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## POSITIONING INTERNAL AUDIT IN THE CORPORATE GOVERNANCE SYSTEM: CASE OF THE REPUBLIC OF SERBIA

Pozicioniranje interne revizije u sistemu korporativnog  
upravljanja u Republici Srbiji

### Abstract

The aim of this paper is to determine the position of internal audit in the corporate governance system in the Republic of Serbia. In this regard, it analyzes the achieved level of internal audit establishment in companies, with special focus on different factors affecting it, to provide a clearer view of the current situation. Given the fact that the internal audit position is determined by the scope and role of this function, the study also covers these issues. Empirical research focuses on a sample of 113 companies from the private sector. Research results indicate that the establishment of internal audit in companies in the Republic of Serbia is at a satisfactory level, as it is significantly influenced by regulatory obligations, origin of capital, and number of employees. Also, research reveals that internal audit has exceeded its traditional assurance role, and that, by auditing all the processes and activities in a company, it provides advisory services to managers.

**Keywords:** *establishment of internal audit, role and activities of internal auditors, creating added value, Republic of Serbia.*

### Sažetak

Cilj autora ovog rada jeste utvrđivanje pozicije interne revizije u sistemu korporativnog upravljanja u Republici Srbiji. U tom smislu, analiziran je ostvareni nivo uspostavljenosti interne revizije u privrednim društvima, i posebno je ispitivana njegova uslovljenost različitim faktorima kako bi se obezbedilo jasnije sagledavanje postojećeg stanja. Činjenica da je pozicioniranje interne revizije determinisano delokrugom rada i ulogom koju ova funkcija preuzima, istraživanjem su obuhvaćena i ova pitanja. Empirijsko istraživanje sprovedeno je na uzorku koji je činilo 113 privrednih društava iz privatnog sektora. Rezultati istraživanja ukazuju na to da je nivo uspostavljenosti interne revizije u privrednim društvima u Republici Srbiji na zadovoljavajućem nivou, pri čemu značajan uticaj na to ima regulatorna obaveza društava, poreklo kapitala i broj zaposlenih. Takođe, istraživanjem je utvrđeno da je interna revizije prevazišla svoju tradicionalnu ulogu uveravanja i da revidirajući sve procese i aktivnosti u privrednom društvu, upravljačkim strukturama pruža i savetodavne usluge.

**Ključne reči:** *uspostavljanje interne revizije, uloga i aktivnosti interne revizije, kreiranje dodate vrednosti, Republika Srbija.*

## Introduction

If, in the broadest sense, corporate governance is defined as a structure and process of management and control of an enterprise, and if internal audit is defined as an internal control mechanism of an enterprise, it can be reliably concluded that the interrelation of the two is not a new phenomenon. Internal audit has always been focused on evaluation of effectiveness, efficiency and legitimacy of business processes and activities in an enterprise, and therefore it has significantly influenced quality and business outcomes. However, at the end of the 20th century, it became clear that the previous practices of corporate governance are not suitable for responding to the increasingly complex business environment. This was additionally confirmed at the beginning of the 21st century, when poorly established mechanisms of corporate governance and control have been identified as two causes of financial and economic crisis. The need for overcoming these problems has, among other reasons, caused setting new requirements that internal audit must satisfy.

In addition to a significant improvement of services related to assurance about outcomes and implementation of strategic processes, internal audit was expected to get involved in their development and advancement as well. The management of any enterprise was in need of greater support from internal audit in terms of getting constructive solutions for business enhancement and overcoming identified problems. Thus, requirements for the development of internal audit were oriented toward defining consultative services, based on which internal audit would assist managers in corporate governance. Since internal audit has accepted these challenges, its place, role and activities in the system of corporate governance, as well as its relationship with corporate governance, have attracted interest of both theorists and practitioners.

Today, internal audit, as an independent organizational function, provides assurance about effectiveness of all business functions in an enterprise, and it also provides advice to managers in fulfilling their responsibilities.

Internal audit continuously performs activities which are proactively oriented toward creating additional value for an enterprise, which is why it has a strategic

role in managing its business operations. More precisely, internal audit is integrated into corporate governance system, and its activities are directed toward providing support to other participants in the corporate governance by evaluating the best business practice and reviewing possibilities for its adoption. By performing the described role and activities, internal audit becomes connected to all participants in the processes of management and control of an enterprise, and therefore its position in the corporate governance system is considered unique. Recognition of the value of support it provides to the abovementioned participants in fulfilling their own responsibilities made internal audit a common practice in an increasing number of enterprises.

The paper, comprising three parts, is structured as follows. The first part includes a short revision of internal audit's role and activities which made it the key participant in the corporate governance system. Empirical research on positioning of internal audit in the corporate governance system in Serbian enterprises, including the main results, is described in the second part of the paper. The third part provides recommendations related to raising the level of awareness about the importance of internal audit and the contribution it could provide to the management, which would surely strengthen its position in the corporate governance system.

## Theoretical basis of the research: Internal audit's position in the corporate governance system

Internal audit, according to the definition of the Institute of Internal Auditors (IIA), a professional organization with the greatest impact on its development and organization, is "*an independent, objective assurance and consulting activity, designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes*" [14]. With this definition, IIA emphasizes that internal audit plays the role of: (1) provider of objective and independent assurance of adequacy of the established management structure and efficiency in carrying out specific management activities; and (2) catalyst

for change by providing advice and guiding activities, with the aim of improving corporate governance structure and practice [15, p. 4]. Its function is characterized by 3R:

- Referencing – determining observation parameters, i.e. translating strategic objectives into parameters that the audited entity should adopt;
- Representing – providing details about the observed parameters that have been previously defined, and thus giving a clear picture of the audited entity, and
- Recommending – providing recommendations depending on the real situation of the audited entity [3].

In addition, internal audit activities aim at: promoting appropriate ethics and values in the company; providing assurance about the effectiveness of management performance and responsibilities; communication of information on risk and control and the extent to which risks are controlled; coordinating activities and communicating information between board of directors, external auditors and management; evaluating the design, implementation, and effectiveness of achieving ethical goals, programs, and activities; checking and verifying the level of company's business compliance with policies and procedures; providing recommendations for improving policies and procedures when there is an adequate opportunity to improve performance [1, p. 165], [7].

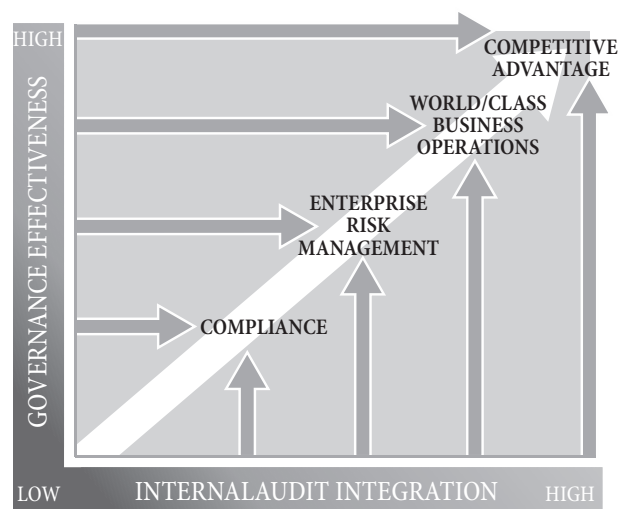
By doing this, internal audit is able to provide very important information for more reliable, safer, and faster business decision-making or to provide assistance to management in carrying out their obligations. Therefore, the work of internal auditors, materialized in the form of analyses, recommendations, assessments, relevant comments on audited activities, etc., is considered to be the work aimed at creating added value and represents "the necessary assistance in collecting the information necessary for effective management" [6, p. 37]. In fact, the IIA clearly advocates the view that the fundamental concept of modern internal audit is the creation of added value for the company in a way that "ensures the achievement of company goals, identifies opportunities for improvement, and reduces risk exposure through assurance and consulting services" [16]. It is understood that internal audit creates added value by integrating itself into the corporate governance system, and the achieved

level of integration, again, determines the value this function is able to provide (Figure 1).

Certainly, in order for internal audit to be proactive – the driver of changes in a company, innovative – creating opportunities to increase value, focused – on the management and the company within which it operates, and motivated to offer suggestions that lead to continuous improvement, it needs to be functionally independent (planning activities independently, carrying out work and reporting on performed audits without any influence) and organizationally independent (independence in relation to other organizational parts of the company and smooth access to them). Such independence implies the organization of internal audit as a separate function in a company, occupying the very top of the management hierarchy, while carrying out work under the direct control of the appropriate board of directors (administrative or supervisory).

Previously described internal audit action defines it as a frontal function which, by applying the partnership approach to management, becomes a link vital to the company. Its position is strategically important, allowing it to greatly improve company's performance [5, p. 81]. However, although there is no doubt that internal audit is, due to its dual role (assurance and consulting) which covers the functioning of the entire business system, one of the key players in the corporate governance system, in

**Figure 1: Increased organizational value through the integration of internal audit and governance**



Source: [8].

practice it is only experiencing its expansion. This is due to the fact that its development from “management audit” to “corporate governance audit” [13, p. 3] is associated with relatively recent past. More precisely, for a long time, internal audit was characterized as “the subfunction of the accounting function which it audits” [11, p. 51]. By the 1980s, the scope of its work reached a high level of control over all business functions in a company, and internal audit became a combination of [4, p. 54]: financial audit, compliance audit, operational audit and management audit. As such, its role was significant, but at the same time it provided only partial benefit to the management. The development of an additional role, the role of consulting, which ensures that internal audit is not seen as a “policeman” whom management is avoiding, but rather as an expert sought by the management [9, p. 33], is related to early 1990s. That is when, in fact, the affirmation of internal audit as the key participant in the corporate governance system and the esteemed part of the company’s management has begun [2].

Recognizing the importance of internal audit and its establishment in the company surely requires an appropriate temporal distance, not only in countries in transition, but also in those in which this profession is most developed. As a result, efforts have been made in this regard by a number of professional bodies, which deal with the issues of internal audit organization and functioning in their reports. Also, legislative bodies of all countries are increasingly obliging companies to establish internal audit and regulate its position and role. Thus, in the United States, the Treadway Commission and the Blue Ribbon Committee reports have made significant contribution to the development of the role of internal audit in the corporate governance system. In addition to these reports, the Sarbanes-Oxley Act, a radical corporate governance law, has a significant impact on internal audit practice, although it does not contain specific provisions that point to its position and role. In the EU member states, the report issued by the European Confederation of Institutes of Internal Auditing (ECIIA) and the Eighth Directive (2006/43/EC) showed a significant shift in the positioning of internal audit in the corporate governance system. In this respect, in most countries today, internal

audit is mandatory in companies listing their shares, as well as in financial organizations.

In the context of the Republic of Serbia, it can be said that today’s regulatory solutions are satisfactory, since the first institutional framework was set by the National Bank of Serbia in the mid-1990s, passing decisions binding banks to establish an internal audit service. It was not until the beginning of the 21st century that the situation changed significantly with the adoption of the Law on Banks, the Insurance Law and the Law on Companies. More specifically, the Law on Banks and Insurance Law oblige these organizations to establish internal audit. However, the 2004 Law on Companies did not place internal audit in an affirmative position that allows it to capitalize on its potentials. This is because the law saw internal audit, supervisory board, and audit committee as three identical, equal, and mutually interchangeable forms of internal control, with the same objectives and scope of work [17], which is why internal audit did not need to be established. The described shortcoming of the 2004 Law on Companies was remedied by the new Law on Companies adopted in 2012. More specifically, according to Article 451 of the new Law, the company regulates the way of conducting and organizing internal control by its acts, whereby only public joint stock companies undertake that at least one person in charge of internal control must meet the requirements prescribed for the internal auditor. In other companies, there is no obligation to establish internal audit, and the Law on Companies only encourages them to do so.

The relevant laws also define internal audit’s responsibilities (Table 1).

In addition to legislation, a more specific definition of the role and scope of internal audit in companies is determined by the Corporate Governance Code adopted by the Serbian Chamber of Commerce. The recommendation of the Code which, truthfully, does not have a binding character, is that “the company should establish an internal audit function which, in addition to assurance, can provide the management with advisory services and objective, independent opinions on numerous issues related to corporate governance, risk management and internal control processes, adding value and contributing

**Table 1: Internal audit regulatory framework in the Republic of Serbia**

Law on Companies	<p>Article 452 specifies the tasks performed by internal auditors:</p> <ul style="list-style-type: none"> <li>• control the compliance of a company with the law, other regulations and corporate acts,</li> <li>• oversee the implementation of accounting policies and financial reporting,</li> <li>• check the implementation of risk management policies,</li> <li>• monitor compliance of the organization and activities of the company with the corporate governance code and</li> <li>• evaluate policies and processes in a company, as well as proposals for their improvement</li> </ul>
Law on Banks	<p>According to Article 85, internal audit is obliged to:</p> <ul style="list-style-type: none"> <li>• assess the adequacy and reliability of the bank's internal control system and the compliance function,</li> <li>• ensure that risks are appropriately identified and controlled,</li> <li>• identify weaknesses in the operations of the bank and its employees, as well as non-execution of obligations, overstepping of authorizations and preparation of proposals for removing these weaknesses</li> </ul>
Insurance Law	<p>Article 137 stipulates that the internal audit of the insurance company shall carry out a permanent and comprehensive control of all business activities, in particular:</p> <ul style="list-style-type: none"> <li>• continuous monitoring, checking and improving the system of internal control and compliance,</li> <li>• identification of risks to which the company is exposed or can be expected to be exposed,</li> <li>• assessment and evaluation of the established internal control system,</li> <li>• issuing appropriate recommendations for remedying detected irregularities and deficiencies and for improving the procedures and work procedures applied</li> </ul>

Source: [18], [19], [20].

to increasing the overall efficiency and improvement of a company” [10].

## Achieved position of internal audit in the corporate governance system in the Republic of Serbia – empirical research

### Research description

#### *Subject, objective, and methodology of research*

The research subject in this paper is the position of internal audit in corporate governance in the context of the Republic of Serbia. The research objective is to provide an answer to the question whether internal audit is incorporated into the corporate governance system in the Republic of Serbia and how it contributes to the said system. For the purpose of achieving this goal, the following research questions have been defined:

- (1) What is the level of internal audit establishment in companies in the Republic of Serbia?
- (2) What are the factors that determine internal audit establishment in companies? and
- (3) What is the scope of internal audit and does it, in addition to traditional assurance services, also provide advisory services?

With the aim of determining the level of internal audit establishment in companies in the Republic of Serbia and the factors affecting it, two-level research was carried

out. The representation of internal audit was examined based on several criteria, first in all companies from the sample, and then in different groups of companies. This way, it was possible to obtain more detailed findings and a better insight into the level of internal audit organization in different types of companies. The research relied on data referring to the obligation of organizing internal audit, on the one hand, and actual situation in companies in the Republic of Serbia, on the other. In particular, the position of internal audit in the corporate governance system is determined by the level of (non)establishment of internal audit in companies in the Republic of Serbia with regard to (1) the obligation arising from the provisions of relevant laws and other regulations, and (2) the existence of managers' awareness of benefits and contributions this function provides.

Also, internal audit position is significantly determined by its scope and role. In addition to providing assurance about efficiency and effectiveness of all processes and activities in the company, internal audit is also better positioned since it provides advice to the management aimed at improving their activities and processes, and, in general, the overall company operations. In this sense, the achieved extension of the role and scope of internal audit will be determined by comparing the actual role and activities of internal audit in companies, on the one hand, and regulatory solutions and theoretical settings, on the other.

*Data collection and sample*

The initial research was conducted in the period from July to November 2015, and again from February to April 2016. The sampling frame, comprising active companies in financial and non-financial sectors registered with the Business Registers Agency (BRA), was limited to:

- Limited liability companies and joint stock companies in which the ownership function is separated from the management function<sup>1</sup>
- Companies in the private sector<sup>2</sup>.

First, the research included collecting data on whether internal audit was established in companies. The relevant data were obtained for 113 out of 372 randomly selected

companies meeting the predefined selection criteria, both from companies' official websites and in direct contact with them – either by e-mail or telephone. The response rate, which in this case was 30.37%, can be considered acceptable for this type of research, and therefore research requirements fulfilled. Internal audit was established in 68 (60.18%) out of the total number of companies from the sample, while in 45 (39.82%) it was not. Descriptive statistics of companies are presented in Tables 2 and 3, for those with established internal audit and for those without it, respectively.

Due to the fact that 39.82% of companies in the sample did not have internal audit established, we considered it important to identify reasons for this by collecting and analyzing the data, as well as to determine future tendencies regarding its potential establishment. Accordingly, the questionnaire was sent to the managers of these companies. At the same time, in companies with internal audit established, the questionnaire was sent to chief audit executives to collect data on its scope and roles.

**Table 2: Characteristics of companies in which internal audit is established**

Sector affiliation and form of companies	Non-financial sector			Financial sector		Σ
	Public JSC	JSC	LLC	Banks	Insurance companies	
Frequency	18	11	9	18	12	68
Relative participation	26.47%	16.18%	13.24%	26.47%	17.65%	100%
<b>Origin of capital</b>	<b>Domestic</b>	<b>Foreign</b>	<b>Mixed, majority domestic</b>	<b>Mixed, majority foreign</b>		<b>Σ</b>
Frequency	9	35	16	8		68
Relative participation	13.24%	51.47%	23.53%	11.76%		100%
<b>Number of employees</b>	<b><math>X \leq 50</math></b>	<b><math>50 &lt; X \leq 250</math></b>	<b><math>250 &lt; X \leq 500</math></b>	<b><math>X &gt; 500</math></b>		<b>Σ</b>
Frequency	8	19	16	25		68
Relative participation	11.76%	27.94%	23.53%	36.74%		100%

Source: Results of authors' research.

**Table 3: Characteristics of companies in which internal audit is not established**

Sector affiliation and form of companies	Non-financial sector			Financial sector		Σ
	Public JSC	JSC	LLC	Banks	Insurance companies	
Frequency	4	24	17	/	/	45
Relative participation	8.89%	53.33%	37.78%	/	/	100%
<b>Origin of capital</b>	<b>Domestic</b>	<b>Foreign</b>	<b>Mixed, majority domestic</b>	<b>Mixed, majority foreign</b>		<b>Σ</b>
Frequency	25	7	7	6		45
Relative participation	55.56%	15.56%	15.56%	13.33%		100%
<b>Number of employees</b>	<b><math>X \leq 50</math></b>	<b><math>50 &lt; X \leq 250</math></b>	<b><math>250 &lt; X \leq 500</math></b>	<b><math>X &gt; 500</math></b>		<b>Σ</b>
Frequency	9	16	11	9		45
Relative participation	20%	35.56%	24.44%	20%		

Source: Results of authors' research.

## Analysis and discussion of research results

Determining internal audit position in the corporate governance system implied, firstly, an analysis of internal audit establishment in companies in the Republic of Serbia. The results of this analysis revealed, as already mentioned, that internal audit was established in 68 out of 113 companies (60.18%), which makes a rather high share. In contrast, in 45 companies, or 39.82%, internal audit was not established. In order to examine the existence of specifics or particular characteristics of companies in such defined groups (those in which internal audit was established and those in which it was not), the analysis was expanded and companies from both groups were additionally classified according to supplementary criteria. The characteristics based on which these two groups of companies were observed and which were used to define independent variables, assuming that they are the ones with the greatest influence on internal audit establishment (taken as dependent variable), are as follows:

- (a) Sectoral affiliation and legal form (established variable being regulatory obligation – RegOb<sup>3</sup>)
- (b) Origin of capital (OrCap), and
- (c) Number of employees (NumEmp).

In order to confirm the assumption of influence of regulatory obligation on the establishment of internal audit, a correlation analysis was conducted and the Pearson correlation coefficient calculated in Table 4.

Data in Table 4 indicate that the correlation analysis of regulatory obligation and internal audit establishment confirms the positive correlation between these variables, i.e. the assumption that the regulatory obligation affects

internal audit establishment in companies in the Republic of Serbia. In fact, this is a moderately strong correlation, since  $r = 0.606$ . The clarification of this strength with a more detailed presentation of internal audit positioning in companies in the Republic of Serbia is given in descriptive statistics. Specifically, 48 out of 68 companies (70.59%) in which the internal audit was established had a regulatory obligation to do so, while the remaining 20 companies did not have this obligation. In almost 1/3 of the identified companies internal audit was established as a result of management's awareness of the contribution this function can provide, and it is precisely this fact that indicates that internal audit has the opportunity to capitalize on its potentials to improve the corporate governance. On the other hand, among the companies where internal audit was not established, the vast majority (91.11%) was not obliged to do so. In fact, in this group, there were 4 public joint stock companies legally obliged to establish internal audit, which is certainly a matter of concern. However, a deeper look into the issue revealed that in these companies internal audit formally existed, foreseen by work systematization, but the process of appointing an internal auditor and organizing their work was in progress.

The impact of the remaining two factors (the origin of capital and the number of employees) on the establishment of internal audit was observed in a narrow context – only in those companies not obliged by legislation to establish internal audit. This is because financial organizations (banks and insurance companies) and public joint stock companies, regardless of the origin of capital and the number of employees, need to have internal audit, and it is not very useful to analyze the impact of other factors. Therefore, financial organizations (40) and public joint stock companies (22) were excluded from the impact analysis of these two factors.

3 According to the relevant laws in the Republic of Serbia, and taking into account the defined research subject, only financial organizations (banks and insurance companies) and public joint stock companies have the obligation to establish internal audit.

**Table 4: Correlation analysis of the establishment of internal audit and regulatory obligations**

		RegOb	Establishment
RegOb	Pearson's correlation	1	.606 <sup>**</sup>
	Significance of the difference		.000
	N	113	113
Establishment	Pearson's correlation	.606 <sup>**</sup>	1
	Significance of the difference	.000	
	N	113	113

\*Correlation is significant at the 0.05 level (2-tailed).

\*\*Correlation is significant at the 0.01 level (2-tailed).

The study of the influence of the origin of capital on the establishment of internal audit included conducting the correlation analysis and the calculation of the Pearson correlation coefficient, as shown in Table 5.

Data in Table 5 indicate that the origin of capital had influence on the establishment of internal audit ( $r = 0.338$ ,  $N = 61$ ,  $p < 0.05$ ). In companies where internal audit was established, foreign capital was dominant (87% have exclusively foreign capital or mixed, mostly foreign). In contrast, predominantly domestic capital (73.19% exclusively domestic or mixed, mostly domestic) was found in companies in which internal audit was not established. In addition, the fact that foreign capital was dominant in all 20 companies that did have internal audit although they were not obliged to have it, further points to the conclusion that internal audit practice in companies in the Republic of Serbia is largely carried out and developed under the influence of good practice in countries from which the capital originates.

Investigating the impact of the number of employees on the establishment of internal audit was done by comparing the arithmetic mean of the number of employees between the groups of companies that have and those that do not have internal audit. A statistical t-test was used, along with the Levene's equality of variances test, and the results obtained are shown in Table 6.

Table 6 shows that enterprises with internal audit had a significantly higher average number of employees (829.93)

than those in which this function was not established (430.95). The difference between the average number of employees is 467.88, and the investigation revealed that this difference was statistically significant ( $\text{Sig} = 0.01$ ). A linear relationship between the number of employees and the establishment of internal audit was confirmed by the Pearson correlation coefficient, as shown in Table 7.

The data presented in Table 7 shows that the increase in the number of employees (in enterprises within the research sample) influences the increase, of the same degree, in the number of enterprises in which the internal audit is established. This further suggests that the management of a company with a larger number of employees recognized the need to establish partnership relations with internal audit in business management.

The presented results of the conducted empirical research provide a sufficient basis for expressing the opinion that internal audit establishment in companies in the Republic of Serbia is at a satisfactory level. This opinion is further confirmed by the fact that internal audit, although a profession with a long history, has experienced its expansion even in the most developed countries of the world in the last twenty years, and its institutionalization in the Republic of Serbia is linked to relatively recent past. Also, recognition of this function's potential and the adoption of the best practice certainly require a certain temporal distance, especially if the general economic situation in our country is taken into account.

**Table 5: Correlation analysis of the establishment of internal audit and origin of capital**

		OrCap	Establishment
OrCap	Pearson's correlation	1	.338(**)
	Significance of the difference		.005
	N	61	61
Establishment	Pearson's correlation	.338(**)	1
	Significance of the difference	.005	
	N	61	61

\*Correlation is significant at the 0.05 level (2-tailed).

\*\*Correlation is significant at the 0.01 level (2-tailed).

**Table 6: The difference in the number of employees in companies that have/do not have internal audit**

Establishment of internal audit	Number of companies	Mean	Std. deviation	Std. error of mean
Yes	20	829.93	861.83	157.91
No	41	362.05	430.95	69.91

	Mean difference	Std. error of difference	t	df	Sig. (2-tailed)
Employment	467.88	172.18	2.717	40.35	0.01



This is indicated by the data obtained from companies in which internal audit was not established, related to future tendencies to establish internal audit and the existence of reasons for which it has not yet been established (Table 8).

Data in Table 8 show that 9 out of 45 companies (4 due to legal obligations and 5 aware of the importance of this function) plan to introduce internal audit in the upcoming period, which does not present a particularly enviable situation. However, an additional analysis of the reasons why the remaining companies do not plan to establish this function provides further clarification of the matter. Specifically, the respondents were given the opportunity to provide multiple answers as to why they do not plan to set up internal audit in their companies. Most of them pointed out that the introduction and operation of internal audit would incur high costs and require large organizational efforts (which would again bring corresponding costs), which the company could not bear. A relatively small number of respondents did not recognize the benefits of internal audit, and there was also a small number of those whose answers (“The company has internal control”, “Existing controls of

production processes through the application of HACCP quality control systems are sufficient”, “Application of SRPS ISO 9001, SRPS ISO 14001, OHSOS 18001, SRPS ISO 27001 standards sufficiently regulates operations”), in fact indicate that these are the companies where internal audit is not properly understood. Based on this data, it can be concluded that managers of the vast majority of these companies understand the importance of internal audit, which implicates a positive attitude. However, the behavioral aspect, which includes internal audit establishment and implementation activities, is now in most cases lacking, not because of the lack of understanding of its importance and lack of will, but because of organizational constraints.

Previous data indicate that a satisfactory number of Serbian companies in the sample incorporated internal audit into their organizational structure. In the majority of companies (61 out of 68, i.e. 89.71%), internal audit is organized as a separate function in the company, while in other cases (7 out of 68, i.e. 10.29%) it is organized within the function of accounting and finance. Furthermore, in addition to organizational independence, appropriate functional independence was established (internal audit

**Table 7: Correlation analysis of the establishment of internal audit and number of employees**

		NumEmp	Establishment
NumEmp	Pearson's correlation	1	.266 (**)
	Significance of the difference		.028
	N	61	61
Establishment	Pearson's correlation	.266 (**)	1
	Significance of the difference	.028	
	N	61	61

\*Correlation is significant at the 0.05 level (2-tailed).

\*\*Correlation is significant at the 0.01 level (2-tailed).

**Table 8: Prospects for the establishment of internal audit in the future**

Future tendencies for establishment of internal audit		
	Number of companies	%
Establishment is planned in the upcoming period	9	20
Establishment is not planned in the upcoming period	36	80
Total:	45	100

Reasons why internal audit establishment is not planned		
	Number of companies	%
They do not recognize the benefits	6	10.00
Great organizational efforts	19	31.67
High operating costs	27	45.00
Other	8	13.33
Total:	60	100

Source: Results of authors' research.

independently planned its activities, which in 77.4% of cases were approved by the relevant management body – administrative or supervisory board, and in 84.9% of cases it was responsible for its work to the administrative/ supervisory board). However, the fact is that mere establishment of internal audit does not necessarily imply that the management places a lot of trust in it. The significance of its position in the corporate governance system, among other things, also depends on its scope and the services it provides to management structures.

The role and activities of internal audit in companies in the Republic of Serbia have been examined in the conducted research. The results point to a high level of compliance of Serbian companies' internal audit practice with legal provisions and contemporary trends in the development of this profession. More precisely, in addition to performing various administrative tasks (5.9% of share in their everyday work), internal auditors are significantly focused on:

- Financial audit, i.e. verification of the reliability of the accounting and information systems, and the annual reports that result from it (31.7%),
- Audit of risk management processes and policies (46.12%), and
- Audit of efficiency and effectiveness of business processes (16.58%).

In addition, the abovementioned audits include the verification of consistent application of regulations and the efficiency and effectiveness of established internal controls related to the given areas. As expected, there are differences in the share of individual activities of internal auditor's everyday work between companies in non-financial and financial sectors. More precisely, audit in financial organizations predominantly includes the audit of risk management processes and policies with 51.02%, while in the non-financial sector internal auditors still mostly focus on the adequacy of accounting policies and financial reporting (64.28%).

Also, the research findings indicate that in almost all companies internal audit provides advice on the elimination of the identified deficiencies, i.e. further improvement of the audited processes and activities, which consequently contributes to the improvement of the overall business operations of the company.

## Instead of conclusion

The results of the conducted empirical research indicate that the development of internal audit practice in the Republic of Serbia is at a satisfactory level. Nevertheless, further improvement of its position in the corporate governance system is, of course, possible.

Regarding internal audit establishment, the fact is that the existing legislation in Serbia does not differ from that in developed countries, and according to it, this function is mandatory only in public companies and financial organizations, while in others it is recommended. For these reasons, raising the level of internal audit establishment may be aimed at raising the company management's awareness about its significance. This can be ensured by the continuous promotion of this profession, its scope, as well as by presenting information on the best practice. An important role, most certainly, has already been taken over by the Association of Internal Auditors of Serbia. This association accomplishes its mission of promoting internal audit in Serbia, supporting professional development of its members, and strengthening their influence in the corporate environment by organizing professional seminars, conferences, roundtable discussions, etc., providing translations of foreign literature, announcing regional events in public, etc. For these reasons, greater support of state institutions to this professional organization would certainly have positive influence on the development of internal audit profession and practice in Serbia.

At the same time, although the research results suggest that internal audit respects the adopted professional regulations by assuming a dual role directed at the entire company operations, improvements are possible in this direction. More precisely, it is not enough to align internal audit functioning with standards, but it is also necessary to make additional efforts that will enable it to reach its full potential. The best practice indicates that an important condition of the proper functioning of internal audit is, among other things, the establishment of an organizational culture in a company that would lead to employees' awareness of the significance and possible contribution of internal audit. This would lead to a true understanding of the purpose of this function and eliminating the view that it is an activity carried out to detect errors and find

the culprits. Significant efforts in this direction include the improvement of communication between internal audit and stakeholders because, through open communication, this function would properly assess their needs and direct its activities toward delivering the required value, not only toward legally required activities.

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