IOSR Journal of Business and Management (IOSR-JBM)
e-ISSN: 2278-487X, p-ISSN: 2319-7668. Volume 16, Issue 1. Ver. IV (Jan. 2014), PP 68-72
www.iosrjournals.org

Analysis of the Myths and Realities of the Internal Checks And Balances In An Organisation

Atu, Osahenoma Vivian; Atu, Omimi-Ejoor Osaretin Kingsley;
Dr. Adediran Samson; Aruomoaghe Jude

Staff Manager Atu, Omimi-Ejoor Osaretin & Co. (Chartered Accountants) 5 Urubi Street, Iyaro Benin -City
(Aca, Fcma, Acti, Aat, Mba, M.Sc, Pdg, Comp.Sc; Dipl. Ph.D(In-View)) Lecturer: Igbinedion University, Okada. Edo State, Nigeria-West Africa
(B.Sc., M.Sc., Ph.D, Aca) H.O.D Department Of Accounting Igbinedion University, Okada. Edo State, Nigeria-West Africa
(B.Sc., M.Sc., Ph.D(In-View)) Lecturer- Department Of Accounting Igbinedion University, Okada. Edo State, Nigeria-West Africa

Abstract: *This article analyzed the myths and realities of internal checks and balance in organizations. The research method includes the administration of questionnaires to the account department that constitutes the sample size. Data was sourced by means of a well structured questionnaire and data collected were presented by using relevant table. Internal control system is an essential part of an organization, and therefore, should be taken very seriously in the organization because an effective internal control system is able to detect fraud, shortcoming and the misuse of assets among others. The hypotheses were however tested with the use of chi-square (x^2) statistical tool. The first hypothesis, which states that internal control system has no effect in an organization, was rejected. The second hypothesis which states that there is no significant relationship between the operation and previewed internal control mechanism in the organization was also rejected. The finding of this study reveals that internal control can detect all forms of human errors, internal control is not a witch haunting strategy, and managements are the only ones responsible of establishing internal control system. Based on the findings, it was recommended that the management should ensure training to all staff about internal control system, its purpose and each employee's adhere to an effective internal control system. There should be a regular audit by external auditor of the organization's financial statements.*

Keywords: *Myths, Realities and Internal Checks and Balances*

I. Introduction

All organizations make decisions everyday as to the optimal use of their scarce resources to produce their best products. Many times, government cannot exercise firsthand control or supervision on their operations; therefore, the need arises to protect these resources for mismanagement, waste, and Irregularities. It is acknowledge that, the management in all organizations, private or public irrespective of their size and nature, use financial statements as their means of presenting accounting and stewardship to the government and other users of the information since they qualify their goals and objectives in financial terms for effective reporting and realization. It is in this area that internal audit has proven to be of value. An effective organization is one that has good and valuable internal control that could check problem areas in the organization so that remedial action could be taken. It is; therefore, important for the staff and management to understand the concept of internal control, its functions and the appropriate implementation of the system.

Internal checks and balances, also known as internal control, is an essential element of sound management. It ensures that senior management has the problem and takes remedial actions as soon as possible. Onochie (2005).

1.1 STATEMENT OF PROBLEM

Internal control is very essential for every business today and most organizations undertake this process to plan and control the activities of the organizations, yet it has its own ebb and flaws. It would be very difficult to imagine an organization achieving and sustaining its effectiveness and efficiency if there is no internal control in the organization.

Thus, internal control system is one of the many techniques through which any organization could meet its objectives. However, it is therefore displeasing to know that the internal control system puts in place in some organizations to check wrong practices like fraud, embezzlement of funds, excessive expenditure e.t.c are becoming inefficient because staff, even management of an organizational have their own point of view of what internal control is and what it ought to do.

Thus, this research therefore seeks to establish what internal control actually means and match it up against what the organization the public thinks of internal control.

1.2 OBJECTIVES OF THE STUDY

The main objectives of the study are to:

- To know the effect of internal control systems in an organization
- To know if there is any significant relationship between the operations and previewed internal control mechanism in the organization.

1.3 RESEARCH HYPOTHESES

HYPOTHESIS 1

Hi: Internal control system has effect in an organization

HYPOTHESIS 2

Hi: There are significant relationships between the operations and previewed internal control mechanism in the organization.

II. Literature Review

Internal control is the whole system of control, financial and otherwise established by the management, in order to carry on the business of the enterprise in an orderly and efficient manner, ensure adherence to management policy, safeguard the assets and secure as far as possible the completeness and accuracy of records.

According to Oladipupo (2003), by internal control we mean not only internal check and internal audit. Is a whole system of controls, financial or otherwise, established by management in order to carry out business of the organization in an orderly manner, safeguard its assets and to secure as far as possible the accuracy and reliability of its records. Internal control involved all the various control measures instituted by management to facilitate the conduct of company's business in an orderly manner, security of company's assets and accuracy and reliability of its record. Management plans, organizes and direct the performance of sufficient actions to control risk to an acceptable level or to increase the probability of a desired outcome. Internal control is a process within an organization designed to provide reasonable assurance regarding the achievement of the organizational objective.

Control, whether they relate to financial or operational area, ensures that processes act to meet the system's objectives. When evaluating internal control systems the internal auditor should consider the effect, which all the control have on each other and on related systems. As part of the planning process the internal auditor should identify the whole range of system within the organization. For those systems to be examined, the internal auditor should establish appropriate criteria to determine whether the controls are adequate and assist in achieving the objectives of the system.

Basically, internal control cuts across every human organization at varying degrees.

Millichamp (2002) gives a detailed definition of internal control as, "the world system of controls, financial and otherwise, established by the management in order to carry on the business of the enterprise in an orderly and efficient manner, ensure adherence to management policies, safeguard the assets and secure as far as possible the completeness and accuracy of the records".

Bradford (2013) internal controls are procedures established by a business to safeguard assets and ensure the reliability of business information. Think of them as a system of checks and balances that assure the accuracy of accounting data and records of transactions. A system of internal control built into business practices and not just written policy and procedure manuals is fundamental for best results. This makes it important to dispel some of the myths and common misconceptions that circulate concerning the subject of internal control. Because there are many misconceptions about internal controls, knowledge sharing is vitally important to an effective control system. Here are a few myths and corresponding reality:

1. SUFFICIENCY MYTH

MYTH: If internal controls are strong enough, they will prevent fraud and keep financial statements from errors.

THE REALITY: Internal control provides at best, only a reasonable expectation that accounting data is accurate and fraud has been prevented.

2. AUDITOR'S MYTH

MYTH: Internal controls are the responsibilities of the internal Auditor. Many have expressed this.

THE REALITY: It is the managers and employees who work with internal controls and use them to validate their duties on a daily basis.

3. NEGATIVITY MYTH

MYTH: Internal controls are a negatively oriented list of ''don'ts'' that slow down the transaction process.
THE REALITY: Internal controls are positive. They provide guidance with what they do. Compliance with established procedure and controls ensure that business is conducted correctly and everyone gets it right the first time.

4. MYTH: internal controls are all about finance and accounting. We do what the office of financial affairs or the department of finance tells us to do.

THE REALITY: Internal controls are integral to every aspect of the organization.

2.1 OBJECTIVES OF INTERNAL CONTROLS

The committee of sponsoring organizations of taredway commission (COSO), an online publication available through the America Institute of Certified Public Accountants (AICPA) (2003) gives the main objectives of an effective internal control system. A few is stated below;

- Effectiveness and Efficiency of Operations. This objective addressed an entity's basic business objectives, including performance and profitability goals and safeguarding of resources.
- Reliability of Financial Reporting. This relates to preparation of reliable and condensed financial statements and select the financial data derived from such statements, such as earnings released, reported publicly.
- Compliance with Applicable Laws and Regulations. This entails complying with those laws and regulations to which the entity is a subject.

2.2 TYPES OF INTERNAL CONTROL

Physical Control: Assets must be kept physical secured and this must be particularly important for valuable and portable items e.g. stocks, motor vehicles, etc.

Accounting/Arithmetical Control: These controls are designed to ensure that transactions are correctly calculated, recorded and processed.

Personnel Control: These controls are developed in order that staff allocated to duties is capable and sufficiently motivated to ensure that they carry out their duties efficiently and effectively with complete integrity.

Authorization/ Approval Control: This requires that the document to be processed should be authorized by a responsible officer(s) within the clearly defined limitation of authority.

Management Control: These are controls outside the day-to-day routine of the control system. This may include the establishment of an internal audit department or the use of budget or management accounts to control operations.

Organizational Control: A plan of the organization should exist to define and allocate the responsibilities and identifies line of reporting. It is important that every employee should know the precise power delegated to him and to whom he should report.

Segregation of Duties: This is to ensure that no single individual is responsible for all aspects of the transaction form the beginning to the end. This is fundamental to a good internal control system. The involvement of more individual reduces the risk of accidental error or deliberate fraud.

Supervisory Control: These are controls exercises by higher level management on their subordinate. They are designed to ensure that the company is operating as intended.

Acknowledgement Of Performance: Procedures should designed, communicated and enforced to ensure that every person performing a function acknowledge his activities by means of signature, initial and other means.

Budget and Budgetary Control: This entails the setting of standards and determination of variances, which help the organization to remain on course.

2.3 LIMITATIONS OF INTERNAL CONTROLS

Internal controls are essential features of any organization, that is, to run effectively. However, as explained by Millichamp (2002), it is important to realize (especially for an auditor) that internal controls have inherent limitations, which include: A requirement that the cost of an internal control system is not disproportionate to the potential loss that may result from its absence; internal controls tend to be directed at routine transactions. The one-off or unusual transactions tend not to be subjected to internal control. Potential human errors cause by stress of workload, alcohol, carelessness, distraction, mistakes of judgment, cussedness, and the misunderstanding of instructions.

III. Statistical Method For Data Analysis

The purpose of the chi-square is to provide an answer to the question of how great a departure from expected frequency can be located before we can accept or reject the null hypothesis.
The determination of chi-square (X^2) is shown as:

$$X^2 = \frac{\Sigma (O-E)^2}{E}$$

WHERE: X^2 = Chi Square
Σ = Summation
O= Observed Frequency
E= Expected Frequency
The outcome of the above calculation would either confirm on null hypothesis resulting from the discrepancy between "O" and "E' could be attributed to the chance or otherwise reject it.
Rejection means that the discrepancy is so large that it cannot be attributed to chance.

IV. Test Of Hypotheses

4.1 TABLE OF RESPONSE
HYPOTHESIS 1: Does internal control system have any effect in organizations?
TABLE 4.1.1
Source: Fieldwork 2013
ANALYSIS: from the above table, it is understandable that 87% i.e. majority of the staffs, agreed that internal

Alternatives	Number of Respondents	Percentage %
Yes	13	87%
No	2	13%
Total	15	100%

control has effect in all organization.
Hi: Internal control system has effect in an organization
Ho: Internal control system has no effect in an organization
CHI-SQUARE CALULATION

TABLE 4.1.2

VARIABLE	O	E	O--E	$(O--E)^2$	$(O--E)^2/E$
YES	13	7.5	5.5	30.25	4.0
NO	2	7.5	-5.5	30.25	4.0
TOTAL	15	15	0	60.5	8.0

Level of significance = 5%
Level of confidence = 95%
Degree of freedom=1
Chi-square table value= 3.84
Decision rule: Since the computed value (8.0) is greater than the chi-square value (3.84), we therefore reject the null hypothesis that implies that internal control system has no effect in organization and accept the alternative.
HYPOTHESIS 2: Is there significant relationship between the operations and previewed internal control mechanism in the organization?

TABLE 4.1.3

Alternatives	Number of Respondents	Percentage %
Yes	12	80%
No	3	20%
Total	15	100%

Source: Fieldwork 2013
ANALYSIS: from the above table, it is understandable that 80% i.e. majority of the staffs, agreed that is there significant relationship between the operations and previewed internal control mechanism in the organization.
Hi: There is significant relationship between the operations and previewed internal control mechanism in the organization.
Ho: There is no significant relationship between the operations and previewed internal control mechanism in the organization.
CHI-SQUARE CALULATION

TABLE 4.1.4

VARIABLE	O	E	O--E	$(O-E)^2$	$(O-E)^2/E$
YES	12	7.5	4.5	20.25	2.7
NO	3	7.5	-4.5	20.25	2.7
TOTAL	15	15	0	40.5	5.4

Level of significance = 5%
Level of Confidence = 95%
Degree of Freedom=1
Chi-Square Table Value= 3.84
Decision rule: Since the computed value (5.4) is greater than the chi-square value (3.84), we therefore reject the null hypothesis that states that there is no significant relationship between the operations and previewed internal control mechanism in the organization and accept the alternative which states that there is significant relationship between the operations and previewed internal control mechanism in the organization.

4.2 DISCUSSION OF THE FINDINGS

The research revealed that:
There is significant relationship between the operation and previewed internal control mechanism in the organization. The staff and management of the organizations are of the opinion that internal control system is not a "witch hunting" strategy and is a must for all organizations.
However, the existing internal control mechanisms in the organization are:
Securing cabinets which store all sources documents; No one person starts and ends a complete transaction; The Chief Accountant delegates functions to responsible subordinate within the department; every unit prepares and submits up to date records; and also, adherence to policies and procedures are encouraged.
The internal control system is functional and operational in the organization.

V. Conclusion

Internal checks and balances is an essential element of sound management. It is therefore the management's job to ensure that the internal control put in place is both functional and operational; the management should also ensure that the employee's orientation matches that of the organization's objective.

5.1 RECOMMENDATIONS

Internal control system is an essential part of an organization and therefore should be taken very seriously in the organization. An effective internal control system is able to detect fraud, short and misuse of assets amongst others.

However, there is a significant relationship between the perceived and operational internal controls mechanisms existing in the organizations; therefore, the following are the recommendations made and they include:

- The management should ensure training to all staff about internal control system, its purpose and each employee's responsibility towards an effective internal control system.
- There should be a regular audit by eternal auditor of the organization's financial statements.
- Management should make sure that all staff members are adhering to all policies and procedures.
- The internal control system should incorporate procedures to verify that the system is working, review the systems evaluate its appropriateness and amend the systems to accommodate new circumstance.

Reference

[1]. America Institute of Certified Public Accountants (2005). Internal Control-Internal Framework. The Committee of Sponsoring Organizations of Taredway commission (COSO). Retrieved April 29, 2006 from http://www.coso.org/publications/executive-summary-integrated-framework.ht
[2]. Bariyima, D.K (2002). *Auditing Basic Principle (4th Ed)*. Springfield Publishers, Lagos, Nigeria.
[3]. Bereson, S M & Levin, D (1998) *Business Statistics: A First course*. Prentice Hall, Inc. New Jersey.
[4]. Boritz J. (1993), *Risk Assessment Do's and Don'ts*. Schools of Accountancy, University of Waterloo, Waterloo, Canada Retrieved June 12 2006 on http//www.jebcl.com/riskdo/riskdo.htm.
[5]. Bradford C. (2013), myths and facts on internal controls/ business and entrepreneurship available at www.yourbusiness.azcentral.com/myths-internalcontrols-15761.html accessed on 07/10/3013
[6]. Malaysian Institute of Accountants (2004). Internal Audit Guidelines. Retrieved June 12, 2006 from http//www.mia.or.my/handbook/guide/IAG.htm.
[7]. Millichamp A.H. (2002). Auditing (8th Ed).The Bath Press, London.
[8]. Marks G. (2011), myths of internal controls available at www.accountingtoday.com/ato_issues/25_11/myths-of-internal-controls-60569-1.html accessed on 07/10/2013
[9]. Northwest State University (2000) Internal Control. Office of Internal audit retrieved June 12, 2006 from http://www.nsula.edu/internalaudit/internal5
[10]. Oladipupo, A. (2003). *Principle and Practice of Auditing*. Mindex Press, Benin, Nigeria.
[11]. Onochie, V. (2005). *Auditing and investigation*. Vindo Associates ltd, Lagos, Nigeria.
[12]. UBC Internal Audit (2006 February, 27) Internal Controls. University of British Columbia. Retrieved April 29, 2006 from http://www.intaudit.ubc.ca/internalcontrols.html