THE IMPORTANCE AND ROLE OF INTERNAL AUDIT MISSIONS OF STOCKS

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Abstract: In the case of entities with a significant inventory/stocks turnover, the implementation of internal audit function must be a concern of both management and shareholders, in order to prevent and detect the risk of embezzlement of these assets. This procedure must provide assurance that the inventoried stocks are correct and in a proper condition to be used according to their nature in the entity's activity. It is necessary for the entity to implement its own appropriate policies and procedures regarding these categories of assets' management and administration due to the fact that these assets present a very high risk of fraud and, in most cases, this can be provoked even by entity's employees.

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1. INTRODUCTION

Auditors provide, through their audit reports, a professional, objective and independent opinion on the presentation in the financial statements of the correct reality and vision of the most significant aspects of the financial position and performance, in accordance with accounting regulations. The internal audit documentation helps the financial auditor to adopt a starting point, capable of expressing an opinion on the financial statements and operations presented by the economic entities.

Stocks are for many economic entities, the assets that have a significant value in the financial statements, therefore they are considered as the category of assets with the highest share in the total assets held by some economic entities.

Internal audit is an independent and objective assurance and consulting activity designed to add value and improve an entity's operations. Internal audit helps entities to meet their proposed objectives, by imposing a systematic and disciplined approach to the process of evaluation and the increase of efficiency in the processes of risk management, control and governance (Institute of Internal Auditors - IIA, 2015).

2. OBJECTIVES

The purpose of this article is to demonstrate the importance and role of the internal audit mission of stocks in the activities of economic entities, regardless of their specificity and purpose. Throughout this article we want to answer the following questions: What is the role of internal audit mission? How does the internal audit of stocks help the economic entity?

3. IMPORTANCE OF INTERNAL AUDIT MISSION

The importance of internal audit was recognized by the Romanian Chamber of Financial Auditors by adopting Decision no. 88/2007 for the approval of Internal Audit Norms and International Standards of Internal Audit Professional Practice. According to GEO no. 75/1999 on the financial audit activity, republished, all entities with financial statements subject to financial audit have the obligation to organize the internal audit

The audit has undergone, over time, many changes and improvements to meet the needs of the business environment. The audit has existed since the beginning of human civilization, initially focusing on the form of financial audit and later refining by identifying fraud, determining its extent and recovering it.

Through the audit process, the auditor helps to increase confidence in the information provided by the financial statements, providing an external but also independent perspective, based on rigorous rules, a perspective that will support future decision-making by financial information users (Manolachi, 2018, pp. 44).

Inventory/stocks auditing is a complex process due to the deficiencies that internal stock control procedures sometimes have so that stocks may be exposed to increased risks of fraud (Iovu, 2017, p. 277).

Țurlea and Mocanu argue in the paper entitled *The Profile of the Internal Auditor in the Romanian Banking Sector* (2016, p. 1183), that internal audit has two roles, namely: to make estimates that ensure the correct design and efficient functioning of governance structures and processes and to issue advices on potential improvements in governance structures and processes.

Collaboration between auditors and managers of the audited entity is of major importance in the prevention of fraud and errors related to (Avram et. al., 2008, p. 933):

- correcting weaknesses related to the entity's internal control, whenever they are identified by the auditor;
- improving the internal control system and the accounting system;
- developing a set of proposals and recommendations for improvement of activity.

Among the factors that determine the complexity of stocks audit, we can mention (Ocnean et. al., 2010, p. 2):

- stocks are an important part of current assets;
- stocks are stored in various locations, which complicate their physical control and storage. Economic entities are obliged to ensure the accessibility of stocks in order to produce and market products efficiently, but this dispersion of stocks creates significant problems for auditors.
- stocks valuation is difficult due to factors such as moral wear and tear and the need to allocate part of the total production costs to the stocks' value;

- there are several reasonable methods of valuing the stock, but each entity must apply a sequential method from year to year. Moreover, an entity may prefer different valuation methods for different categories of inventories, and this is permitted by generally accepted accounting principles.

The audit "is an opinion mission, given to an independent professional (internal / external auditor), which uses a specific methodology and justifies an acceptable level of divergence against the rules" (Obert, 1998, p. 33). The auditor's main objective during his mission of auditing the financial statements is to obtain reasonable assurance the financial statements do not contain significant falsifications caused by fraud or error, relying partially on the reports prepared by internal auditors.

To obtain reasonable assurance, the auditor should (Avram et. al., 2008, p. 930):

- maintain an attitude of professional skepticism throughout the audit process;
- analyze the entity's ability to circumvent controls;
- acknowledge that the procedures used may detect errors or falsifications.

We can say that the general objective of stocks' audit is to determine whether the stocks are accurately presented in the financial statements. The audit of financial statements is the one that guarantees the authenticity of the information in financial statements and increases the quality of the information provided by financial statements. Economic entities need to organize the operation of internal audit as well as employ external audit missions to increase the reliability of financial reporting and the effectiveness of the internal systems' operation.

In the audit of stocks, the control of accounts addresses the following issues (Florea et. Al., 2005, p. 25): the existence of stocks, their correct limits and employment groups, the valuation of stocks at the appropriate cost, respecting the principle of separation of financial years; adjusting the value of slow-moving stocks, mathematical accuracy of calculations; the principle of consistency of the method, identification of the movement of stocks (purchases, sales, consumption); analysis of a very high volume of stocks. To achieve these objectives, the auditor may rely to some extent on the internal control system, but should not neglect the need and usefulness of direct controls.

The internal audit through the specific procedures and techniques used has the role of analyzing the destination of expenditures occasioned by the consumption of stocks, how these costs were assessed and the tax treatment, but also to periodically monitor efficiency indicators on stock use (Iovu, 2017, p 281). We can say the internal audit of stocks is a verification process to reduce fraud and detect errors that may occur in the activity of economic entities. In the beginning, the internal audit was assimilated to a basic activity, useful for the external audit. Currently, management considers the internal auditor to be a basic consultant in the normal course of business (Chersan, 2016, p. 987). Internal auditors support management by actively involving in finding solutions to solve the most important problems of entities, but also by providing recommendations to management and the audit committee (Zinca-Voiculescu, 2016, p. 1110). The external auditor takes into account the internal audit's independence and objectivity in assessing the effectiveness of controls, risk management and governance processes. Internal audit is an independent activity meant to provide objective security and advisory activity, designed to add value and improve the organization's actions.

In most works addressing the topic of internal audit, the authors state that internal audit has a dual character: independent and preventive, and the authors Morariu and Crecană (2009, p. 37) state in the paper entitled *Internal Audit Strategy in Management Counseling* that the main purpose of internal audit is to prevent dysfunctions.

Internal audit is a necessity for economic entities, not just an obligation (Iovu, 2017, p. 277), it is a process that examines and evaluates effectiveness and verifies whether procedures, policies and activities have been implemented by management. The complexity and size of economic entities make it impossible for managers to personally control whether the entity operates efficiently. To make sure the entity operates efficiently, it is necessary for the internal audit service (department / compartment) to operate within the entity and only in random situations should be used the provision of services. The functioning of internal audit in the entity influences the effectiveness because, with the support of the internal auditor, the entity implements the recommendations. The internal audit is considered a filter used before the external audit is performed.

According to the International Federation of Accountants (IFAC), the objective of auditing financial statements is to enable the auditor to provide an opinion on the financial statements, i.e. how they are elaborated, in all material respects, in accordance with an applicable financial reporting framework, this being also the auditor's general objective.

The auditor's general objectives are related to his specific objectives, the latter representing the objectives that make the difference between the audited objects and are related to each type of assertion and customized for each area of the entity under auditing (Manolachi, 2018, p. 36). In order to be able to formulate specific objectives, the auditor is compelled to verify management's assertions, which according to ISA 500 "Audit Evidence", are grouped into: assertions or statements for categories of transactions, account balances, presentations and descriptions of information. Because the audit objectives are related to the assertions or statements of the entity's management, the auditor should verify whether these assertions are correct.

Verification by the internal auditor of compliance with the legal regulations in force of the procurement and / or output related to stocks from patrimony / inventory, contributes to increasing the degree of control of stocks management, as well as to the prevention of fiscal risks.

The procedure related to stocks management is very important because it must provide assurance that the stocks inventoried are the correct ones. The responsibility for managing and maintaining stocks is significant in that it ensures the correctness of expenditure on recorded stocks and, consequently, influences the operating result. As such, it is necessary for the entity to implement its own appropriate policies and procedures regarding the management and preservation of these categories of assets given that these assets present a very high risk of fraud and, in most cases, this can be generated even by the company's employees.

In the article entitled *Quality of Accounting Information and Internal Audit Characteristics in Nigeria* (2017, p. 343), the authors (Ogundana et. Al.) came up with proposals to strengthen the independence of internal auditors:

- the internal audit department must be independent of both the leadership and the executive director. If possible, internal audit should not be directly subordinated to the executive management / executive director;
- in order to further ensure the credibility of accounting information, internal auditors should be allowed, by law, to have a space/ paragraph allocated in the financial statements, where they can present an opinion / report on the position and performance of organization;
- professional accounting bodies and accounting regulating authorities should provide ways to improve the independence and competence of internal auditors;
- establishing new features of internal audit, in terms of monitoring the quality and reliability of accounting information.

5. CONCLUSIONS

We consider this paper was able to answer the two questions mentioned at the beginning, thereby the audit plays an important role in the betterment of any entity's management and administration. Public and private entities, in which both internal and external audit operate, are efficient, use assets in the entity's interest and provide reliable and credible information to internal and external users. The need and role of internal audit in the prevention and detection of fraud should not be overlooked, because such aspects are often underestimated and neglected by many entities. We can say that the audit of stocks' general objective is to determine whether the stocks are presented accurately and faithfully in the financial statements, are properly managed and through a continuous verification process contribute to reducing fraud and errors within economic entities.

In the case of entities that give an important role to stocks' management and storage, the implementation of an effective internal control system as well as the internal audit function must be a concern of their leadership and / or stakeholders in order to prevent and detect the risk of embezzlement of this category of assets. The internal audit is responsible for analyzing, by means of specific audit procedures and techniques, the destination of expenditure on stock consumption, the manner in which these costs are assessed and their tax treatment, as well as the regular monitoring of efficiency indicators for the use of stocks.

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