



THE IMPORTANCE OF INTERNAL AUDIT IN ACHIEVING SUCCESSFUL MANAGEMENT

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Abstract:

Applying internal audit and its mechanisms of internal control systems contributes significantly to business resilience, with the potential to design new strategies to promote business stability and enhance business operations and success. This paper introduces results of a study based on examining the present state and degree of internal auditing on a sample of companies doing business in the Republic of Serbia. In line with the results of the empirical research, it can be concluded that internal audit helps improve business management in companies in the Republic of Serbia. Also, the level of development of internal audit does not correspond to the level of development of this profession observed in countries with highly-developed market economies.

Keywords:

auditing, internal audit, internal control, management.

1. INTRODUCTION

Internal auditing is a part of the internal monitoring system of a company's operations. It includes all monitoring and preventive measures applied within companies to protect assets, accuracy, and reliability of accounting records and activities based on objectives and focusing on the compliance comparison between the existing condition and accepted criteria, according to all applicable standards and legal regulations. It is a complex process by which it is possible to determine the correctness or deviations of procedures and processes in relation to defined rules and standards. This paper illustrates research results on the role and importance of internal audit in corporate governance in sampled companies in the Republic of Serbia. The research results indicate the presence of internal audit and its role in the companies' business operations in the Republic of Serbia as well as that internal audit, contributes to the improvement of corporate governance. Still, the level of development of internal audit does not correspond to the level of development of that profession observed in countries with developed market economies.

2. LITERATURE REVIEW

An audit is a segment of an organization's control system and has several important roles. According to Lee & Alan (1984), if a person has a certain suspicion or doubt about the quality and status of particular business processes and cannot eliminate it independently, there is a need for an audit to resolve the problem. An audit has an important function as a kind of control mechanism, bearing in mind that auditors identify and investigate deviations from defined standards to deter

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individuals from making careless mistakes and creating false financial reports (Kagermann et al., 2008). According to Stanišić and Radović (2013), control as an element of management represents an essential link in the processes of successful business management of a company, and it is present in all phases of business activities - planning, organizing, and management. The projected business goals, processes, risks, and defined business management standards are reviewed, corrected, and monitored.

The internal audit examines and evaluates the implementation of policies, plans, and procedures, the credibility of operational and financial information, the functioning and organization of the accounting system, and related internal controls (Todorović & Vukoja, 2020). Coderre (2009) points out that The Institute of Internal Auditors (IIA) defines internal audit as an objective and independent activity of assurance and counseling, thereby improving business and adding value to the company. A systematized and disciplined approach helps the company achieve its goals. The task of internal audit is to “investigate, examine, and evaluate the system of internal controls and their effectiveness in the activities of each separate part of the business, to report on findings and propose solutions to the management” (Blay et al., 2007). According to Pickett (2010), the internal audit ensures effective organizational management and responsibilities, coordination of activities, and transfer of information between internal and external auditors, board, and management, giving appropriate recommendations for improving the management process, and promoting ethical values. To optimize data collection and achieve better results, Todorović & Perić (2020) highlight the importance of software applications in the audit processes.

Internal audit in Serbia began to develop extremely late compared to countries with developed market economies. Bearing in mind that the subjects of the analysis are companies from Serbia, this research's contribution lies in better understanding internal audit and its relationship with corporate governance through analysis of obtained results.

3. METHODOLOGY

Research on the role and importance of internal audit in corporate governance was carried out in an anonymous survey questionnaire conducted on a sample of 130 companies in the Republic of Serbia. The survey was addressed to internal audit department managers and employees who carried out other forms of internal supervision if the internal audit department was not established in the company. The survey was conducted in November 2020. The survey questionnaire had 23 questions, of which 17 were closed-ended questions with two or more pre-defined

responses. The questions were structured following the objectives of the research. Using Cronbach's Alpha test, it was corroborated that the selected numerical variables are very well connected and form a group of questions related to the functional focus of the internal audit. The mentioned results are illustrated below.

In the first part of the questionnaire, we collected general data on respondents, including gender, years of service, professional qualifications, and certificates, if any. Other data referred to the company's activity the number of employees, and information about the existence/non-existence of an internal audit department.

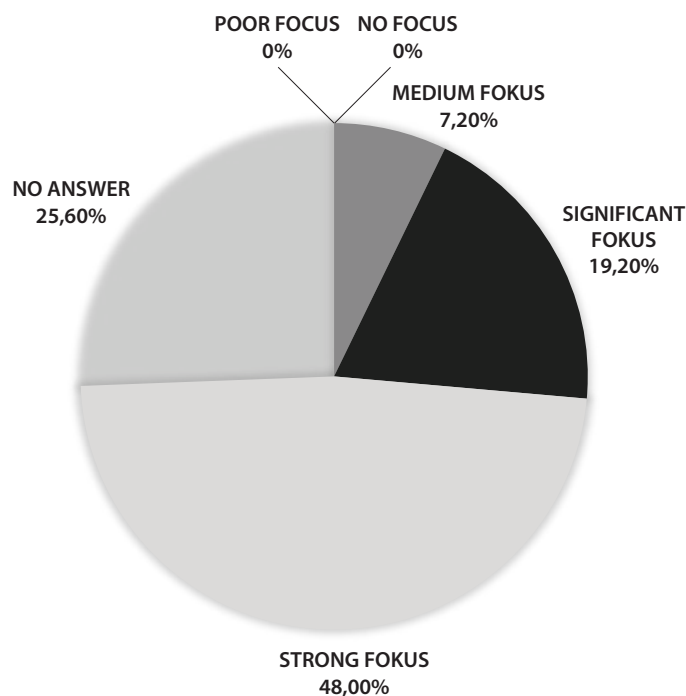
4. RESEARCH RESULTS

According to obtained data, 34.4% of respondents are male, and 65.6% are female, with the longest working life of 34 years and the shortest 3 years of service. As part of the organizational structure, the internal audit department is present in 56.25% of companies, with the number of employees in that department ranging from 1 to 3. As many as 43.75% of companies do not have an internal audit department, but some have developed other internal supervision forms, such as risk control and internal control.

Respondents rated the intensity of internal audit functional focus on internal control on a scale from 1 to 5, whereby a rating of 1 indicates that internal audit functional focus is not directed toward internal controls, and a rating of 5 shows that it is strongly directed toward internal controls (Fig 1.). Not one respondent defined ratings 1 (no focus) and 2 (poor focus) as a choice for internal audit functional focus on internal controls. Approximately half of the respondents opted for a strong focus, while about 1/5 of the respondents considered it to be significant.



Figure 1. Internal audit functional focus on internal control

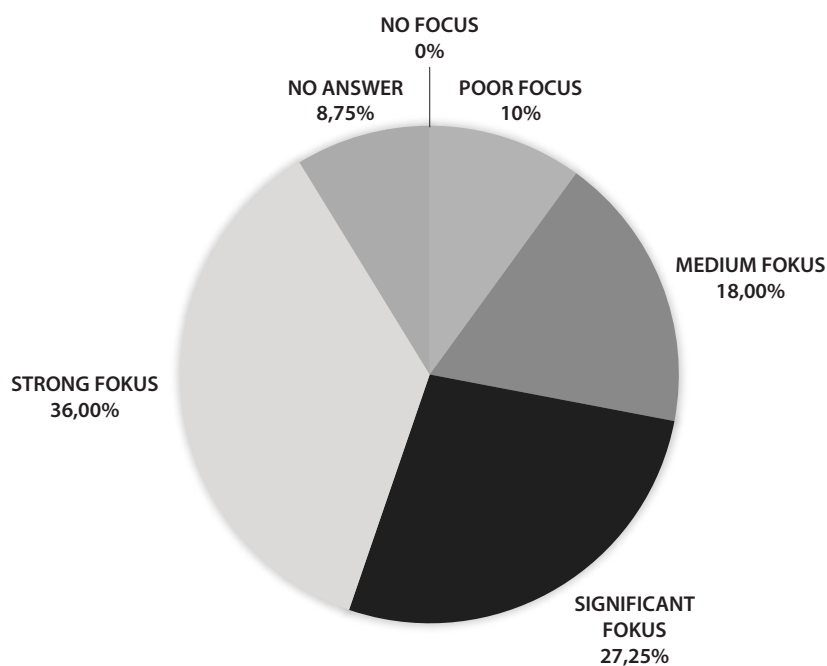


Source: Author's

Respondents evaluated the intensity of the internal audit functional focus on improving business processes on a scale from 1 to 5, whereby a rating of 1 indicates that the internal audit functional focus is not directed toward the improvement of business processes. A rating of 5 shows that it is strongly directed toward improving business processes.

Within this segment of the survey, 36% respondents believe that the functional focus of the internal audit is strongly directed toward the improvement of business processes in their companies, and 27.25% believe that this focus is significant (Fig. 2), which by consequential analysis indicates that more than half of the respondents observe the internal audit processes as successful.

Figure 2. Internal audit functional focus on the improvement of business processes



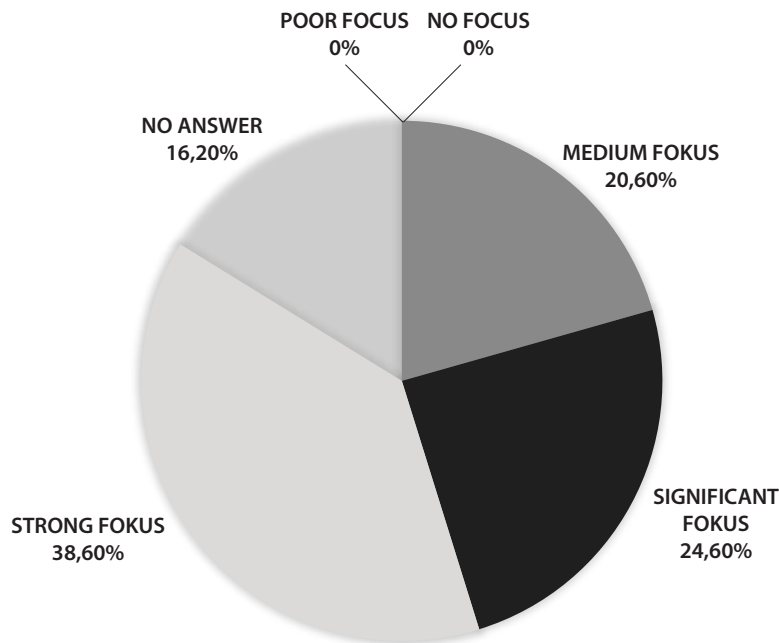
Source: Author's



Respondents rated the intensity of the internal audit functional focus and orientation toward information technologies on a scale from 1 to 5, whereby a rating of 1 indicates that the functional focus of internal audit is not directed toward information technologies and a rating of 5 means that it is strongly directed toward informa-

tion technologies. 63.2% of respondents recognized the orientation and synergy of internal audit and information technologies as significant and strongly (Fig. 3), and 20.6% of respondents' orientation is medium. 16.2% of respondents did not provide an answer.

Figure 3. Internal audit functional focus and orientation toward information technologies



Source: Author's

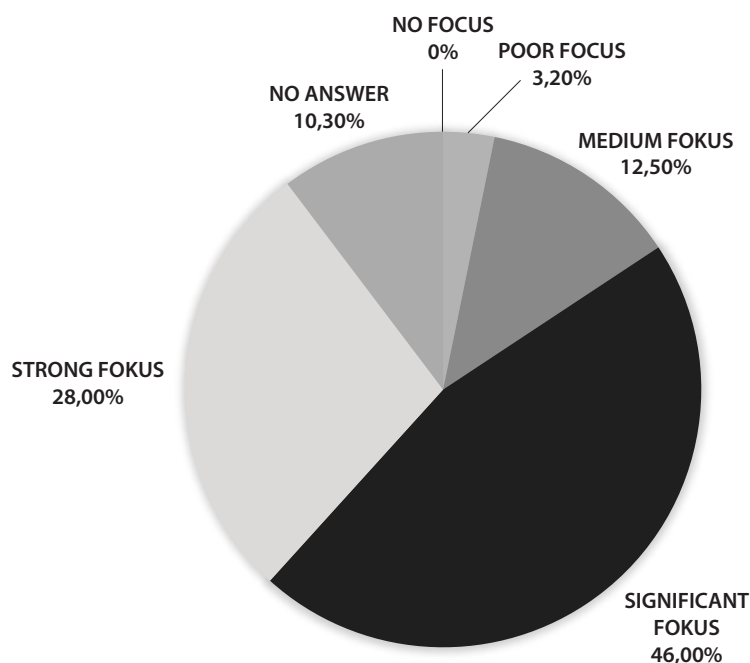
Based on the obtained results, it can be inferred that the focus of internal audit function in companies in the Republic of Serbia is significantly directed toward information technologies. In contrast it is strongly directed toward internal controls. The same number of respondents answered that in their company focus of the internal audit function is significantly and strongly directed to the improvement of business processes. 48% of those surveyed assessed that the focus of the internal audit function is directed toward internal controls, which points to the slow development of the internal audit as a profession. In those companies, there was no change in the focus of internal audit function. Therefore it cannot actively participate in the creation of value, i.e., in providing support and assistance to the company in achieving its projected goals.

The effectiveness of the internal audit department is assessed by the impact of internal audit on the quality of corporate decision-making and governance and its contribution to improving the quality of business operations. The respondents rated the effectiveness of the internal audit department on a scale from 1 to 5, where a rating of 1 indicates that the internal audit does not affect the quality of corporate decision-making and governance.

In contrast, a rating of 5 indicates that internal audit substantially impacts the quality of corporate decision-making and governance. 3.2% of respondents believe that internal audit's impact on the quality of corporate decision-making and governance is poor, while 12.5% believe that it is medium. The highest number of respondents, 46%, believe that internal audit's impact is significant, while 28% of them believe it to be strong. The answer was not provided by 10.3% of respondents (Fig. 4).



Figure 4. Impact of internal audit on the quality of corporate decision-making



Source: Author's

Based on the conducted research, it can be inferred that the internal audit department is very effective. In line with the results of the empirical research, it can be concluded that the internal audit contributes to the improvement and quality of corporate governance in the Republic of Serbia. This is supported by the fact that the internal auditor acts independently and makes objective assessments and recommendations and that the internal audit is very effective in providing an additional, higher level of supervision over the functioning of internal controls. Internal audit has a vital role in the risk management process.

5. CONCLUSION

Internal audit must continuously develop new approaches to internal audit and design new audit products and services as the entire future-oriented business becomes the scope of its examination. Internal auditors must maintain a high level of expertise, objectivity, and independence to be able to provide support and assistance to management in managing risks and designing and maintaining a complete system of internal controls. They must significantly change their approach to work – from the old, conservative, inspective, and passive approach in auditing to a new, proactive, customer-focused orientation. It can be expected that in the future, internal audit will continue to develop and evolve, enhancing its impact on the improvement of corporate governance and significantly contributing to business performance.

In line with research results, it can be inferred that internal audit improves corporate governance in the Republic of Serbia. This is supported by the internal auditor acting independently and providing objective assessments and recommendations. The internal audit effectively provides an additional, higher level of supervision over the functioning of internal controls. Internal audit has a vital role in the risk management process. Internal audit significantly impacts the quality of corporate decision-making and governance and contributes to improving business operations' quality. Sufficient attention is paid to internal audit planning, although in 13% of the surveyed companies, the plans are not flexible enough. As many as 53.12% of companies provide sufficient resources for quality internal auditing. Given the above, we can infer that the level of development of the internal audit in companies is not fully aligned with the modern understanding of its role in managing business operations. The research results indicate the presence of internal audit, its role in the companies' operations in the Republic of Serbia, and its contribution to corporate governance improvement. Still, the level of development of internal audit does not correspond to the level of development of that profession observed in countries with developed market economies. Properly defining the place and role of the internal audit in business entities can provide tremendous benefits in improving a company's performance and increasing operational and financial discipline and risk management quality. All this creates the added value of internal audit in the business environment of Serbia.



6. LITERATURE

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