

Vulnerabilities and Risks in Romanian Public Financial Accounting

Terinte Paula-Andreea
Cărăușu Dumitru-Nicușor
„Alexandru Ioan Cuza" University of Iași,
Faculty of Economics and Business Administration
paula.terinte@yahoo.ro
nicusor@live.com

Abstract

Internal audit plays an important contributive role in the economic credibility of an economy. By improving, the quality of internal audit and control in public institutions we can increase the efficiency of public spending and the whole economy in general. The aim of our paper is to identify the main vulnerabilities and risks in Romanian public sector after based upon the analysis performed by the Romanian Court of Accounts. Based upon the annual reports of the Romanian Court of Accounts from 2009 to 2016, we identify several issues and risks in the Romanian public sector, and especially in the local government financial accounting. In order to prevent more deviations and errors and to improve the quality of internal auditing and internal control systems, in the Romanian public sector, this paper proposes a series of measures in this matter.

Key words: audit, public sector, financial audit, court of accounts

J.E.L. classification: M42, M48, H83

1. Introduction

The efficiency of public sector spending in modern economies has been the key focus of policy makers, academics and government officials since the inception of the modern state. The amount of revenues collected and the efficiency of public spending in a country is dependent on many factors like economic development, economic cycle, population, political party orientation, type of tax system etc. Achieving an efficient tax system together with an adequate public spending mechanism involves not only an adequate budget planning and execution process, but also an efficient control mechanism. Thus, improving the efficiency in the public sectors needs to take into account not only internal and external factors, but also the quality of the external control mechanism.

One of the main drivers in reforming public spending in the European Union in general and in Romania in particular involves around improving the efficiency of internal and external control mechanisms in the public sector. By improving, the quality of control in public institutions we can increase the efficiency of public spending and the whole economy in general. An efficient public control mechanism can reduce the amount of fraud, corruption or any other illegal activities in the public sector, improving the quality of public services offered by local and central governments.

The quality and effectiveness of internal public audit (in the case of local public administration), the emerging risks encountered and the shortcomings of the public sector in Romania were examined by (Cioban et.al 2015) from annual reports of 2011 and 2012. They concluded with the idea that identifying the risks and removing them quickly and accurately represents an important factor for the efficiency of internal audit and good administration of the public incomes. Moreover they found that the shortcomings regarding “the internal public audit are due, to a large extent, to the faulty management of human resources”. They consider that an analysis with the staff can improve the audit quality and can strengthen the public organizational structure.

An analysis of the relationship, from various perspectives, between internal audit and management was made by (Munteanu, et al. 2010) in which they found some factors that may affect the efficiency of this relationship such as: "the managerial culture, deficient communication, legislative incoherency and also in some areas lack of regulations, the degree of adapting the audit system to the stage of the economic development, and they also motioned the insufficient academic debate for this topic".

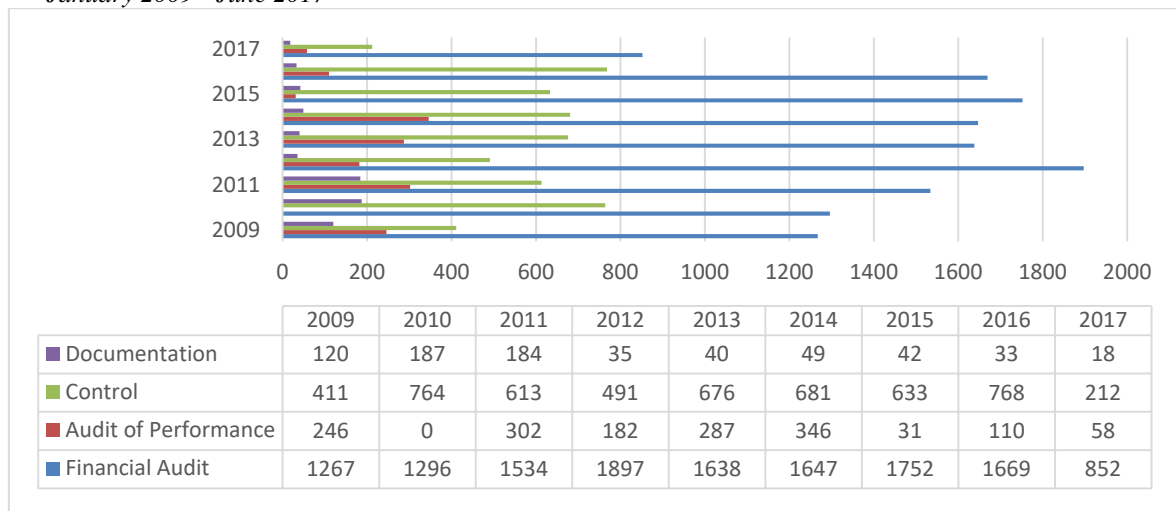
In Romania, the public sector has undergone numerous reforms and changes in the past 27 years due to transition process from the planned economy to market economy and ascension in the European Union. This process involved changes in the regulatory framework which improved the methods and mechanisms used in the Romanian public financial accounting. From the early stages of internal and external audit in the beginning of the 1990, to modern managerial control mechanism from 2010 that help to prevent and stop common types of fraud and other illegal activities. Thus, the aim of this paper is to identify, what are the main vulnerabilities and risks associated with the public financial accounting in Romania.

This paper analyses what are the major vulnerabilities in the Romanian public financial accounting according to data provided by the Romanian Court of Accounts. The rest of this paper is organized as follows: section 2 presents flaws in the financial accounting in the Romanian public sector while section 3 concludes.

2. Flaws in the financial accounting systems in the Romanian public sector

The Romanian Court of Accounts is an important factor in the search to improve the efficiency of public spending in the Romanian public sector. Each year, the external audit performed by the Romanian Court of Accounts indicates numerous issues involving the financial administration of public institutions in Romania. With the help of financial audit and performance audit missions, the efficiency of revenue collecting and public spending is thoroughly analyzed improving the efficiency of the entire Romanian public sector.

Figure no. 1. The evolution of types of control/audit performed by the Romanian Court of Accounts January 2009 - June 2017



Source: Own computations by the authors on data provided by the Romanian Court of Accounts

Data from figure no. 1 reveals that the most common type of control performed by the Romanian Court of Accounts is financial Audit in all the analyzed period. The prevalence of the financial audit missions derives from the need of certifying the annual financial statements in accordance with the legislation and procedures that are in place. Meanwhile, the lower prevalence of the performance audit missions derives from the lower focus on quantifying and determining the efficiency of public spending. The other types of control missions documentation and control are in conjuncture with performance and financial audit, thus they are less common.

Table no. 1 Types of errors found by the Romanian Court of Accounts

| Year | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--|------|-------|------|------|-------|-------|-------|-------|------|
| Drafting the budget and modifying the initial budget during the execution of the budget | 1438 | 1123 | 589 | 443 | 905 | 841 | 807 | 690 | 256 |
| The accuracy and the reality of the data reflected in the financial statements | 2309 | 1972 | 4358 | 4147 | 5364 | 4899 | 4672 | 4249 | 2248 |
| Organizing, implementing and maintaining internal / managerial control systems | 256 | 1920 | 3798 | 3181 | 2691 | 2310 | 1925 | 1654 | 725 |
| How to set, highlight and track the revenues of the consolidated general government budget | 750 | 2543 | 4661 | 4625 | 5454 | 5559 | 5478 | 4492 | 2133 |
| Quality of economic and financial management | 863 | 11253 | 8700 | 8461 | 11270 | 11920 | 12342 | 10085 | 4922 |
| Public procurement | 16 | 477 | 156 | 1696 | 1567 | 1678 | 1876 | 2243 | 1254 |
| Other violations | 65 | 1639 | 389 | 98 | 78 | 95 | 97 | 101 | 56 |

Source: Own computations by the authors on data provided by the Romanian Court of Accounts

The most common type of error found by the Romanian Court of Accounts from 2010 onwards relates to the poor quality of economic and financial management in the public sector, which relates to: illegal payments from the budget, payments of goods or services without a proper documentation or invoices, illegal salary rights, failures in establishing the required annual provisions etc. Other important types of errors found by the Romanian Court of Accounts relates to errors in setting and calculating the consolidated general government budget and the accuracy and reality of the annual financial statements. We also note that since the adoption of the SCM, there was an increase in the number of errors found in the managerial control systems in 2010-2012, while later the number declined indicating a higher degree of compliance to the new system.

Table no. 2. Types of Deviations from legality found following audit/control actions Romanian Court of Accounts (thou RON)

| No. | Year | Number of Cases | Additional Income | Illegal payments | Infringements in financial accounting | TOTAL |
|--------------|---------------|-----------------|-------------------|------------------|---------------------------------------|------------------|
| 1 | 2009 | 12257 | 717609 | 718267 | 41638787 | 43074663 |
| 2 | 2010 | 20927 | 1748390 | 727202 | 41874335 | 44349927 |
| 3 | 2011 | 19632 | 2411804 | 756020 | 38488447 | 41656271 |
| 4 | 2012 | 23809 | 2448003 | 1412257 | 54862984 | 58723244 |
| 5 | 2013 | 25836 | 2302850 | 1620600 | 27682400 | 31605850 |
| 6 | 2014 | 25529 | 2719658 | 2372439 | 33293276 | 38385373 |
| 7 | 2015 | 25224 | 3617614 | 1761119 | 22747297 | 28126030 |
| 8 | 2016 | 23514 | 1522276 | 1843222 | 29065418 | 32430916 |
| 9 | 2017 (sem. I) | 9406 | 608910 | 737289 | 11626166 | 12972365 |
| TOTAL | | 186134 | 18097114 | 11948415 | 301279109 | 331324639 |

Source: White Paper of Romanian Court of Accounts (Romanian Court of Accounts, 2017, p.501)

The high number of errors in the quality of economic and financial statements in the Romanian public sector mirrors in the total amount infringements found in financial accounting, which is the most important type of error found by the Romanian Court of Accounts. During 2009-2017 infringements in financial accounting, represent more than 80-90% of the total value of the errors found by the Romanian Court of Accounts. While these types of infringements do not mean actual losses from the local budget as they relate often relate to mismanagement of patrimony or

deviations regarding the application of the provisions, but they can also involve illegal payments from the state and local budget. The main, driver of these types of errors relates mostly to inadequate personal management procedures or the lack of a true internal control mechanisms in some public institutions. Meanwhile, errors in relation to addition income and illegal payments are actual losses from the local and state budgets. The main factors, than contribute to these types of errors are: erroneous setting of the amount of taxes and fees; lack of a true forecasting for the collected revenues; unlawful granting of tax incentives to pay taxes and duties; lack in personnel training and internal procedures in relation to public spending; flaws in procedures that relate to public procurement process; the frequent changes in legislation; misinterpretation of the legal provisions concerning the salaries of staff etc.

While the total value of the errors found by the Romanian Court of Accounts indicates major flaws in the internal management and control mechanism in the public sector appendices 1, 2 and 3 reveals what is the main cause of the issues. In all the analyzed period, the local and the state budgets are the main drivers of the total value of deviations from legality in the Romanian public sector. Therefore, the central government budget is the main driver for errors found in relation to lower revenues collected; the local budgets are responsible for illegal spending, while for infringements in financial accounting the two budgets are similar.

4. Conclusions

We argue that local public administration the internal control and audit systems do not work at the desired audit parameters, the deviations and errors found by the audit activity in the period analysed is at very high levels. The activities of the internal audit in some public institution are formal and inefficient or insufficiently rigorous as there is a lack of significant coverage in certain areas. Thus, the external audit performed by the Court of Accounts reveals several medium and high risks. Moreover in the local public administration, the leaders don't manifest an interest in improving the internal audit quality at this level. There is a lack of training staff and there are malfunctioning processes in the organization of the internal audit in public institutions. This exerts a negative impact on the efficiency of the internal audit and control systems, as they cannot function to a level that ensures an efficient management of the public funds and budgets revenues in conditions of legality, regularity and efficiency.

If this deviations and errors are not corrected they can have a negative impact on the effectiveness, correct use and founding the public financial resources and can also lead to loss of patrimony, the lack in some public budgets of some important income and even acts of corruption.

In order to prevent more deviations and errors we consider that there is a need in the Romanian public sector of implementing a training courses, professional training for the staff regarding the internal audit and internal control activity. The public institution must pay more attention regarding the internal control systems and internal auditing in order to arrange the necessary measures to ensure the internal audit function is more independent and objective in the process of evaluation of the management system in a public entity.

5. References

- Cioban (Lucan), A.N, Hlaciuca, E., Zaiceanua, A.M., 2015, The impact and results of the internal audit activity exercised in the public sector in Romania., *Emerging Markets Queries in Finance and Business*, *Procedia Economics and Finance* 32, pp.394 – 399
- Munteanu, V., Zuca, M., Țiță, A., 2010, Internal audit regulations in Romania And their convergence to European exigencies, *Annales Universitatis Apulensis Series Oeconomica*, 12(1), pp.267-273.
- Romanian Court of Accounts, Annual public reports 2009-2016, <http://www.curteadeconturi.ro/Publicatii.aspx?niv1=1>

*Appendices 1: Additional income calculated between January 2009-June 2017,
]for budgets 2008-2016 (thou RON)*

| Year | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|--------|---------|---------|--------|---------|---------|---------|---------|--------|
| State budget | 263865 | 1140076 | 1861130 | 716609 | 1740450 | 2047060 | 2846188 | 1046837 | 418735 |
| State social security budget | 11254 | 23461 | 25035 | 65646 | 19600 | 33842 | 17424 | 2456 | 98 |
| Local budgets | 317299 | 156315 | 269041 | 212716 | 430400 | 374936 | 312661 | 285139 | 114056 |
| The unemployment insurance budget | 138 | 175641 | 13575 | 10359 | 0 | 3618 | 544 | 742 | 297 |
| Budget of the national health insurance found | 24278 | 85679 | 172142 | 637413 | 48700 | 88997 | 11243 | 2086 | 834 |
| Budget of the state treasury | 0 | 0 | 0 | 0 | 0 | 84 | 0 | 832 | 333 |
| Budget of public institutions financed entirely from own revenues | 9202 | 3685 | 10977 | 7337 | 5700 | 23439 | 37224 | 24542 | 9817 |
| Own revenues of public institutions | 3643 | 57281 | 35094 | 160394 | 24300 | 91249 | 181242 | 35373 | 14149 |
| Revenues and expenses of economic agents | 87929 | 106252 | 23751 | 637413 | 33700 | 56432 | 207405 | 124269 | 49.708 |

Source: Own computations by the authors on data provided by the Romanian Court of Accounts

*Appendices 2: Illegal payments calculated between January 2009-June 2017,
for budgets 2008-2016 (thou RON)*

| Year | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|--------|--------|--------|---------|--------|--------|--------|--------|--------|
| State budget | 203939 | 509847 | 360062 | 1462305 | 203100 | 370621 | 219892 | 109373 | 136682 |
| State social security budget | 982 | 4138 | 27341 | 10798 | 7000 | 5944 | 14627 | 8602 | 419 |
| Local budgets | 346796 | 866990 | 699824 | 590706 | 625200 | 513192 | 356117 | 400229 | 185474 |
| The unemployment insurance budget | 1570 | 3925 | 8815 | 9726 | 5700 | 1946 | 1038 | 1341 | 345 |
| Budget of the national health insurance found | 43240 | 108101 | 16472 | 21578 | 39800 | 184351 | 21202 | 4757 | 1437 |
| Budget of the state treasury | 2635 | 6587 | 41193 | 11193 | 222500 | 38483 | 21 | 1714 | 111842 |
| Budget of public institutions financed entirely from own revenues | 5104 | 12760 | 2161 | 26946 | 12500 | 99456 | 4542 | 6386 | 2324 |
| Own revenues of public institutions | 14149 | 29933 | 90607 | 14028 | 28700 | 13904 | 20634 | 18713 | 12427 |
| Revenues and expenses of economic agents | 120375 | 300937 | 504700 | 225159 | 475300 | 184351 | 116828 | 176086 | 267317 |

Source: Own computations by the authors on data provided by the Romanian Court of Accounts

*Appendices 2: Infringements in financial accounting calculated between January 2009-June 2017,
for budgets 2008-2016 (thou RON)*

| Year | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|----------|----------|----------|----------|----------|----------|---------|----------|---------|
| State budget | 20283042 | 12543958 | 12094262 | 30299727 | 15707000 | 21581301 | 9572548 | 15049401 | 6019760 |
| State social security budget | 129471 | 68374 | 389533 | 176431 | 358700 | 49867 | 275676 | 243230 | 97344 |
| Local budgets | 10546200 | 12137331 | 20982504 | 17152107 | 8287900 | 6591893 | 4507077 | 5028027 | 2011211 |
| The unemployment insurance budget | 4866 | 219133 | 152931 | 326698 | 443900 | 59539 | 176137 | 77662 | 31065 |
| Budget of the national health insurance found | 758576 | 118798 | 1227327 | 1943891 | 773500 | 2073704 | 94886 | 42427 | 16971 |
| Budget of the state treasury | | 61405 | 157721 | 270746 | 28000 | 146898 | 2148 | 15.066 | 6026 |
| Budget of public institutions financed entirely from own revenues | 1345915 | 280609 | 340434 | 893003 | 97800 | 298633 | 67918 | 37628 | 15051 |
| Own revenues of public institutions | 176297 | 367585 | 563136 | 1756481 | 736500 | 851064 | 1022234 | 650714 | 260286 |
| Revenues and expenses of economic agents | 8392998 | 16077142 | 2580115 | 184351 | 475300 | 1640282 | 7020807 | 7920618 | 3168247 |

Source: Own computations by the authors on data provided by the Romanian Court of Accounts