

# THE PROCEDURE FOR INTERNAL CONTROL OF ACCOUNTING 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 accountings, internal control of the verification balances, capitalization of the findings of internal control. Errors found as a result of the internal control of the accounts may relate either to the current financial year or to previous financial years.*

*The correction of errors found during the internal control is made on the date of their finding. If the errors are related to the current financial year, their correction is made on behalf of the profit and loss account (class 6 / class 7). The correction of significant errors related to previous financial years is made on account of retained earnings (1174).*

***Keywords:** internal control, internal control procedures, internal accounting control, , capitalization of internal control findings*

## **1. Control of the way of completing and using the supporting documents**

The control of the way of completing and using the supporting documents has as an object to verify:

***(a) all the entries in the accounts are based on legal documents, whether the printouts corresponding to the nature of the operations recorded in them are used.***

Order of the Minister of Public Finance no. 2364/2015, includes a "Nomenclature on the models of the common standard registers and forms regarding the financial and accounting act". All entities are obliged to use these models of the accounting registers and of the common forms regarding the financial-accounting activity, to comply with the methodological norms regarding their use, and in case of using the IT equipment for the preparation of supporting documents and for the processing of data, the accounting registers and the common forms on the economy, they can be adapted

according to the needs of the users, but provided that the content of information of the model of forms approved by the Ministry of Public Finance.

In addition to the forms provided in this nomenclature, private entities may also use in their financial-accounting activity specific forms elaborated by ministries, departments, professional associations or patrimonial entity, depending on the needs.

***b) the way of completing the documents***

The internal control must monitor that they are drawn up in time and contain all the necessary elements, without artificial simplifications and omissions which may lead to or give rise to processing errors, fraud, forgery and which hinder control.

The supporting documents usually include the following main elements: the name of the documents; the name, address and particulars identifying the issuer; the document number and the date of drawing up; the content of the operation (sometimes also the legal basis, or the contract number); the quantitative and value parameters of the operation; the name, surname and signature of the persons who drew up, endorsed and approved the document and of those who participated in the performance of the respective operation or transaction, etc.; other particulars required by vat regulations.

***c) if the legal rules on the correction of errors in documents are observed***

For example, we specify that the correction of the information entered in the invoices is made in accordance with the requirements of the Tax Code, as follows:

- a. if the invoice has not been sent to the beneficiary, it shall be cancelled and a new invoice drawn up;
- b. if the invoice has been sent to the beneficiary, the correction can be made:
  - either by issuing a new invoice, in which the number and date of the corrected invoice are entered, and the value is passed with minus and at the same time the correct values are entered;
  - either two invoices are issued, in the first one the number and date of the corrected invoice are entered, and the values are written with a minus sign, and in the second the correct information and values are written.

If the taxable amount is changed, suppliers must issue invoices, in which the values are written with a minus sign or a plus sign, in the following situations:

- if the recipient refuses part or all of the quantity, quality or price of the goods or services invoiced;
- if price reductions (rebates, draws, scraps, discounts) are granted after the delivery of the goods or the provision of services;
- if after delivery, there is an increase in prices and tariffs;
- if the customer picks up the packaging, which has been invoiced, at the same time as the goods.

***d) the documents in question are authentic.***

In order to be able to establish whether the signatures on the documents belong to the authorized persons, the signatures on the respective documents shall be compared with those on the documents concerned, with those on other documents and those in the sheets of specimen signatures and, ultimately, the recognition and confirmation of the writing and signature by their authors shall be carried out.

The document in electronic form, to which an extended electronic signature has been attached, generated with the help of a secure device, is assimilated to documents in private form (Law no. 455/2001 on electronic signature, art. 5).

***e) if the basis of the records are the centralizing documents.***

It shall be verified that they cover only operations of the same nature and of the same management period.

***f) if the numbering of documents allows the detection of missing documents or those registered more than once (completeness of the records).***

This numbering shall ensure that the documents on the basis of which the recordings were made are easily located.

For forms numbered within the private entities that use them, it follows: if their numbering was still done or serially by compartments, so as to avoid the assignment of several similar documents with the same serial number (the forms in stock at the end of the year can still be used without another numbering) and if all copies of a document have the same serial number.

After completion, the forms shall become supporting documents and shall be kept, at the declared premises, in the order of the numbers, thereby ensuring a permanent control over them. The supporting documents can be stored by any method, including by electronic means, under the conditions required by the Fiscal Code. g) ***arithmetic verification of documents, also in terms of form, but also affecting the content, an arithmetic check is also carried out,*** aiming at the accuracy of the figures entered in the

documents, of the measurement units, of the calculations, being aware that sometimes they are intentionally wrong, with the purpose of temporarily hiding cases of poor management, fraud or other irregularities.

## **2. Control of the correct organization and management of accounting**

In order to ensure the objectivity, accuracy and promptness of the information, the process of organization of the accounting information system in a private entity must be carried out under a strict control, on behalf of the Administration Council, the heads of departments and the executors.

The main tasks of the internal control related to the organization of accounting records are focused on the way in which the implemented accounting information system corresponds to the legal regulations and specific characteristics of the respective entity.

The control of the way of organizing the accounting must start with a documentary basis on the criteria, which must be respected by the informatic programs. The main criteria that a computer program must satisfy are:

- to ensure the processing of information in accordance with the provisions of accounting and tax regulations;
- to protect program products against unauthorized access by persons, with the purpose of "modifying" programs;
- ensure the confidentiality of the data. Access to these data must be restricted by various codes or other means;
- to ensure the archiving of data for a period of time required by the law of compatibility;
- ensure the listing of accounting records. These listings must be intemible and complete and must contain: the type of document listed, the name of the entity, the period to which it refers, the date of listing, the chronological pagination, the specification of the computer program and the version used.
- not to allow insertions, modifications or deletions of data, for the periods completed. Any errors or omissions found shall be corrected in the current period;
- to allow verification of the functioning of the programmes and of the correction of the accounting records.

At the same time, the software must not allow: opening two analytical accounts with the same symbol; change in the account symbol, after recordings have been made in it; the suppression of an account in which registrations have been made; listing (editing) several documents of the same type, with the same order number, but with different content, etc.

The internal control goes through the logical sequence, in which the accounting processes and instruments are used.

As a result, internal control over accounting involves tracking how to ensure:

- the recording of operations in documents and their entry in the accounting books;
- verification of the consistency between accounting information and reality by means of inventory;
- checking the correctness of the accounting records, with the help of verification balances;
- the synthesis and generalization of accounting information, with the help of financial statements.

With regard to the accounting system in the entity, internal control shall monitor the quality of information and in particular, whether the following criteria are met: completeness and integrity of records; the reality of the recordings; the accuracy of the records.

***a. Completeness and integrity of records***

This criterion requires that all transactions and operations, which take place in an entity, be reflected in appropriate supporting documents and be entered in the accounts without omissions and without repetition, in this respect, the internal control shall follow the reliability of the document numbering system (manual or automatic) practiced in the entity.

In order to ensure the full takeover of the supporting documents in the automatic data processing system, several procedures are used, among which we mention:

- by checking the records in the registers and journals, the internal control can detect situations, in which some documents have been omitted or have been recorded several times.
- analysis of the correlations between the turnovers and balances of some accounts, as well as of the abnormal balances. Thus, the internal control can analyze the correlations between customer accounts, sales revenue and collected VAT. Also, the debtor balance of the supplier account may be due to the failure to correctly register the supply invoices, confusions between the analytics of this account, the payment of invoices several times: through the cash register, through the bank or through different payment instruments.
- control of accounting records that are based on the manual processing of a sample of documents or on processing according to another informatic program and comparison of results.

***b. Reality of the recordings***

All information recorded in the accounts and summarised in the financial statements must be justifiable and verifiable on the basis of supporting documents. All patrimonial elements reflected in the accounting must be in accordance with the factual reality established by physical inventory, by confirmations received from third parties, by laboratory analysis or by other procedures. All revenue and expenses must be real (justifiable and verifiable), concern the period in question and the entity concerned.

***c. Accuracy of records***

The correct entry in the accounts and the correct presentation of the accounting information are verified in terms of: the correct period, the correct valuation, the correct imputation and the correct presentation, as follows:

- ***Correct period.*** The principle of accrual accounting requires that transactions and transactions be recorded during the period in which they took place, according to the requirements of a commitment accounting.

Internal control must consider how, in which the accruals accounting principle is respected and how the work on reconciliation and accounting rectification is carried out.

The independence of the year is controlled by several procedures, among which we mention the analysis of the first and last documents of a financial year, with the purpose of detecting unreal or illegal "carryovers" between the management periods.

- ***Correct assessment.*** Law on accounting no. 82/1991, amended and republished, establishes the evaluation rules: at the entry into the patrimony, on the occasion of the inventory, at the closing of the exercise and at the exit from the patrimony or at the release for consumption. Accounting regulations, approved by MFP Order no. No 1802/2014, supplements the rules for valuation at historical cost and the rules on depreciation and provisions, with other rules, called "alternative rules", which refer to the replacement value or fair value. This legal norm establishes the principle of separate valuation of assets and liabilities and the principle of valuation at acquisition cost or production cost.

- ***Correct imputation.*** Internal control must aim at recording transactions and transactions in the corresponding accounts, knowing that non-compliance with correspondence between accounts can contribute to the mass of fraud or other irregularities, to illegal compensation, to distortion of indicators, etc.

• ***The correct preparation of financial statements.*** The internal control must follow the correctness of the accounting records, based on the synthetic and analytical trial balances, on the basis of the confrontations between the accounting and the operative records (stock records, cash registers, management reports, etc.), on the basis of the work of reconciliation and rectification of the accounts, including, on the basis of the inventories and on the basis of the confrontations between the chronological records and the systematic records.

After carrying out these checks, the internal control shall aim at the correct centralization and retrieval of the information in the annual financial statements or in other reports and information.

Errors found as a result of the internal control of the accounts may relate either to the current financial year or to previous financial years.

The correction of errors found during the internal control is made on the date of their finding.

If the errors are related to the current financial year, their correction is made on behalf of the profit and loss account (class 6 / class 7).

The correction of significant errors related to previous financial years is made on account of retained earnings (1174).

Correction of insignificant errors for previous financial years shall also be corrected on account of retained earnings. However, according to the approved accounting policies, insignificant errors can be corrected on behalf of the profit and loss account.

In the notes to the financial statements, additional information on the errors found must be presented.

### **3. Internal control of accounting and tax rationales**

Private entities submit accounting reports according to size criteria, annually or semi-annually.

The internal control department verifies with the accounting department at the beginning of each fiscal year, the classification in the size category according to the indicators in the balance sheet and establishes the manner of accounting and tax reports according to the legal provisions.

The internal control department at the due dates verifies the submission of reports by the accounting department.

At the end of each reporting period, the internal control department will analyze whether the chart of accounts used by private entities and the development of accounts on analytics is sufficiently comprehensive or on the contrary too complex, making it difficult to analyze the financial information.

At the end of each period, the internal control department will check together with the accounting department whether: the tax returns have been submitted according to the fiscal vector; the tax file was checked; the fees have been paid in accordance with the amounts declared.

#### 4. Case studies on internal control of accounting

##### Example No. 1

---

At a company on the occasion of the closing works of the financial year 2022, the economic director finds the existence of material errors related to the current year, as follows:

1. nu an invoice for the purchase of a laptop worth 2,500 lei was registered;

214 = 404            2.500 lei

2. no invoice was registered for services provided to third parties, in the amount of 3,000 lei;

4111 = 704            3.000 lei

3. there was no electricity bill in the amount of 2,000 lei;

605 = 401            2.000 lei

4. the profit tax was not registered according to D 101, in the amount of 2,500 lei.

691 = 4411            2.500 lei

5. there were no increases compared to suppliers in the amount of 2,000 lei.

6581 = 401            2.000 lei

6. the salary of an employee in the amount of 4,000 lei was not registered;

641 = 421            4.000 lei



7. the annual depreciation of the cars was not registered, in the amount of 3,000 lei;

$$6811 = 2813 \quad 3.000 \text{ lei}$$

8. no prescribed debts in the amount of 4,500 lei were removed from the record;

$$401 = 7588 \quad 4.500 \text{ lei}$$

9. an invoice for the purchase of goods, worth 15,000 lei, was registered twice;

$$371 = 401 \quad - 15.000 \text{ lei}$$

10. the electricity related to the spaces rented to third parties, in the amount of 2,000 lei, was not re-invoiced;

$$4111 = 708 \quad 2.000 \text{ lei}$$

11. no late payment penalties were invoiced, related to unpaid rent invoices, in the amount of 3,000 lei;

$$4111 = 7581 \quad 3.000 \text{ lei}$$

12. the internet invoice worth 1,500 lei was not registered;

$$626 = 401 \quad 1.500 \text{ lei}$$

### **Example No. 2**

---

At a company during the closing work of the financial year 2022, the economic director shall find that there are material errors for the previous year, as follows:

1. nu a phone purchase invoice worth 2,000 lei was registered:

$$303 = 401 \quad 2.000 \text{ lei}$$

2. there was no invoice for the sale of goods, in the amount of 3,000 lei:

$$4111 = 1174 \quad 3.000 \text{ lei}$$

3. there was no invoice for repairs of the company's car, in the amount of 2,000 lei:

1174 = 401          2.000 lei

4. no income tax was registered according to D 100, in the amount of 1,500 lei:

1174 = 4418        1. 500 lei

5. there were no interest on late payment to the state, in the amount of 2,000 lei:

1174 = 4481        2.000 lei

6. the salary of an employee in the amount of 3,500 lei was not registered:

1174 = 421          3.500 lei

7. for the accommodation and daily allowance expenses at the time of the inspection, the travel statement was submitted, in the amount of 2,000 lei:

1174 = 542          2.000 lei

8. the depreciation of computers in the amount of 4,000 lei was not recorded:

1174 = 2814        4.000 lei

9. the lack of goods in the amount of 5,000 lei in the inventory was not recorded:

1174 = 371          5.000 lei

10. no prescribed claims in the amount of 3,500 lei were removed from the record:

1174 = 4111        3.500 lei

11. an invoice for the sale of goods worth 10,000 lei was registered, twice:

$$4111 = 1174 \quad -10.000$$

12. no rents related to the spaces rented to third parties, in the amount of 5,000 lei, were invoiced:

$$4111 = 1174 \quad 5.000 \text{ lei}$$

## 5. CONCLUSIONS

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.

The main tasks of the internal control related to the organization of the accounting records are focused on the way in which the implemented accounting information system corresponds to the legal regulations and the specific characteristics of the respective entity

As a result, internal control over accounting involves tracking how to ensure:

- the recording of operations in documents and their entry in the accounting books;
- verification of the consistency between accounting information and reality by means of inventory;
- checking the correctness of the accounting records, with the help of verification balances;
- the synthesis and generalization of accounting information, with the help of financial statements.

With regard to the accounting system in the entity, internal control shall monitor the quality of information and in particular, whether the following criteria are met: completeness and integrity of records; the reality of the recordings; accuracy of records

Errors found as a result of the internal control of the accounts may relate either to the current financial year or to previous financial years.

The correction of errors found during the internal control is made on the date of their finding.

If the errors are related to the current financial year, their correction is made on behalf of the profit and loss account (class 6 / class 7).

The correction of significant errors related to previous financial years is made on account of retained earnings (1174).

Correction of insignificant errors for previous financial years shall also be corrected on account of retained earnings. However, according to the approved accounting policies, insignificant errors can be corrected on behalf of the profit and loss account.

In the notes to the financial statements, additional information on the errors found must be presented.

The internal control department verifies with the accounting department at the beginning of each fiscal year, the classification in the size category according to the indicators in the balance sheet and establishes the manner of accounting and tax reports according to the legal provisions.

## **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.