

The Romanian Internal Public Audit System – An X-Ray Analysis of Audit Compartment Activities

Adelina DUMITRESCU PECULEA¹

Abstract

Closely following the Romania's EU-Integration, the public administration began a drastic reform process of all its systems, including internal public audit. In this regard, even right after 1989, a connection to European governance mechanisms and the implementation of European best practices were sought. Thus, building an efficient and sustainable public administration migrated over time from intention to necessity and lately to priority of all development strategies. For implementing such mechanism, clear and transparent decision processes, a good management of available resources, an adequate institutional and administrative structure and standards centered on public interest promotion are necessary. This paper presents an X-Ray like image of the public audit system in Romania, for the implementation of an efficient management in public entities as part of public sector good governance. The sustainable development of public administration is in need of an audit system consolidation, based on specialists contributing to reaching objectives by improving information flows and efficient risk management.

Keywords: *internal public audit, system evaluation and implementation, efficient management, public administration and public interest.*

JEL classification: M42, O16, P41.

Introduction

Currently, internal audit experiences a significant development, and efforts to increase the efficiency of this activity are aimed mainly at the economic and financial aspects specific to judicial entities and/or public institutions. The theme of the paper revolves around internal public audit in Romania. Internal public audit is an independent and objective activity, meant to add value, which helps organizations reach their objectives evaluating through a systemic and methodical approach the quality of management and its decisions, risk management and internal control systems implementation. The finality of this activity is represented by a set of recommendations for improvement of risk management, internal control and governance processes efficacy (*International Standards for the Professional Practice of Internal Auditing*, IIA, 2012).

¹ **Adelina DUMITRESCU PECULEA**, Romanian Academy,
The Institute for World Economy, Email: adelinadumitrescu02@yahoo.com

The dynamics of this change process had an important influence on public entities, also determining a migration of internal public audit's role from appreciation, monitoring and evaluation to assurance, consultancy and management assistance (Ghita et al., 2009; Togoe, 2007; Dumitrescu Peculea, 2015).

The present work aims to present, first, a review of the relevant literature and the fundamental aspects about normative framework in public audit system. Secondly, it is important to make an analysis of the evolution of this activity and present the degree of organization/implementation between 2011 and 2013, with additional information from the reports of the Romanian Court of Accounts.

1. Literature review and legal context

Even though audit, seen in a broad sense, finds its origin in the dawn of time (Carmichael and Willingham, 1987), the term used in the present meaning is relatively new. It is described by the emergence of the consequences following the economic crisis which hit the United States of America in year 1929, but also the great financial scandals (Enron, Parmalat, Worldcom etc.), which had as consequence the improvement of the elaboration processes of the accounting and audit standards (Dobroteanu and Dobroteanu, 2002). At the same time, the specialty literature states that until the emergence of internal audit, the American companies were audited by the External Audit Offices, which had the task of verifying the accounts and the accounting balance sheets and to certify the final financial statements (Boulescu et al., 2001).

Being in continuous evolution, internal audit suffered several conceptual changes, caused by the changing economic context and the legislative changes. The IIA's International Standards for the Professional Practice of Internal Auditing (Standards) define internal audit as an independent, objective assurance and consulting activity designed to add value and improve an organization's operations" (IIA's Standards, 2013). As society developed, audit evolved from detecting frauds (Meigs et al., 1989) to risk assessment and to the evaluation of the internal control systems, in order to ensure the fulfillment of the organization's objectives (Ghita et al., 2009). In Romania, the internal audit activity appeared after the 1990's, in the context of the economic changes and of the international economic integration, a first recommendation having been received by Romania after signing the European Accession Agreements (1993) and before submitting the application to join the European Union (1995). Thus, we witness the creation of a unitary system of measurement and assessment, which allows the comparison of processes, actions and even public administration systems in all EU member countries (Dumitrescu, 2012).

The financial auditors were first to organize, through the issuance of Government Expedite Ordinance no. 75/1999 regarding the financial audit activity, published in the Official Gazette of Romania no. 256 of 06.04.1999, subsequently approved and complete through Law no. 133/2002, published in the Official Gazette no. 598/2003. Afterwards, for the first time in Romania, internal audit and

internal control were established and introduced, through Government Ordinance no. 119/1999 regarding public internal audit and preventive financial control, published in the Official Gazette no. 430/1999, approved and modified through Law no. 301/2002, published in the Official Gazette no. 339/2002. The activity of internal audit in Romania, corroborated with the European Commission's recommendations, materialized through the issuance of Law no. 672/2002 regarding public internal audit, published in the Official Gazette no. 953/2002, which officially described the function of internal audit with respect to the creation and use of public funds and the administration of the public patrimony and the profession of internal auditor in public entities.

At present, the organization and running of the internal audit activity targets missions of assurance, counseling and assessment. The regulatory and legal framework for the internal audit activity is briefly presented in the following table.

Table 1. Regulations in the field of public internal audit

| No. | Legal and regulatory framework | Content |
|------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | Law no. 672/2002, regarding public internal audit | <ul style="list-style-type: none"> • defines public internal audit as a functionally independent and objective activity which "gives assurance and counseling" to management; • sets the bases of the implementation methodology at the level of the central and local public administration |
| 2 | Government Decision no. 1086/2013, for the approval of the General regulations regarding the exercising of the public internal audit activity, as subsequently modified and completed | <ul style="list-style-type: none"> • approval of the Methodology for running the assurance public internal audit missions; |
| 3 | Order no. 252/2004, issued by the Ministry of Public Finance, for the approval of the Ethical Code of the internal auditor | <ul style="list-style-type: none"> • defines the principles of behavior of the internal auditor; |
| 4 | Order no. 1707/2005, issued by the Ministry of Public Finance, for the approval of the Regulations regarding the organizing and exercising of the counseling activity performed by the internal auditors within the public entities. | <ul style="list-style-type: none"> • approval of the methodology for running the counseling activity while exercising the public internal audit function. |

Source Ministry of Public Finance

Benefitting of a modern legal framework and of regulations and procedures elaborated according to the internationally accepted audit standards and with the good practice within the European Union, public internal audit is in a development process, which targets both the actions it performs and its role and importance within the public administration system.

2. The analysis of the evolution of the internal public audit system

The study uses data published at the beginning of this year (2015) by the Ministry of Public Finance. For the purpose of this exercise data from 2013, 2012 and 2011 has been considered to be sufficient. For consistency, data has been collected from one single source, in this case, the UCAAPI Report for Public Audit Activity in 2013, 2012 and 2011. Newer reports were not published.

The present study will concentrate on analyzing key figures that will give a bird's eye view on the general status of internal public audit activities in Romanian public institutions. A separation of figures will be performed, in order to make a comparison between audit activities in central public administration and local public administration. Since the number of central public institutions is by far smaller than the number of local institutions, differences in the way in which this activity is held appear intrinsically. The study will take into consideration the following aspects:

- Spreading of public audit activities throughout public institutions;
- Workload of public auditors;
- Audit mission typology;
- The degree of recommendation implementation.

2.1 The spreading of public audit activities in institutions

There are three factors which were taken into consideration when the spreading of public activities:

- The total number of public institutions in Romania;
 - The number of institutions that have assured the organization of internal public audit activities;
 - The number of institutions who actually have carried out audit missions.
- The collected data is shown in below.

Table 1. Public entities which organize and exert internal public audit activities

| Internal public audit activities | 2013 | | 2012 | | 2011 | |
|----------------------------------|----------|------------|----------|------------|----------|------------|
| | Absolute | Percentage | Absolute | Percentage | Absolute | Percentage |
| Public entities | 11190 | 100,00% | 11667 | 100,00% | 8570 | 100,00% |
| Organized | 6530 | 58,36% | 6805 | 58,33% | 2159 | 25,19% |
| Exerted | 4775 | 42,67% | 2812 | 24,10% | 1583 | 18,47% |

Source: Author's calculations based on Ministry of Public Finance, UCAAPI Report for Public Audit Activity in 2013, 2012, 2011

A clear increase of internal public audit activities can be observed from the percentages of public entities which have exerted such activities; also, the number

of public entities which have organized. For 2012, the evolution in percentage is not that impressive, however, given the increase in public entities of over 3000 units, the absolute variation is significant. However, the percentage of under 50% for the year 2013 is quite low. The main reason for this low percentage is indicated in all three reports to be the deficit of internal public auditors.

2.2 The workload of internal auditors

For the workload of internal auditors only entities that have carried out audit missions have been taken into consideration. Since the main reason for not exerting public audit activities at all public institutions was the lack of appropriate personnel, this assumption was considered to be correct. The data is presented in table 2.

Table 2. Average number of internal auditors per public institution

| Internal public audit activities | 2013 | | | 2012 | | | 2011 | | |
|----------------------------------|----------|----------|---------|----------|----------|---------|----------|----------|---------|
| | Entities | Auditors | Aud/Ent | Entities | Auditors | Aud/Ent | Entities | Auditors | Aud/Ent |
| Central | 660 | 1466 | 2,22 | 669 | 1589 | 2,38 | 732 | 1588 | 2,17 |
| Local | 485 | 804 | 1,66 | 459 | 726 | 1,58 | 424 | 799 | 1,88 |
| Total | 1145 | 2270 | 1,98 | 1128 | 2315 | 2,05 | 1156 | 2387 | 2,07 |

Source: Author's calculations based on Ministry of Public Finance, UCAAPI Report for Public Audit Activity in 2013, 2012, 2011

It can be clearly seen, that the average number of internal auditors per public institution does not vary over the studied years, ranging from 2,17 to 2,38 for central public entities and from 1,58 to 1,88 for local institutions; differences can be attributed to workforce migration causes.

Table 3. Average workload per auditor

| Internal public audit activities | 2013 | | | 2012 | | | 2011 | | |
|----------------------------------|----------|----------|---------|----------|----------|---------|----------|----------|---------|
| | Missions | Auditors | Average | Missions | Auditors | Average | Missions | Auditors | Average |
| Central | 2224 | 1466 | 1,517 | 2759 | 1589 | 1,736 | 2013 | 1588 | 1,268 |
| Local | 4078 | 804 | 5,072 | 4013 | 726 | 5,528 | 3307 | 799 | 4,139 |
| Total | 6302 | 2270 | 2,776 | 6772 | 2315 | 2,925 | 5320 | 2387 | 2,229 |

Source: Author's calculations based on Ministry of Public Finance, UCAAPI Report for Public Audit Activity in 2013, 2012, 2011

Taking into account the number of audit missions carried out by these auditors as shown in table 3, a huge difference in average yearly audit missions can be observed. Thus institutions of the central administration carry out an average of 1,5 missions per auditor per year, as opposed to institutions of the local administration who carry out an average of 5 missions per auditor per year. However, since there is no mention about the complexity of these missions, these averages are not fully eloquent. It is safe to assume, that missions at units of the central public administration are more complex than the ones carried out at institutions of the local administration. But it is equally safe to assume, that missions carried out at central units do not require three times the amount of work of the missions in local institutions. Thus the conclusion that the workload of public auditors in local institutions is higher than the workload in institutions of the central administration.

Another interesting fact is that the number of missions carried out in the public administration (6302 missions in 2013) does not cover all public institutions (11190 institutions), despite the legal obligation to do so. The missing audits are completed by missions of the “Romanian Court of Accounts”, which carried out a total of 2067 missions in 2013 (Report of the Romanian Court of Accounts, 2014), and by 518 contracts of audits which were externalized to private licensed auditors. This leaves at least 2200 institutions which were not audited in 2013, thus emphasizing the need to further extend the network of public institutions which carry out internal public audits.

2.3 Audit mission typology

There are nine types of audit carried out in public institutions: audits of budgetary processes, financial audits, audits of public acquisitions, audits of HR, audits of the utilization of EU-funds, IT-audits, audits of judicial activities audits of specific entity functions and counselling audit missions. The distribution of these types of mission is represented in table 4.

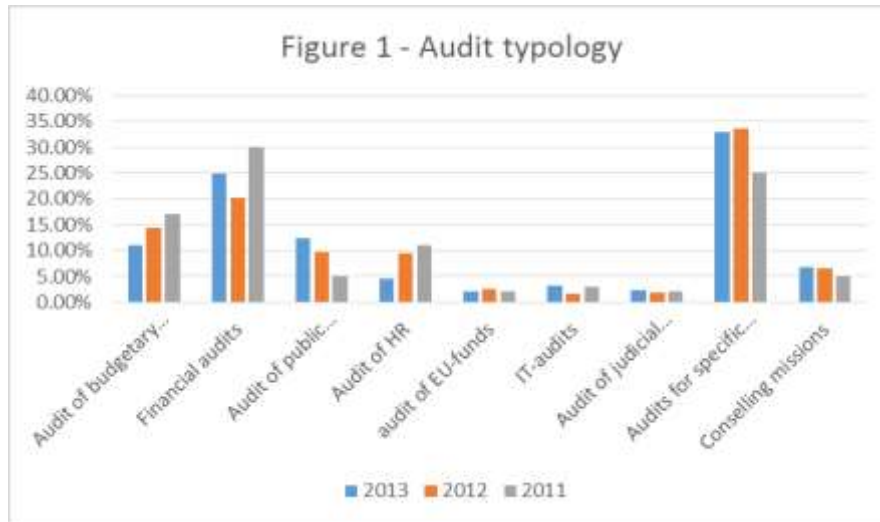
Table 4. Audit mission typology for 2013/2012/2011

| No | Audit mission types | 2013 | 2012 | 2011 |
|-----------|--------------------------------------|-------------|-------------|-------------|
| 1 | Audit of budgetary process | 11,03% | 14,31% | 17,00% |
| 2 | Financial audits | 24,93% | 20,26% | 30,00% |
| 3 | Audit of public acquisitions | 12,31% | 9,73% | 5,00% |
| 4 | Audit of HR | 4,54% | 9,48% | 11,00% |
| 5 | Audit of EU-funds | 2,20% | 2,47% | 2,00% |
| 6 | IT-audits | 3,14% | 1,58% | 3,00% |
| 7 | Audit of judicial activities | 2,30% | 1,96% | 2,00% |
| 8 | Audits for specific entity functions | 32,85% | 33,56% | 25,00% |

| No | Audit mission types | 2013 | 2012 | 2011 |
|----|------------------------------|---------|---------|---------|
| 9 | Assurance missions (sum 1-8) | 93,30% | 93,35% | 95,00% |
| 10 | Counselling missions | 6,70% | 6,65% | 5,00% |
| 11 | Total missions (9+10) | 100,00% | 100,00% | 100,00% |

Source: Author's calculations based on Ministry of Public Finance, UCAAPI Report for Public Audit Activity in 2013, 2012, 2011

For a more graphic representation figure 1 is to be referred to.



Source: Author's interpretation

It comes as no surprise that most audits carried out (more than 50% of all audits) refer to financial and accounting or to the specifics of the audited entity. Also, a decrease in audits of budgetary processes and in HR-audits can be observed. However, these decreases can be conjunctural, as can be the increase of audits of public acquisitions.

Surprisingly, there is no increase in audits of EU-fund utilization. Since the absorption of EU funds has intensified in the last years, an increasing preoccupation in this area was to be expected. During the studied period of time, there have been carried out only 152 audits (for 2011), 167 audits (for 2012) and 145 audits (for 2013). Also, from these, almost 2/3 were carried out at institutions of the central administration. The deficit of audit activities in the field of EU-funds utilization, especially for local public institutions is serious, since these are regulated very strictly by the EU, and infringements can have grave implications.

Another aspect to mention is the steady increase in counselling missions. Thus for 2011/2012/2013, 274, 450 and 422 missions have been carried out, meaning an increase from 5 to 6,5% of such missions in the total number of audit missions.

2.4 The degree of recommendation implementation

In 2013, following the carrying out of the above mentioned 5880 assurance missions (6302 missions in total minus 422 counselling missions) a total of 48.516 recommendations were formulated, meaning an average of 8,25 recommendations per mission. Also, a total number of 529 irregularities have been uncovered, which caused an estimate damage of RON 9,6M (at 4,419 RON/EURO approximately EUR 2,2M). It is also interesting to mention, that IT-audits have nor uncovered any irregularities of IT systems in the public administration, and consequently, no damage has been recorded.

Regarding the formulated recommendations, their distribution over the different types of audit missions is represented in table 5.

Table 5. Recommendations of public audit missions

| Mission typology | Missions | Total rec | Average | Implemented | Partially implemented | Unimplemented recommendations | | |
|--------------------------------------|--------------|---------------|---------|---------------|-----------------------|-------------------------------|-----------------|------------------|
| | | | | | | Total | Within deadline | Outside deadline |
| Audit of budgetary process | 695 | 3.869 | 5,57 | 2.466 | 598 | 805 | 534 | 271 |
| Financial audits | 1.571 | 12.047 | 7,67 | 7.605 | 1.913 | 2.529 | 1.087 | 1.442 |
| Audit of public acquisitions | 776 | 4.248 | 5,47 | 2.725 | 647 | 876 | 327 | 549 |
| Audit of HR | 286 | 3.635 | 12,71 | 1.940 | 505 | 1.190 | 665 | 525 |
| Audit of EU-funds | 145 | 452 | 3,12 | 273 | 74 | 105 | 54 | 51 |
| IT-audits | 198 | 1.103 | 5,57 | 588 | 234 | 281 | 75 | 206 |
| Audit of judicial activities | 139 | 1.167 | 8,40 | 639 | 208 | 320 | 81 | 239 |
| Audits for specific entity functions | 2.070 | 21.995 | 10,63 | 12.486 | 4.252 | 5.257 | 2.148 | 3.109 |
| Total | 5.880 | 48.516 | | 28.722 | 8.431 | 11.363 | 4.971 | 6.392 |

Source: Author's interpretation

Note: Average Leu/Euro parity for the year 2013 according to the Romanian National Bank. See also <http://www.bnr.ro/Cursul-de-schimb-3544.aspx> accessed on 30.07.2015

Of the 48.516 recommendations 37.153 have been totally od partially implemented, reaching an implementation degree of 76,58%. The most recommendations that have been implemented were in the field of public acquisitions (79,38%), while the least implemented recommendations regarded HR-activities (67,26%). An interesting fact raises an interesting question: does the fact that HR is the audited domain with the most recommendations per mission

(12,71) and the domain with the lowest rate of recommendation implementation (67,26%) and that public acquisitions is the audited domain with the second lowest number of recommendations per audit mission (5,47) and also the domain with the highest rate of implementation (79,38%), imply that there is a relationship between the number of implementations per audit mission and the rate of implementation?

To determine that, the Bravais-Pearson correlation coefficient (Andrei and Bourbonasis, 2008; Neacsu, 2009) has been calculated for the two series of data, and a value of -0,68 was determined. This shows a medium-strong inverse correlation between these two data series. As opposed to this, the correlation coefficient between the total number of recommendations and their implementation rate is 0,22 which signals a significantly weaker relationship between these two data series.

When analyzing the typology of audit missions, a remark regarding the need for an intensification of EU funds utilization audits has been made. Another fact to support this is that, although only 9 irregularities have been identified, the value of the estimated damage per irregularity is by far greatest (RON 122.000 or EUR 27.500). As a comparison, the next highest damage per irregularity is 53.000 RON or EUR 12.700.

Conclusions

Internal public audit is undergoing an intense process of development and evolution, aimed not only at discovering irregularities and infringements, but mostly at perfecting and optimizing processes in public institutions. For this, a whole range of tools and instruments stand at the disposal of public auditors, permitting them to audit all aspects of the activities of public entities. The modernization and evolution of public audit must take place to cover the aspects highlighted by the present study on the following coordinates:

- Increasing the number of public entities that are being subjected to public audit missions;
- Ensuring the adequate human resource and funding for internal public audit activities;
- Widening the range of audited domains according to the current economic and legal framework and EU requirements and tendencies;
- Reducing fraud levels and economic damages within public institutions;
- Increasing the rate of counselling missions.

As a general conclusion, the development direction of public audit activities is correct. It is very important, that public institutions acknowledge the role of internal public audit. However, this evolution process still has a lot of deficiencies to cover.

As future directions of study, there is the continuation of the time series begun in this study, and the derivation of a mathematical development model. There is data published starting with the year 2004. Based on these time series, a regression model can be calculated thus outlining the future development of

internal public activities. The results should be interesting, since the time series includes the period in which the financial crisis has had its effects. Another point of interest is the determination of a break-even point for public audit activities at national level. This means, determining the point where public audit costs the same as the amount of money it saves.

Acknowledgements

This paper has been financially supported within the project entitled “Horizon 2020 - Doctoral and Postdoctoral Studies: Promoting the National Interest through Excellence, Competitiveness and Responsibility in the Field of Romanian Fundamental and Applied Scientific Research”, contract number POSDRU/159/1.5/S/140106. This project is cofinanced by European Social Fund through Sectoral Operational Programme for Human Resources Development 2007-2013. Investing in people!

References

1. Andrei T., Bourbonasis R. (2008), *Econometrie*, Editura Economica, Bucharest
2. Boulescu, M., Ghiță, M., Mareș, V. (2001). *Fundamentele auditului*, Editura Didactică și Pedagogică, Bucharest
3. Carmichael D.R., Willingham J.J. (1987). *Auditing concepts and methods: A guide to current auditing theory and practice*, Fourth Edition, McGraw – Hill, Inc., USA
4. Dumitrescu Peculea, A. (2015), “Governance process improvement and development by audit consolidation”, *Theoretical and Applied Economics*, Volume XXII No. 2(603), Summer, pp. 215-222
5. Dumitrescu, A. (2012), *Audit și contabilitate. Baze ale performanței în administrația publică*, Editura Economică, Bucharest
6. Ghiță M., Menu M., Vilaia D., Popescu M., Croitoru I. (2009). *Guvernanță corporativă și audit intern*, Editura Tehnica-Info, Chișinău
7. Meigs W.B., Whittington O.R., Pany K., Meigs R.F. (1989). *Principles of Auditing*, Ninth Edition, Irwin, Boston.
8. Neacsu G. (2009), *Concepte si metode utilizate in statistica*, Editura Universitara, Bucharest
9. Renard, J. (2002). *Theory and practice of internal audit*, Public Ministry of Finance, Bucharest
10. Țogoe D. (2007). “Auditul public intern între exigențele cadrului normativ și realitățile perioadei de tranziție”, *Revista de Științe Juridice*, no. 2, pp. 190-198, available at <http://drept.ucv.ro/RSJ/images/articole/2007/RSJ2/022Togoe.pdf> (accessed on 23.07.2015)

11. Government Decision no. 1086/2013, for the approval of the General regulations regarding the exercising of the public internal audit activity, as subsequently modified and completed, published in the Official Gazette no. 17/2014
12. Law no. 672/2002 regarding public internal audit, published in the Official Gazette no. 953/2002
13. Ministry of Public Finance (2012), UCAAPI Report for Public Audit Activity in 2011, Bucharest, available at http://discutii.mfinante.ro/static/10/Mfp/audit/Rap_activ_auditintern_sectorpublic_2011.pdf (accessed on 27.07.2015)
14. Ministry of Public Finance (2013), UCAAPI Report for Public Audit Activity in 2012, Bucharest, available at http://discutii.mfinante.ro/static/10/Mfp/audit/Rap_activ_audit_intern_sect_public_2012.pdf (accessed on 27.07.2015)
15. Ministry of Public Finance (2014), UCAAPI Report for Public Audit Activity in 2013, Bucharest, available at http://discutii.mfinante.ro/static/10/Mfp/audit/Rapactivitauditintern2013_20ian2015.pdf (accessed on 27.07.2015)
16. Romanian Court of Accounts, December 2014, Public Report for the year 2013, available at <http://www.curteadeconturi.ro/Publicatii/Raport%20Public%202013.pdf> (accessed on 29.07.2015)
17. The Institute of Internal Auditors (IIA), International Standards for the Professional Practice of Internal Auditing, 2012, available at <https://na.theiia.org/standards-guidance/Public%20Documents/IPPF%202013%20English.pdf>.
18. <http://www.mfinante.ro/ucaapi>
19. <http://www.bnr.ro/Cursul-de-schimb-3544.aspx>