FEATURES ENSURING FINANCIAL CONTROL IN A COMMERCIAL BANK: RUSSIAN AND FOREIGN EXPERIENCE

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Current global trends in financial management and in banking in particular are demonstrating a gradual shift in focus from remote external financial control over bank's operations to more internal risk-oriented financial control. Against this background, there is a fundamental change in organization of financial control in commercial banks, associated with the implementation of international norms and standards as well as Russian Federation legislation compliance with these norms and standards.

In the context of rapid development and changes of nearly all technologies, the impacts from real and potential threats to internal and external environments, internal financial banking

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control is becoming increasingly important in ensuring growth of banks' financial performance.

Thus, given the importance of the very institution of financial control in the banking sector for financial and economic stability of any state, the presence of problematic issues in this area necessitates further studies of the characteristics of financial control in a commercial bank stemming from the already accumulated Russian and foreign experience.

Keywords: financial control; commercial bank; financial and economic stability; financial management

Theoretical approaches to definition of the concept and classification of financial control

Control acts as one of the most important and integral functions in management as it is carried out at all of its levels and represents the detection system of compliance of the actual functioning of a management object with the parameters set via management decisions for the purposes of feedback collection on administrative influence efficiency.

One type of control is financial control. The problem of determining the essential contents of this category at the present stage of Russian economy's development is very relevant and significant. A unified approach to understanding financial control did not work out, thus, this notion, still, is also not fixed by law. As a result, there are too many viewpoints in Russian science concerning the interpretation of this concept.

For quite a long time, financial control was considered solely as an activity aimed at carrying out verification of accounts and monitoring the completeness of the receipt of funds that form government revenues. Many researchers, however, support quite different points of view. In particular, (Arzumanova, 2018) interprets financial control as "regulated by law activities of bodies and organizations, the purpose of which is to ensure financial, budget, credit, accounting and cash discipline in the implementation of plans and expressed in verifying the legality, validity and rationality of monetary costs".

Broader definition is offered by A.Yu. Ilyin and M.A. Moiseenko who understand financial control as "special form of activity by authorized public authorities and economic entities based on imperious instructions of law precepts, directed to check the timeliness and accuracy of financial planning, validity and completeness of income receipt to the relevant funds, correctness and efficiency of their use, implementation of compulsory withdrawals in the budgetary system, imposing responsibility for violation of financial legislation" (Ilyin, 2014).

From the legal point of view, financial control is the control behind execution of the federal budget and off-budget funds, organization of money circulation, credit resources' usage, monitoring of both internal and external debts, the state reserves, granting financial and tax concessions and advantages (Presidential Decree, 1996).

Such a variety of interpretations of the concept "financial control" causes the existence of various bases for classification of financial control which is visually presented in the figure above (Abdulkhanova, 2011).

For our research specifically, differentiating between external and internal financial control is of vital importance.

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Figure 1 - Types of financial control

As target orientation of financial control, external in relation to organization, first of all, assessment is needed by an authorized body responsible for norms and rules of financial and economic activity (Regulations on organization of internal control, 2004). For example, concerning the activity of commercial banks such control is exercised by the Central bank of the Russian Federation, Federal Tax Service of the Russian Federation and also external independent auditors.

Internal financial control represents the set of control actions, the main objective of which is checking financial and economic activity of the organization, as a rule, by own efforts. Such control gives the chance to reveal, on a permanent basis, the level of current risks and also to predict and prevent financial and operational risks and also possible abuses of power by public officials.

Internal financial control in organizations is carried out in the following forms – preliminary, current and subsequent. Preliminary and current control are conducted directly by employees of firms in the course of performing their immediate functions, while subsequent control can be carried out by both department of internal control and commission on internal control.

According to foreign literature sources, internal financial control aims at strengthening the reliability of accounting (Bokova, 2016). Internal control is the policy and the procedure established for ensuring reliability of accounting systems. Accuracy and reliability have paramount value in the world of accounting. Without exact accounts heads cannot make completely justified financial decisions, and financial statements will eventually contain mistakes (Ingram, 2018).

Internal financial control, provided its systemic application is guaranteed, allows increasing the efficiency of resource usage, their safety and also improves overall results of the firm. In this case, the role of internal financial control consists mostly in prevention of violations of the financial legislation by organizations and enterprises as well as

minimization of risks and increasing the responsibility of enterprises' top management for business results.

Introducing the system of internal financial control in a commercial bank

In today's conditions implementation of financial control in banks is a must since this activity provides observance of the existing financial legislation, internal rules and procedures and also allows reducing reputational risks and the risk of unforeseen financial losses.

In this context, financial position of a credit institution, validity of the adopted management decisions, effectiveness of financial transactions and so forth in many respects depend on the creation of an effective system of internal financial control.

Importance of having an internal financial control system in commercial banks is predetermined, first of all, by:

- the need of ensuring sustainable development of bank;
- existence of a large amount of risks of bank's activities;
- active participation of the state in the banking business overall;
- social importance of commercial banks as institutions ensuring normal activity of country's population etc.

For a commercial bank itself, it is necessary to understand the set of interconnected and interdependent elements aimed at providing efficiency of financial and economic activity of bank. The system of financial control consists of the following elements:

- the subject and the object of financial control;
- directions in implementation of internal financial control;
- procedures of internal financial control which are to be carried out by the subjects of control.

This rather wide range of elements in the organizational system of a commercial bank acts as subjects of financial control which is imposed in the following directions:

- financial and economic activity of a bank, including all of its structural divisions and also all of its branches;
- separate economic processes, separate banking products, operations and transactions;
- financial and information flows;
- activity of all staff affiliated to this bank.

One of the main instruments of financial control in a commercial bank is internal audit which ensures the achievement of the goals of implementing control measures by applying a consistent and systematic approach to assessing the effectiveness of internal control and risk management systems.

According to Bogdanova N.A., internal audit is the control system for observance of an established order of accounting in an organization, operating in the interests of its management (owners) and regulated by internal documents.

A.V. Kucherov considers internal audit to be independent control activity providing real evaluation of work of an economic subject and formation, on this basis, of the opinion about the results of its activity in general and activities of separate structural divisions in particular.

P.P. Andreyev defined internal audit in the banking sector as an activity which helps top managers with the achievement of the objectives set for a bank, using the consecutive and systematized approaches to assessment of the internal control system and for increasing its efficiency. Internal audit is supposed to help the heads/owners of business with managing it, but it cannot and should not substitute management as such, moreover, it should not substitute internal control.

Thus, analysis of the features of the internal financial control system in a commercial bank demonstrates the presence of the system-structural elements and process approaches available in any credit institution. At the same time, specifics of formation and functioning of this system depends on the development level of financial and economic institutes in this or that country. In this regard we

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will consider practices of financial control implementation in commercial banks of the selected foreign countries.

Foreign experience of financial control in commercial bank: principles of the organization and implementation

Formation and operation of internal financial control systems in banking organizations of most foreign countries are carried out in accordance with the model developed by the Committee of Sponsoring Organizations of the Treadway Commission, hereinafter referred to as COSO, and also basing on the principles developed by the Basel Banking Supervision Committee (Switzerland).

COSO was established in the USA back in 1985 as a voluntary private organization the goal of which is to develop recommendations for top managers on various aspects of financial management: internal control, risk management, antifraud campaigns etc.

Control environment is an element of organizational culture that influences control consciousness of banks' employees, ensures compliance with discipline and prevention of opportunistic behavior among them. The factors determining the state of control environment in a commercial bank include corporate values, managerial style, the system of duties' distribution and authority delegation, personnel development processes inside organization and so on.

Internal documents and procedures of a commercial bank that assist management in implementation of their decisions are defined, according to COSO regulations, as the means of control.

Information system, in this context, is supposed to ensure formation and logistics of information flows related to implementation of financial control in a bank, from top to bottom, also organizing effective communication channels with the external environment.

The system of monitoring over the implementation of internal financial control provides feedback on the effectiveness of control implementation.

Acting as one of the most conceptual adherents of the ideas and concepts of COSO, the Basel Committee on Banking Supervision in 1998 formulated the basic principles for organizing internal financial control in a modern banking organization, publishing them in the document titled "The System of Internal Control in Banks: The Basics of Organization".

Let's consider some aspects of the internal financial control organization on the example of a number of European commercial banks (HSBC Bank, Deutsche Bank, BNP Paribas, UniCredit, UBS and so forth), Asia (Industrial and Commercial Bank of China, Mitsubishi UFJ Financial Group and so forth) and those in the USA (Zions Bancorporation, JPMorgan Chase and so forth).

Organizational clearance of internal financial control in most of the studied commercial banks is built in a similar way. Thus, it covers: the board of directors, the supervisory board of the bank, the executive committee, as well as various services and committees (for example, the UBS audit and risk committee, the mediation committee, the anti-corruption committee in Deutsche Bank, the Financial System Vulnerability Committee at HSBC Bank) and individual employees.

For example, in Nordea, Sweden, the internal financial control system of a bank consists of: the management bodies of the Bank, including permanent collegial bodies (committees) under the board of directors and the management board, an audit committee that oversees financial and business activities; chief accountant of the bank; internal control

service; internal audit service etc. (Financial statements Nordea, 2014). At JPMorgan Chase, risk management is carried out through the board of directors by delegating the related functions to various subcommittees (Financial statements JPMorgan Chase).

Table 1 - International Principles of Internal Financial Control Organization in Banks

(Source: The System of Internal Control, 1998)

payment order No.	Direction of financial control	Main contents of the principle
1.	Management and control culture	responsibility of bank management for creation and functioning of efficient internal control system
		responsibility of bank management for implementation of bank's internal financial control policy
		shared responsibility for observing the culture of control
2.	Recognition and assessment of risk	identification and assessment of risks on a regular basis
3.	Control activities and separation of powers	control activities should be an integral part of bank's daily operations
		efficiency of segregation of duties and elimination of the conflicts of interest
4.	Information and its transmission system	availability of comprehensive information
		reliable information systems
		effective information systems
5.	Activity monitoring and correction of deficiencies	The overall effectiveness of bank's internal controls should be monitored on a regular basis.
		effective and comprehensive internal audit
		timely reporting of management deficiencies
6.	Evaluation of internal control systems by supervisors	banking supervisors should require all banks to have effective internal control systems

The reporting documents of the analyzed banks reflect the following:

- compliance with legal and regulatory requirements (for example, Nordea, Danske Bank);
- countering money laundering and terrorist financing (for example, Agricultural Bank of China, Citigroup);
- verification and testing of the accuracy, completeness and timeliness of accounting and reporting, as well as reliability (for example, Zions Bancorporation, Nordea);
- financial risk management and valuation (for example, JPMorgan Chase, Nordea, Natixis, Zions Bancorporation);

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- avoidance of tax evasion (for example, Credit Suisse, Mizuho Financial Group) etc.

Figure 2 - The total number of fines and penalties for non-compliance with the requirements for compliance with sanctions regimes, combating money laundering, terrorist financing and tax evasion, 2007-2016

(Source: Financial Crime Compliance, 2017)

At the same time, despite the fact that the COSO model and the Basel principles are embedded in the activities of a significant number of banking institutions, not all banks have internal financial control systems functioning effectively. This is evidenced by the fact that the system of internal financial control is subject to external study and analysis by the authorities and other institutions whose authority is to impose sanctions on commercial banks.

For example, in September 2018, the Federal Financial Supervision Authority of Germany issued an order to Deutsche Bank to strengthen its internal financial control in order to prevent a repetition of money laundering cases and the financing of terrorism through this bank. Over the past decade, the mentioned German bank has spent the total of € 17 billion in fines and settling the related lawsuits (German regulator appointed KPMG...).

Thus, it should be noted that, despite the standardization of approaches and principles to implementation of internal financial control in commercial banks of foreign countries, the effectiveness of a financial control system depends primarily on the goals of its implementation, competent management of control processes and also on how effective are the risk assessment mechanisms. In this regard, it is also interesting to study the experience of organizing financial control in commercial banks of various, different from each other, countries.

Formation, evolution and the current state of financial control in commercial banks in Russia

Foundations of the financial control system in the Russian Federation began to take shape in the 1990s, when the first private commercial banks began to function in the country

and thus the need arose to protect these institutions against erroneous or deliberately criminal actions of bank personnel.

In 1997, the Bank of Russia adopted the Order dated August 28, 1997 No. 02-372 “On the enactment of the Regulation “On organization of internal control of banks”, which for the first time acknowledged the need to create a system of internal financial control adequate to the scale of bank activities, defining its goals and tasks, features of organization, rights and obligations of the internal control service, powers of the Bank of Russia over the state of internal control in banks etc.

At the same time, provisions of this and further Regulations did not find their effective practical implementation, mostly due to the financial crisis that started in 1998. As a result, “internal control services were absent in more than 10% of credit institutions. In 65% of credit organizations that created the internal control services at the head offices, internal control was not organized for the activities of branches, and only 6% of credit organizations had internal control services at branches” (Order of the Bank of Russia, 1997).

Since early 2004, the Regulation on the Organization of Internal Control in Credit Institutions and Banking Groups No. 242-P began to operate, which made it possible to adapt foreign models and principles of financial control in domestic commercial banks. In addition, subjects of internal financial control were specified in detail.

In 2014, amendments to Regulation No. 242-P came into force, which was a turning point in formation of the internal control concept in commercial banks of Russia. If earlier the functions of the internal control service were to identify regulatory risks, conduct an assessment of financial activities, identify conflicts of interest, then, in accordance with these changes, their functionality expands to compliance control. At the same time, the powers of internal control service were transferred to the internal audit service, which now checks bank as a whole and its structural subdivisions as to how the established internal procedures are carried out.

Thus, the models of internal control in the banking sector in Russia have undergone a certain evolution and are currently based on the principles of internal financial control organization generally recognized in world practice within the regulatory and legal framework governing the credit and financial sphere overall.

Let us now consider more closely the practice of building a system of internal financial control on the examples of Sberbank of Russia, VTB Bank and CB Center-Invest.

In Sberbank of Russia, construction of a system for internal financial control and risk management is based on the classic model of the three lines of defense.

The subject structure of internal financial control in the Sberbank of Russia is represented in addition to the governing bodies of internal control services and the internal audit service.

So, in 2017, the internal audit service of the Sberbank of Russia conducted 9.9 thousand inspections, of which 5 thousand were planned and 4.9 thousand were unscheduled. According to the results of these inspections, the management gave 1.3 thousand instructions on solving systemic problems. During the year, 22.3 thousand actions were taken to eliminate various violations (82% executed, 18% at the implementation stage), and 8 thousand disciplinary measures were taken against the Sberbank employees.

Internal audit services of the Sberbank of Russia conducted 184 inspections of its subsidiary banks and 63 inspections of other subsidiaries. According to the results of these

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inspections of the companies of the Group, more than 2.1 thousand recommendations were given (Annual report of PJSC “Sberbank of Russia”, 2017).

In VTB Bank under the Management Committee of the VTB Group, the coordination committee for internal audit and the coordination committee for compliance and internal control operate to counter money laundering and terrorist financing.

To assist management in ensuring effective operation of the VTB Group, the Bank has its Internal Audit Department, which monitors the internal control system, audits, and provides independent recommendations for improving banking and control procedures. In 2017, the Internal Audit Department conducted 40 audits, including 10 audits of business processes of the head office of the Bank and 30 audits of the activities of its territorial divisions. In addition, within the framework of the current monitoring, the Department's staff carried out 713 thematic checks in the territorial divisions (Annual report of VTB Bank, 2017).

To assist the Bank's management bodies in effective management of regulatory (compliance) risks, the Bank has a Compliance Control and Financial Monitoring Department.

In the commercial bank "Center-Invest" the system of internal financial control is represented by the internal audit service (Internal control in PJSC CB "Center-Invest", 2017).

So, Center-Invest has the following functionalities included into its internal audit:

- assistance to the Board of directors and the Board of bank in ensuring steady effective functioning of business;
- implementation of constant control over the employees' observance of the established procedures, functions and powers and also over the accuracy of the execution of the decisions made;
- participation in updating of regulations over the interaction of divisions and staff of the bank in development of assessment procedures, management and supervision of the risks arising in the course of its operations and so forth.

Conclusion

The carried out and presented here analysis of the features and implementation of financial control in the commercial banks of the Russian Federation and abroad shows quite significant similarities in organizational and procedural aspects of its embodiment.

At the same time, specific aspects of financial control implementation can be very different due to different level of development of the institutional, financial and economic environment in this or that country.

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