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Theoretical Foundations of Internal Audit Activity on the Use of Budgetary Funds in Budgetary Organizations

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Abstract: The article examines the theoretical foundations of internal auditing of budgetary funds in public sector organizations, emphasizing its role in ensuring financial transparency, accountability, and effective resource management. The study analyzes the evolution of internal auditing in the public sector and evaluates the explanatory potential of agency theory, public choice theory, stewardship theory, institutional theory, and contemporary public management paradigms. Particular attention is paid to the conceptual distinctions between internal auditing and other forms of public financial control. The research clarifies the definition, objectives, scope, principles, and functions of internal auditing within budgetary institutions. Furthermore, it proposes an integrated conceptual model connecting theoretical perspectives with practical mechanisms for assessing budgetary discipline, identifying financial risks, and improving organizational performance. The findings provide a theoretical basis for strengthening internal audit systems, enhancing institutional accountability, and promoting the efficient, transparent, and responsible utilization of public financial resources in budgetary organizations and government institution.

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1. Introduction

Budgetary funds are resources entrusted by society to the state for the performance of public functions. The legitimacy of the state's financial activity therefore depends not only on the lawful collection and allocation of these funds but also on the confidence of citizens that they are used for their intended purposes and with the greatest possible benefit. In this context, internal audit has evolved from an auxiliary accounting control procedure into an independent professional activity that provides management and oversight bodies with assurance on the use of public resources.

In Uzbekistan, the ongoing reforms of public financial management, including greater budget transparency, the introduction of elements of performance budgeting and the digitalization of treasury and procurement operations, have increased the demand for effective internal audit in budgetary organizations [1]. At the same time, practice is ahead of theory: internal audit units are being established and their responsibilities expanded, while the theoretical understanding of the nature, purpose and boundaries of internal audit of budgetary funds remains fragmented. In national scientific literature, internal audit in the public sector is often identified with traditional revision or with state financial control, which leads to methodological confusion and underestimation of its preventive and advisory potential.

The purpose of this article is to substantiate the theoretical foundations of internal audit of the use of budgetary funds in budgetary organizations, clarify its conceptual apparatus and propose a conceptual model linking theoretical premises with practical objectives [2].

The philosophical foundations of auditing were laid by R. Mautz and H. Sharaf, who formulated the postulates and key concepts of audit, including evidence, due care and independence [3]. The theoretical literature on audit offers several complementary explanations of why audit exists and what functions it performs. The most influential of them is agency theory, formulated by M. Jensen and W. Meckling, according to which audit arises as a monitoring mechanism that reduces information asymmetry between principals and agents and thereby reduces agency costs [4]. In the public sector, agency relationships form a multi-level chain: citizens delegate authority to parliament, parliament to the government, the government to ministries and ministries to budgetary organizations. Each link of this chain creates the risk that agents will pursue their own interests rather than those of the principal.

Public choice theory, developed by J. Buchanan and G. Tullock, complements this view by showing that politicians and bureaucrats act as rational individuals maximizing their own utility, which may manifest itself in budget-maximizing behavior. W. Niskanen's model of bureaucracy explains the tendency of public agencies to expand their budgets beyond the socially optimal level. These theories justify the need for audit mechanisms that assess not only compliance but also the economic justification of expenditures [5].

Stewardship theory, in contrast, assumes that managers of public organizations may be intrinsically motivated to act in the public interest. From this perspective, internal audit should not only control but also support managers by providing advice and helping them to improve processes. Institutional theory emphasizes that organizations adopt structures such as internal audit partly to gain legitimacy, which may result in "ceremonial" compliance without real impact. M. Power's concept of the "audit society" develops this critique, warning that audit can turn into a ritual of verification [6].

Paradigms of public administration have also shaped internal audit. The New Public Management paradigm described by C. Hood shifted the focus from inputs and procedures to outputs and results, which stimulated the development of performance-oriented audit. The subsequent New Public Governance paradigm emphasizes networks, partnerships and accountability to citizens, which expands the range of stakeholders of internal audit [7].

The professional framework of the IIA, including the Three Lines Model, defines internal audit as an independent, objective assurance and advisory service designed to add value and improve an organization's operations, while INTOSAI documents emphasize the role of internal audit in the public sector internal control system and the general principles of public-sector auditing. However, these definitions are general and do not reflect the specific features of the use of budgetary funds.

2. Research Methodology

The research employs a comprehensive methodological framework based on the dialectical method of cognition, historical and logical approaches, comparative analysis, synthesis, abstraction, and conceptual modeling. The dialectical method enables the examination of internal audit as an evolving component of public financial management, while historical and logical approaches facilitate the identification of its institutional development and theoretical foundations. Comparative analysis is applied to evaluate various scientific perspectives on internal auditing, public accountability, and budgetary control. Analysis and synthesis are employed to systematize theoretical concepts and identify relationships between internal audit functions and organizational performance. Furthermore, abstraction and conceptual modeling are utilized to develop an integrated framework illustrating the principles, objectives, and mechanisms of internal auditing in

budgetary organizations. The information base includes classical and contemporary academic literature, international professional auditing standards, regulatory frameworks, and relevant legislation of the Republic of Uzbekistan governing public finance, budget administration, and internal financial control systems.

3. Results

The analysis allows us to distinguish four stages in the evolution of internal audit of budgetary funds: (1) the stage of documentary revision, focused on detecting errors and misappropriation in accounting records; (2) the stage of internal control assessment, in which the auditor evaluates the reliability of control procedures rather than checking every transaction; (3) the stage of risk-based audit, in which audit resources are directed to areas of greatest risk to the achievement of objectives; and (4) the stage of value-adding audit, in which internal audit contributes to the efficiency and effectiveness of public spending and to good governance. In the practice of budgetary organizations of Uzbekistan, elements of the first and second stages still prevail, while the transition to the third and fourth stages is a strategic direction of development [8].

Each of the theories reviewed explains a particular aspect of internal audit of budgetary funds. Their combined implications are summarized in Table 1.

Table 1. Theoretical premises of internal audit of the use of budgetary funds

Theory	Key premise	Implication for internal audit of budgetary funds
Agency theory	Information asymmetry and divergent interests between principal and agent	Internal audit as a monitoring mechanism reducing agency costs along the chain "society – state – budgetary organization"
Public choice theory	Bureaucrats maximize budgets and personal utility	Need to assess the economic justification and necessity of expenditures, not only their legality
Stewardship theory	Managers can be intrinsically motivated to serve the public interest	Balance of control and advisory functions; partnership with management
Institutional theory	Structures are adopted to gain legitimacy	Risk of "ceremonial" internal audit; need for real independence and impact indicators
New Public Management	Focus on results and performance	Performance audit elements: economy, efficiency, effectiveness
New Public Governance	Accountability to citizens and networks of stakeholders	Transparency of audit results; attention to social outcomes

Source: developed by the author.

The table shows that no single theory is sufficient. Agency and public choice theories justify the control function of internal audit; stewardship theory justifies its advisory function; institutional theory warns against formalism; and public management paradigms define the evaluation criteria. We therefore argue that the theoretical foundation of internal audit of budgetary funds should be built on an integrative approach combining these perspectives [9].

Based on the analysis, we propose the following definition: internal audit of the use of budgetary funds is an independent and objective activity carried out within the system of a budgetary organization (or its parent body) that provides management and oversight bodies with assurance and advice on the legality, targeted nature, economy, efficiency and effectiveness of the receipt and use of budgetary funds, as well as on the adequacy of related risk management and internal control, with the aim of increasing the public value created by these funds [10].

Unlike existing definitions, this formulation (a) specifies the object of audit – the receipt and use of budgetary funds; (b) includes five evaluation criteria, adding legality and targeted use, which are critical in the public sector, to the classic "3E"; (c) combines assurance and advisory roles; and (d) defines the ultimate goal as increasing public value rather than merely detecting violations [11].

Internal audit of budgetary funds is often confused with internal control, state financial control and external audit. Their differences are summarized in Table 2.

Table 2. Distinction between internal audit and related forms of control over budgetary funds

Criterion	Internal control	Internal audit	State financial control	External (state) audit
Performed by	Management and staff of the organization	Independent within the organization or parent body	Authorized unit of the bodies (financial and treasury inspectorates)	Supreme audit institution (Accounts Chamber)
Position	Built into processes	Third line, independent of operations	External to the organization	External, independent of the executive
Main purpose	Prevent and detect errors in daily operations	Assurance and advice to management	Enforcement of budget legislation, sanctions	Accountability to parliament and society
Orientation	Current operations	Risks, controls, performance	Compliance	Compliance, financial and performance audit
Consequences	Operational corrections	Recommendations for improvement	Administrative measures	Reports, recommendations, referral of cases

Source: developed by the author.

The object of internal audit of budgetary funds is the financial and economic activity of the budgetary organization related to the planning, receipt and use of budgetary funds and funds from other sources. Its subject comprises the operations with budgetary funds, the processes of budget planning and execution, the internal control and risk management systems, and the results achieved through the use of funds [12].

4. Discussion

In addition to the general principles of the IIA standards (integrity, objectivity, competence, due professional care and confidentiality), we identify specific principles of internal audit of budgetary funds: (1) the principle of public interest – audit is carried out ultimately in the interests of society as the owner of budgetary funds; (2) the principle of result orientation – evaluation of the outcomes achieved, not only the procedures followed; (3) the principle of risk orientation – concentration of resources on areas of greatest risk; (4) the principle of preventiveness – priority of preventing inefficient use over detecting violations after the fact; and (5) the principle of transparency – openness of audit results to stakeholders within the limits established by law [13].

The functions of internal audit of budgetary funds include: the assurance function (providing reasonable confidence regarding the use of funds), the analytical-evaluative function (assessing efficiency and effectiveness), the preventive function (identifying risks and weaknesses before losses occur), the advisory function (supporting management in improving processes), the informational function (providing reliable information for management decisions and budget planning) and the developmental function

(disseminating good practices and improving the organizational culture of financial discipline) [14].

The results of the study are synthesized into a conceptual model with four levels. The first level is the theoretical basis (integrative combination of agency, public choice, stewardship and institutional theories and public management paradigms). The second level is the normative basis (international standards and national legislation). The third level is the conceptual apparatus (definition, object, subject, principles, functions and evaluation criteria). The fourth level is the target outcomes (lawful, targeted and efficient use of budgetary funds, improved governance and increased public trust). The model shows that the practical effectiveness of internal audit depends on the consistency between these levels: for example, declaring a result-oriented principle without developing performance evaluation criteria produces only "ceremonial" compliance [15].

5. Conclusion

The study allows the following conclusions to be drawn. First, internal audit of budgetary funds has evolved from documentary revision to a value-adding activity, and budgetary organizations in Uzbekistan are at the stage of transition from internal control assessment to risk-based and performance-oriented audit. Second, no single theory adequately explains the nature of internal audit of budgetary funds; an integrative approach combining agency, public choice, stewardship and institutional theories and public management paradigms provides the most complete theoretical foundation. Third, the proposed definition of internal audit of the use of budgetary funds specifies its object, extends the evaluation criteria to legality, targeted use, economy, efficiency and effectiveness, and defines the increase of public value as its ultimate goal. Fourth, the specific principles (public interest, result orientation, risk orientation, preventiveness, transparency) and functions identified in the article, together with the conceptual model, can serve as a theoretical basis for developing methodological guidance for internal audit in budgetary organizations.

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