

THE INFLUENCE OF THE INTERNAL MANAGERIAL CONTROL ON THE CORPORATE GOVERNANCE WITHIN THE PUBLIC ENTITIES

Silvia Mioara Ilie (Troii)¹ and Aurel Dincă²

^{1) 2)} *University of Craiova, Romania*

silviailie28@yahoo.com; aureldinca@yahoo.com

Ilie (Troii), S.M. and Dincă, A., 2020. The Influence of the Internal Managerial Control on the Corporate Governance Within the Public Entities. In: R. Pamfilie, V. Dinu, L. Tăchiciu, D. Pleșea, C. Vasiliu eds. *6th BASIQ International Conference on New Trends in Sustainable Business and Consumption*. Messina, Italy, 4-6 June 2020. Bucharest: ASE, pp. 746-752

Abstract

The instability that characterizes the current economy has a significant impact on the way in which the economic entities carry out their activity. The internal managerial control can provide to the management data regarding its progress or regression in reaching the proposed objectives. The purpose of the internal management control system is to prevent errors and irregularities, preventively eliminate the causes that determine them and to improve the controlled activities within the corporate governance. The internal management control offers a reasonable assurance, but not absolute, that the public entity fulfills its proposed objectives. Public entities must adhere to all concepts, principles, standards and regulations of corporate governance, in order to be evaluated and achieve the relevant expected policies and performance, and corporate governance codes and policies have become a balance between compliance and performance. Corporate governance is a concept that encompasses a wide range of activities, rules, processes and procedures, designed to ensure the optimal use of the resources and strategies of the entities, so that its objectives are achieved. This article represents the analysis of the objectives of the main internal control procedures regarding the optimization of the corporate governance process.

Keywords: internal managerial control, corporate governance, procedures, process.

JEL Classification: G34

Introduction

Control in its semantic acceptance is a permanent or periodic analysis of an activity, of a situation in order to track its progress and to take measures to improve it. At the same time, control means continuous moral and material supervision, as well as the control of an activity, of a situation (Bunget et al., 2009).

Internal control is made up of all the forms of control exercised at the level of the public entity, including the internal audit, established by the management in accordance with its objectives and with the legal regulations, in order to ensure the management of the funds economically, efficiently and effectively, which includes the organizational structures,

methods and procedures. Internal control standards have a general form that was necessary to allow managers to customize them according to the legal, organizational, personnel, and financing characteristics of each public entity (Morariu et al., 2008).

Corporate governance means the management of the entire organization as a whole by accepting all internal components, which work together, which will ultimately be integrated with the management, and the implementation of risk management within the organization and the system of financial management and internal control. In international practice, most solutions for the implementation of corporate governance policy and principles have taken the form of codes of good practice and they appear as regulations or guidelines and represent a way of organizing and managing organizations and public services. Corporate governance describes the methods and systems used to run organizations of all types and sizes, public or non-profit, and also companies in the private sector and those built in the form of partnerships (Achim and Borlea, 2013).

The concept of (corporate) governance has been used in national institutions, commercial organizations, but also in the administration of the occupied colonies and territories. Subsequently, the concept of corporate governance was developed in the private sector and was taken over and applied in most areas of activity. In recent years it has expanded rapidly, especially to public sector organizations (Feleagă, 2008).

The main purpose of the research is the analysis of the objectives of the main internal control procedures regarding the optimization of the corporate governance process.

The structure of this article is based on the concept of internal control and corporate governance as the main functions of management within public entities, which are responsible for the organization.

The subject of this article is concerned with the permanent updating of the internal control system, due to the evolution of the risks faced by the entity.

Literature Review

The expression internal control comes from the English term internal control, which for Anglo-Saxons to control, first of all means to have control (to keep under control) and secondly to erect, while in Latin-speaking countries, the meaning this expression is the exact opposite, coming from the combination of the words against and the role used in the Romanian military environment and it is understood, in the broad sense, the verification of an act after the original (Morariu et al., 2008). Within public entities, Internal Control has a considerable impact on the credibility of a government and its operations. In the United States of America in 1992, the Integrated Internal Control Framework was published by COSO; In the beginning, this framework referred only to private companies, currently being applied on a large scale, worldwide, in both the public and private sectors. In 1996, the European Parliament initiated the formation of a commission of independent experts to analyze how this body detects and treats fraud, practices in awarding financial contracts, mismanagement and the practice of nepotism. In 1999, the Prodi Commission of the European Parliament introduced a number of reforms in the field of internal control. The White Paper on managerial reforms within the European Commission services is published in 2000; With the entry into the European Union of the new member countries and the allocation of funds to them, it was desired to respect the principles established by the White Paper and to put in place a unitary internal control framework, in all public entities, in order to analyze the way in which these funds are administered. In 2017, the European Commission updates its Internal Control Framework to align it with the Integrated Internal Control Framework - COSO 2013 (Bunget et al., 2009).

In the last decades, the management of all public entities realized the need for a basic control framework, which would be the support for the construction of their own internal control

systems and became, increasingly concerned about the organization and functioning of the internal control, constantly seeking practical solutions (Avram, 2003).

A simple definition of corporate governance would be all of the systems and processes implemented to run and control a company in order to increase its performance and value (Morariu et al., 2008). Basically, it refers to the efficiency of the management systems, insisting on the role of the board of directors, on the responsibility and remuneration of the members, the credibility of the financial statements, and on the efficiency of the risk management systems. Corporate governance defines all the principles, rules and norms that ensure the management and management by the entities of the entities, in the interest of the current and potential investors; this interest is classic and the most common. In its context, managers are studied in relation to shareholders. In terms of a political relationship, in which other stakeholders are found, governance is gaining an extended interest. A distinct place is occupied by the managers, shareholders, creditors and employees, with their claims. Governance and accounting are mutually dependent, although governance dominates accounting. In principle, it refers to the decision and control support of a company, obtained through formal and informal rules and procedures, internally or externally imposed by the competent bodies, implemented at both strategic and operational level. It is estimated that corporate governance systems in the US, Germany, Japan and the UK are some of the best in the world, and the differences between them are not so significant compared to other states (Ghiță et al., 2009).

In less developed countries, including those in transition, corporate governance mechanisms are virtually non-existent. Corporate governance mechanisms differ quite a lot internationally. In the US and the UK, legal protection of investor interests is considered very important and, under these circumstances, the occurrence of investor concentration phenomena is relatively sporadic, with the exception, perhaps, of takeover operations. In continental Europe and Japan the phenomenon is exactly the opposite. In Germany, for example, large commercial banks, through commitments on voting power, can control more than a quarter of large companies, collecting relatively consistent parts of their cash flow, as a significant shareholder or as and creditors (Dragomir, 2012). The diversity of corporate governance systems leads us to the fundamental question: which of these is more appropriate when the question of external financing is raised? Both the legal protection of investor interests and the presence of their concentration phenomenon (US, Germany, Japan) are forms of manifestation of corporate governance systems (Feleagă, 2008).

Research and method

The research objective is the evaluation of the main internal control procedures that are applied within public entities regarding the optimization of the corporate governance process. In the research carried out, 250 managers from Romania were involved in four public entities in the fields: education, healthcare, emergency situations and public administration. The research took place between December 2019 and February 2020. The research was based on the use of the questionnaire that was sent by email and was greatly honored in this study, and it was a succession of electorates.

In the socio-economic universe, the economic decision assisting problems are generated by the multi-criteria decision processes; this is why we used the *maximum global utility method* in the study.

The model tries to use, at maximum, in a scientific way, the informational base, and the procedures for imitating the rational mode of decision making is, in more or less elaborate forms, the conceptual essence of the models.

The steps of the global utility method are as follows:

Step 1. We build the utilities matrix with the elements x_{ij} , $i = 1, \dots, r$ and $j = 1, \dots, n$. (1)

Each matrix element is calculated for the maximum criterion with the expression:

$$x_{ij} = u_{ij} = \frac{x_{ij} - x_{i \min}}{x_{i \max} - x_{i \min}}, \quad (2)$$

and each minimum criterion with the expression:

$$x_{ij} = u_{ij} = \frac{x_{i \max} - x_{ij}}{x_{i \max} - x_{i \min}}, \quad (3)$$

where:

x_{ij} = value of the i indicator associated to the j indicator;

$x_{i \max}$ = minimum value of the i indicator;

$x_{i \min}$ = maximum value of the i indicator.

Step 2. We calculate the global utility for each project, as the sum of the products between the utility matrix elements (the column vector corresponding to the project) and the importance coefficient given for each indicator.

$$UG_j = \sum_{i=1}^r \alpha_i u_{ij}, \text{ unde } \sum_{i=1}^r \alpha_i = 1 \quad (4)$$

Step 3. We choose the project to which the V_j maximum global utility corresponds.

$$\max\{UG_j\} \Rightarrow V_j \quad j = 1, \dots, n \quad (5)$$

For differentiating a decisional V_i variant (given n variants), and for selecting the best offer by simultaneously considering various assessment criteria (C_j , $j = 1, \dots, n$) we use the maximum global utility method. Finding the best combinations of attributes (characteristic of a variant) forms the object of the multi-attribute problem. This involves the transformation of all number values a_{ij} (expressed in the associated measure units) and qualitative characteristics in utilities u_{ij} , i.e. numerical values (adimensional) located in the range $[0, 1]$. The basic hypothesis in the correct functioning of the weighted sum method is the criteria independence. The greatest of the synthesis utilities shows the best variant.

The research study is based on analyzing how to apply the main main internal control procedures that influence the optimization of the corporate governance process. In the process of data analysis, the process of influencing the internal control over corporate governance was approached as a complex system based on five objectives:

O1 - Carrying out at the appropriate level of quality, the tasks of public entities, established in accordance with their own mission, under conditions of regularity, efficiency, economics and efficiency;

O2 - Compliance with law, regulations and management decisions;

O3 - Protecting public funds against losses caused by errors, abuse or fraud;

O4 - Development of systems for collecting, storing, processing, updating and disseminating financial and management data (information);

O5 - Application of the notions and tools necessary for the implementation and development of the internal management control system.

Table no. 1 presents the informational basis of the study, respectively the weight of the importance accorded to the managers of each objective.

Table no. 1 Importance of system objectives

OBJECTIVES	FIELD OF ACTIVITY			
	EDUCATION % (v1)	HEALTHCARE % (v2)	EMERGENCY SITUATIONS % (v3)	PUBLIC ADMINISTRATION % (v4)
O1 (c1)	16.45	22.35	27.5	12.5
O2 (c2)	10.55	15.15	11.9	23.61
O3 (c3)	8.9	13.25	9.8	10.54
O4 (c4)	23.45	16	11.82	23.55
O5 (c5)	40.65	33.25	38.98	29.8

Source: developed by the authors based on the collected data

The main results indicate that the managers first consider O5 - Applying the notions and tools necessary for the implementation and development of the internal management control system, and ultimately O3 - Protecting public funds against losses caused by errors, abuse or fraud (fig. no.1).

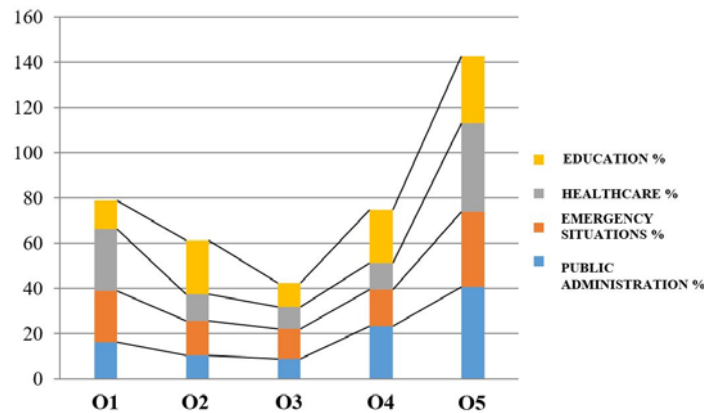


Fig. no. 1 The importance given to the objectives of the system

Source: the author's own concept

The execution of the calculation algorithm implied:

Step 1 – Building the unit matrix with the elements x_{ij} (fig. no 2)

$$\begin{bmatrix} 0.26 & 0.66 & 1.00 & 0.00 \\ 1.00 & 0.65 & 0.90 & 0.00 \\ 0.00 & 1.00 & 0.21 & 0.38 \\ 0.99 & 0.36 & 0.00 & 1.00 \\ 0.00 & 0.68 & 0.15 & 1.00 \end{bmatrix}$$

Fig. no. 2 Unit matrix

Source: the author's own concept

Step 2 – Calculating the global utilities for each organization (table no. 2):

Table no. 2 The results of the calculation of the global units

GLOBAL UTILITY	RESULT
EDUCATION	2.25
HEALTHCARE	3.34
EMERGENCY SITUATIONS	2.26
PUBLIC ADMINISTRATION	2.38

Source: the author's own concept

Step 3 - From the table no. 2 is observed by the calculation of the global utilities, the largest global utility has the healthcare organization.

Therefore, following the application of the algorithm of calculation of the method of maximum global utilities, it can be concluded that the public entities in the healthcare field have evaluated the importance of the objectives of the main internal control procedures regarding the optimization of the corporate governance process.

Conclusions

Based on the information provided by the internal managerial control, the management of the entities has the possibility to consolidate the managerial decisions regarding the activity plan, the organization and coordination of the entity structures, the exact establishment of the responsibilities on structures and the persons involved in the activities of the entity. The construction and proper functioning of this process, which is a long-term one, requires collective and individual efforts, so that it can be adapted as best to the specific and the size of the public entity, but in compliance with the legal provisions and the general principles of internal management control. The internal managerial control through its objectives and procedures aims to: ensure a good use of the resources (financial, human) and their correlation with the objectives of the public entity; improving the information flow; increased intelligibility, risk management, fraud prevention and detection and document quality. The management of the public entity must design the system of internal managerial control so that they are effective and reduce the risks to an acceptable level. Considering a number of internal or external factors (which could not be taken into account when designing the internal management control), the probability of achieving the objectives of the public entity is prejudiced by the limits of the internal control, such as:

- current changes in the internal and external environment of the public entity;
- human errors: inaccurate interpretations, errors of reasoning, negligence, inadvertence;
- abuses of authority demonstrated by some persons with the role of management, coordination or supervision;
- limitation of the independence of the personnel, in the exercise of the duties of the service;
- control procedures not adapted or adapted and not applied;
- the costs of internal managerial control.

The internal managerial control must be efficient, not generate additional costs, leading to the saving of material, financial and human resources. Although a public entity can define a good internal management control system, it can be implemented or treated subjectively by the personnel within it, due to the lack of professional training. The implementation of the internal managerial control system, through its own human resources, ensures both their continuous professional self-improvement and the elimination of additional expenses of counseling in the field

The inefficient governance of public entities adversely influences the economic-financial results and their future development possibilities through the following levers:

- the priority pursuit of short-term interests of employees and managers, the increase of salaries and other allowances, stability and protection of work places;
- lowering the pace of restructuring and reorganization or postponing the bankruptcy of companies in financial difficulty;
- the impossibility of using managers' remuneration programs according to the real value created;
- excessive mobility of staff due to internal conflicts and lack of promotion and stimulation programs according to value criteria.

Good corporate governance is based on increasing the performance of the entities, efficient risk management, as well as on the confidence of the public in these entities.

References

- Achim, M. and Borlea, S., 2013. *Corporate Governance and Business Performances. Modern approaches in the new economy*. Lambert Academic Publishing.
- Avram, V., 2003. *Managementul procesului de creare a valorii în contextul guvernării întreprinderii*. București: Editura Economică.
- Bunget, O., Florea-Ianc Z., Ghiță, M., Nicolau, C., Pereș, C. and Pereș, I., 2009. *Guvernanța corporativă și auditul intern*. Timișoara: Editura Mirton.
- Dragomir, V., 2012. *Guvernanță corporativă, suport de curs*. București: Editura ASE.
- Feleagă, N., 2008. Corporate governance between classicism and modernism. In *Proceeding of the 4th European Conference on Management, Leadership and Governance*. University of Reading, UK, pp.39-46.
- Ghiță, M., 2008. *Guvernanță corporativă*. București: Editura Economică.
- Ghiță, M., Iațco, C., Brezuleanu, C. and Vorniceanu, M., 2009. *Guvernanța corporativă și auditul intern*. Iași: Editura Polirom.
- Morariu, A., Stoian, F. and Suci, G., 2008. *Audit Intern și Guvernanță Corporativă*. București: Editura Universitară.