ROMANIA'S FACTS ABOUT INTERNAL CONTROL ENVIRONMENT OF EUROPEAN SOCIAL FUND FINANCED PROJECTS

Dănescu Tatiana
"Petru Maior" University Târgu Mureș

Dogar Cristian
"1 Decembrie 1918" University Alba Iulia

The malfunctioning of internal control system of European Social Fund (ESF) financed interventions may prejudice the sound financial management principle. Incorporating COSO principles in the beneficiary's internal control systems may provide some warranties about compliance to the above mentioned principle as described in the EC Regulation 1605-2002. This study aims to explore some facts in actual internal control environment, as a base for future improvements of Romanian ESF beneficiary's internal control systems
ESF financed interventions covers a large range of costs for implementing labor market related services. But supporting costs according to the sound financial management principle calls for best value for money in real and legal operations. Without some specifics from the donor or a mutual accepted best practice model, most of the ESF beneficiaries are reporting their efforts to actual researches and specialized literature regarding internal control system implementation in services.
This study was realized in April 2012 by applying an investigation instrument, an on-line questionnaire collecting both opinions and factual data as well to a number of 962 members of a practice community for ESF interventions implementation. This technique was used to test hypotheses regarding the premises existence for a future improvement of the existing internal control system model. 100 members of this community: managers, accountants, auditors financial responsible and other team members answered anonymously, revealing a real concern for internal control, providing as well a different side image for this. Analyzing all stakeholder answers, we may consider that our hypothesis is correct and there is a real need for internal control environment improvements.
This study is a part of a larger research "New models of the accounting and internal control systems of ESF financed interventions in Romania", addressing a qualitative approach of ESF absorption through improved practices. The research is coordinated by Prof. Dr. Tatiana Dănescu and elaborated by PhD student Cristian Dogar.
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1. Introduction

Addressing ESF projects is claimed as difficult by most of Romanian beneficiaries. Even if they already implemented PHARE – Human Resources Development financed projects in the past, they are now facing something new, something bigger: larger project teams, target groups, implementation periods and budgets as well. Reported to last programming period problems, new risks may occur and project management has to deal with these according to ever adjusting rules, enforced by the Managing Authority and lasting principles such as: transparency and sound financial management.
With this respect, we consider that an adequate internal control environment may be extremely useful in meeting sound financial management principle.
Even if National legal framework exists and imposes for public institution a yearly evaluation of internal control, there is no such obligation for private companies. Considering the INTOSAI

GOV 9100 creation process and the latest developments of COSO and ESF origin we may appreciate COSO's framework as appropriate for internal control investigation and diagnose.
Hereinafter some questions arise. Are COSO's principles recognized in practice by the stakeholders and in what extent? Do they have convergent opinions and if no, why? We processed here answers at these questions, as a part of a more comprehensive research dealing with new models for accounting and internal control systems for ESF projects.

2. Literature review

Our study aim is to collect opinions from stakeholders of the ESF financed projects and to provide a conclusion about the actual facts about internal control environment of ESF project implementation. We are not comparing now different models of internal control environment, so we do not rely on any internal control dedicated studies. Anyhow, the general context is described in the regulatory framework and in selected references as referred to in the study.

3. Methodology

For relevant conclusions, collecting opinions and factual data from ESF implementation teams has to cover a large area and an important number of opinions. In 2010 – 2011, an ESF financed project created a virtual community of financial responsible, accountants and auditors of ESF projects. That community, comprising more than 950 people from all over the country, working in some of the about 2000 projects in implementation at that time was relatively active at the end of 2011. The list of communities' members is available at: www.practicifse.ro An opinion and factual data on-line questionnaire was applied to all members of this community, asking for an anonymous reply by choosing the most suitable version of the answer at every questions. Questions followed the COSO's principles as they can be applied in ESF project beneficiary's organizations. We assume that no one answered the questionnaire more than once. Answers provided by managers, accountants, auditors, financial responsible and other members of the teams were collected in a table, using Google docs during April 2012.

4. Study results

There are 100 respondents: 18 managers, 15 accountants, 15 auditors, 33 financial responsible and 19 other members of implementation teams, so the response rate is more than 10%. Interaction between internal control and accounting systems is essential for sound financial management, so we asked information about respondent's knowledge on organized management accounting in their entities implementing ESF projects.

Table no. 1. Organizing management accounting

Opinions	Managers/ Assistant	Auditors	Accountants	Financial responsible	Other team's members
Yes	33,33%	20,00%	18,75%	21,21%	47,37%
No	66,67%	80,00%	81,25%	78,79%	52,63%

Accountants and auditors are single functions/positions in project teams, so we could receive more information from one single project from other members or managers and their assistants. We may consider so that projects organizing management accounting are less than 20%, even less than 15% according to one of our previous studies, applied only to accountants.
COSO's principles are to be investigated in our target entities through perceptions of respondents. Separate questions were prepared, at least one for a COSO principle, adapting the COSO's integrated framework to our target and to the sound financial management principle. Answers received for each category of respondents have their importance in creating a broader image of the internal control, as is it seen in implementation by various participants. The first principle: "The organization demonstrates a commitment to integrity and ethical values" relay basically on ethics and integrity of the managers, from the tone of the top perspective. This can be rephrased from sound financial management perspective in the above two questions:

Table no. 2. Perception of COSO's principle 1

Opinions	Managers/ Assistant	Auditors	Accountants	Financial responsible	Other team's members
How much you consider project manager as involved in implementing activities at lowest costs?					
Extremely involved	61.11%	33.33%	26.67%	24.24%	52.63%
Very involved	16.67%	46.67%	46.67%	39.39%	21.05%
Involved	11.11%	13.33%	26.67%	24.24%	21.05%
Sometimes or never	11.11%	6.67%	0.00%	12,12%	5.26%
How do you appreciate management supervision follow costs with activities?					
Always for all activities	77.78%	73.33%	60.00%	54.55%	73.68%
Always for important activities	0.00%	26.67%	20.00%	21.21%	21.05%
Frequently	16.67%	0.00%	13.33%	15.15%	5.26%
Sometimes or never	5.56%	0.00%	6.67%	9.09%	0.00%

As long as a good and very good opinion is expected from the managers, we may observe and not only at this question, the trustee relationship between the manager and the other team members, except financial responsible. The last category has an important opinion for our study, because of its position, dealing both with activities and money. Auditors and accountants are external independent experts, so they rely more on paper work than in day-by-day implementation realities. The second COSO's principle "Exercises oversight responsibility" relay on hieratically supervision of the management and on internal control related tasks assumed by the ones are supervising the management. This may be broadly investigated through the above question:

Table no. 3. Perception of COSO's principle 2

Opinions	Managers/ Assistant	Auditors	Accountants	Financial responsible	Other team's members
Has your organization a hieratically structure managers to report to?					
Existing structure, periodically reports	50.00%	46.67%	26.67%	57.58%	47.37%
Existing structure, often reports	11.11%	13.33%	6.67%	9.09%	10.53%
Existing structure, occasionally reports	5.56%	0.00%	6.67%	3.03%	5.26%
There is no structure or no report or NA	33.33%	40,00%	60.00%	30,30%	36,84%

We may observe that both managers and financial responsible claim that there is a supervision structure (in average 67-70%), but there are differences of perception referring to the frequency of reporting. We may assume that managers ask for reports to the financial responsible and they know exactly how much and when do they report. The fact that the accountants have a separate position, dealing mainly with financial accountancy is confirmed by the answer given here. 60% of them don't know if reports are made by the management to their superior structures.

The third COSO's principle "Establishes structure, authority and responsibility" was investigated through questions collecting respondent's perception on internal structure – segregation of duties, subordination lines and number of position. At first question, accountants assumed that everything goes right in 55,33% of the cases, far more than other respondent categories, as long as, managers and financial responsible have almost the same opinion about the accuracy of subordination lines; about 27% assumed that there is unclear subordination, independent of the positions in the organizational structure. The second question received relevant answer from the auditors, accountants and financial responsible. The auditor, as a contracted expert receives the product of the manager's concern and involvement, as long as the financial responsible, entities employee collaborates with the manager in practicing segregation of duties.

Table no. 4. Perception of COSO's principle 3

Opinions	Managers/ Assistant	Auditors	Accountants	Financial responsible	Other members
How do you consider internal structure, number of positions and subordinating relationships?					
Enough positions, clear subordination	38.89%	33.33%	53.33%	33.33%	57.89%
Enough positions, unclear subordination	22.22%	20.00%	26.67%	18.18%	10.53%
Enough positions, more people needed	5.56%	33.33%	13.33%	15.15%	15.79%
Too many positions, clear subordination	0.00%	0.00%	0.00%	0.00%	5.26%
Too many positions, unclear subordination	5.56%	0.00%	0.00%	9.09%	5.26%
Not enough positions, more people needed	22.22%	13.33%	0.00%	24.24%	0.00%

Others	5.56%	0.00%	6.67%	0.00%	5.26%
How do you perceive the project manager in the segregation of duties context?					
Extremely involved	38.89%	13.33%	20.00%	21.21%	31.58%
Very involved	27.78%	20.00%	26.67%	21.21%	21.05%
Involved	16.67%	33.33%	46.67%	33.33%	47.37%
Sometimes or never	16.67%	33.34%	6.67%	18.18%	0.00%

The fourth COSO's principle "Demonstrates commitment to competence" is investigated through the question: "How do you consider competence is taken into consideration by the management when members of the team are employed?" Manager's registered opinions are confirmed by the financial responsible and by the others members of the teams. All the answers are convergent for "Always" and "Often" in about 70 – 80% of the answers.

Table no. 5. Perception of COSO's principle 4

Opinions	Managers/ Assistant	Auditors	Accountants	Financial responsible	Other team's members
How do you consider competence is taken into consideration by the management when team members are employed?					
Always	50.00%	20.00%	46.67%	51.52%	47.37%
Often	27.78%	53.33%	20.00%	36.36%	36.84%
Sometimes	11.11%	20.00%	20.00%	3.03%	10.53%
Not a factor, I don't know	11.11%	6.67%	13,33%	9.09%	5.26%

The fifth COSO's principle: "Enforces accountability" was a subject of investigation through the following question: "How do you consider the accuracy of team's member responsibilities and the control done by the management?" Financial responsible has a slightly different opinion from the ones of managers and auditors, considering responsibilities and control.

Table no. 6. Perception of COSO's principle 5

Opinions	Managers/ Assistant	Auditors	Accountants	Financial responsible	Other team's members
How do you consider the accuracy of team's member responsibilities and the control done by the management?					
Clear responsibilities / appropriate control	38.89%	40.00%	33.33%	39.39%	63.16%
Clear responsibilities / some kind of control	50.00%	53.33%	26.67%	36.36%	0.00%
Responsibilities and control	11.11%	6.67%	40.00%	24.24%	36.84%

Stakeholder's perception on risk assessment was also investigated. In ESF implementation internal and external risk may occur and managers have to deal with these. The way organizations identifies risks and analyzes them is a very important issue in sound financial management. Even if risk management involves a dynamic process of identifying and assessing risks, the process must be a formal and iterative one. Using specific procedures and risk registers could bring a plus of rigor, and help also to keep track of past experiences. Nevertheless formal or informal meetings when risks may occur have their advantages, but formalizing the process by using a risk register and adequate procedure is undoubtedly the best way of managing risks.

Answers received indicate auditors are not aware in a significant measure about risk management in ESF beneficiary's organizations. Financial responsible consider that there is a procedure in a more substantial way than management declares it, accountants being just skeptical. They all seem to agree that risks are discussed in periodically meetings, probably during progress meetings, and also in instant meetings, when risks may occur. Management doesn't recognize but in small extent the importance of instant meetings, all the rest of the stakeholders seem to agree about it.

Table no. 6. Perception of project's risk management approach

Opinions	Managers/ Assistant	Auditors	Accountants	Financial responsible	Other team's members
How do you consider the risks are identified, analyzed, and managed risks?					
Specific procedure and/or risk register	16.67%	33.33%	6.67%	21.21%	5.26%
Periodically meetings when we discuss about risks	66.67%	13.33%	53.33%	48.48%	52.63%
Discussions about risks when they may	11.11%	33.33%	40.00%	27.27%	36.84%

occur					
Don't know	5.56%	20.00%	0.00%	3.03%	5.26%

Potential for fraud in assessing risk is another important issue from sound financial management perspective. Are the assets protected, are there potential conflicts of interest?

Table no. 7. Perception of project's potential for fraud

Opinions	Managers/ Assistant	Auditors	Accountants	Financial responsible	Other team's members
Do you consider fraud may occur in the project?					
Very possible with all taken measures	5.56%	0.00%	6.67%	6.06%	0.00%
Possible but there are control activities and procedures in force	11.11%	26.67%	6.67%	15.15%	5.26%
Slightly possibility, but there are control activities and procedures in force	33.33%	60.00%	60.00%	60.61%	47.37%
Impossible, management took all necessary measures to avoid fraud	44.44%	6.67%	20.00%	18.18%	47.37%
I do not know	5.56%	6.67%	6.67%	0.00%	0.00%

Received answers confirm over rating of management from other team members, but also the criticism of management done by financial responsible. They agree in less than half extent with managers declaring that fraud cannot occur because they done everything to avoid. We may conclude that financial responsible believe more in control activities and procedures in avoiding fraud than in management statements.

5. Conclusions

Considering ESF financed projects internal control environment from COSO's approach we may observe that relevant stakeholders: managers, accountants, auditors, financial responsible and other members of the teams have different opinions about the subject. As long as the other members of the team are relying on managers and trust them, as an average, their answers are the same or even better than the consideration of management. Auditors and accountants, as contractors may deliver an external opinion, more accurate for auditors. Financial responsible may deliver an internal, relatively objective opinion, as long as the questions are not directly subject of their work.

We may conclude than that ethics and integrity are declared by managers as implemented in a favorable and very favorable way in a total extent of 77% , opinion endorsed by the financial responsible in a substantial manner (64 to 76%) and perceived as declared by 81 to 100% of the auditors. Limitations of audit mission may be an explanation for the auditors super rating of managers ethics and integrity.

On over sighting responsibilities, managers and auditors have the same opinion, as long as, financial responsible is over rating this. We may assume that, as team members they don't know exactly when and what is reported by the management. As an average, more than 60% of ESF projects are seen to have a hieratic authority they are supervised from and sent reports to.

The entities structures meet some inconsistencies; with a general stakeholder's opinion of about 27 – 30 % of employed personnel unclear responsibilities, management declare itself as "involved" and "very involved" in enforcing segregation of duties in a substantial manner (76%), partially endorsed by financial responsible (42%) and recognized much less by the auditors (only 33%). We may observe that auditor's perception's level is half of the management's statement but consistent with financial responsible opinion.

We may also consider management's statement on commitment to competence, as long as both financial responsible and the auditors have a better opinion on this. We may assume that in no less than 70% of the projects competence has been taken into consideration always and often by management in employing team members.

Accountability is enforced in a substantial manner, even if managers are declaring 89%, this is more than 75% according to financial responsible perception.

Risk management is perceived by all stakeholders as dealt in meetings; periodically or instant. Managers declare this for 77% of the cases, financial responsible endorse it for 75%, team members agree in 89% and accountants in 93%.
Potential for fraud is considered as very possible or possible by less than a quarter, and auditors are the most prepared to face it. Financial responsible (19%) and managers (18%) are also considering the potential for fraud.
Based on this study, we may consider that COSO's principles are recognized by ESF projects practicing stakeholders in an appropriate extent and their perceptions are convergent in most of the cases. Stakeholder's perception is confirming the initial hypotheses and there is room for internal control environment improvements for ESF projects to comply with the sound financial management principle.
Are COSO's principles recognized in practice by the stakeholders and in what extent? Do they have convergent opinions and if no, why?

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