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Internal Control Systems and Management of Organisational Resources of Firms in Nigeria: A Review

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Abstract: *The globalizations of economies, technological advancements, complexity of business and allegations of fraudulent financial reporting have sharpened the ever-increasing attention to internal control in organizations. These developments have thus led to a continuous reflection of internal control and its importance in the development of firms. It is therefore against this background that this paper reviewed internal control system and management of organisational resources of firms in Nigeria. The review should the internal control system has significant effect on stolen cash recovery, credit control; safety of non-current assets and efficient management of working capital. The paper concluded that effective internal control systems as observed from the findings are necessary in the effective management of organisational resources in Nigeria. The paper recommended amongst others that effective internal control system should be used to support the organization in achieving its objectives by managing its risks, while complying with rules, regulations, and organizational policies.*

Key Words: *Internal Control System, Cash Recovery, Credit Control, Non-Current Assets, Working Capital.*

1. INTRODUCTION:

As a concept, internal control is distinguished by its scope and its high level of the services offered. In the modern business world, the term internal control is being used to refer to two basic concepts: the internal control system and the internal control itself. The internal control system refers to an organized amalgamation of functions and procedures, within a complete system of controls established by the management and whose purpose is the successful function of the business (Cheung and Qiang, 2007). The internal control system is all the methods and procedures followed by the management in order to ensure, to a great extent, as much successful cooperation as possible with the director of the company, the insurance of the capital, the prevention and the detection of fraud, as well as the early preparation of all the useful financial information. According to (Papadatou, 2005) the internal control system resembles the human nervous system which is spread throughout the business carrying orders and reactions to and from the management and it is directly linked to the organizational structure and the general rules of the business.

According to American Institute of Certified Public Accountant (AICPA) (1963) a system of internal control extends beyond those matters which relate directly to the functions of accounting and the financial statements. In addition, internal control is a systematic procedure which will lead to evaluate the degree of correlation between those established criteria and the real results of the business. Internal control, as defined from the APC (Auditing Practices Committee, 1980), is an independent examination and certification from an inspector appointed by the business to control the finances according to the legal framework established each time.

According to Miller and Bailley (1989) internal control is a systematic review and a subjective investigation of one element and encompasses the verification of the specific information as these are determined from the general practice. Thus, internal control helps the company to achieve its goals using a systematic approach of assessing the effectiveness of handling dangers. Internal control, as defined from the Hellenic Institute of Internal Auditors (H.I.I.A, 2004) is an independent, objective, adequately designed and organized procedure, which through the technical and the scientific approaches; assess how adequately the system of internal control functions. From the above definitions, it is clear that the internal control is not just an one-sided tool for controlling the order and rightness of certain situations, but it is a method of detecting the value added up to a company, achieving the index of effectiveness and profitability of the company.

Besides, the purpose of this control is the intentional, the programmed and focused effect of the company on the current situation, so as this situation to be reformed in the future and become the one that ought to exist (Goodwin, 2004). The deviation between the already achieved and the programmed situation can also become possible through controlling the parameter of correct handling of danger situations. Bounton and Keller-Walter (2000) claimed that the objective purpose of internal control is, on the one hand, the allowance of specific and high level of services offered towards management, and on the other hand, the allowance of assistance towards the members of the organization for the most effective practicing of their duties. Hence, internal control system is being implemented in businesses as tools that add up value to the company. In this way, the firm can achieve a systematic approach towards the most effective operation of the organization, as a unity.

According to COSO report (Committee of Sponsoring Organizations of the Treadway Commission, 1992), internal control is defined as a procedure which offers fundamental security to the business concerning the credibility of financial affairs. The report defines internal control and describes a framework for internal control. However, as stated by Aldridge and Colbert (1994) the difference of this report is that it also provides criteria for the management to utilize such reports to evaluate effective internal controls system.

From these views of the concept of internal control, it can be argued that internal control system assists the organisation to effectively manage its resources. However, several problems militate against effective internal control system of organisational resources. The problems include poor accountability, backward economic development, in-effective legal punitive measures which leads to poor performance. The management of modern businesses therefore requires the investors to put their hard earned resources in a business that will yield the desired returns.

This is made possible by the fact that such business would operate by full adherence to the principles of good corporate governance. Some of such principles are that of internal control and fraud prevention. Aguolu (2009) sees error as an unintentional mistake. This may occur at any stage of the transaction of a business. Thus, today businesses face considerable difficulties and problems when they try to identify their strengths, assess their risk and manage uncertainties in its financial resources.

Financial resources concern the ability of the business to finance its chosen strategy. Such a strategy needs to be very carefully managed from a finance point-of-view. Hence, this paper reviewed internal control systems and management of organisational resources of firms in Nigeria. The subsequent sections of this paper are divided into three sections. In section two, this paper reviews extant literature in this area of accounting. In section three, the paper explored the implications of findings of this review and lastly in section four, the paper concludes.

2. LITERATURE REVIEW:

Compliance is concerned with adherence to rules, applicable laws and regulations, and internal policies and procedures (Reider, 2004). However, the purpose of control devices is to ensure a planned, systematic and orderly operation (Ratliff et al., 2008). Failure to comply with those controls jeopardises the coordinated efforts that such controls promote. In addition to determining compliance with those controls, internal auditors also review and evaluate the adequacy of policies, plans and procedures. This control is the most visible and physical design to protect the organisation's assets.

Reider (2004) states that achieving the optimal balance between cost and results and this is related to one of the fundamental concepts of economics, namely "scarce resources", which simply means that there is a limited supply of resources to satisfy all wants. The accomplishment of established objectives and goals for operations or programmes is concerned with results and accomplishments achieved and the benefit provided by the controls (Reider, 2004). When evaluating the effectiveness of operations, the internal auditor should ask whether the activity is achieving its ultimate intended purpose.

Ratliff et al. (2008) states that internal auditors play an important role in this area because of their broad perspective of the overall organisation and its internal control systems and this means that internal auditors are in a position to assess the overall direction in which the organisation is moving, thus, for instance, suppose that corporate management, with the guidance of the board of directors, has established a policy to maintain a long-term conservative stable image in order to develop long-term customer trust and loyalty. In that case, the internal auditors are in a position to point out the inconsistencies in the organisation's operations and the apparent conflict in development (Ratliff et al., 2008).

Woolf (2007) states that many organisations produce and keep up to date charts that depict the organisational hierarchy in linear terms, such charts have the advantage of indicating most departmental functions as well as identifying the staff responsible for executing them. Robertson (2002) states that the Committee of Sponsoring Organisation (COSO) report defines internal control as a process, affected by an entity's board of directors, management and other staff, and designed to provide reasonable assurance regarding the achievement of objectives in the following three categories: reliability of financial reporting; compliance with applicable laws and regulations and effectiveness and efficiency of operations From the above it is clear that in today's complex organisation environment, the role of internal control is of such importance that an organisation (especially an administrative unit) cannot operate effectively unless it has the four fundamental concepts of COSO in place (Robertson, 2002). Those concepts are process; people; reasonable assurance and category objectives.

Glance (2006) provided that internal control system refers to "the local government process and procedure that is been established with the aim of objective achievement." Similarly, the internal control system also serves as a process that guides an organization towards achieving its established objectives (Aguolu, 2009). From the above definition of internal control system, it can understand clearly that it all about the provision that will assist to the achievement of objectives. Therefore, for the purpose of this study effective internal control system refers to the effective control measures established by an organization with the aim of safeguarding their assets ensure the reliability of records both financial and non financial as well as compliance with relevant policies and procedure that will ensure the achievement of organizational objective.

In this context, management should ensure that their internal control system is well established in order to assist internal audit towards achievement of organization's objective. Similarly, quality of an organization internal control system has significant impact on the accuracy of management guidance, likewise firms that disclose ineffective internal controls system have larger tendency of experiencing management errors in their operation than those firms that report effective internal control system (Feng, Li and McVay, 2009). Therefore, it is the responsibility of management of an organization to ensure that effective internal control system is put in place that will ensure the achievement of organizational established objectives. This is because establishment and supervision of effective internal control systems are the responsibility of management, not auditors (Changchit et al, 2001).

At the same time effective internal control system are fundamental drivers toward earnings quality (Church and Schneider, 2008). In the same vein, effective internal control system has an essential role to play in a firm's success (Jokipii, 2010) in line with the above issue; effective internal control system could also play an important role in the effectiveness of internal auditors particularly at government. All of government should improve the effectiveness of internal control system, internal audit function and organization commitment because they improve good governance (Eko and Hariyanto, 2011) in addition, such effective internal control system can provide information to management about the entity's progress, or lack of progress toward the achievement of their objectives (Verdina, 2011).

Al-Twaijry et al (2004) also found that effectiveness of internal control system helps external auditors to rely on the work of internal auditors and thereby improve their effectiveness. Therefore, internal control systems are integral component of the management processes of a public sector which should be establish in order to provide reasonable assurance that the operations are carried out efficiently and effectively. Effective internal controls systems are essential to the effectiveness of local governments operation because it deals with the activities or procedures that are designed to provide reasonable assurance that operations are performing according to plan and these can also influence the effectiveness of internal audit. COSO also provides the basic principles representing the fundamental concepts of effective internal control in five components of the framework (Candreva, 2006).

Though, Amudo and Inanga (2009) argued that the weakness of the COSO mechanism is failure to recognize Information Technology as one of the major control components of internal control system and Information Technology is very crucial to internal control framework. That is why most organizations today used Information Technology for authorization, initiation, recording and processing of transactions, because its ensures effectiveness of internal controls system and thereby making it six. At the same time advancements in technological have increased the importance placed on internal controls system (Rezaee et al, 2001). These components must be present and functioning effectively for any internal control system to achieve organizational objectives.

Control environment is the major aspect of managing an organization this is because is a reflection of the attitude and the policies of management in regard with the importance of internal audit in the economic unit (Theofanis, et al 2011). It has influence over organization goals achievement. However, it is the foundation for the other components of internal control and providing structure (Sudsomboon and Ussahawanitchakit, 2009). Control environment assist toward reducing the level fraudulent activities within organizational operation also the quality of an entity's internal controls system depend on the function and quality of their control environment. Therefore, providing a proper control environment for a local government is very essential to the effectiveness of their operation.

Feng et al (2009) also carried out a study on internal control and management guidance, used questionnaire and finally found that internal control quality has an economically significant effect on the accuracy of management guidance. Similarly, Aikins (2011) under take a research on an examination of government internal audits' role in improving financial performance, in which he used the local government financial performance as dependent variable and independent variables of; the effects of years between audits, internal control adequacy, internal control system effectiveness, and evaluation of financial performance monitoring, used online survey, 387 audit department head and questionnaire for methodology. The research results indicate significant relationships between years between audits, internal control adequacy, internal control effectiveness and evaluation of financial performance monitoring on local government financial performance.

Thus, Beckmerhagen et al (2004) also argued that the audit effectiveness should not be measured based on achievement of the audit objectives or on the number of findings of the internal auditor alone, but also more important is to determine the quality and suitability of the audit plan, execution and follow-up. Similarly, Shareholders should have the power to remove any internal auditor that is ineffective (Dhamankar and Khandewale, 2003). This should also be in line with local council by removing all internal auditors that are not effective despite the provision of all necessary that might have improve their effectiveness.

Ahmad et al (2009) on the effectiveness of internal audit in Malaysian public sector, using simple percentage for data analysis found the lack of audit staff is ranked as the major problem faced by internal auditors in conducting an effective internal auditing. The study concluded by suggesting that future studies should adopt other methods such as field survey of wider groups of internal auditors both in public and the private sectors. Likewise, Theofanis, et al (2011) examine the relationship between element of internal control system and internal audit effectiveness and the result of the study reveal positive relationship between the two relationships and they conclude that if future studies should carried out research on internal audit effectiveness with large sample, the result will be better than their own.

According to Flesher (1996) management is responsible for establishing an effective internal control system and also according to the Institute of Internal Auditors – UK (Red Book 300.5 Guidelines, 1998), the primary objectives of the internal control system are to achieve: the reliability and integrity of information; compliance with policies, plans, procedures, laws and regulations; the safeguarding of assets; the economic and efficient use of resources; the accomplishment of established objectives and goals for operations or programmes.

The objectives of each control should be readily recognisable as contributing to the objectives of the organisation as a whole. No wonder Stearn and Impey (2000) point out that the success of the organisation rests with management, and therefore with any action taken by management to enhance the likelihood that established objectives and goals will be achieved through enactment of objectives that are effectiveness efficiency and enhance security.

Internal control has the following characteristics: it is a process – not an end in itself, but a means to an end. This means that internal control is a dynamic function operating every day. It is operated by people. This means that an organisation may have policy manuals, procedures, forms, computer-controlled information and accounting and other features of control, but people make the system of internal control work at every level of management. Therefore, staff or management establish the objectives, put control mechanisms in place and operate them. It provides reasonable assurance. It can help to prevent and detect failures, but it cannot guarantee that they will never happen. It is not an absolute assurance. Because people operate the controls and breakdowns can occur.

3. IMPLICATIONS OF REVIEW:

Internal control systems are affected by an entity's board of directors management and other personnel and are designed to provide reasonable assurance regarding the achievement of objectives of organisations. Thus, a good internal control system will ensure that organisational resources are properly secured and well utilized. In this paper the specific objectives were to examine internal control systems and management of organisational resources of firms in Nigeria vis-a vis quick recovery of stolen cash, credit control, safety of non-current assets and working capital of firms in Nigeria.

This review indicates that for effectiveness and efficiency of operations, reliability of financial and management reporting, compliance with applicable laws and regulations and protect the organisation’s reputation (Kaplan, 2008), internal control systems is internalized as well as institutionalized in the organisation. This will ensure enhanced management of the organisational resources. According to Cunningham (2004), internal control systems begin as internal processes with the positive goal of helping a corporation meet its set objectives. Management primarily provides oversight activity; it sets the entity's objectives and has overall responsibility over the internal control systems.

Since internal controls are an integral part of any organization’s financial and business policies and procedures (International Organization of Supreme Audit Institutions (INTOSAI), 2004). Internal controls must thus consist of all the measures taken by the organization for the purpose of; protecting its resources against waste, fraud and inefficiency; ensuring accuracy and reliability of accounting and operating data; ensuring compliance with the policies of the organization; evaluating the level of performance in all organizational units of the organization, (Kaplan, 2008; Cunningham, 2004; INTOSAI, 2004). This will assist at ensuring proper management of organisational resources as observed from the findings of this study.

Also, internal control system lead to the promotion of adherence to laws, regulations, contracts and management directives and the development and maintenance of reliable financial and management data, and accurately present that data in timely reports. This insightful role of the internal control systems of manufacturing firms could be observed in the result of this paper that internal control systems have significant effect on stolen cash recovered, credit control, safety of non-current assets and efficient management of working capital of firms in Nigeria.

4. CONCLUSION AND POLICY RECOMMENDATIONS:

Internal control is an integral part of an organization’s governance system and ability to manage risk, which is understood, effected, and actively monitored by the governing body, management, and other personnel is to take advantage of the opportunities and to counter the threats to achieving the organization’s objectives. Internal control is a crucial aspect of an organization's governance system and ability to manage risk, and is fundamental to supporting the achievement of an organization's objectives and creating, enhancing, and protecting stakeholder value. High-profile organizational failures typically lead to the imposition of additional rules and requirements, as well as to subsequent time-consuming and costly compliance efforts.

Internal control is often perceived and treated as a compliance requirement, rather than as an enabler of improved organizational performance. Effective internal control can help organizations improve their performance by enabling them to take on additional opportunities and challenges in a more controlled way. Therefore, there is a need to have a better understanding of how organizational performance relates to effective risk management and the role and effectiveness of internal control.

Organizations always face uncertainty in achieving their strategic, operational, and other objectives. However, they can decide the level of risk they wish to be exposed to in the pursuit of those objectives. Proper risk assessment and internal control assist organizations in making informed decisions about the level of risk that they want to take, and implementing the necessary controls, in pursuit of the organizations' objectives. However, risks should not be taken without an explicit understanding of their potential consequences for achieving an organization's objectives. Therefore, decision makers require relevant and reliable information, produced through the internal control system, to effectively implement and execute their strategic and operational plans. Therefore, this paper concludes that effective internal control systems as observed from the findings of this paper are necessary in the effective management of organisational resources not only in Nigeria but also all over the world.

Therefore, internal control should be used to support the organization in achieving its objectives by managing its risks, while complying with rules, regulations, and organizational policies. The organization should therefore make internal control part of risk management and integrate both in its overall governance system. Again, organisations also should determine the various roles and responsibilities with respect to internal control, including the governing body, management at all levels, employees, and internal and external assurance providers, as well as coordinate the collaboration among participants. This will enhance effective credit control system of firms in Nigeria.

Management should foster an organizational culture that motivates members of the organization to act in line with risk management strategy and policies on internal control set by the governing body to achieve the organization's objectives. The tone and action at the top are critical in this respect to ensuring safety of non-current assets of manufacturing firms in Nigeria. Also, there should be a link achievement of the organization's internal control objectives to individual performance objectives. Each person within the organization should be held accountable for the achievement of assigned internal control objectives. This will increase the relationship between internal control system and efficient management of working capital of manufacturing firms in Nigeria.

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