

THE ASSESSMENT OF THE INTERNAL AUDIT APPROACH IN THE CONTEXT OF CORPORATE GOVERNANCE

Ph.D. Student Alexandra Diana BAICU

”Valahia” University of Târgoviște, Romania

E-mail: baicudianaalexandra@yahoo.ro

***Abstract:** Internal audits emerged and developed against the background of the need to prevent economic fraud and closely linked to the basic requirement of the existence of good corporate governance, namely to establish appropriate techniques and tools for managing critical situations that may affect the interests of all concerned. For a functioning within the parameters expected by all interested parties, any public interest entity shall take steps towards creating a strong link between risk management, the degree of development of the internal management control system and corporate governance. This becomes achievable only with the well-positioned support of the internal audit.*

***Key words:** internal audit, corporate governance, risk management, public interest entity, audit committee.*

***JEL Classification:** M42.*

1. Introduction: Public enterprise and corporate governance

More and more governments around the world are improving their governance practices at the level of public enterprises, in order to increase their competitiveness, but also of the entire economy, to reduce the fiscal burden but also the financial risk to which they are exposed. to provide them with better access to financing, as well as to increase the degree of transparency and accountability of their own management. The guide of good practices in the corporate governance of the Ministry of Transport explains how the personnel employed, as well as the members of the Board of Directors and the executive management of the public companies that are subordinated, respectively under its supervision, as the supervisory authority, are to apply the specific current legislation. The guide is based on relevant legislative acts, supplemented by the good practices used in Romania and internationally.

The first Code of Corporate Governance in Romania, respectively that of the Bucharest Stock Exchange, was dedicated, in particular, to companies listed on the Stock Exchange. Its implementation was done only voluntarily. The only mandatory element of the Code was that companies must publish a Declaration of Conformity with the Corporate Governance Code, which mentions the extent to which they intend to comply with the recommendations contained in that Code. Although public undertakings under the authority of the Ministry of Transport are generally not listed on the Stock Exchange, they were expected to comply with the corporate governance standards of listed companies. In turn, the Public Enterprise Governance Guide (OECD Guide) has long been the only international guide dedicated to corporate governance of state-owned enterprises. The OECD Guide is a unique and valuable resource for state institutions that have the quality of guardianship authority, offering detailed explanatory recommendations and notes. Although it was established as a standard of good practice for enterprises in advanced countries, this Guide together with the provisions of the O.U.G. no.109 / 2011, updated, regarding the corporate governance of public enterprises, were the reference elements for the Ministry of Transport of our country.

The governing bodies that fulfill the specific tasks of the management of public enterprises in Romania are: the General Meeting of Shareholders; Board of Directors, Directorate of the company. According to the Guide, from the point of view of its shareholder role, the Ministry of Transport is represented by the Supervisory Unit.

2. Literature review

Authors like Iain, Stuart (Gray, Manson, 2008) mentioned that internal audit is a management function that seeks to establish recommendations for improving the real situation of the entity. Other specialists consider that the internal audit experienced a more marked development after the 1980s, when the internal audit function began to develop and the role of internal audit is to bring value to the entity (Renard, 2002).

Addressing the relationship with the management of the entity, Saam (2007) considers that the internal audit "supports the management of the entity in fulfilling its obligations and strengthens the confidence of the owners of the entity in the integrity of the management", and J. Renard, 2006, argues that "the internal audit is all that should be done" to be responsible for ensuring that he has good control over business if he has time or if he knows how to proceed.

In Romania, internal audit first appeared in public sector entities and was recommended to private sector entities (Ghita, 2004), as opposed to the global situation, where internal audit first appeared in multinational entities and then it was transferred to the national ones and adopted by the administration (Renard, 2002).

In our country, the specialists support explanations regarding the practices and procedures of internal audit necessary to reach the purpose of the entity (Dobroțeanu, Dobroțeanu, 2002).

Authors such as Morariu and Stoian ("Internal audit and corporate governance", Morariu, Suci, Stoian, 2008) and Sabău and Nagy ("The necessity and role of the performance audit in ensuring enterprise's competitiveness", Sabău, Nagy, 2009) they analyzed the importance of internal audit missions and their role in increasing economic performance.

3. Research methodology

The methodology applied in the present study is characterized by the combination of the deductive-inductive research methods (the data interpretation method: comparative and interpretive), respectively, mainly inductive (data collection, information processing and interpretation methods).

Referring to the systematization of research methods developed by Septimiu Chelcea, 2001, transversal (observation) and longitudinal (case study), experimental and observation methods (documentation), case methods (organization analysis) were used in the research carried out. internal audit approach to a public company).

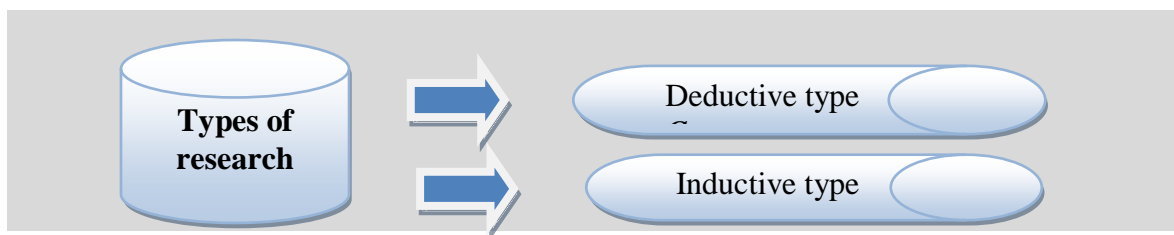
The elaboration of this research started from the theory, applying a deductive type research, to reach individual conclusions regarding the improvement of the internal audit, but also an inductive type research, starting from particular judgments to the formulation of general conclusions, by verifying the transposition. in practice the information obtained. In order to be able to achieve the objectives proposed in this scientific endeavor, the methodology used was based on:

Theoretical research, inspired by the following sources: corporate governance codes, international and national regulations regarding the internal audit activity, specialized books, information published on the Internet.

Empirical research, by applying research methods that verify the research hypotheses and establish their own conclusions of a general nature.

The conclusions of the theoretical and empirical research that have contributed to the argument of improving the internal audit approach and increasing its efficiency in the public interest entities.

Figure no. 1. Research methodology



Source: Own projection

The main methods used in the research that were the basis of this study were documentation, observation, deductive and inductive reasoning, analysis, synthesis.

The categories of documentation sources were obtained on the basis of bibliographic documentation and webographic documentation.

Of the two types of observation (external observation and participatory observation), participatory observation was used mainly, which led to generalizations and interpretations synthesized in conclusions and comments. The participatory observation involved the qualitative approach and the case study, which allowed a detailed description and a thorough analysis of the aspects analyzed.

3. Analysis of the internal audit approach in the context of corporate governance

The sample of economic entities analyzed is represented by the companies and autonomous authorities under the authority of the Ministry of Transport, in number of 25 entities with majority state capital.

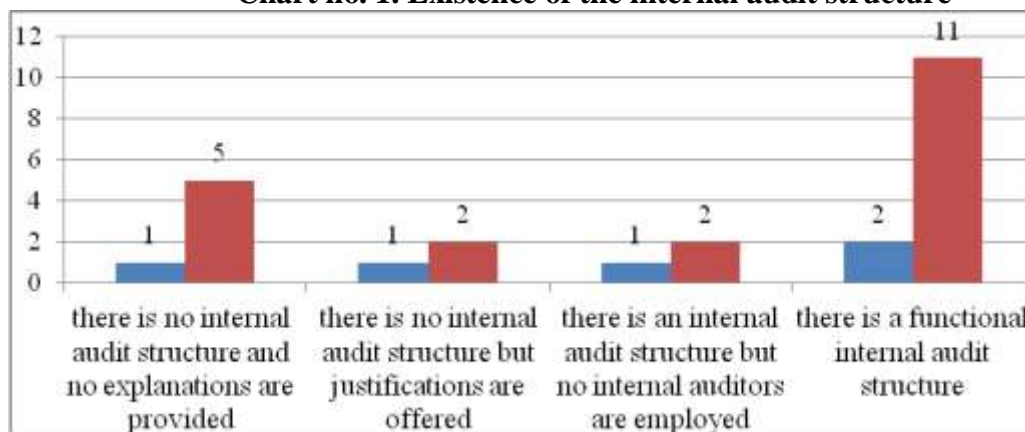
In the first stage, the level of assurance of the internal audit function was investigated within the 25 public interest entities, more precisely, the existence of the structure, the assurance of independence, responsibilities, the organization, the publication of the annual report on the internal audit activity.

3.1. Existence of the internal audit structures

From the total number of 25 entities, divided into 5 autonomous regions and 20 companies, the situation is presented, according to the graph above, as follows:

- 20% of the autonomous authorities did not set up an internal audit structure and did not explain why, 20% did not set up an internal audit structure but they motivated its non-existence, 20% set up an internal audit structure but this does not work in the absence of the internal auditors employed and 40% of the autonomous companies have functional internal audit structures;
- 25% of the analyzed companies did not set up an internal audit structure and did not provide relevant information on this situation, 10% did not set up an internal audit structure but explained the reason, 10% have an internal audit structure but no internal auditors employees and 55% have functional internal audit structures.

Chart no. 1. Existence of the internal audit structure



Source: Own projection

Comment: The Management of the analyzed public interest entities did not take into account the legal obligation to establish a functional internal audit structure in accordance with the provisions of Law no. 672/2002 regarding the internal public audit, republished with the subsequent modifications. Although in large numbers the managers have adhered to the legal provisions in the field of internal audit, there are exceptions, subsequently putting this aspect also on account of the lack of promotion at national level of the importance of this activity for the public interest entity.

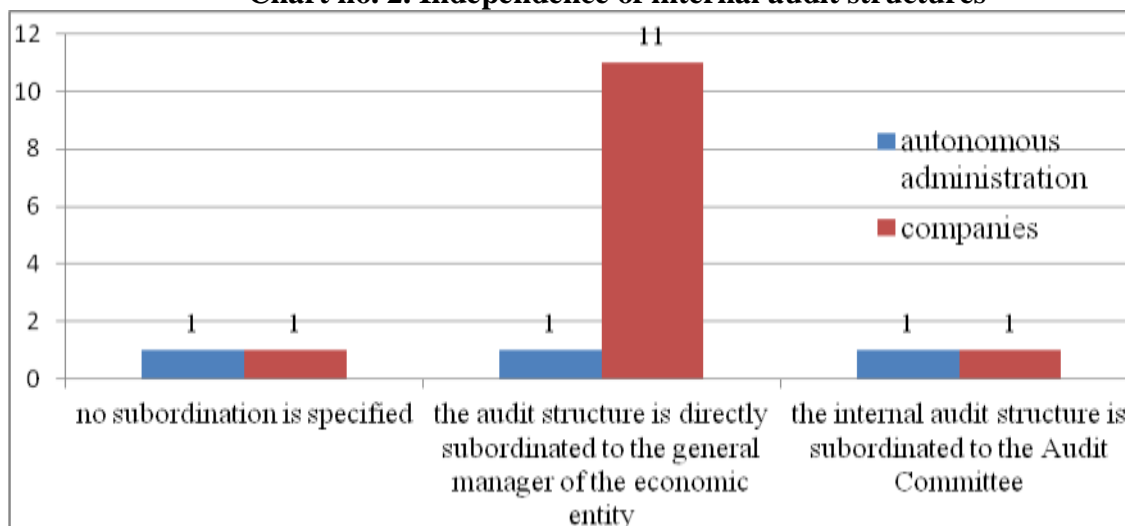
3.2. The independence of the internal audit structure

From the analysis of the position of the internal audit structure within the analyzed public interest entities, the following were found:

- 33% of the autonomous authorities did not locate the position of the internal audit structure within the organizational chart, in 33% of the cases the internal audit structure is subordinated to the general director of the autonomous administration and in 34% of the cases the internal audit structure is subordinated to the Audit Committee.

- 7.6% of companies failed to specify the degree of independence of the internal audit structure, 84.8% have internal audit structures that are subordinated to the general manager of the company and 7.6% of the companies have internal audit structures that shall be subordinated to the Audit Committee.

Chart no. 2. Independence of internal audit structures



Source: Own projection

Comment. The legislation in the field of internal audit, applicable to us in the country, explicitly provides that the internal audit structure is directly subordinated to the general director of the public interest entity. Moreover, the legislation in the field of corporate governance specifies that the internal audit structure reports to the Board of Directors, meaning that it reports the annual results of the internal audit activity or reports on the issues on which references were requested. The lack of concrete explanations but also the arbitrary interpretation of the legislation in the field of internal audit in conjunction with the one in the field of corporate governance has led to situations of subordination of the internal audit structure to the Audit Committee, which from the author's point of view is inappropriate, especially from the point of view of the advisory nature of this committee.

3.3. Responsibilities of the internal audit structure

The study considered the identification within the competences of the internal audit structure, if it:

- performs an evaluation of the efficiency with which all the operations within the public interest entity are performed;
- provides reasonable assurance on compliance with an applicable legal framework, internal rules and procedures;
- performs ad-hoc internal audit missions;
- monitors the risk management system, together with the risk management department;
- monitors ensuring the compliance of the public interest entity with the applicable corporate governance code.

The functional structures of internal audit both within the autonomous regions and within the analyzed companies provided for the first three competences as their own attributions. None of the internal audit structures provided for responsibilities related to the last two points.

Comment. As the empirical analysis shows, the functional internal audit structures took over the provisions of the legislation in the field of internal audit when they created their competence framework, but did not operate appropriate updates as the legislation developed. A normative act was passed, approving the Code comprising the standards of internal managerial control, and then appeared the legislation in the field of corporate governance, aspects on which the internal auditors did not focus or did it timidly or did not not directed at all. This is clearly the lack of promotion of the links between internal audit and corporate

governance, respectively internal control. It can be noticed that the concerns of the internal auditors are not intense in this field, due to inadequate professional training.

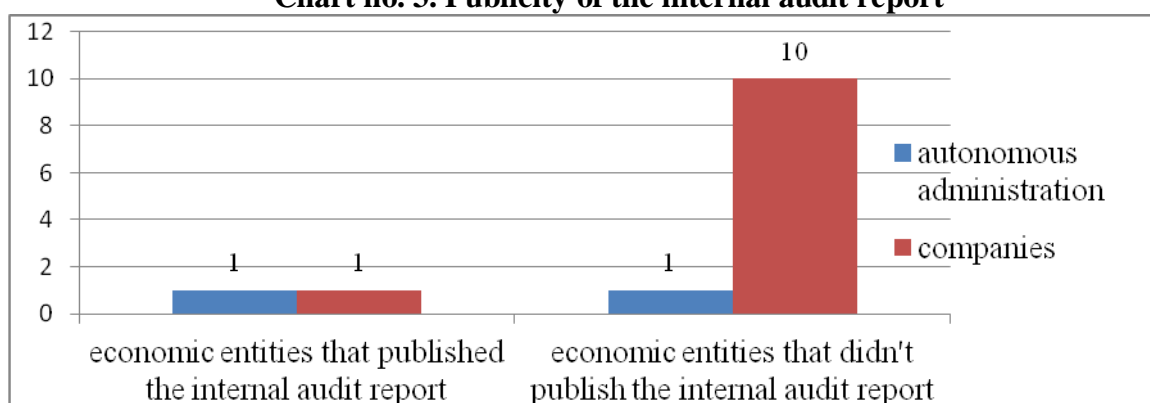
3.4. How to organize the internal audit structure

Following the analysis, it was noted that the functional internal audit structures at the level of the autonomous administrations and the companies analyzed are populated with internal auditors. In neither case are collaborations with third parties registered nor is the internal audit replaced with the external audit, which exists in all cases.

3.5. Publication of the annual internal audit report

The legislation requires that the financial reports be accompanied by the internal audit report on the reliability of the financial-accounting system. This report exists in a few cases due to the extension of the internal audit structure which does not allow an internal audit mission to be carried out on this subject at least every three years and due to the faulty planning of the internal audit activity.

Chart no. 3. Publicity of the internal audit report



Source: Own projection

The analysis reveals the following:

- 50% of the autonomous companies posted the internal audit report on the official website, the others not publishing this information;
- 9% of the companies analyzed posted on the official website the internal audit report the other 91% not having this information available

Comment. It can be seen that the financial reporting is incomplete in the absence of the internal auditor's report. Here the legislator intervenes annually and unfortunately has different approaches to the respective problem, sometimes specifying the obligation of the internal audit report on the reliability of the financial-accounting system to others, leaving the management of the subject to the public authority. Neither the organization of the internal audit activity or the level of consistency of the internal auditors helps much to get out of the deadlock.

4. Analysis of the Audit Committee's practices in the context of corporate governance

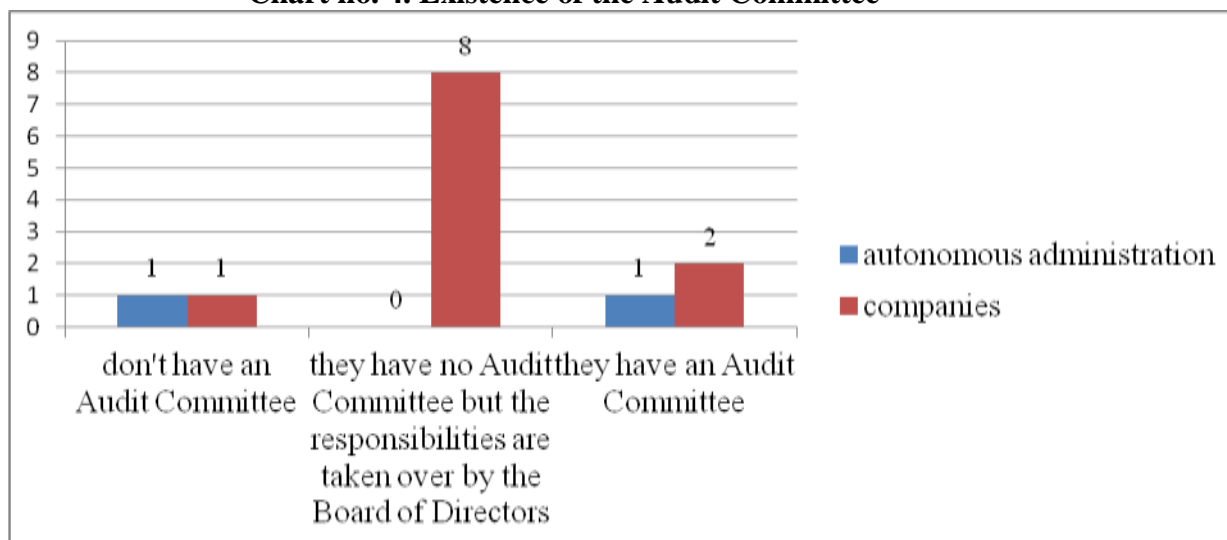
In the second phase of the study we set out to observe where the Audit Committee was set up, which is its level of independence, what powers the chairman of this committee has, what is the structure and how the meetings are conducted.

4.1. Existence of the Audit Committee

Chart no. 4 reveals the following:

- 50% of the autonomous regions do not have an Audit Committee and 50% have constituted an Audit Committee;
- 0.9% of the companies do not have an Audit Committee, 1.8% set up an Audit Committee and 97.3% do not have an Audit Committee, but its prerogatives are executed by the Board of Directors.

Chart no. 4. Existence of the Audit Committee



Source: Own projection

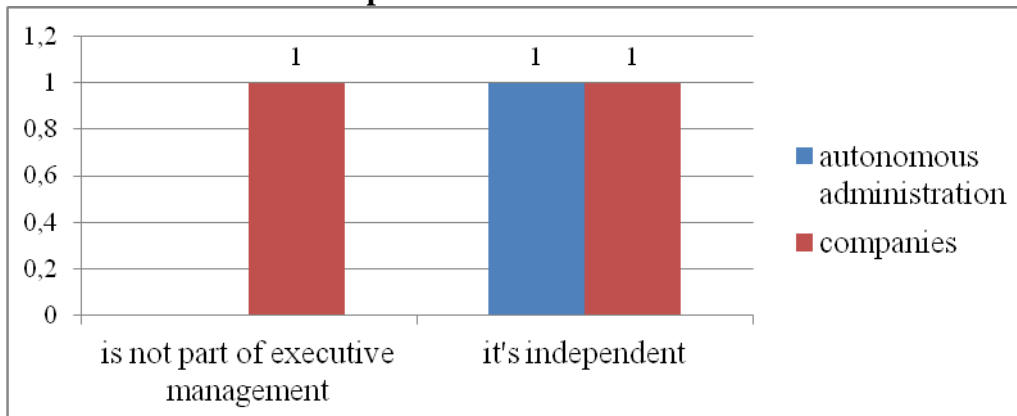
Comment. It is deduced that the legislation in the field of corporate governance did not have an expected echo among the public interest entities under the supervision of the Ministry of Transport, regarding the establishment of the Audit Committee. There are also some limitations imposed by the legal framework that does not allow the establishment of any committee without it being provided in the statute of the public interest entity, which makes the process somewhat difficult. In addition, there are limitations to the powers of the members of the Board of Directors that could also become members of the Audit Committee. But above all, there are obvious limitations to the perception of the role of this body in terms of internal control, external audit and internal audit.

4.2. Independence of the chairman of the Audit Committee

Chart no. 5 notes that:

- At the level of the autonomous regions 100% of the leaders of the Audit Committee are independent;
- Within the companies 50% of the chairs of the Audit Committee are independent and 50% of the companies have an Audit Committee headed by a president who is not part of the executive management.

Chart no. 5. Independence of the chairman of the Audit Committee



Source: Own projection

Comment. The independence of the Audit Committees is adequately ensured, being conducted by persons holding positions of non-executive directors within the Boards of Directors or even by directors with independent status that make it possible to carry out, under safe conditions, the responsibilities incumbent on them of this organism.

4.3. The powers of the Audit Committee's members

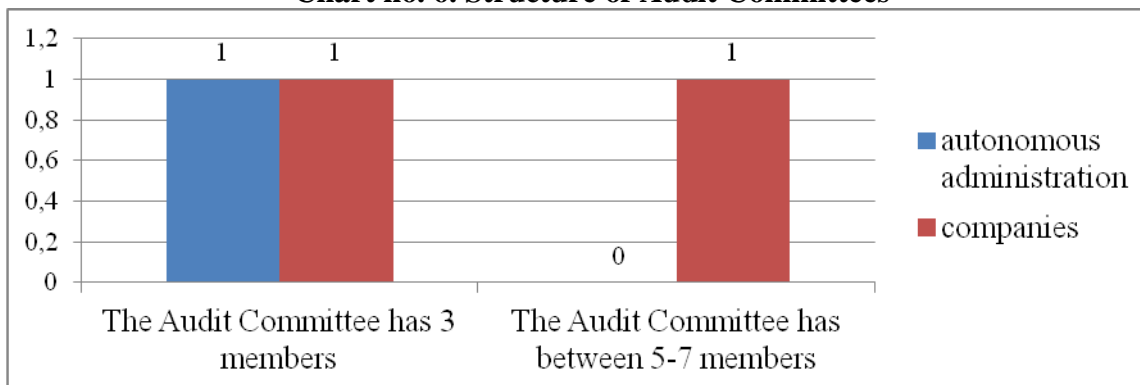
For the Functional Audit Committees within the public interest entities under the authority of the Ministry of Transport, an analysis of the competences held by their members in the financial accounting or audit fields was carried out. It was found that the legal provisions in force regarding these aspects are respected.

4.4. Structure of the Audit Committees

The analysis of the data presented in the previous graph allows us to find the following:

- At the level of the autonomous management that has organized the Audit Committee it consists of 3 persons, two members and a president;
- Within the companies that set up the Audit Committee, at 50% of them the structure of the body has three members, and at 50% of the companies the Audit Committee consists of 5 members.

Chart no. 6. Structure of Audit Committees



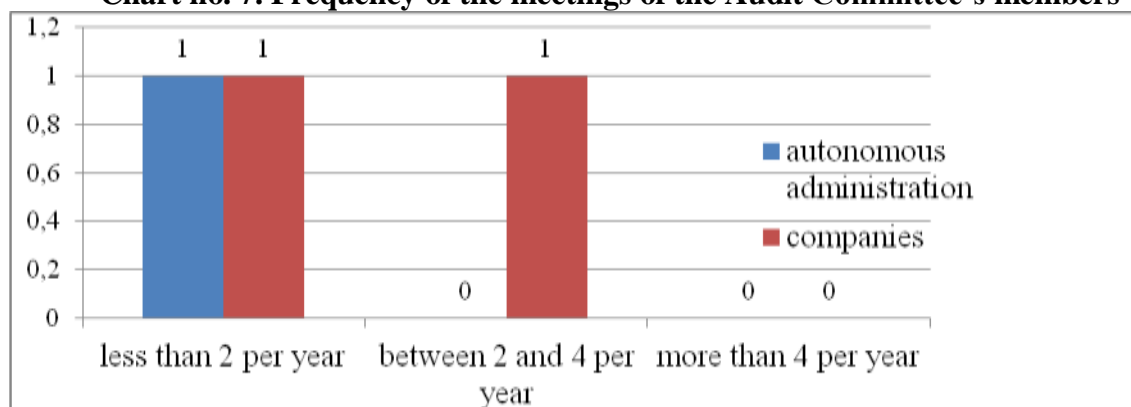
Source: Own projection

Comment. As we can see from the small number of Audit Committees set up, there was not much interest in this aspect and we consider that also due to the difficulties

of understanding the importance of the existence of this body. The number of members is not in this context relevant. It could change its significance if the Audit Committees were set up at all public interest entities that apply the principles of the code of good practice in corporate governance, interact and direct the audit and control missions in support of the management act and of the entity's ultimate goal: maximizing profit.

4.5. How the meetings of the Audit Committee's members are held

Chart no. 7. Frequency of the meetings of the Audit Committee's members



Source: Own projection

The results of the analysis are as follows: The members of the Audit Committee within the autonomous management meet less than twice a year, while the members of the Audit Committee from the analyzed companies meet less than twice a year, in the one committee and up to four times a year in another committee.

Comment. The schedule of the meetings of the members of the Audit Committee must be drawn up in order to take into account several elements: the level of development of the internal audit function; the level of development of the control function; the degree of implementation of the standards of managerial internal control, especially of the one of risk management; the need to select the financial auditor; periodic assessments on the relevance, transparency and credibility of financial reporting. This is how at the level of an economic entity that is adapting to the rigors of corporate governance, the Audit Committee becomes a busy body, as well as for the organizations that have gone through the aforementioned stages, proposing their systems and functions, respectively monitoring measures to remedy errors and deficiencies.

5. Conclusions

The financial crises that have arisen and evolved in the economic life of the entities both in Europe and on the American continent have highlighted the fact that frauds have occurred due to the absence of control.

As a promoter of the efficiency of the internal control system, but also as an evaluator and management consultant, the internal auditor must play a very important role in changing the attitude, conduct and action of the management towards the requirements that must be covered for the implementation of good corporate governance. . Supporting the management through the two insurance and advisory components ensures, in the near and far end, the success of the public interest entity.

An entity of public interest develops good corporate governance within it if the internal audit is functional, it is based on long-tested procedures and adapted to the specific activity of the entity and formulates recommendations and proposals for solutions that

adequately assist the management to achieve performance.

The evaluation of the research results justifies us to affirm that the process of corporate governance is the pillar on which the efficiency of the public interest entities should be supported, supported closely by the extension and development of the competences of the internal audit structure, as well as the establishment and functioning of the Audit Committees, which they come to facilitate the fluidization of the processes, the responsibility of the personnel, the improvement of the managerial act, the strengthening of the internal and external control.

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