CONSIDERATIONS ABOUT THE RISK ASSESSMENT AND THE INTERNAL CONTROL SYSTEM RELATED TO INVENTORIES

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Abstract
Internal control related to inventories includes the mechanisms and procedures in place implemented by the entity to assess the effectiveness of their use. The risk associated to the entity is the starting point in the elaboration and implementation of internal control procedures related to inventories. Their evaluation is analyzed from the perspective of management, financial statements audit and internal audit. Emphasis was placed on factors that could have a negative impact on the objectives and strategies in the field of inventories accounting and reporting of the entity. The research was conducted based on the analysis of conceptual content, using investigations by local specialists, as well as advanced international practices. The investigations were initiated with the analysis of the national and international regulatory framework, followed by the examination of the risk elements, and at the end of the research are presented the evaluation stages of internal control and quantitative and qualitative factors necessary to consider in inventories risk assessment from the perspective of presentation in the financials statement.

Key words: audit; financial statements; internal control; inventories; risks

JEL classification: M41, M42

I. INTRODUCTION

The evolution of the global economy determines the expansion of international trade and investments. The realization of global programs both at the level of countries and at the level of corporations, regulated by multinational treaties or agreements between different countries, determines the accelerated development of communications both through the Internet and through internal communication systems, ensured by easy access to information. These factors stimulated the need to create strong internal control systems, based on internationally recognized principles and standards that are equally understood in both the public and private sectors, in order to boost national economies, protect shareholder investment, company’s assets, as well as ensure transparency in capital markets.

This research aims to investigate issues related to inventory management, the organization and evaluation of internal control at the entity level. Although the management of the entity is responsible for their integrity, in practice there are problems related to: which function is responsible for inventory management and who is accountable for the design, implementation, operation, evaluation and reporting of internal control procedures? During the audit of the financial statements, the internal control system is tested at the level of the inventory-storage cycle, being verified in terms of access to the information system and the audit risk components. The need to improve the internal control system of inventories in the context of internal and external audit is determined by the insufficiency of theoretical research of the issue and the importance practical methodology for performing them.

The research is based on a deductive approach, from general to specific, starting from the current state of knowledge of the practical and theoretical aspects related to the audit of inventories. The applied methods such as the analysis of the specialized literature in the explored field, the comparative method, the induction and the deduction, the scientific abstraction allowed a deeper analysis of the approaches regarding the inventory audit. In the research process, the results of the investigations of local specialists were taken into account, as well as aspects of advanced international practices. The investigations were initiated with the analysis of the national and international regulatory framework, followed by the examination of risk elements, and at the end of the research are presented the evaluation stages of internal control and quantitative and qualitative factors necessary to consider for inventories risk assessment.
II. THEORETICAL AND REGULATORY APPROACHES TO DEFINE CONTROL

The word "control" has its origin in the Latin expression "contra rolus" which means "verification of a duplicate act performed after an original one". The control, from a semantic point of view, represents a "permanent or continuous verification of an activity, situation, etc., in order to follow its course and to take measures for improvement; permanent, periodic or unexpected verification, made in a certain field in order to know the realities and the way the activity is carried out in the respective field in order to prevent or eliminate the possible deficiencies and to improve the activity " (The Little academic dictionary, 2010). The other meaning of “control” is a continuous supervision, moral and material, as well as detailed research, understanding of an activity or a situation.

The specialized literature offers several meanings of the control, but the most common are:

- **Francophone significance**, which defines the control as “verification, a careful inspection of the correctness of an act” (Larousse, 1975);
- **Anglo-Saxon meaning**, according to which “the control is the act of supervising someone, something, a thorough examination or the power to lead as a tool to regulate a mechanism” (The New Merriam - Webster Dictionary, 1989).

The international regulations in the field of auditing and the specialized literature contain various approaches regarding the organization of the internal control system and its evaluation in the context of the process of financial statements audit.

In the period of ‘90s, a series of financial scandals took place in the world that highlighted the unethical and non-transparent behavior of managers of large corporations, which led to the emergence of the concept of corporate governance, which represents the system through which a company it is managed and controlled.

The control, as a function of management, has evolved continuously through the improvement of organizational systems, as well as the environment in which it is applied and which in turn is in a continuous development.

The modern evolution of the concept of corporate governance is reflected in several internal control models, which have evolved in the countries where they were created and internationally recognized:

- **COSO framework (USA)** - defines internal control as a process implemented by the entity’s management, in order to provide reasonable assurance on the achievement of objectives, in terms of effective and efficient operation, reliability of financial information and compliance with laws and regulations;
- **CoCo model (Canada)**, characterizes the control as comprising “those elements of an organization including its resources, systems, processes, culture and tasks that, taken together, support people in the achievement of the organization's objectives”;
- **United Kingdom Corporate Governance (Turnbull Report or Combined Code)** describes the internal controls as a sound system of policies, processes, tasks, behaviors and other aspects of a company.

In Europe, the concept of internal control has become more pronounced in the United Kingdom. In order to establish best practices of internal controls for entities listed on the London Stock Exchange and correct application of the UK Corporate Governance Code (initially Combined Code) was issued the guidance “Internal Control Guidance for Directors on the Combined Code” or the so-called Turnbull Report, first published in 1999. The definition of “control” according to the guide is illustrated in Figure 1 below.

![Figure 1](image_url)

**Figure 1 – The definition of “control” according to the UK Corporate Governance Code (1999)**

Source: Elaborated by the author
All mentioned frameworks and guidelines recognize the critical importance of internal control in the corporates. Therefore, in the 1990s the key internal control frameworks emerged, some of which have recently been reviewed and updated or supplemented. In addition, there are many other publications on the theory and benefits of internal control.

According to Romanian researchers Pirvan and Nişulescu (2018) the concept of internal control is not understood in all countries in the same way. Thus, there are countries with specialized internal control institutions independent of those controlled, just as in other countries the responsibility for internal control is given to the administrative institutions concerned. In decentralized systems, top management is required to report on the operation of internal control systems. More and more countries in the European Union are calling on entities to apply management systems and reduce the risk of failing to meet set targets.

International regulations in the audit field and specialized literature contain different approaches and interpretations on internal control. At the international level, the most widely recognized definition of internal control is that formulated by COSO (see www.coso.org), namely “a process, effected by an entity’s board of directors, management and other personnel, designed to provide reasonable assurance of the achievement of objectives in the following categories: effectiveness and efficiency of operations, reliability of financial reporting, compliance with applicable laws and regulations.”

According to International Standard on Auditing (IAS) 315 “internal control is the process designed, implemented and maintained by those responsible for governance, management and other personnel in order to provide reasonable assurance about the achievement of an entity’s reporting credibility objectives. financial, efficiency and effectiveness of operations and compliance with applicable laws and regulations” (see www.ifac.org).

According to scientists Arens and Loebbecke (2003) the internal control system consists of policies and procedures created to provide management with a reasonable assurance that the entity achieves its set goals and objectives.

In legislation of Republic of Moldova, internal control is defined in the National Standards for internal control in the public sector, accordingly as “a system organized by the manager of the public entity and its staff, including internal audit and financial management and control, which includes all policies, procedures, internal rules, processes and activities carried out within the public entity to manage risks and provide reasonable assurance on the achievement of planned objectives and results” (see http://lex.justice.md/md/362172/).

According to the Law on Accounting and Financial Reporting of Republic of Moldova, article 18, p. 3, letter e) among the obligations of the persons responsible for accounting and financial reporting, it is the organization of the internal control system (see http://lex.justice.md/md/373601/).

Internal control systems are a topical issue as a result of global fraud scandals and accounting scandals in both developed and developing countries. A proactive preventive approach to the issue requires a critical assessment of existing internal control structures within organizations to determine their ability to ensure that the organization’s activities are conducted in accordance with established objectives, policies and procedures.

Romanian researcher Sîrbu (2010) considers that “internal control represents the policies adopted by the management of an entity to ensure managerial objectives regarding the systematic and efficient assurance of the activity, including asset protection, prevention and detection of errors and frauds, accuracy and authenticity of instrumenting the accounting techniques, thus the financial information is credible”.

Summarizing the above statements, internal control covers all policies and procedures designed and implemented by the management of the organization, to ensure: achieving the objectives of that organization in an economical, efficient and effective way, compliance with external rules and management policies and rules, protection of assets and information, prevention and detecting fraud and errors, as well as the quality of accounting documents and the timely production of reliable information on the financial and management segment.

Duties of external and internal audit in the organization of internal control procedures related to inventories

The evaluation of internal control is one of the main tests at the planning stage of the audit mission. Understanding the internal control system and its mechanisms has significant importance in achieving the objectives of auditing financial statements. For the purpose of effectively evaluate internal control in order to reduce the planned amount of audit evidence, the auditor’s role is to understand the key concepts of the entity’s internal control and the risks associated with the audit. At the same time, the evaluation of internal control is not just an exercise in the audit mission, the company’s management must organize the internal control system even if it does not perform the audit of financial statements.

According to IAS internal control is regarded as a process “designed, implemented and maintained by those responsible for governance, management, but also by other categories of staff, to provide certainty about the fulfillment of an entity's objectives regarding credibility of situations financial, efficiency and effectiveness of operations and compliance with applicable laws and regulations”. This definition corresponds to the previous
provisions, but IAS 210 "Agreeing the terms of audit engagements" provides some additional explanations: management maintains such internal control, which it deems necessary, to allow the preparation of financial statements that do not contain significant misstatements, caused by fraud or error (see http://mf.gov.md). In our opinion, it remains at the discretion of management to determine the structure of internal control procedures necessary to provide data on the state of inventories in the financial statements.

According to IAS 265 “Communicating Deficiencies in Internal Control to Those Charged with Governance and Management” indicates two specific concepts: deficiency in internal control and significant deficiency in internal control. This distinction refers to the audit of financial statements and does not apply to the assessment of internal control by executive management. Significant internal control deficiencies related to inventories must be disclosed in writing to the person responsible for the management of the entity, accompanied by additional explanations regarding any circumstances that may arise as a result of these deficiencies. In this regard, the effectiveness of internal control procedures is assessed from the perspective of supervising the financial statements.

The auditing standards of the financial statements clearly explain the relationship between internal control and internal audit. IAS 610 "Using the work of internal auditors" states that the role of internal audit in assessing internal control is to make recommendations for improvement, ensuring the management of the entity regarding the design, implementation and efficiency of the internal control procedures. Internal audit, unlike the external one, does not only refer to the security of data from the financial statements, but assures the management of the entity to achieve its objectives, by adding value to stakeholders by using the principles of corporate governance and risk management.

In the process of testing the internal control elements, auditors could face multiple difficulties, such as:
1) the existence of approved but inefficient internal control procedures;
2) the association of two or more persons in order to exclude internal control or its inadequate ignorance by the management;
3) the psychological tendency of the management factors of the entity to reject any control, even the audit;
4) pressures to underestimate the expenses generated by the need to report, erroneously, the achievement of high performances and yields;
5) pressures for the undervaluation of commercial bonds generated by the desire to present higher levels of working capital requirements;
6) lack of internal audit within the entity;
7) essential changes in the internal control system during the year;
8) lack of analytical evidence regarding inventories, suppliers, customers, foreign exchange transactions,
9) lack of approved Chart of Authorities.

In the research of American scientists Arens and Loebbecke (2003) it is considered that the assessment of internal control and the estimation of control risk is based on three key concepts:
- management’s responsibility, which assumes that management, not the auditor, must establish and apply the entity’s internal control mechanisms
- reasonable assurance, which consists in designing an internal control system of the entity that would provide, after a cost-benefit analysis, a reasonable assurance, not absolute, that the financial statements present a true and fair view.
- the inherent restrictions, i.e. the internal control mechanisms, cannot be considered perfectly effective, regardless of the rigor of their design and application.

**Entity risk - the starting point in the design of internal control procedures for inventories**

Risk is a normal feature of a competitive economy, but the level of risk must be assessed, dimensioned and correlated with the expected profitability and the results obtained. In this perspective, corporate entities can have many risks, the main categories of which relate to operating risk, financial risk and bankruptcy risk. The risk assessment in the audit of financial statements is different and is assessed by audit firms with reference to the inherent risk, the risk of internal control and the undetected risk.

In general, the risk is the probability that an unwanted event will occur, but its intensity is different depending on the field, market trends, country, etc. The management team has to design and evaluate internal control procedures based on the entity’s risk, but the financial audit, in the process of performing the fieldwork; auditors are responsible in determining a level of risk specific to the audit activity. Therefore, the risk management requires management to focus on those issues that are difficult to resolve, and from the point of view of internal inventory control, it refers to those possible events that may distort financial-accounting information on inventories. However, the entity’s management must constantly consider actions that are favorable to the entity. Sustainability expectations of shareholders are a pressure factor for the entity’s employees. The pace of technology development and consumer demand determines strategic sustainability initiatives. Consumers are not indifferent
to the social impact on the environment and to the products or services they buy and consume. However, the opportunities in question may drive some form of risk.

The *tolerance risk* (risk appetite) means the general level of risk that the entity is willing to accept or reject certain actions in order to record value. This type of risk sets the limits for the decisions taken by the board of directors and the executive management. Entities that have adopted expanding strategies accept a higher level of risk. In the process of assessing the severity of the risk, it is compared with the risk of tolerance. The risk assessment process involves several steps. The first stage involves identifying the business risk with relevant influences on its results. The next steps are to assess the probability of their achievement, and the control procedures are implemented only for the risk with high probability of occurrence and impact on the objectives. The multitude of risks can be complemented by the separate political risk, because, lately, a series of events have taken place that have determined significant changes in the economic activity of the entity both at national and international level.

From the perspective of financial statements, we can talk about the risk of not including true information on economic operations and the value of the entity's assets in full. Management must be aware that it cannot reduce risk to zero and cautiously accept the degree of risk tolerance. For example, the decision to change some suppliers of raw materials implies the admission of a certain level of risk. The risk affects the entity's ability to compete in the market, maintain financial strength, maintain position, maintain staff, improve the overall quality of products and services, etc. At the same time, in the process of identifying and assessing risk, an entity may have opportunities. These refer to the possibility for an event to take place and to positively affect the achievement of the objectives, as presented in the Figure 2.

![Figure 2](image-url)

**Figure 2** – *The relation between the entity's risk and the internal control procedures related to inventories*

Source: Elaborated by the author

According to the Figure 2, the starting point in the design and implementation of internal control procedures is the identification of the entity's risk. The risk is evaluated according to the probability of occurrence of events that may have a negative impact on the entity's objectives and strategies. The internal control procedures related to inventories are established only for those risks with a high probability of occurrence, which means the level of controlled risk, and the residual risk represents that level specific to possible events with low and medium probability of occurrence.

**Procedure of internal controls related to inventories**

The scheme of internal control processes related to inventories is a component part of the entity's risk management. Processes are designed and implemented, usually, only for the high risk areas. The operating logarithm of these processes is illustrated in the Figure 3.

![Figure 3](image-url)

**Figure 3** – *The scheme of internal control procedures related to inventories*

Source: Elaborated by the author
As shown in Figure 3, the procedures are designed according to the risk of the entity, but in their design the three main objectives of internal control must be taken into account. The operation of internal control refers to the various actions, documented and numbered, in correspondence with the objectives to be achieved at the previous stage of control. The evaluation of these procedures is performed by the executive management based on a questionnaire structured according to the 17 control principles provided in the COSO Conceptual Framework. The results of the evaluation are presented in the management report, and its structure does not have a standardized form. This report, in addition to the financial statements and the auditor's report, must also contain other information of a financial and non-financial nature. And the information on internal control and risk is of a non-financial nature which ensures that the data in the financial statements do not contain fraudulent information (Birca, 2018).

According to IAS 315, the auditor's objective is to identify and assess the risks of material misstatement, whether due to fraud or error, in the financial statements and assertions, by understanding the entity and its environment, including the entity's internal control, thereby providing a basis for developing and implementing responses to assessed significant distortion risks.

The general stages of evaluation of the internal control system

The evaluation of the internal control from the perspective of the financial audit is performed in several stages. A preliminary assessment of the internal control system is needed to determine the level of confidence that can be placed in it. The evaluation will be performed following the determination if:

a) the internal control system has been properly designed;

b) the internal control system has been designed so as to be able to prevent and correct - improper management and non-compliance with the principles of economy, efficiency and effectiveness of the entity's resources.

In the opinion of researcher Slobodeanu (2012), the assessment of control risk can be divided into two main stages: 1) understanding the accounting and internal control system, in which the auditor tests the effectiveness and formulates a preliminary assessment of the entity's internal control system and 2) inclusion in the audit program of tests to verify the effectiveness of the internal control system to confirm the preliminary assessment.

In the audit of inventories, the general objective is to determine whether the components of inventories and the cost of goods sold are accurately presented in the financial statements, so the main tests are to obtain sufficient and adequate evidence for each significant statement contained in the financial statements. In order to perform them, auditors must apply a combination of control tests and substantive procedures depending on the strategy chosen.

Thus, the evaluation of internal control is to be focused on two important components:

1) highlighting the internal control mechanisms within the inventories-storage cycle that would minimize the control risk

2) understanding the internal control through the prism of the cost accounting system.

The local researcher lachimovschii (2007) in his doctoral thesis, offers an original view on the applicability of internal control tests at different stages of the audit. We consider that the attribution of the techniques for assessing subsequent events to the subsequent stage, after reporting the results, does not correspond to the recommendations of ISA 560, which treats the procedures for following subsequent events as a stage of completion of the audit. However, in support of the above position, we consider that in practice, during the fieldworks this process lasts even after reporting the results of the mission and expressing the audit opinion by following the degree of compliance with the recommendations being analyzed by the author in Table 1.

<table>
<thead>
<tr>
<th>No.</th>
<th>Steps for testing internal control</th>
<th>Techniques for testing internal control</th>
<th>Comments</th>
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</thead>
<tbody>
<tr>
<td>1.</td>
<td>Preliminary stage of the audit - preventive planning</td>
<td>Examination of the file previous missions, studying another relevant information</td>
<td>The auditor's documents that are part of the previous mission file of the audited subject are studied. The auditor prepares questionnaires, tests, organization charts, to be completed, updated following discussions with client staff. The control environment is evaluated under the following aspects: ethics, competence, independence of the board of directors, management style of work, policies practiced in relation to the entity's staff.</td>
</tr>
<tr>
<td>2.</td>
<td>Planning of the audit</td>
<td>Internal control risk assessment</td>
<td>The internal control risk is estimated at the level of the operations cycle and / or at the level of significant transactions depending on the specifics of the branch of activity. The assessment of the level of control risk takes</td>
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As results from Table 1 the audit of the financial statements is performed in several stages, but the testing of the internal control is performed in each stage. The management of inventories plays a key role in information in financial statements, so detailed testing often includes the recognition, measurement and accounting of inventories.

The objectives of the inventories-storage cycle audit include the following assurances:

- inventories are correctly accounted for in accordance with the requirements of the applicable regulatory framework;
- inventories posted in the accounting are confirmed by the stock-count results;
- inventories held by the entity are included in the total value of inventories at the end-of-year.
- inventories are valued in accordance with accounting policies and policies are applied consistently;
- the quantitative information presented in the inventory balance at the end of the period are correctly disclosed;
- inventories are differentiated for each financial year and a distinction is made between raw materials, work in progress and finished products, as well as between correctly recorded inventories, purchases and sales;
- slow-moving, damaged items and obsolete inventories are properly identified, assessed and recorded;
- the valuation of the work in progress is in line with accounting policies;
- records in connection with ongoing production of long-term contracts are recognized on the basis of a credible estimate to revenues and expenditures up to the completion of specific works;
- the allocation of the included indirect costs is reasonable and is made in accordance with the entity's accounting policies;
- the provisions for work-in-progress are recognized, measured and accounted for in accordance with going concerns principles and economic realities.

Within the entities, the internal controls are guarantees established by the management that come to protect the business from the technological, financial, strategic and reputational risks. In terms of auditing, internal controls ensure that the entity’s operations remain efficient and effective. From a cybersecurity perspective, internal controls protect the business from the risks that can compromise an information technology environment, and there are three main types of internal controls.

### Internal controls assessment from perspective of external auditors

From the external auditor’s perspective, the risk assessment procedures that will be sufficient to have a reasonable basis for identifying and assessing the risk of material misstatement and for designing additional audit procedures to address the material risks.

Material risks can arise from a variety of factors or can be attributed to them. Some of these factors are external by nature and could include global macroeconomic trends or internal conditions that affect the entity's industry and environment. Other factors are entity-specific and would consider issues that impact an entity's internal processes and controls, are specific to the customers an entity serves, or are the result of the type of contracts concluded by the entity. Some of the factors ultimately impact several elements present in the entity's financial statements, while others are more particular and apply to certain accounts in a very specific transaction cycle or statement.

The identification and assessment of risk factors associated with the entity and its environment is performed at the entity level risk assessment through the "top-down" procedure. The framework for conducting top-down risk assessment procedures - to gain a broad understanding of the entity and its environment and a broad understanding of its internal control over financial reporting - includes, inter alia, conducting analytical procedures for the quantitative identification of the entity, unique trends; conducting a discussion between the members of
the engagement team to collectively form a perspective on where they may be present at material risks. Therefore, gain an understanding of the entity's control environment, including all relevant processes and controls, and conduct management and governance investigations of their views on the risks of material misstatement.

**Risk assessment of internal control related to inventories**

Information regarding inventories is of significant importance in the entity's financial statements. The presented information should provide to users with a real framework, based on commercial transactions, for risk assessment at the level of accounts, respectively those specific to inventories. All bottom-up risk assessment factors should be supplemented by applicable entity-specific and environmental risk factors identified by the top-down entity-level risk assessment that could directly or indirectly affect the associated risks related to inventories and the inventories-storage cycle.

The risk assessment procedures at the level of inventory accounts must contain the following actions:

a) in-depth understanding of inventory accounting requirements in the applicable financial reporting framework;  
b) in-depth understanding of the nature of the transactions leading to the account balance, the relevant controls and processes (including related accounts / statements) covering the transactions circulating in the account balance, and the competence of the persons and / or reliability of the systems actually performing such controls and processes;  
c) a current view of inventories account activity or account composition in relation to historical norms (time series observations) and / or current external or internal activities (cross-sectional observations) using a variety of relevant analytical procedures.

The analysis of the content of the inventories valuation actions leads us to state that they must be carried out separately in the first stage because separate documents are verified. Subsequently, due to their unique risk profile, they need to be compared and merged through a single conclusion.

There are a number of unique considerations that need to be verified whenever possible, namely:

- possible fraud considerations;
- economic transactions with related parties;
- significant economic transactions (nonroutine) that do not take place daily;
- does the entity use the LIFO method in the current valuation of inventories?
- does the entity use the Retail method in inventories recognition?
- were sales-purchase contracts detected without delivery?
- the entity's accounting policies related to the transfer of tangible assets and decommissioning to inventories;
- the entity's accounting policies related to the valuation and recognition of spare parts, consignment goods.
- management attitude and staff towards onerous contracts and hedged inventories (Hedged inventory);
- purchases and sales of inventories with the same third parties;
- entity's accounting policies related to the use of accounts for impairment of inventories and provisions for risks and expenses;
- criteria for classification and evaluation of inventories according to quality and value (eg differentiated liquids based on purity or concentration levels).

For example, a manufacturing entity has stocks of raw materials, finished products and work in progress. The turnover and the quantity available at the end of the management period are analyzed on each type, assortment separately. Therefore, it is recommended to evaluate each category of inventories separately. The evaluation criteria of the finished products are different from those of the raw materials - the entity may have different systems and / or controls due to their nature and location.

Similarly, a manufacturing entity may have inventories held in different locations, including third party warehouses. The third party may have different policies and strategies in the field of inventory management and valuation. Based on this agreement, the level of risk of existing inventories in third-party deposits may be different from that in the entity's deposits. Thus, it is recommended to divide, in the first stage, the risk assessment of existing inventories in the entity's warehouses from those held by third parties. Subsequently, they are compared, analyzed, and finally a unique conclusion is established.

The research shows that information on inventories presented in financial statements represents a significant factor in risk assessment. In the Figure 3 represents details of possible factors that usually generate risks and have an impact on the information related to the inventory presentation in the financial statements prepared by the entity.
As shown in Figure 4, the criteria used in assessing the risk of internal control related to inventories are covering differing aspects of the company activity. Their complexity is determined by the significance and role in decision making. Therefore, information on inventories has a key role in the financial statements which requires a detailed analysis in terms of quantity and quality.
III. RESULTS AND CONCLUSIONS

The modern evolution of internal controls systems knows several periods, mainly intensified after big scandals in the corporate word. The internal controls importance resulted in the concept of corporate governance, regulated in the frameworks such as COSO, COCO and UK Corporate Governance Code. Internal control refers to those policies and procedures designed and implemented by the management of the organization, to ensure reliable information in financial reporting. The system of internal controls in the entity are assessed from differed perspective – management, internal audit and external audit. At the same time, the entity must provide a level of assurance for the quality of the information provided in the financials statement as well as accounting documents.

The starting point in the design and implementation of internal control procedures related to inventories is the identification of entity's risks. It is evaluated according to the probability of occurrence of events that may have a negative impact on the entity's objectives and strategies. The internal control procedures related to inventories are established only for those risks with a high probability of occurrence, which means the level of controlled risk, while the residual risk represents that level of specific, possible events with low and medium probability of occurrence.

The financial statements provide users with a real framework, based on commercial transactions, for risk assessment at the level of accounts, respectively those specific to inventories. The bottom-up risk assessment factors should be supplemented by top-down risk factors that could directly or indirectly affect the risks associated with inventories balances as well as transaction in the inventory-storage cycle. At the same time, all the factors that can affect the level of risk must be taken into account, namely: quantitative factors, economic transactions, the level and fluctuation of prices for all types of inventories. From the perspective of the external audit, assessment of internal controls related to inventories are performed considering the risk factors associated to volume/qualitative, processes, transaction specific, nature of inventories, pricing/valuation and accounting and reporting.

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