

Updating and Developing the Normative Framework for Strengthening the Internal Public Audit Function in State Institutions and Companies

Nicoleta Asaloş

“Ovidius” University of Constanta, Faculty of Economic Sciences, Romania

nasalos20@gmail.com

Ionel Bostan

“Stefan cel Mare” University of Suceava, Doctoral School of Economics, Romania

ionel_bostan@yahoo.com

Abstract

In Romania, nearly 14,000 institutions and various state entities are subject to internal public audit. Among these, about 90% belong to local public administration. A recent report by the Romanian Ministry of Finance categorizes the auditable entities as follows: 21 ministries; 1,456 units subordinate to the ministries; 45 autonomous administrative authorities (including those with special reporting formats); 173 units subordinate to autonomous administrative authorities; 982 local administrative units and 5,713 entities subordinate to local administrative units. The legislation required internal public audit departments to carry out specific missions on the entity's activities at least once every three years; subsequently, a new amendment extends this period to four years. Our approach focuses not only on the findings of the internal public audit structures within the institutions and state-owned companies in Romania, reported on established objectives, but also on some legislative changes reflecting the updating and development of the regulatory framework to strengthen the internal public audit function.

Key words: normative framework, internal public audit, public authorities, audit structures

J.E.L. classification: D73, H83, H89, M42, M48

1. Introduction

Establishing the activity of public audit within the entities of the Romanian state, through Law no. 672 from 2002, aimed for better management of the formation and use of public funds, as well as optimal administration of public assets. Today, after more than two decades since its legislation, we observe that the situation is far from being considered as evolving strictly based on the mentioned norm. Even though internal public audit (IPA) has been assigned the purpose of „assisting the public entity in achieving its objectives (...), assessing and improving the efficiency and effectiveness of risk management, control, and governance processes.” (RP, 2002), in a considerable number of institutions, the audit function hasn't even been established (Bostan, 2022).

Overall, the results are not as expected, even though, in accordance with Order no. 600 dated April 20, 2018, regarding the approval of the Internal Managerial Control Code for public entities (SGG, 2018), these entities are required to establish internal public audit departments (or ensure access to competent audit capacity) with the aim of improving management through assurance and advisory activities (Standard 16). The major requirements in this context stipulate that (SGG, 2018): „The internal auditor concludes their actions through internal audit reports, which encompass the general framework, objectives, findings, conclusions, and recommendations.” Simultaneously, „The head of the public entity takes necessary measures considering the recommendations presented in the internal audit reports.” Additionally, auditors in this category, among other obligations they have, „must enhance their knowledge, skills, and values through continuous professional development and ensure the compatibility of their training with the type and nature of internal audit missions that need to be conducted.”

Obviously, in this regard, there are other requirements as well (Figure 1).

Figure no. 1. General requirements of Standard 16 - Internal Audit



Source: Authors' elaboration based on (SGG, 2018)

Against this backdrop, our work addresses the issue of internal public audit in terms of its exercise, existing challenges, and legislative perspective - emphasizing the latest adopted norms. We observe that, through proper implementation, these norms can lead to strengthening the function of internal audit in both central and local public entities and to better monitoring of the establishment and use of public resources.

Simultaneously, we pay attention, in connection with the aforementioned aspects, to the findings derived from the most recent report by the Romanian Ministry of Finance (2022) regarding internal public audit missions within the authorities of central and local public administration.

In this context, we articulate specific criticisms, draw certain conclusions, but most importantly, endeavor to suggest proposals to improve the situation in the analyzed field.

2. Theoretical background

Over time, it has been demonstrated that internal public audit is a vital function in ensuring transparency, control, and efficiency within organizations, significantly contributing to their success and sustainability. Several works on the exercise of public audit in Romania adequately address the issue at hand (Bostan & Radu, 2003; Dascălu & Nicolae, 2006; Munteanu, 2010; Trincu-Drăgușin & Ștefănescu, 2020; Ionescu & Nica, 2021), covering aspects related to history, norms, institutions, standards, or techniques/procedures for conducting specific missions.

Based on the literature, we note that this type of audit holds particular importance in ensuring healthy and efficient corporate governance (Costea, 2005; Calotă & Vânătoru, 2009; Dascălu et al., 2016; Ștefănescu & Trincu-Drăgușin, 2020), its significance being evident in several ways. Thus, internal public audit helps organizations comply with legal norms and current regulations, evaluating and monitoring whether activities align with established policies, regulations, and procedures.

By continuously evaluating and monitoring processes and internal controls, internal audit contributes to preventing and detecting fraud or errors in a timely manner. Additionally, by identifying deficiencies or inefficiencies in processes, it aids in improving operational efficiency and optimizing resources and processes. Moreover, internal audit evaluates operational, financial, and compliance risks, recommending and implementing management measures to minimize their negative impact on the organization.

Providing objective information and assessments of the organization's processes and activities enables managers to make optimal decisions, making internal public audit an important support in achieving organizational objectives. On the other hand, it provides a framework for evaluating how

the organization achieves its established objectives and recommends ways to improve performance and strategic direction. Equally important is the considerable increase in stakeholders' trust, as internal public audit provides assurances to shareholders, investors, or the general public that the organization effectively manages risks and adheres to established standards and regulations.

3. Research methodology

Our investigation into this topic ('Updating and developing the normative framework for strengthening the internal public audit function in state institutions and companies') is based on researching various works in the field of internal public audit, the current normative framework applicable to internal public audit within state institutions and companies (laws and general/specific regulations regarding the exercise of internal public audit activities).

We delve into reports from specific institutions (Ministry of Finance (UCAAPI/ Central Harmonization Unit for Internal Public Audit), documents related to the development/implementation of policies/programs/strategies for government sector audits, as well as official statistics, etc.

In our endeavor, we found useful the explanatory notes and justifications of certain normative acts relevant to the addressed field, available on the websites of the Romanian Government and Parliament.

4. Findings

4.1. Internal Public Audit in Romania: From Specific Norms to Effective Implementation

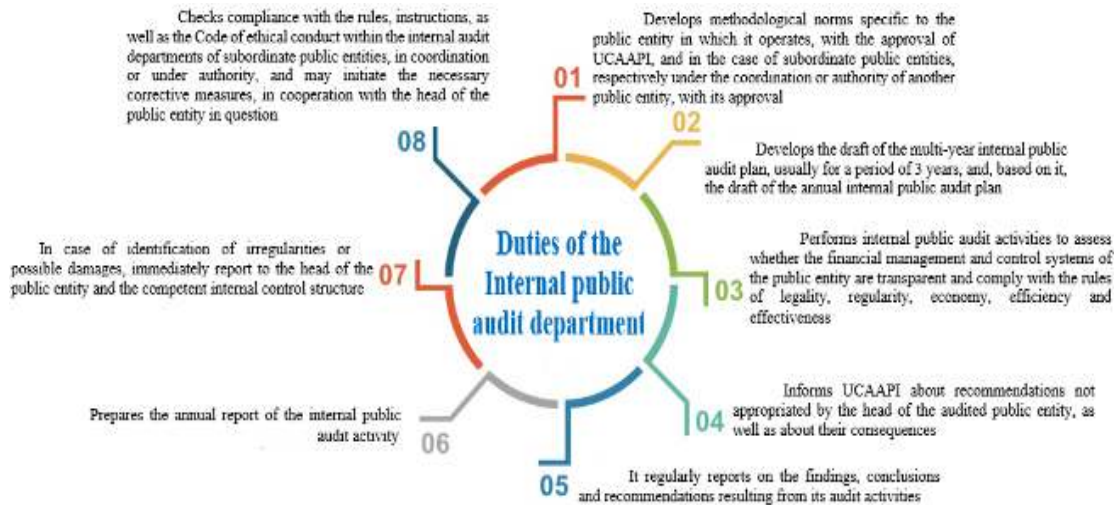
In the case of all public entities in Romania, their leaders have a legal obligation to ensure the organizational and functional framework necessary for conducting internal public audit activities. Regarding the creation of functional departments for internal public audit within state institutions and companies, specifically under the direct subordination of the leader/manager or the collective/cooperative management body, legal norms are imperative. In terms of size, „The Internal Public Audit Department is sized, in terms of the number of internal auditors, based on the volume of activity, the size and complexity of the entity and the entities under the authority, coordination, or supervision of the public entity, taking into account the duties and competencies provided in its establishment, organization, and operation acts, considering the risks associated with the activities carried out by the public entity.” (RP, 2002).

Internal public audit - manifested as system audit, performance audit, regularity audit, or information technology audit – „is conducted on all activities carried out in a public entity, at least once every 4 years, including activities of entities under its authority, coordination, or supervision, and the prioritization of internal audit missions is based on risk analysis and requests from the Court of Accounts.” (RP, 2002). The regulated duties of the internal public audit department are depicted using Figure 2.

For a minimal understanding of how internal public audit is conducted in Romania, we introduce certain data and information contained in the Report on the Activity of Internal Public Audit in the public sector in Romania in 2022 (MF, 2023). According to this report, within the central and local public administrations, regardless of the type of credit ordinator (primary, secondary, or tertiary), there were reported to be 13,802 institutions obligated to maintain a functional internal public audit structure.

Concerning the functioning of internal public audit structures, they are categorized as follows: 10,784 entities have established internal public audit, and it is operational, representing an operational rate of internal audit of approximately 78%. Among 3,018 entities, internal public audit is not operational (about 22%): 1,630 entities have established internal public audit but it is not operational; 1,388 entities have not established internal public audit, thus, it is not operational.

Figure no. 2. Duties of the internal public audit department



Source: Author's elaboration based on (SGG, 2018)

Internal public audit faces multiple issues that hinder its proper functioning. These include limited resources, both human and financial, which are insufficient to ensure an efficient internal public audit structure. Additionally, there is a lack of interest from some entities/managers in organizing competitions for filling vacant positions of internal public auditors, and when such competitions were organized, they did not result in filling the positions.

According to the previously mentioned source, in public administration, although approximately 90% of entities have established an internal public audit structure, only 78% of these are effectively operational. In 2022, the reporting of internal public audit activities had significant deficiencies, as 3,034 entities did not compile appropriate annual reports. Specifically, 16 entities did not compile annual reports even though the internal public audit structure was functional; 1,630 entities did not provide reports because the internal public audit structure was not functional, and 1,388 entities did not prepare reports because internal audit was not established. Furthermore, the independence of internal audit was compromised in numerous situations. In central and local public administration, 32 cases were identified that could affect the independence of internal public audit structures. These include one case where internal public audit was not subordinate to the entity's management, 27 cases where approval was missing in the appointment or dismissal of internal auditors, and 4 cases where approval was missing in the appointment or dismissal of internal public audit structure management.

Additionally, in assessing the objectivity of internal public auditors, 44 cases were found where internal public audit was involved in auditing activities, but there were also 6 cases where the independence statement was not properly completed in the same reporting period.

Recently, internal public audit structures in public administration have established the necessary human resources for sizing the internal public audit function in accordance with applicable legal frameworks (Table 1).

Table no. 1. The need for human resources to size the internal public audit function in accordance with the applicable legal framework

Year 2022	Filled positions exercising internal audit duties	Positions needed to perform internal audit duties	Deficit (-) / Surplus (+)
Ministries and Autonomous Administrative Authorities	431	587	- 156
Units subordinate to ministries and autonomous administrative authorities	1,054	1,764	- 710
Local Administrative Units through Associative Structures	405	561	- 156
Local Administrative Units through Regional Directorates of Public Finance	552	1,084	- 482
Units Subordinate to Local Administrative Units through Regional Directorates of Public Finance	343	552	- 209
Total	2,785	4,498	- 1,713

Source: (MF, 2023)

Studying the data presented in Table 1, we can conclude that the 2,785 filled positions as of December 31, 2022, are not sufficient for the proper conduct of internal public audit activities, with the total number of necessary filled positions to perform internal public audit activities being 4,498.

Despite the existing difficulties, in 2022, within public administration, a total of 237 irregularities were identified and reported (Table 2), most of which were in the financial accounting and public procurement domains.

Table no. 2. Trends regarding irregularities in public administration

Years	2019	2020	2021	2022
Number of identified irregularities	201	316	527	237
Budgetary domain	7	24	39	13
Financial accounting domain	63	80	116	40
Public procurement domain	39	29	48	13
Human resources domain	7	28	20	40
IT domain	2	7	4	8
Legal domain	2	7	23	11
European funds domain	33	4	1	0
Specific functions domain	17	78	155	85
SCIM domain	14	7	29	11
Other domains	17	52	92	16

Source: (MF, 2023)

To address the identified and reported irregularities, recommendations were formulated, most of which were adopted by the audited entities (with few exceptions), some of these recommendations have already been implemented, while others partially implemented.

Beyond what's presented here, in our opinion, the most serious issue is the non-establishment of this function. It is true, the situation stems from various quite real causes that have led to the absence of internal public audit activity in hundreds of institutions to this day. Among these: insufficient financial resources, existing service provision contracts (for internal public audit activities) in progress, abolishment of specific departments during institutional restructuring, followed by the redistribution of positions to other structures within the entity. Notably, there have been instances where internal auditor positions were taken over and transformed into advisor positions by the main credit ordinator.

4.2. Recent legislative changes aimed at strengthening the internal public audit function

As mentioned in the preceding section, after more than two decades since its legislation, we observe that the internal public audit activity is far from strictly evolving based on existing legal norms. In our view, the most significant factor has been the lack of enforcement of penalties for not organizing internal audits, although this situation falls under the scope of Article 23(a) of Law 672/2002, constituting an offense. The level of the fine is not negligible, ranging from 3,000 to 5,000 lei.

The explanation for not applying sanctions can be linked to the disregard for Article 24 of the same law, which obliges the main budgetary credit ordainers (ministers, other heads of central institutions, etc.) to empower their representatives to ascertain and impose sanctions. Even the Ministry of Finance only issued an order in this regard in 2020 (OMFP no. 7/2020). Therefore, it can be argued that overall, the difficulties we mentioned are also due to the legal framework. Although Law no. 672/2002 on internal public audit has been amended several times since its inception, it was unable - for a long period - to strengthen the regulatory system. A major text revision, considering best practices from other countries, only occurred in the latter part of 2022, but its effects could not be reflected in the results of the respective year's internal public audit activity (due to the delayed entry into force).

This concerns Government Ordinance no. 29 of August 26, 2022, amending and supplementing Law no. 672/2002 on internal public audit (RG, 2022), which brings 22 amendments and additions to the basic law. The initiator (Ministry of Finance) describes the anticipated benefits and costs following the enactment of this normative act as follows: „The implementation of the provisions of the draft normative act leads to: (i) consolidating the internal audit function in public entities and better tracking the formation and use of public resources; (ii) improving the quality in its exercise; (iii) strengthening the internal public audit departments within the associative structures of local public administration, which ensure the internal audit function in a cooperative system.” (MF, 2022).

The amendments and completions of the law cover various aspects ranging from defining certain terms (the organizational and functional framework of internal public audit activities, certification, unimplemented recommendations) to certifying the associative structures of local public administration to ensure the internal public audit function in a cooperative system, etc. Presently, the organizational and functional framework of internal public audit activities has the following significance: „The organization and ensuring the functioning of internal public audit through the approval in the organizational chart of an internal public audit department with at least two full-time internal auditors and providing the necessary financial resources for operation or ensuring the internal public audit function by the higher hierarchical body or adhering to the cooperation system for the internal public audit function.” (RG, 2022; MF, 2022).

This definition is important primarily because, for a long time, due to uncertainties surrounding this concept, the normative act (Law no. 672/2002) couldn't fulfill its coercive function. Article 23(a) of Law no. 672/2002 stipulates that „violation of the obligation to ensure the organizational and functional framework necessary for the conduct of internal public audit activities, according to the provisions of Article 11(a) of the law”, constitutes an offense (fines range from 3,000 to 5,000 lei). The obligation to ensure this framework lies with the head of the public institution or, in the case of a public entity, the collective governing body. However, due to the lack of an exact definition of the term „organizational and functional framework of internal public audit activities”, significant difficulties arose in applying the offense prescribed in Article 23, item a) of Law no. 672/2002, risking annulment of sanctions due to potential challenges.

Precisely, the major ambiguity in determining the offense (according to the initiator) was whether „the organizational and functional framework involves establishing a department with a minimum of two approved and budgeted full-time internal auditor positions (Article 2, item f) or if this also includes sizing the internal public audit department based on the volume of activities and associated risks (Article 12, paragraph (4)).” (RG, 2022; MF, 2022). Furthermore, explanations from public entities indicated difficulties in organizing internal public audit, often attributed to the insufficiently defined and explained notion in the legal norms.

Now, it is very explicitly stated (RG, 2022): (i) „The internal public audit department consists of a minimum of two full-time internal auditor positions, with the necessary financial resources for occupying the prescribed positions and operating the department.” (if „the higher hierarchical body does not ensure the internal public audit function or through adherence to the cooperative system for ensuring the internal public audit function.”); (ii) „Internal public audit is conducted on all activities carried out within a public entity, at least once every 4 years, including the activities of entities subordinate, coordinated, or under its authority, as applicable, and the prioritization of internal audit missions is based on risk analysis and requests from the Romanian Court of Accounts.” (Exception: „when developing the multiannual plan, the head of the entity or the collective governing body can approve an extension beyond the 4-year term, by a maximum of one year, upon the reasoned proposal of the head of the internal public audit department.”).

The text of the normative framework regarding Offenses and Sanctions has a new content, reflected in Figure 3.

Figure no. 3. Contraventions and sanctions for violating the internal public audit regime

<p>It constitutes a misdeemeanor and is punishable by a fine from 3,000 lei to 5,000 lei:</p> <ul style="list-style-type: none">a) violation of the obligation to ensure the organizational and functional framework necessary for carrying out the internal public audit activity, according to the provisions of art. 11 lit. a);b) violation of the obligation to develop internal public audit rules specific to the public entity, as well as not presenting them for approval, according to the provisions of art. 13 lit. a);c) violation of the obligation to prepare the draft internal public audit plan, according to the provisions of art. 13 lit. b);d) the refusal of the executive or management staff, involved in the audited activity, to present the requested documents during the performance of internal public audit missions, in accordance with the provisions of art. 18 para. (3);e) non-compliance with the provisions regarding the appointment/dismissal of the head of the internal public audit department, respectively the appointment/revocation of internal auditors, in accordance with the provisions of art. 12 para. (2), respectively of art. 20 para. (2);f) non-elaboration by the head of the internal public audit department of the annual report of the internal public audit activity, by March 15 of the following year for the completed year;g) non-approval by the persons mentioned in art. 19 para. (4), within 45 working days, of the internal public audit report, according to art. 19 para. (4¹).	<p>Contraventions and sanctions for violating the internal public audit regime</p>	<p>Finding contraventions and applying sanctions are done as follows:</p> <ul style="list-style-type: none">a) by the authorized representatives of the Ministry of Finance, for the contraventions provided for in art. 23 lit. b), c) and e), found in public entities where the manager exercises the capacity of principal credit orderer;b) by the authorized representatives of the higher hierarchical body, at the level of subordinate public entities, in coordination or under authority, for the contraventions provided for in art. 23 lit. b), c) and e);c) by the representatives authorized by the head of the public entity, for the contraventions provided for in art. 23 lit. d);d) by representatives of the Court of Accounts for the contraventions provided for in art. 23 lit. a), f) and g).
---	---	--

Source: Articles 23 and 24 of Law no. 672/2002, republished, following the entry into force of Government Ordinance no. 29/2022

In our opinion, once Government Ordinance no. 29 of August 26, 2022, amending and completing Law no. 672/2002 on internal public audit (RG, 2022) has been adopted, it visibly sets the groundwork for changes aimed at ensuring better management of public funds. By properly implementing the new regulations regarding internal public audit, managers could become more accountable, and the activities of the local administrative units could become more transparent - both concerning the establishment, collection, and utilization of budgetary resources, as well as the management of public assets.

5. Conclusions

The paper provides a concise overview of the public audit activity within the entities of the Romanian state and finds that overall, the results are not as expected, even though, in accordance with national standards, these entities are required to establish internal public audit departments (or ensure access to competent audit capacities) aimed at improving management through assurance and advisory activities. Difficulties are also attributed to the legal framework, with Law no. 672/2002 on internal public audit being incapable of consolidating the regulatory system. A major text revision, considering best practices from other states, only occurred in the latter part of 2022.

The implementation of the new provisions, while aiming to improve the functioning of internal audits in public institutions and enhance their quality, acts in a manner emphasizing coercive measures. These changes introduced new contraventions according to Law no. 672/2002, reissued, and amended with fines ranging from 3,000 to 5,000 lei. Among the established contraventions are failure to review internal public audit reports within 45 days of receipt by the public entity's management and the non-preparation of the annual report on the entity's internal public audit activity.

We believe that in the long term, approaches based on coercive measures are not the most effective, and greater attention should be given to adequate motivation and enhancing the professional training of all personnel involved in public audit activities.

Nevertheless, we believe that recent legislative changes aimed at strengthening the internal public audit function can generate significant social impact. These contribute to increasing transparency in the use of public funds and in managing public assets. Moreover, they are expected to improve the quality of evaluating and monitoring the establishment and utilization of public resources by the local administrative units.

Regarding the research limitations, beyond the descriptive nature of our work, it is important to note that the recent legislative changes aimed at consolidating the internal public audit function, to which we refer, only occurred in the latter part of 2022. Consequently, the effects of these changes could not be reflected in the results of the respective year's internal public audit activity (due to the delayed implementation), necessitating updated analyses on the internal public audit activity in the Romanian public sector in the following years.

6. References

- Bostan, I., Radu, P. 2003. *Controlul financiar și auditul intern la instituțiile publice [Financial control and internal audit at public institutions]*. Iasi: Sedcom Libris Publishing House
- Calotă, G., & Vânătoru, S. 2009. The implementation of the internal audit in the public sector from Romania. *Annals of „Constantin Brâncuși” University, Târgu Jiu, Economics Series*, No. 3, pp. 377-390.
- Costea, I.M. 2005. Adaptarea instituției auditului public în România la sistemul comunitar [Adaptation of the public audit institution in Romania to the community system]. *Analele științifice ale Universității „Al. I. Cuza” Iași*, Tomul LI, Științe Juridice, 2005, 157-165
- Dascălu, E.D., & Nicolae, F. 2006. *Auditul intern în instituțiile publice publice [Internal audit in public institutions]*. Bucharest: Economica Publishing House
- Dascălu, E.D., Marcu, N., & Hurjui, I. 2016. Performance Management and Monitoring of Internal Audit for the Public Sector in Romania. *Amfiteatru Economic* 18(43), pp. 691-705.
- Ionescu, L., & Nica, D. 2021. *Audit public intern [Internal public audit]*. Bucharest: “Romania de Maine” Foundation Publishing House
- MF/Ministerul finanțelor/Unitatea Centrală de Armonizare pentru Auditul public intern. 2023. *Raportul privind activitatea de audit public intern din sectorul public din România, în anul 2022 [The report on the internal public audit activity in the public sector in Romania, in 2022]*. Available at: <https://mfinante.gov.ro/documents/35673/5090618/Raportdeauditannualnational2022.pdf> [Accessed on October 17, 2023].
- MF. 2022. *Notă de fundamentare la Proiectul OG pentru modificarea și completarea Legii nr. 672/2002 privind auditul public intern [Substantiation note to the OG Project for the amendment and completion of Law no. 672/2002 regarding the internal public audit]*. Available at: https://mfinante.gov.ro/documents/35673/5553347/NFProiectOGMODIFL672_18072022.pdf [Accessed on October 18, 2023].
- Munteanu, V. 2010. *Auditul intern la întreprinderi și instituții publice [Internal audit at companies and public institutions]*. Bucharest: Wolters Kluwer Publishing House
- RG/Romanian Government. 2022. *Ordonanța Guvernului României nr. 29 pentru modificarea și completarea Legii nr. 672/2002 privind auditul public intern [Ordinance of the Government of Romania no. 29 for the amendment and completion of Law no. 672/2002 regarding the internal public audit]*. Available at: <https://legislatie.just.ro/Public/DetaliiDocumentAfis/258697> [Accessed on October 19, 2023].
- RP/Romanian Parliament. 2002. *Legea no. 672/2002, republicată, privind auditul public intern [Law no. 672/2002, republished, regarding the internal public audit]*. [online]. Available at: <https://legislatie.just.ro/Public/DetaliiDocument/40929> [Accessed on October 13, 2023].

- SGG/Secretariatul General al Guvernului, 2018. *Ordinul nr. 600 privind aprobarea Codului controlului intern managerial al entităților publice [Order no. 600 regarding the approval of the Code of Internal Managerial Control of Public Entities]*. Available at: <https://legislatie.just.ro/Public/DetaliiDocument/200317> [Accessed on October 19, 2023].
- Ștefănescu, A., & Trincu-Drăgușin, C.-P. 2020. Performance audit in the vision of public sector management. The case of Romania. *Accounting and Management Information Systems*, Vol. 19, Nr. 4, pp. 778-798, 2020. <https://doi.org/10.24818/jamis.2020.04007>
- Trincu-Drăgușin, C.-P., & Ștefănescu, A. 2020. The External Public Audit in the Member States of the European Union: between Standard Typology and Diversity. *Audit Financiar*, Vol. XVIII, no. 3(159)/2020, pp. 555-567. <https://doi.org/10.20869/AUDITF/2020/159/019>