

PROCEDURE OF INTERNAL CONTROL BY INVENTORY IN PRIVATE ENTITIES

Radu Dorin LENGHEL

***Abstract:** The main procedures of internal control are: internal control by inventory, control of receipt of goods, control of the way of completion and use of justifying documents, control of the correct organization and management of accounting, internal control of the verification balances, capitalization of the findings of internal control. Inventory control is the most effective internal control procedure, as it allows to know the reality, to discover possible shortcomings and other forms of waste, contributing to a large extent to the integrity of the patrimony of private entities.*

***Keywords:** internal control, internal control procedures, internal control by inventory, internal control of accounting, capitalization of internal control*

1. Procedure for internal control by inventory

Control by inventory is the most effective internal control procedure, since it allows to know the reality, to discover possible shortcomings and other forms of waste, contributing to a large extent to the integrity of the patrimony of private entities.

The inventory of the patrimony is a complex work, which involves going through several stages: the preparation of the inventory; the inventory itself; the establishment, regularization and recording in the accounts of the differences found at the inventory.

The determination of the amounts, which are imputed to the guilty persons, is made at the replacement value, which represents the acquisition cost of the goods at the date of finding the damage.

According to the legislation in force, the managers are fully liable to the private entities for the damages (lacks in management) that they have caused in the management.

When the manager has caused damage in management at the workplace and it is not fully covered within one month, the entity will be compensated from the cash guarantee provided.

In order to correctly solve the inventory gaps, the inventory commissions will take from the managers complete explanatory notes, showing the character of the gaps, losses, depreciations found and the circumstances of their occurrence.

Based on the explanations received and other documents and facts investigated, the inventory committees formulate conclusions and propose concrete measures to the attention of the management, which are to be adopted (compensations, perishables, imputations, decreases in management).

Basically, the differences found on the occasion of the general inventory of the patrimony are regularized by the following ways (see applications): direct registration of the pluses and minuses of the inventory; offsetting pluses with inventory minuses; combined granting of compensations and perishables; granting of perishables or permissible deductions.

2. Procedure for the direct registration of inventory pluses and minuses

In principle, for storable items, the pluses are recorded as inputs into the assets of the units (class 3 = class 6), and the minuses are passed on to the expenses (class 6 = class 3), as the case may be, minuses, which are to be imputed, if applicable $(4282/461) = 7588$

The taxable person must adjust, on the date of the change, the deductible tax related to goods of the nature of the stocks not in management $(635 = 4426)$.

The initial deduction of the fee shall not be adjusted in the case of:

- a) goods destroyed or lost as a result of natural disasters or causes of force majeure, provided that these situations are properly demonstrated or confirmed, as well as stolen goods legally proven by a final court decision;
- b) goods of the nature of qualitatively degraded stocks, which can no longer be capitalized, as well as scrapped fixed tangible assets, other than capital goods, under the conditions established by the norms;
- c) perishables, within the limits provided by law, as well as technological losses or, as the case may be, of other own consumptions.

Example No. 1

At the general inventory of the patrimony there is a lack of 100 pcs of goods, at a purchase cost of 10 lei / piece, which is imputed to the manager. It shall then withhold the damage from the security initially lodged by the manager.

Solution:

1. registration lack attributable to the manager $100 * 10 \text{ lei} / \text{pcs}$:

$$607 = 371 \quad 1.000 \text{ lei}$$

2. adjustment of the VAT deducted at the time of purchase ($1000 * 19\% = 190 \text{ lei}$)

$$635 = 4426 \quad 190 \text{ lei}$$

3. imputation of the absence to the manager in the amount of 1,190 lei (the imputed amounts are not considered as supplies of goods according to the fiscal code):

$$4282 = 7588 \quad 1.190 \text{ lei}$$

4. forfeiture of damage from the security initially lodged by the manager:

$$4281 = 4282 \quad 1.190 \text{ lei}$$

Example No. 2

At the general inventory of the patrimony, there is a lack of 10 pcs of goods at a purchase cost of 10 lei / piece not attributable.

Solution:

1. registration lack of power of the manager $10 * 10 \text{ lei} / \text{kg}$:

$$607 = 371 \quad 100 \text{ lei}$$

2. adjustment of the VAT deducted at the time of purchase ($100 * 19\% \text{ lei} = 19 \text{ lei}$)

$$635 = 4426 \quad 19 \text{ lei}$$

2. Procedure for compensating the pluses with the minuses found at the inventory

When determining the value of the debt, in cases where the deficiencies in management are not considered as offences, it is taken into account the possibility of compensating the gaps with the possible pluses found.

The compensation of the gaps with the pluses found at the inventory allows the correction of some errors in the handling of the goods due to the confusions between the assortments.

The danger of confusion is determined by the similarity between products, a danger that arises as a result of careless handling, when labels disappear from packaging, as well as due to the negligence of managers.

The power to approve compensations lies in all cases with the directors of private entities.

According to the rules on the organization and carrying out of the inventory of patrimony (approved by OMFP no. 2861/2009), the compensation of the pluses with the inventory minuses operates only if the following conditions are met:

- the existence of a likelihood of confusion between the same groups of material goods because of their similarity in terms of external appearance: colour, pattern, dimensions, packaging and other elements;
- the pluses and minuses must relate to the same management periods and the same management.

Lists of sorts of products, goods, packaging and other material values that meet the conditions of compensation shall be established annually by the administrators of private entities.

The following rules on compensation shall also be taken into account:

(a) the quantitative equality between pluses and minuses is obtained by removing from the calculation the quantities, which exceed this equality (pluses or minuses, as the case may be), starting with the assortments, which have the lowest unit price, in increasing order of prices (the managers are liable for the lesser damage);

(b) the differences in value, at equal quantities of pluses and minuses, shall be established between the total value of the assortments found in excess and the total value of the assortments found below, within the same group of material values;

(c) as a result of the compensation, unfavorable differences cannot result for the firm and if they still exist, they are recovered from the guilty ones (as a result of the compensation, the entity's patrimony cannot be reduced).

Example No. 3

Following the inventory of a warehouse of goods with confundable assortments, inventory differences were found, according to the table below.

Assortment	Acquisition cost	Quantitative differences	
		+	-
S 1	1		35
S 2	2	35	
S 3	3		35
S 4	4	35	
S 5	5		5

Source: own projection

Compensation will be made in the table below.

Assortment	Acquisition cost	Quantitative differences		Value differences	
		+	-	+	-
S 1	1		35		35
S 2	2	35		70	
S 3	3		35		105
S 4	4	35		140	
S5	5		5		25
Total inventory		70	75	210	165
Eliminations from compensation -5S1*1 = 5 lei, at the lowest price			5		5
Compensation		70	70	210	160

Analysis of the compensation process:

1. uncompensated absence: 5 lei;
2. total missing: 5 lei;
3. plus after compensation 50 lei
- 4.1 registration in accounting of the total lack of 5 lei, which is fully covered by perishability:

$$607 = 371 \quad 5 \text{ lei}$$

- 4.2. se ajustează tva-ului dedus la momentul achiziției, ajustarea tva-ului dedus la momentul achiziției ($5 * 9 \% = 0,45 \text{ lei}$)

$$635 = 4426 \quad 0,45 \text{ lei}$$

- 4.3. the imputation of the absence to the manager in the amount of 5.45 lei (the imputed amounts are not considered as supplies of goods according to the fiscal code):

$$4282 = 7588 \quad 5,45 \text{ lei}$$

4.4. forfeiture of damage from the security initially lodged by the manager:

$$4281 = 4282 \quad 5,45 \text{ lei}$$

5. registration of pluses following compensation

$$371 = 607 \quad 50 \text{ lei}$$

3. Procedure for the combined award of compensation and perishables

In the case of goods for which deductions are accepted, in the case of compensation for shortages with the pluses fixed for the inventory, the deductions shall be calculated only if the missing quantities are greater than the quantities ascertained in excess, and only within the limit of these differences.

Within each category, the order of granting perishability is that used to include the goods in compensation (starting with the missing assortment that has the highest unit price).

The deductions are granted, first of all, for the assortments, to which it was found that the lack was found, and if there are still quantitative differences in minus, they can be granted for the other assortments to which there were pluses.

Value gaps, which may be covered on account of perishables, shall consist of the value of the missing quantities, which exceed the quantities ascertained in addition, plus the negative differences in value resulting from the compensation of equal quantities.

Quantitative shortfalls removed from compensation remaining after the granting of quantitative perishables shall be charged, in the order in which they were eliminated from the compensation (starting with the lowest unit price).

The difference established in minus as a result of the compensation and application of all the deduction quotas, representing damage to the entity, shall be recovered from the guilty persons, in accordance with the legal provisions.

Example No. 4

Following the inventory of a warehouse of goods with confundable assortments, inventory differences were found, according to the table below. The VAT rate is 9%.

Establish the situation in the inventory knowing that the perishables allowed during storage are 0,05 %, of turnover.

	Acquisition cost ~ lei	Quantitative differences (Kg)		Turnovers of entries (Kg)
		+	-	
S 1	1		50	1.000
S 2	2	50		2.000
S 3	3		50	3.000
S 4	4	50		4.000
S 5	5		5	5.000

Source : own projection

Compensation will be made in the table below

Assortment	Acquisition cost	Quantitative differences		Value differences		Perishability		
		+	-	+	-	Calculate	Granted	Value
S 1	1		50		50	0,5	0,5	0,5
S 2	2	50		100		1	-	-
S 3	3		50		150	1,5	1,5	4,5
S 4	4	50		200		2	0,5	2
S5	5		5		25	2,5	2,5	12,5
Total inventory		100	105	300	225	7,5	5	<u>19,5</u>
Eliminations from compensation -5S1*1 = 5 LEI,			5		<u>5</u>			
Compensation		100	100	300	220			
Result of compensation		-	-	80				

The analysis of the compensation and granting of perishability process is:

1. uncompensated absence: 5 lei;
2. missing from compensation: 0 lei;
3. total missing: 0 lei;
4. perishability granted during storage: 19.5 lei;
5. imputable absence: 0 lei.

6. registration in the accounts of the total lack of 5 lei, which is fully covered by perishability:

$$607 = 371 \quad 5 \text{ lei}$$

7. does not adjust the VAT deducted at the time of purchase for the missing goods covered by perishables

8. registration of pluses following the compensation of 80 lei:

$$371 = 607 \quad 80 \text{ lei}$$

4. Procedure for granting perishability

Perishables means deductions which occur during the transport, handling, storage and disposal of goods as a result of natural transformations of goods leading to their weight loss or depreciation, including fermentation processes.

These normal quantitative losses are not the fault of the manager or other persons and must therefore be deducted from management as losses not attributable to them.

The power to approve the deduction quotas lies in all cases with the management of the entity.

Perishables shall be approved on the occasion of the inventory, only under the conditions of actual lack of inventory and only within the limits thereof.

These perishables diminish the patrimonial responsibility of the managers.

1. Perishability during storage shall be determined according to the turnover of entries recorded between two successive inventories, the most common method of calculation, etc.

2. Perishability during transport

It refers to the losses, which occur in the quantitative and sometimes qualitative volume of goods and is calculated, as a rule, by applying the percentage quotas of subtractions on the quantity or value of the goods transported.

For some categories of goods, the percentage rates may differ depending on the distances of the transport, the duration of the transport or the season in which the transport takes place and the means of transport used.

3. Perishability during unwrapping (handling) shall be calculated, as a rule, by applying the percentage quotas of deductions to the quantity sold between two successive inventories.

Example No. 5

Following the inventory of a warehouse of goods with unmistakable assortments, inventory differences were found, according to the table below.

Establish the situation in the inventory knowing that the perishables allowed during storage are 0,05 %, of turnover.

	Acquisition cost ~ lei	Quantitative differences (Kg)		Turnovers of entries (Kg)
		+	-	
S 1	1		25	1.000
S 2	2	25		2.000
S 3	3		25	3.000
S 4	4	25		4.000
S 5	5		5	5.000

Source: own projection

The granting of perishability will be made according to the table below:

	Acquisition cost ~ lei	Quantitative differences(Kg)		Turnovers of entries (Kg)	value	value
		+	-			
1	1		25	1.000		25
2	2	25		2.000	50	
3	3		25	3.000		75
4	4	25		4.000	100	
5	5		5	5.000		25

Entries in the accounts following the granting of perishables:

- the pluses are charged in management (50 kg in the total amount of 150 lei)

$$371 = 607 \quad 150 \text{ lei or}$$

$$607 = 371 \quad -150 \text{ lei}$$

- at shortages, quantitative perishables will be granted individually during storage, and the lack of perishability will be imputed to the manager.

- at S1
 - a. missing 25 kg * 1 lei = 25 lei
 - b. Pd = 1,000 kg * 0.05% = 0.5kg * 1 lei = 0.5 lei,
 - c. imputable lack (a-b) = 25 – 0.5 = 24.5 lei

- at S3
 - a. missing 25 kg * 3 lei = 75 lei
 - b. Pd = 3,000 kg * 0.05% = 1.5kg * 3 lei = 4.5 lei,
 - c. imputable missing (a-b) = 75 – 4.5 = 70.5 lei

- at S5
 - a. missing 5kg * 5 lei = 25 lei
 - b. Pd = 5,000 kg * 0.05% = 2.5kg * 5 lei = 12.5 lei,
 - c. imputable missing (a-b) = 25 – 12.5 = 12.5 lei

The main accounting records following the granting of perishables for perishable goods are:

1. registration of the lack covered by perishability (0.5+4.5+12.5 lei):
17.5

$$607 = 371 \quad 17,5 \text{ lei}$$

2. registration of the total imputable absence of (24.5 + 70.5 + 12.5 lei) = 107.5 lei, after the decrease of perishability: 5

$$607 = 371 \quad 107,5 \text{ lei}$$

3. adjustment of the VAT deducted at the time of purchase (107.5 * 9% lei = 9.68 lei)

$$635 = 4426 \quad 9,68 \text{ lei}$$

4. imputation to the manager totally missing:

$$4282 = 7588 \quad 117,18 \text{ lei}$$

5. imputation to the manager totally missing:

$$4281 = 4282 \quad 117,18 \text{ lei}$$

5. Conclusions

Control by inventory is the most effective internal control procedure, since it allows to know the reality, to discover possible shortcomings and other forms of waste, contributing to a large extent to the integrity of the patrimony of economic entities.

The inventory of the patrimony is a complex work, which involves going through several stages: the preparation of the inventory; the inventory itself; the establishment, regularization and recording in the accounts of the differences found at the inventory.

The determination of the amounts, which are imputed to the guilty persons, is made at the replacement value, which represents the acquisition cost of the goods at the date of finding the damage.

According to the legislation in force, the managers are fully liable to the private entities for the damages (lacks in management) that they have caused in the management.

In order to correctly solve the inventory gaps, the inventory commissions will take from the managers complete explanatory notes, showing the character of the gaps, losses, depreciations found and the circumstances of their occurrence.

Based on the explanations received and other documents and facts investigated, the inventory committees formulate conclusions and propose concrete measures to the attention of the management, which are to be adopted (compensations, perishables, imputations, decreases in management).

According to the legislation in force, the managers are fully liable to the private entities for the damages (lacks in management) that they have caused in the management.

In order to correctly solve the inventory gaps, the inventory commissions will take from the managers complete explanatory notes, showing the character of the gaps, losses, depreciations found and the circumstances of their occurrence.

Based on the explanations received and other documents and facts investigated, the inventory committees formulate conclusions and propose concrete measures to the attention of the management, which are to be adopted (compensations, perishables, imputations, decreases in management).

When determining the value of the debt, in cases where the deficiencies in management are not considered as offences, it is taken into account the possibility of compensating the gaps with the possible pluses found. The compensation of the gaps with the pluses found at the inventory allows the correction of some errors in the handling of the goods due to the confusions between the assortments.

In the case of goods for which deductions are accepted, in the case of compensation for shortages with the pluses fixed for the inventory, the deductions shall be calculated only if the missing quantities are greater than the quantities ascertained in excess, and only within the limit of these differences.

Perishables means deductions which occur during the transport, handling, storage and disposal of goods as a result of natural transformations of goods leading to their weight loss or depreciation, including fermentation processes. These normal quantitative losses are not the fault of the manager or other persons and must therefore be deducted from management as losses not attributable to them. The power to approve the deduction quotas lies in all cases with the management of the entity. Perishability is approved on the occasion of the inventory or reception of goods, only in the conditions of effective lack of inventory they have at the reception, and only within their limits.

BIBLIOGRAPHY

1. Oprean, I., Lenghel, R.D., Oprean, D.B, Audit of financial statements, Risoprint Publishing House, Cluj-Napoca, 2015.
2. Lenghel, R.D., Financial-accounting control, Risoprint Publishing House, Cluj-Napoca, 2017.
3. Guide to a quality audit, CAFR Publishing House, Bucharest, 2019.
4. Manual of international regulations for Quality Control, Audit, Review, Other Insurance and Related Services, Volumes 1, 2, Publishing House, CAFR, Bucharest, 2018.

NOTE ABOUT THE AUTHOR

Radu Dorin LENGHEL, PhD in Economics, associate professor at the Department of Finance and Accounting, within the Faculty of Economic Sciences in Cluj-Napoca. He is the author of numerous scientific papers and specialized books in the field of accounting, control and financial audit. Currently, he holds the bachelor's and master's courses in the disciplines: Financial Control, Internal Control, Auditing of Financial Statements, Internal Control and Audit, International Auditing Standards, Accounting of Public Institutions.