

INTERNAL AUDIT AND RISK MANAGEMENT

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ABSTRACT

Maybe we have never spoken in Romania at such a high level about an activity which for the western internal auditors represents a subjects that caught attention long time ago, and which is very useful in their activities concerning internal audit activities. We are talking about risk management.

Keywords: *risk Management, internal audit, implementation of risk management an internal audit in Romania.*

1. INTRODUCTION

Actually it is very popular in our days to name an activity that involves a decisional element and a group of specialists hired to solve certain problems "Management of X activity".

In this context, we plan to treat this subject with great openness, in a simple manner, in everybody's language. Those who work in this field must permanently take into account their work ethic, approaching every goal of their mission with great common sense (as the western auditors like to say).

We will try to find or to develop in this article a way of approaching this topic that may be introduced at any time in the internal audit plan of an organization.

The ups and downs that take place in this period of time in the political, legislative and computational fields, in the market demands, quality of service or products, reputation problems and the dynamic in general of the activities that require management at a very high level, forced people to discuss and to analyse new methods and instruments that can create a system which can predict dysfunctions that may appear in the process of fulfilling the objectives of the organization.

After brainstorming these issues, it is expected that the management's ability to monitor and to evaluate the risks that their activity implies will increase and they will succeed to take the most efficient measures that will keep their activity under control.

For the companies or organization that implemented in their activity the Risk Management, things may go well, but what happens to those that are open to such conceptions, take into account implementing the Risk Management in their work and the internal auditor wants to give a helping hand?

Taking as an example the structure of document A, under procedure P 08 contained by OMF no. 38/2003 for the approval of the general norms regarding the exercise of the public internal audit activity, we should try to see, at least from a theoretical point of view, how this type of document would look like. We will present below an example possibly edited in the case of an internal audit mission that would have the topic "Guidance given to the internal audit management for the risk management implementation activity within an organization".

2. THE PROBLEM

The specific activities concerning management risks and the opportunity of organizing and implementing them in the perspective of the activities carried out by the organization.

3. OBSERVATIONS

In the current period, taking into account the context of the general principles of good practice, internal control is seen as a management function and not as a verification operation.

Through the control function, management discovers the deviations of the results from the objectives, analyses the causes that determined them and provides the necessary corrective or preventive measures.

In order to assimilate the best practice in this field, the management of an organization must have the following types of objectives:

- the full acceptance of responsibility for internal control;
- Increased monitoring of internal control and promoting communication about internal control;
- improving the link between internal control, strategic goals of the organization and associated risks;
- increasing the involvement of the organization's management in internal control;
- increasing commitment in standards of integrity, internal management and control and ethical behavior;
- completing the role and responsibilities of the specialty structures that have responsibilities in controlling, evaluating and auditing the activities of the organization.

Within an organization, there must be concerns about the effective implementation of the coordination, monitoring and supervision tasks foreseen for people with leadership positions in order to achieve a better control of the activities.

There are services which, because of their tasks and attributions, carry out risk analysis activities on specific issues, but at a local level.

Within the other services involved in the internal audit mission, there is generally a positive and open attitude for carrying out the risk analysis activities.

Taking into account the dynamics of the activities and the permanent changes that take place at the level of each activity in the internal or external environment of the organization, the audited structures consider that events that may affect the achievement of their own objectives are risks and need to be identified and known.

Management in this context has the obligation to initiate specific activities to identify those operations and activities that involve a series of risks in their conduct to undertake those actions that place and keep risks within acceptable limits.

Such risk analyses can be carried out at macro level in operations that are included in risk management, which is a continuous, cyclical process and which requires specific steps to identify risks, analyse them, implement and monitor risk mitigation actions.

This activity also comes in the application of the provisions contained in OMF. 946/2005 for the approval of the internal Control Code, comprising the management/internal control standards of public entities and for the development of managerial control systems, with particular reference to the detailed regulations within the Chapter-"Performance and risk management"-standards 7-11 and standard 15.

4. CAUSES / REASONS

We take into account the following:

- the development on a planned basis and the implementation of the activities included in the Risk Management will ensure that each identified risk related to the activities carried out within the organization is being quantified, documented and mitigated accordingly;
- the activities carried out and the specific risk management formulas (risk alert form, action plan form, risk identification guide form, risk management report form and, in particular, the risk register form) will lead to strengthening the internal control related to the activities carried out by the services within the organization;
- the activities carried out and the specific risk management forms (risk alert form, action plan form, risk identification guide form, risk management report form and, in particular, the risk register form) will lead to strengthening the internal control related to the activities carried out by the services within the organization;
- the documents issued and analyzed will increase the efficiency of the control operations which were evaluated and audited, carried out within the regulated internal control system (or

within the control system which will be implemented);

- the management approach will reduce the risk level of the activities and, at the same time, increase the level of assurance to the management of the organization in terms of:
 - the achievement of the objectives assumed by the management
 - protecting the patrimony against fraud, waste, theft and errors
 - Protecting resources
 - Information correctness and availability

5. CONSEQUENCES

The implementation of such a system generally has the following consequences:

- the unitary organization of this activity and the identification of the categories of risks related to the activities carried out by the organizational services will have positive consequences in terms of keeping them under control;
- the purpose of identifying the risks associated with the activities carried out refers precisely at keeping track of those problems that could lead to the non-realization of the assumed objectives, if these would materialize (would become factual situations);
- through risk management it can be achieved an efficiency of integrating the risk categories identified so far within the organization (in the field of IT security, project security, resource strategies, long-term investments, etc.) with other categories that will be identified from other domains of activity such as the proper management of residual risks, which will lead to the organization of a so-called scoreboard that will allow an efficient reporting of the results obtained to management;

The following subcategories of risks related to the organization's activities can be identified and analyzed:

- inherent external risks (which arise from the external environment and may affect the performance of the organization, its strategic options, activities, relations with external partners, organizational structure or economic efficiency etc., but for which mitigation measures can be taken);
- legislative and regulatory risks (changes in legislation, applicability and confusion in interpretation, changes in the structure of the coordinating ministry)

- operational risks (related to current operations: the current mode of the activity evolution, as well as building and maintaining capacity and capability, etc.);
 - organizational risks (non-formalization of some procedures, lack of precise responsibilities for accomplishing the specific attributions, etc.);
 - force majeure risk (loss of documents and records due to fires or other disasters, serious negligence, etc.);
 - control risks (the risk that the organization's control system is insufficiently adequate to ensure economic and efficient functioning, etc.);
 - efficiency risks (inefficient processes and procedures, inappropriate development of operational procedures concerning information technology, etc.);
 - authority risks (deficiencies in the establishment of authority lines, appropriate organizational structures, appropriate job descriptions, existence of regulations on responsibility and delegation of authority, establishment of competence lines for the use of financial funds, definition of reporting relationships, etc.);
 - risks of information processing;
 - risks related to the satisfaction of business partners (weak relationships with key partners, lack of coordination and internal communication, etc.);
 - risks of human resources (Employees do not have the necessary qualifications and skills, the number of employees is inadequate, low efficiency of the staff, the absence of a recruitment and employment policy, etc.);
 - fraud risks (management fraud, conflicts of interest, inadequate separation of duties, inefficient control operations, inappropriate use of resources);
 - reputational risks (events that may affect the organization's image and the prospect of normal performance of specific business);
 - other categories of risks:
- ❖ organizational risk management helps the leadership to achieve their goals while avoiding traps and surprises throughout their activities;
 - ❖ provides tools for identifying and making decisions about the best responses to risks, from their acceptance to their reduction and avoidance leads to increased management skills, so that the potential of adverse events could be recognized, such as hazards, assess risks, and it can establish

appropriate responses, reducing surprises related to costs or losses.

6. RECOMMENDATIONS AND SOLUTIONS

For knowing and identifying the purpose for which the organization of the internal control system is required, it would be useful to debate OMF Nr. 946/2005 which refers to the approval of the Internal Control Code, including the management standards for the public entities and for the development of the management control systems.

At such a debate, which would have the purpose of a correct understanding of the stipulations of the mentioned normative act, should participate the managerial staff within the organization (starting from the head of department and up to the general management of the organization).

The debate should be moderated by specialists in the field, in particular representatives of the Central Unit for the Harmonization of Financial Management and Control Systems – U.C.A.S.M.F.C. (Unitatea Centrală de Armonizare a Sistemelor de Management Financiar și Control) a department within the Ministry of Economy and Finance who participated directly in the drafting of the Superior Order above mentioned.

It is also recommended contracting external consultancy services on specific problems regarding the risk management. Besides external consultancy, the hierarchical management staff should initiate actions to identify the risk categories specific to their own activities as follows:

- they should establish the necessary measures to diminish each identified risk category;
- to establish the responsible personnel within the compartment, who is charged with applying the stability measures to mitigate identified risks;
- through the forms regulated by the organization's internal control system, senior management staff should permanently monitor how the responsible personnel applies the measures established in order to reduce and maintain an acceptable level of identified risks.

Being a long-term process, an analysis of the activity carried out by each head of department should be made periodically, to discuss the progress undertaken on the identification of risks and the actions taken to reduce them and the results that were actually achieved.

Regarding the eventual development of the specific activities included in the Risk Management, this presupposes the knowledge and understanding of the concepts, principles and procedures contained in this activity.

From the good practice in various areas of activity in which activities such as those established by Risk Management have been revealed is that the best presentations, information and training programs are obtained through the direct and neutral expertise of some specialists in the field. This perish employees to

experiment and expose new information and help them understand better the process of managing risks.

7. INTERNAL AUDITORS SHOULD HAVE THE COURAGE...

Regardless of how the subject is handled, internal auditors need to have the courage to address such topics that, in our opinion, are far from being considered delicate or difficult to approach. It is preferable that the topic approached within the internal audit missions exceeds, in a constructive sense for the organization, the requirements imposed by art. 3, par. 2 - "Public internal sphere", within the framework of the law 627/2002 on public internal audit. In our opinion, the provisions of art. 3, par. 2 of the aforementioned law cannot be interpreted restrictively.

That is why we believe that they can be implemented in the annual internal audit plan approved by the management, after the rigorous risk analysis, topics such as the analysis of the legal system of the organization, public relations, the human resources system, the internal control system, including the evaluation of how to manage your organization's classified documents.

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