

Vulnerabilities and Risks in Romanian Public Financial Accounting

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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".

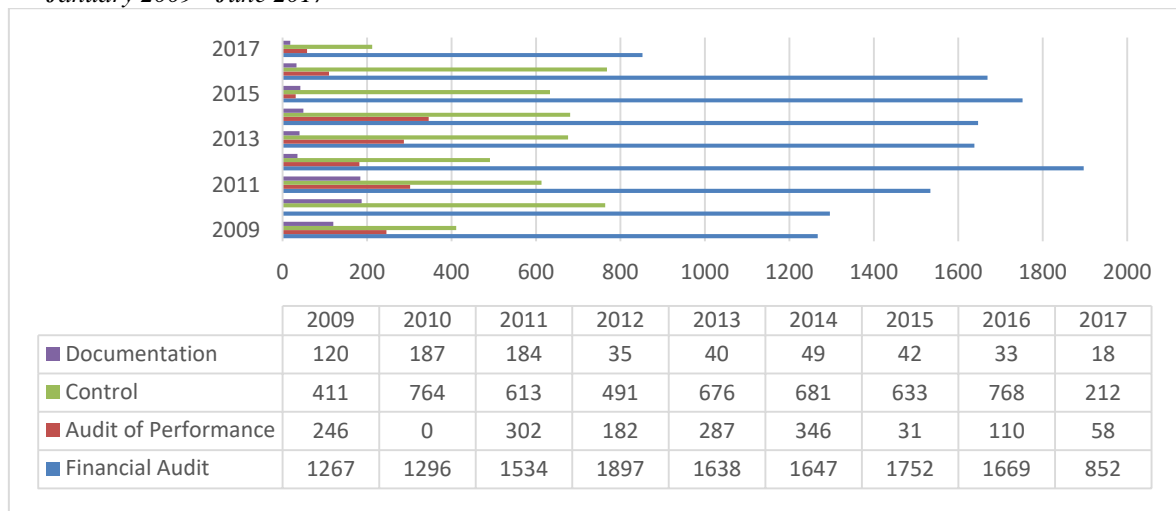
In Romania, the public sector has undergone numerous reforms and changes in the past 27 years due to transition process from the planned economy to market economy and ascension in the European Union. This process involved changes in the regulatory framework which improved the methods and mechanisms used 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

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*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