



## DEFINING MOMENTS IN THE EMERGENCE AND EVOLUTION OF INTERNAL AUDIT IN OUR COUNTRY

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The appearance and improvement of the internal audit activity in the public and private entities from Romania represented and constitutes a natural necessity, a consequence of the tendencies and practices manifested on international and European level in this field. Our country has taken actions for the implementation of the internal audit service in state and private entities with a certain delay and sinusoidal evolutions, determined by the alternation of administrations and regimes (interwar democracies - communist totalitarian - democratic).

The Ministry of National Defence as part of the public administration, through specialized structures and in all its composing entities, applies the provisions of normative acts regarding the development of internal audit activity, fact for which we highlighted reference moments in the process of occurrence, organization and exercise of audit activity internal public in the structures of this ministry.

**Keywords:** internal audit; internal audit function; insurance missions; regularity audit; performance audit; system audit; internal audit advice.

### Introductory aspects regarding the appearance of the internal audit in Romania

The need for the *internal audit function* was also felt in Romania with the transition to a market economy, when economic and social entities began to face a problem related to finding viable solutions so as to improve the performance obtained, by increasing efficiency, effectiveness and economy, by performing the management and internal control over the functioning of these entities by the management teams.

Romania has undertaken a series of measures to connect to international and European accounting requirements, such as: the adoption of International Accounting Standards at the level of economic agents and then the public sector, the introduction in public institutions of a new accounting system, based on the System European Court of Auditors, as well as changes in economic and fiscal legislation. It was also necessary to organize the audit activity, both for private and public organizations. Membership of the European Union requires the existence of well-defined financial management systems, but also viable methods of controlling them<sup>1</sup>.

Any manager of a private or public sector organization feels the need to obtain a certain *reasonable assurance* that the transactions carried out and the decisions taken involving resources with financial connotations are under control and the objectives of the organization are met.

In the context of these concerns of managers, *internal audit* is a significant support to them, in achieving the objectives set, through a systematic and well-organized activity, in order to evaluate and improve the effectiveness and efficiency of management and control processes.

The great merit of the internal audit is that it acts in an independent, objective way, without accepting compromises and without aiming to achieve power, therefore, without endangering the position of managers.

In Romania, the recognition of the importance of this field of internal audit was made quite late compared to other states, due, on the one hand, to the domination of the communist regime until 1989, but also to the economic difficulties generated by the inability of governments after the revolution, to adopt a transition strategy appropriate to the economic conditions in our country, but also due to the positive experience proven by other states in similar situations to ours. In the Romanian economy, the trajectory of the evolution of internal audit was reversed compared to the international one.

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While internationally the internal audit function has developed, starting from large enterprises and multinationals to public sector entities, the situation in Romania has been in reverse.

In Romania, the internal audit targeted, first of all, the bodies and institutions in the public domain and later on, as the investments developed and more and more private companies of increasing size were created, they felt and in this area the usefulness and imperious need of the internal audit function.

Thus, the internal audit in Romania gradually became part of the general effort to improve and enhance the management of both public and private sector organizations, amid the harmonization of the internal regulatory framework with European legislation, taking into account the efforts made by our country on the way to integration among the member countries of the European Union.

According to the opinion expressed by a specialist from our country, quoted earlier, the concept of "internal audit" began to be used a lot in various environments, perhaps even in excess, becoming a fashionable concept in the Romanian economic context, being used by various categories of specialists in all fields, sometimes without being fully aware of what internal audit really means<sup>2</sup>.

### **Highlights on the emergence and development of internal audit in private entities in Romania**

The internal audit activity for the private environment appeared a little later than in the public sector and is currently coordinated in our country by the Romanian Chamber of Financial Auditors – CAFR<sup>3</sup> and the Romanian Association of Internal Auditors – AAIR<sup>4</sup> and has as correspondent to the entities in this sector, internal audit departments or the outsourced service in this field.

In the private environment, the internal audit activity is carried out only in companies and non-profit organizations that are subject to statutory financial audit, according to Law no. 162/2017<sup>5</sup> on the statutory audit of the annual financial statements and the consolidated annual financial statements. This normative act stipulates three very important provisions about the internal audit in the private environment, which we will point out below.

The entities whose annual financial statements are subject, according to the law, to the statutory

audit are obliged to organize and ensure the exercise of the internal audit activity<sup>6</sup>.

The internal audit standards applicable to private entities in our country are the international internal audit standards issued by the Institute of Internal Auditors of the United States of America and adopted by the Chamber<sup>7</sup>.

At the autonomous utilities, the national companies/societies, as well as at the other economic entities with majority state capital, the internal audit activity is organized and operates according to the legal framework regarding the internal public audit of the public entities<sup>8</sup>.

The financial auditors who coordinate the internal audit activity (at private entities) must have the status of active financial auditor member of the Romanian Chamber of Financial Auditors – CAFR<sup>9</sup>.

In the case of internal auditors of companies and non-profit organizations, they have a major social responsibility to the clients of these entities, for the smooth running of their business and actions.

The Romanian Chamber of Financial Auditors – CAFR and the Romanian Association of Internal Auditors-AAIR have jointly developed the Guide<sup>10</sup> on the implementation of International Internal Audit Standards for the private sector. This guide includes as more important provisions for the internal audit of private entities, the following major issues: the objectives of these internal audit missions; the importance and place of internal audit within the governance of the entities (partial or total outsourcing of this audit service to private entities is allowed); types of internal audit missions that can be performed at these private entities (insurance and advisory missions); the specific methodology for conducting audit missions to these entities (the methodology is largely similar to that of public internal audit, but also contains specific elements).

We can conclude that in the private sector, internal audit is an increasingly stringent need for the governance of entities in this field, even if the implementation started a little later than in the public sector, and from the point of view of the regulation of this normative activity in the field, they intervened more timidly and with more modest results regarding the particularization of the internal audit in this environment.

### Moments from the process of appearance, organization and exercise of the internal public audit activity in the Ministry of National Defence

The internal audit activity of the Romanian Army went through the same evolution as that of the public institutions in our country, without having at the beginning of its activity certain nuances and particularities, due to the specificity of the military field.

Only starting with the latest regulations in this field in our country, did the Ministry of National Defence, through the competent bodies, issue normative acts that customize the internal audit activity to the specifics of the military body.

The general objective of the internal public audit in the Ministry of National Defence is to improve the management of the central structures, structures and forces subordinated to them in the Ministry of National Defence.

The public internal audit is organized and conducted, at the level of the Ministry of National

of National Defence, and the exercise of its activity is done according to the provisions of the *Order of the Minister of National Defence no. M. 67/2014*<sup>12</sup> for the approval of the *Methodological Norms regarding the exercise of the internal public audit in the Ministry of National Defence* (amended and updated by the Order of the Minister of National Defence no. 127 / 09.12.2014<sup>13</sup>), normative act that customizes to the army specific the provisions of Government Decision no. 1086/2013<sup>14</sup>.

The fields of activity and the attributions of the Internal Audit Department are included in detail in the Regulation of Organization and Functioning of the Ministry of National Defence, approved by Order no. M.S. 156/2017 with subsequent amendments and completions, being classified according to law.

The organizational chart of the Internal Audit Department of the Ministry of National Defence is currently the one presented in Figure 1.

The main attributions of the Internal Audit Department<sup>15</sup>, resulting from the normative acts

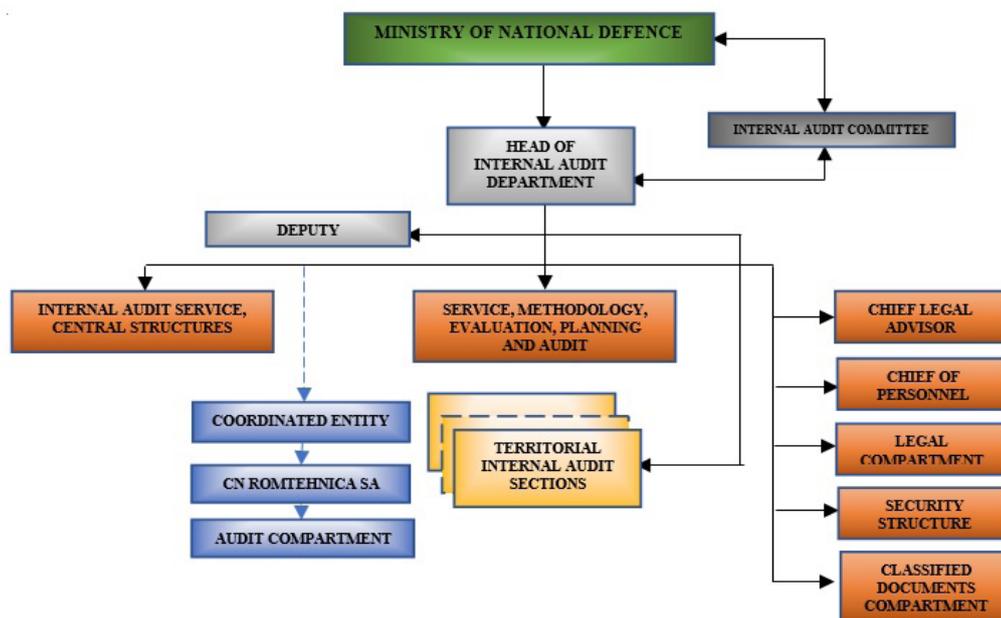


Figure 1 Organizational chart of the Internal Audit Department of the Ministry of National Defence

Source: www.mapn.ro, accessed on 04.10.2020.

Defence, by the Internal Audit Department (DAI), as a distinct, specialized and unique central structure in this field in the army.

The Internal Audit Department as an independent structure is constituted in accordance with the provisions of Law no. 167 of 2017<sup>11</sup> for the amendment and completion of Law no. 346/2006 on the organization and functioning of the Ministry

mentioned above, are the following: it elaborates/ updates the norms regarding the exercise of the public internal audit activity in the ministry, endorsed by UCAAPI; it elaborates the draft of the Multiannual Public Internal Audit Plan and the draft of the Annual Public Internal Audit Plan of the ministry, which it submits to the approval of the Minister of National Defence; it performs



public internal audit activities in order to evaluate the financial management and control systems of the central structures, structures and forces subordinated to them in the ministry, as well as of the structures under its coordination or authority; it informs UCAAPI about the recommendations not adopted by the Minister of National Defence; it reports to the Minister of National Defence, to UCAAPI and to the Court of Accounts, on the established terms, the findings, conclusions and recommendations resulting from the public internal audit activity; it capitalizes on the results of the public internal audit activity and reports to the Minister of National Defence and to UCAAPI, through an annual report, on the way to achieve the objectives of the Internal Audit Department; in case of identification of some irregularities or possible damages, it reports to the Minister of National Defence and the competent internal control structure; elaborates the Charter of the internal public audit; verifies and evaluates the observance of the norms, instructions, as well as of the Code on the ethical conduct of the internal auditor within the subordinated territorial structures and internal audit departments within the autonomous utilities and national companies under the coordination or authority of the Ministry of National Defence.

The Internal Audit Department of the army performs two categories of missions: insurance missions; counselling missions.

The *assurance missions* represent objective examinations of the evidence, carried out in order to provide the central structures, structures and subordinate forces of the Ministry of National Defence with an independent assessment of the risk management, control and governance processes. Insurance missions can be: 1) regularity audit missions; 2) performance audit missions; 3) system audit missions.

The *regular audit missions* aim at examining the actions on the financial effects on the account of public funds or public patrimony, in terms of observing all the principles, procedural and methodological rules that are applied to them.

The *performance audit* is an analysis of activities, processes, programs, projects carried out within the central structures, structures and forces subordinated to them in the Ministry of National Defence, designed to add value to them, by evaluating and comparing the results obtained

with those proposed or expected, in conditions of economy, efficiency and effectiveness.

The *system audit* is an in-depth assessment of the management and internal/managerial control systems within the central structures, structures and forces subordinated to them in the Ministry of National Defence, as well as the coordinating entities, in order to establish whether these systems work economically, effectively and efficiently, to identify deficiencies and make recommendations for correction. In recent years, the share of system audit and performance audit has increased considerably and with it the added value of internal audit work.

*Counselling* is the activity carried out by internal auditors, meant to add value and improve governance processes within the Ministry of National Defence, without internal auditors assuming managerial responsibilities. The counselling activities carried out by the Internal Audit Department and the subordinated territorial structures include the following types of missions: consultancy; facilitating the understanding; professional training and improvement.

The normative act regarding the internal public audit in the Ministry of National Defence also includes important references in the part of Methodological Norms, to the following aspects: General provisions; Organization and competence of the internal public audit; Independence and objectivity of the internal audit structure and of the internal auditors; Peculiarities regarding the framing of the internal audit structure and of the internal auditors; Competence and continuous professional training of internal auditors; The methodology for obtaining and maintaining the attestation certificate by the auditing staff; Evaluation, assurance and improvement of the quality of the public internal audit activity; Planning the public internal audit activity; Carrying out public internal audit missions; Insurance missions; Counselling missions; Missions for evaluating public internal audit activities; Glossary of terms and definitions; The objectives of the public internal audit activity; The procedure for carrying out the public internal audit activity; The general methodology for carrying out the insurance missions; Peculiarities regarding the organization and development of system audit missions within the Ministry of National Defence.



Of these components, we will approach in detail only the part related to the Evaluation, assurance and improvement of the quality of the internal public audit activity within the Ministry of National Defence.

The evaluation of the quality of the public internal audit activity follows the accordance between the organization and functioning of the public internal audit activity within the Ministry of National Defence and the normative framework specific to the field, as well as the analysis of the degree of fulfilment of the established objectives.

The evaluation of the quality of the internal public audit activity is based, mainly, on: the observance of the Norms regarding the exercise of the internal public audit activity and of the Code regarding the ethical conduct of the internal auditor; the adequacy of the Public Internal Audit Charter, of the internal audit rules and procedures, of the objectives, performance indicators and information system; the contribution of the internal public audit to the risk management, control and governance processes of the central structures, structures and forces subordinated to them from the Ministry of National Defence; the contribution of the internal public audit to the creation of an added value and to the improvement of the activities and missions of the central structures, structures and forces subordinated to them from the Ministry of National Defence.

The evaluations of the quality of the internal public audit activity, in the Ministry of National Defence, can be internal or external.

The internal evaluations are performed by the head of the Internal Audit Department or by the persons designated by him and consist of:

- periodic evaluations, performed by assessing the performances of the internal auditors, annually and on the occasion of the completion of the internal public audit mission, as well as by self-evaluations performed in the field of the internal control system;

- continuous evaluations, performed by monitoring the fulfilment of activities/ actions and supervising the internal public audit missions.

*External evaluations* are performed, at least once every 5 years, as follows:

- UCAAPI evaluates the internal public audit activity of the Internal Audit Department, from the point of view of compliance and performance;

- The Internal Audit Department evaluates, from the point of view of compliance and quality, the public internal audit activity carried out by the subordinated territorial structures and, as the case may be, at the level of autonomous utilities and national companies under the coordination/ authority of the Ministry of National Defence.

In order to improve the internal public audit activity, in accordance with the norms regarding the establishment of internal audit committees, elaborated by the Ministry of Public Finance and approved by the Government, at the level of the Ministry of National Defence, the Internal Audit Committee is established and operates, an advisory body, which aims to facilitate the relationship between the Internal Audit Department and the management of the Ministry of National Defence.

The internal audit committee of the Ministry of National Defence comprises 5 members, appointed by the Minister of National Defence, in compliance with the composition provided in art. 9 of Law no. 672/2002, republished, with subsequent amendments and completions.

Membership in the Internal Audit Committee of the Ministry of National Defence ceases in accordance with the express provisions of the Norms on the establishment of internal audit committees, approved by Government Decision no. 554/2014<sup>16</sup> for the approval of the Norms regarding the establishment of internal audit committees.

The internal audit committee of the Ministry of National Defence analyses its activity and evaluates its own efficiency by elaborating an annual activity report, which it sends to the Internal Audit Directorate, in order to process the information and include it in the Annual Report of the internal public audit activity in the Ministry of National Defence<sup>17</sup>.

The internal audit department had and is constantly concerned with the adoption of specific normative acts, in the form of orders of the Minister of Defence, starting from the national normative framework in the field, through which to customize and detail the provisions of acts adopted at national level, in line with the specificity and complexity of the activity of the entities that make up this ministry and which are subject to internal public audit missions. The most recent example in this respect is the Order of the Minister of National Defence no. M. 67/2014, which took over and customized the



provisions of GD no. 1086/2013 to the specifics of the ministry under analysis.

Of course, the activity of public internal audit is one subject to continuous transformations and modifications, under the impact of international standards, regulations of European and NATO authorities (bodies and alliances which we are part of) but also of national bodies in the field (UCAAPI for public audit and the Romanian Chamber of Financial Auditors - CAFR - Romanian Association of Internal Auditors - AAIR for internal audit of private entities), and the Ministry of National Defence and the Internal Audit Department must be permanently connected to the changes and modernizations generated by these authorities, under the effect of the evolution of the socio-economic and military mechanisms, currently and expectedly in the future, and to customize them in a more pronounced and appropriate way to the specifics of the army.

### Conclusions and proposals

In Romania, the process of introducing and modernizing the internal audit activity started later in the interwar period but also in the post-war period, due to a more modest economic evolution until the end of the Second World War (compared to countries like the USA, Great Britain, France, etc.), respectively due to the establishment of the communist regime for almost 45 years and after 1990, due to the prolonged transition, for a much longer time, from the centralized economy to the market economy;

The implementation of the bodies and rules of operation of the internal audit activity started in our country first in the public sector and then in the private one and accelerated in the vicinity, but especially after the accession of Romania, first to NATO (in 2004) and then to the European Union (in 2007), a process which is currently keeping pace with the constant changes taking place in this activity and profession at international and European level;

For the private environment, bodies such as the Romanian Chamber of Financial Auditors-CAFR and the Romanian Association of Internal Auditors-AAIR are established, whose missions include, among others, the regulation and coordination of internal audit in these entities;

The Ministry of National Defence operates internal public audit structures that apply national regulations in the field, with some customizations made through orders of the Minister of National Defence.

Following our research briefly presented through this article we could formulate the following proposals:

- Continuing the cooperation between the bodies that coordinate the public internal audit (UCAAPI) and those that regulate this type of audit for the private environment, in order to establish unique, unitary but customized regulations for the two business environments, so that there are no more acts or norms which create difficulties and ambiguities in understanding and carrying out such missions;
- Adopting a more effective takeover and more pronounced customization of the national regulations for internal audit in the public sector, by the competent bodies of the Ministry of National Defence (the relevant minister and the Internal Audit Directorate), for the more efficient and adequate performance of missions in this area of national security.

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3 [www.cafr.ro](http://www.cafr.ro)

4 [www.aair.ro](http://www.aair.ro)

5 *Official Gazette of Romania*, Part I, no. 548 of July 12, 2017.

6 *Law no. 162/2017*, Art. 20.

7 *Ibidem*.

8 *Ibidem*.

9 *Law no. 162/2017*, Art. 8.

10 [www.cafr.ro](http://www.cafr.ro)

11 *Official Gazette of Romania*, Part I, no. 559 of 14.07.2017.

12 *Order of the Minister of National Defence no. M. 67/2014*, Articles 7-8.

13 *Official Gazette of Romania*, Part I, no. 921 of 18.12.2014; The modification and completion of the Methodological Norms regarding the exercise of the internal public audit in the Ministry of National Defence.

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