER 9, 2024.

In accordance with Resolution No. 384/6 dated April 10, 2026, issued by the Presidium of the Supreme Attestation Commission under the Ministry of Higher Education, Science and Innovation of the Republic of Uzbekistan, this journal is included in the list of recommended international scientific publications for publishing the primary research findings of doctoral dissertations in the field of Economic Sciences.

Partners: Tashkent State University of Economics / American University of Technology in Tashkent (AUT)

Electronic publication. Issue 9. 500 pages.
Approved for publication in September 2026.

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THEORETICAL AND METHODOLOGICAL FOUNDATIONS OF THE INTERNAL AUDIT OF RECEIVABLES AND PAYABLES IN BUDGET ORGANIZATIONS

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Abstract. The article develops a theoretical and methodological framework for the internal audit of receivables and payables in budget (public sector) organizations. The author argues that in the public sector these categories cannot be interpreted through the logic of commercial capital circulation: a receivable represents a temporary immobilisation of budget resources, while a payable is, in the typical case, the accounting trace of an obligation assumed in excess of an approved appropriation limit. Consequently, the audit objective shifts from the fair presentation of balances towards the legality, economy and controllability of the obligation cycle. Drawing on the COSO Internal Control - Integrated Framework, the IIA professional framework, INTOSAI public sector guidance and the accrual-based IPSAS model, a three-level methodological construct is proposed: the conceptual level (object, subject, purpose, principles), the organisational-institutional level (mandate, independence, three lines model) and the procedural-instrumental level (risk assessment, materiality, assertion-mapped procedures, key risk indicators). The study concludes that the transition from a compliance-verification model to a risk-based assurance model constitutes the central methodological problem of internal audit in the budget sphere.

Keywords: internal audit, budget organization, receivables, payables, risk-based auditing, public internal financial control, COSO, IPSAS, materiality, audit assertions.

INTRODUCTION

Public financial management reform in transition economies has consistently moved along three axes: consolidation of cash resources within a Treasury Single Account, migration of public sector accounting from a cash basis towards an accrual basis, and replacement of ex-post inspection by ex-ante and continuous internal control. Within this trajectory, receivables and payables of budget organizations occupy an analytically peculiar position. They are simultaneously an accounting category, an indicator of budget discipline, and a symptom of systemic weakness in commitment control.

The practical significance of the problem is straightforward. A payable in a budget organization is, in most cases, not a legitimate instrument of working capital management but the accounting trace of an obligation assumed beyond the approved expenditure limit, or of an obligation for which the appropriation was authorised while cash was not released. A receivable, symmetrically, is not commercial credit extended to a customer but a withdrawal of public money from the financing cycle: an unsettled advance, an unaccounted imprest, a shortage awaiting recovery, or an unpaid fee for services financed from extrabudgetary sources. Both categories therefore carry a normative charge absent in the corporate sector: their existence beyond a narrow technical minimum is prima facie evidence of control failure.

Schick (1998) formulated this dependency in his well-known thesis that developing and transition states must first get the basics of expenditure control right, since aggregate fiscal discipline is logically prior to allocative and operational efficiency. Government payment arrears are, in this logic, the most visible measurable manifestation of a breakdown in the basics. Flynn and Pessoa (2014), in the IMF technical guidance on the prevention and management of expenditure arrears, demonstrate that arrears arise systematically where commitment control is weak, budgets are unrealistic and cash is rationed administratively rather than planned. This positions the internal audit of receivables and payables not as a narrow accounting exercise but as an instrument of fiscal discipline.

Despite this, internal audit practice in budget organizations remains dominated by a documentary compliance paradigm: the auditor verifies whether a transaction was supported by a primary document and correctly posted, rather than whether the process that generated the obligation was designed to prevent its illegitimate emergence. The purpose of this article is to construct a theoretical and methodological foundation capable of supporting the shift from documentary verification towards process-level, risk-based assurance.

LITERATURE REVIEW

The theoretical treatment of audit as a discipline was placed on a systematic footing by Mautz and Sharaf (1961), who demonstrated that auditing rests on a set of postulates - among them the verifiability of financial data and the absence of a necessary conflict of interest between the auditor and the entity - rather than on a body of technical rules. The value of this framing for the present study is that it directs attention to the conditions under which an audit opinion is meaningful at all, a question that becomes acute where the auditor is administratively subordinate to the audited manager.

Power (1997) advanced a critical perspective in his analysis of the audit society, arguing that the proliferation of verification activity does not automatically produce assurance and may generate ritualistic practices whose principal output is documented comfort rather than substantive control. Power (2004) extended this scepticism to risk management itself. For the budget sector this critique is directly applicable: the routine annual inventory of settlements, formally documented but methodologically hollow, is a textbook instance of the ritual of verification.

Hood (1991), in his account of New Public Management, identified explicit standards, output measurement and disaggregated control as the defining doctrinal components of public sector reform. Internal audit in budget organizations is a direct institutional descendant of this doctrine, which explains both its potential and the resistance it encounters within traditional administrative hierarchies.

In the public financial management literature proper, Allen, Hemming and Potter (2013) provide a systematic treatment of the commitment control cycle, distinguishing the stages of appropriation, commitment, verification, payment order and payment. Their decomposition is the analytical basis on which any meaningful audit of payables must be built, because each stage constitutes a distinct control point with a distinct failure mode. Schick (1998) and Flynn and Pessoa (2014), already cited, supply the diagnostic framework linking arrears to specific weaknesses at these stages.

The accounting dimension has been debated most intensively in connection with the transition to accrual accounting. Jones and Pendlebury, in successive editions of their work on public sector accounting, analyse the specific character of government accounting, where the budget rather than the balance sheet remains the primary accountability instrument. Wynne (2008) advanced a sceptical position, questioning whether accrual accounting should be a priority for developing countries given the capacity required and the uncertain benefits. The IPSASB pronouncements - notably the standards governing presentation, provisions and contingent liabilities, non-exchange revenue and financial instruments - supply the recognition and measurement criteria against which the auditor forms a judgement. The debate is not settled, and the present article treats the transitional state itself as an audit risk factor rather than as a resolved question.

The modern conception of internal audit as an assurance and consulting activity centred on risk is documented in the empirical literature by Sarens and De Beelde (2006), whose study of internal auditors' perceptions of their role in risk management identified a tension between assurance provision and involvement in risk management processes - a tension that recurs acutely in small budget organizations where the auditor is drawn into operational tasks. Lenz and Sarens (2012), reflecting critically on the profession, examined why internal audit has repeatedly fallen short of expectations, pointing to the ambiguity of its mandate and the weakness of its organisational positioning. Griffiths, in his practitioner framework for risk-based internal auditing, developed the operational logic of allocating audit effort by assessed residual risk rather than by balance magnitude.

Within the Russian-language tradition, Burtsev (2000) systematised the organisation of internal control as a management subsystem; Sheremet and Suyts, and Podolskiy, established the methodological canon of audit procedures in successive textbook editions; Bychkova developed the treatment of audit risk and its components. Sokolov's work on the theory of accounting supplies the conceptual analysis of a receivable as a legal claim recognised as an accounting object. These works remain the principal methodological reference point for practitioners in the post-Soviet space, although they were developed primarily for the commercial sector.

Finally, the fraud dimension rests on Cressey's classical formulation of the conditions under which trusted persons violate that trust - pressure, opportunity and rationalisation - subsequently elaborated in the forensic accounting literature. Nigrini's work on the application of Benford's Law to forensic analytics, and Vasarhelyi's foundational research on continuous auditing of online systems, provide the technical basis for the automated detection routines proposed in Part IV of this series.

The gap identified in the literature is the weak articulation between these strands. Control theory offers depth without operational detail; the professional standards offer detail calibrated for large corporate or central-government entities; the accounting normative base offers criteria but no assurance methodology; the PFM literature analyses arrears at the aggregate fiscal level without descending to the entity-level audit programme. Receivables and payables in ordinary budget organizations - schools, clinics, district administrations, cultural institutions - fall into this interstice. The present article addresses that gap.

RESEARCH METHODOLOGY

The research employs a qualitative, design-oriented methodology combining four instruments. Normative-comparative analysis is used to compare national budget accounting and audit regulation with the IPSAS, IIA, COSO and INTOSAI reference frameworks, identifying areas of convergence and divergence. Structural-logical modelling decomposes the receivable and payable life cycle into elementary stages and maps control points and risk nodes onto each stage. Assertion-mapping constructs a matrix linking management assertions - existence, completeness, rights and obligations, valuation and allocation, cut-off and presentation - to specific audit procedures applicable to budget-sector balances. Indicator design formulates key risk indicators capable of supporting continuous rather than periodic monitoring.

The methodological premise of the study is that a theory of internal audit for the budget sphere must be constructive: it is validated not by explanatory adequacy alone but by its capacity to generate an implementable audit programme.

ANALYSIS AND DISCUSSION OF RESULTS

The conventional formulation states that the object of audit is the receivable and payable balance. This formulation is analytically insufficient, because it locates the object at the terminal point of a process while the causes of misstatement and irregularity are distributed across the entire process. A two-tier definition is therefore proposed. The immediate object is the aggregate of accounting balances and turnovers reflecting claims against, and obligations towards, third parties, together with the supporting documentation, contractual base and reconciliation records. The mediated or essential object is the obligation management cycle: contracting, commitment registration, recognition, monitoring and reconciliation, settlement or recovery, and write-off.

The subject of the internal audit is the relationship between the design and operating effectiveness of controls embedded in this cycle and the resulting state of the balances. This reformulation has an immediate practical consequence: an audit that finds correct postings but no functioning commitment control has not produced assurance - it has produced a false negative.

The theoretical claim advanced here is that the three levels are hierarchically nested rather than alternative. Performance-level conclusions are unreliable unless compliance and financial assurance have been obtained, but an audit terminating at the compliance level cannot generate improvement recommendations and therefore forfeits the greater part of its value. This is precisely the failure mode Lenz and Sarens (2012) identify when they observe that internal audit frequently delivers what is easy to document rather than what is valuable to management.

METHODOLOGICAL PRINCIPLES

1. Substantive priority of the obligation over the entry: the auditor tests the legitimacy of the underlying obligation before testing the accuracy of its recording.

2. Limit-anchored assessment: every payable is evaluated against the approved appropriation and cash limit, and the deviation, not the balance, is the primary analytical quantity.

3. Immobilisation logic for receivables: every receivable is evaluated as a diverted public resource, with the ageing profile as the principal measure of severity.

4. Risk proportionality: audit effort is allocated in proportion to assessed inherent and control risk, not to balance magnitude alone.

5. Process continuity: assurance is conceived as continuous monitoring punctuated by engagements, not as a sequence of isolated engagements.

6. Functional independence with administrative embeddedness: the internal auditor reports functionally to the governing body or supervising ministry and administratively to the head of the organization, a duality that must be codified in the internal audit charter (table 1).

The assertion-procedure matrix

Assertion	Principal risk in the budget sphere	Core audit procedure
Existence	Fictitious receivables created to conceal shortages or absorb year-end appropriations	Third-party confirmation; inspection of contracts and delivery evidence; inventory of settlements
Completeness	Unrecorded payables from obligations assumed outside the commitment register	Search for unrecorded liabilities; cut-off testing; reconciliation with Treasury commitment data
Rights and obligations	Claims lacking legal basis; third-party obligations recorded as the entity's own	Legal review of the contractual base; review of assignment and novation documents
Valuation	Receivables overstated through non-recognition of impairment; payables understated through omitted penalties	Ageing analysis; recalculation of contractual penalties; recoverability assessment
Cut-off	Obligations shifted between periods in order to remain within limits	Testing of transactions in the period surrounding the year-end
Presentation	Netting of receivables against payables; misclassification between budget and extrabudgetary sources	Review of disclosure; verification of source-based segregation

The proposed model consists of five interconnected blocks. Block one, the normative-criterial base, comprises budget legislation, accounting instructions, IPSAS-equivalent recognition criteria and contract law provisions on limitation periods. Block two, the institutional architecture, comprises the charter, reporting lines, audit committee or equivalent body, competence requirements and the quality assurance and improvement programme. Block three, the risk architecture, comprises the audit universe, risk taxonomy, risk register, heat map, risk appetite and tolerance thresholds. Block four, the procedural instrumentation, comprises strategic and annual plans, engagement programmes, sampling and materiality determination, working papers and the evidence hierarchy. Block five, feedback and improvement, comprises recommendations, management responses, follow-up, KRI dashboards and periodic recalibration of the risk model.

The blocks are cyclical rather than sequential: the output of block five recalibrates block three, which in turn redirects block four. This closure of the loop distinguishes an assurance system from a sequence of inspections.

CONCLUSIONS AND RECOMMENDATIONS

The internal audit of receivables and payables in budget organizations requires a theoretical foundation distinct from that of commercial audit, because the economic content of the underlying categories is itself distinct. Receivables in the budget sphere are immobilised public resources; payables are, in the typical case, evidence of commitment control failure. This asymmetry with the corporate sector dictates a corresponding asymmetry in audit methodology: the analytical centre of gravity shifts from the valuation of balances to the legality and controllability of the obligation cycle.

The article has proposed a two-tier definition of the audit object, a three-level purpose hierarchy, six methodological principles, an assertion-procedure matrix adapted to budget-sector risks, and a five-block integrated conceptual model. Recommendations follow. First, national methodological guidance for budget organizations should require the separate identification of payables arising within, and in excess of, approved limits. Second, ageing analysis of receivables should become a mandatory element of analytical accounting rather than an audit-time reconstruction. Third, the internal audit charter should codify the dual reporting line as a condition of the function's legitimacy. Fourth, the transitional state of the accounting basis should itself be treated as a documented risk factor during the migration towards accrual reporting.

Further research should address the empirical calibration of key risk indicators against sectoral data, and the design of continuous auditing routines operating directly on treasury and budget accounting information systems.

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Proofreader: Xondamir Ismoilov

Layout and Designer: Hasan Maqsudov

2026. № 9

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