LEVELS OF INTERNAL CONTROL: IMPLICATION FOR FRAUD REDUCTION IN NIGERIA LOCAL GOVERNMENTS.

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ABSTRACT

The Levels of internal Control mechanism, implication for fraud reduction were examined using 48 item questionnaires on internal control checklist formulated by Duncan et al (1999). The aim was to find the extent to which the internal control measures installed in the system were adhered to and the role they played in fraud reduction. 524 respondents comprising 255 males (48.79) and 269 females (51.39) from six local governments in Enugu State answered the questionnaires. The mean age of the respondent is 2.06 SD = .58. The result revealed that the important control measures were not adhered to and this led to fraud. The implication of this finding is discussed and further areas of research suggested.

Keyword – Internal Control, Mechanism, Tool, Fraud, Local Governments.
Introduction

Internal control consists of all measures employed by an organization to safeguard assets from waste, fraud and inefficient utilization and to promote accuracy, and reliability in the accounting records. It also measures compliance with company policy as well as evaluates the efficiency of operation (Meig, Whittington, Meig, 1982; Coe and Sallis, 1991; Committee of sponsoring organization, 1992;). The internal control is just as relevant to local governments as it is to profit making organizations. Inadequate internal control can adversely affect the management responsibilities of local government’s officials and place them in positions where they may be tempted to engage in questionable activities and accounting practices. It could subject individuals to unwarranted accusations of such activities (Duncan, Flesher & Stocks, 1999). Anthony and Young, were of the view that the basic concepts of internal control are the same for both profit and non-profit making organizations.

It is our belief that the employment of internal control measures in the discharge of duties of local governments activities will contribute positively to fraud prevention. It is important to add that the unique characteristics of non-profit making organizations call for an adequate system of internal control that will help prevent fraud. For the purpose of this article, fraud is defined in terms of one’s employment (Campbell, 2006; Langan, 1998). According to Agu’s study in 2002, “fraud is the use of one’s occupation for personal enrichment through the deliberate misuse or misapplication of employing the organization’s resources or
assets.” Clearly, fraud is a pervasive corporate problem affecting organizations across industries and time zones without regard to company size. (Adam 2006). Because of fraud’s disastrous consequences, failures to put deterrent procedures in place could put a company out of business within days. Fraud prevention then, is a defined program of proactive measure to avoid or mitigate fraud (Adams, 2006; Agu 2002; Conway, 1995). Because of relative scaling, the greatest financial impact of fraud can occur in a small business environment. A loss of 6% revenues is significant for any company, no matter how large. Even if an operation survives, the fiscal loss, its business continuity can be in jeopardy and it may no longer be able to function as an independent entity. Failing to address these issues places the local governments at a competitive disadvantage when fraud becomes a cost of doing business (Agu, 2002; Ndebbio, 1998; and Modum, 1995).

In the Local Government, the internal control measures put in place to check fraud, are believed to have been grossly abused. Despite the fact that non-profit organizations, like Local governments, need proper fiscal oversight and supervision by their governing boards (Moody 1978). The Agency theory argues that governing boards must maintain controls over finances, organizational direction, and top management performance to ensure that principal’s interests (shareholder i.e. donors) are adequately attended to by their agents (the managers), Fama and Jensen, 1983). The implication of this is that those involved should enforce the implementation of the control measures put in place so as to check fraud. Since internal control is one of the measures for fraud prevention, it will be
interesting to know how far it has gone to check fraud in Nigeria Local Governments.

The purpose of the study is therefore, to examine the internal control measures put in place in the Nigerian local Governments (Financial memoranda; 1991) and to check if these measures are adhered to, and the extent to which these measures help to curb fraud. This study has become useful because, for some time now, cases of fraud abound in almost all the public enterprises in Nigeria including local government systems. Unfortunately, there has been little investigation on the internal control measures put in place in the Nigeria local government system and the effect of this control measures in fraud reduction. What all these point to, is that there will probably be increase in fraud, in Nigeria local governments. This may well be ahead of the local governments readiness to cope with the high rate of fraud in the Nigerian local governments. (Okoye, 2005). It is very important to find out the extent to which the internal control measures installed in the system are adhered to and the effect of these measures on fraud. This is because the result obtained can assist local government functionaries in the formulation and implementation of these mechanisms and that will positively help to check fraud and improve local government’s performance.

There have been many reported cases of the financial mismanagement of local government resources. In addition, in Nigeria, many governors and local government chairmen were threatened with impeachment because of their involvement in fraudulent activities. The question before us is, are there no
control mechanism installed to check fraud in these local governments and states?. If there are, are they adhered to? and if they are adhered, to what extent?

In the same vain, the Wall Street Journal, recently reported that Roman Catholic Priests and Diocesan Administrators embezzled more than $3.5 million from the Church in a period of three years. These thefts were attributed to lack of coherent outside auditing and a system that relies mainly on faith to control the flow of cash”. Ellen Cook, the former Treasurer of the Episcopal Church Centre in New York embezzled $2.2 million between 1990 and 1995. Cook was able to direct the money because she had Control over auditing, and in violation of Church policies filled out cheque request forms and signed them herself (Staff,1995; Duncan,1999). However Irvin (1996) considered the “tension between the sacred agenda of the Church and often perceived secular nature of accounting” and concluded that accounting was generally viewed as supportive rather than in conflict with the general mission of the Church. This therefore, implies that embezzlement should be checked so as to ensure that the resources derived are used in accordance with the set down rules of the Church. The same thing applies to local governments in Nigeria. The control measures need to be adhered to for fraud reduction..

Materials and Methods

Population: Enugu State is situated in the southern part of the country and are made up of 17 constitutional Local Governments and 56 development centres.
The local governments are Aninri, Awgu, Enugu East, Enugu North, Enugu South, Ezeagu, Igbo-Etiti, Igbo-Eze North, Igbo-Eze South, Isi-Uzo, Nkanu East, Nkanu West, Nsukka, Orji-River, Udenu, Udi and Uzo-Uwani. To make data collection easier, the study was focused on 3 urban and 3 rural governments. The local governments are Enugu-North, Udi, Nsukka, Nkanu Ezeagu and Igbo-Eze South. The population is made up of 255 male and 269 female, mainly Finance Officers. The rationale behind the use of finance officers is because it is believed that they will understand the content of the questionnaires better.

**Sample Size:** The sample size for the present study consists of eight hundred and forty respondents who are senior and junior staff mainly Finance Officers. 3 urban and 3 rural local governments were selected in Enugu State and respondents were selected from these local governments with the help of the Secretaries to the Chairmen. The Secretaries of these local governments considered those who understood the financial memoranda and handbook on local government and also those who have been on the job for more than three years.

The demographic characteristics of the population show that there are 255 males (48.7%) and 269 female (51.3%). The mean age is 2.06 (SD = .58).

**Procedure**

The researcher distributed 140 questionnaires in each local government comprising a total of 840 questionnaires. The Secretaries used their discretion and distributed the questionnaires to those who they felt would understand the implication of the questions. The respondents were required to circle ‘Yes” “No”,
and “Don’t Know”. A total of 524 relevant responses were received for an overall response rate of 65.5%. With any survey data, there is the possibility of non-response bias (Amstrong and Overtun, 1977).

**Independent Measure**

Levels of Internal control measures as an implication for fraud reduction were measured using strict adherence, non-adherence and the partial adherence to the various control measures put in place. The assumption here is that adherence to the various control measures put in place will help to curb fraud while non and partial will lead to fraud. The mean for the respondents in the 3 urban and 3 rural local government included in the study was approximately 3.37 members. Equal number of survey was sent to all the 6 local governments using the stratified random sample. The choice of local governments used in the study was based on their sizes and importance in the state being studied.

**Result**

This research seeks to provide answers to the following questions.

1. Does strict adherence to the various control measures installed in Nigeria local Governments lead to fraud?
2. Does non-adherence to the control measures lead to fraud?
3. Does partial adherence to the control measures lead to fraud?
4. Does accounts reconciliation help in checking fraud?
Table 1 – Descriptive Data of Workers view on Measures of internal Control

<table>
<thead>
<tr>
<th>Item</th>
<th>Frequency</th>
<th>Mean</th>
<th>Standard Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Yes (%)</td>
<td>No (%)</td>
<td>Don’t Know (%)</td>
</tr>
<tr>
<td>Strict Adherence</td>
<td>281.7 (53.75%)</td>
<td>210 (40.1)</td>
<td>30.6 (5.8)</td>
</tr>
<tr>
<td>Non-Adherence</td>
<td>267.8 (51.20)</td>
<td>156.6 (29.88)</td>
<td>98.1 (18.72)</td>
</tr>
<tr>
<td>Partial Adherence</td>
<td>317.14 (60.52)</td>
<td>96.72 (18.46)</td>
<td>110.14 (20.99)</td>
</tr>
<tr>
<td>Account Reconciliation</td>
<td>316 (60.30)</td>
<td>141.3 (26.9)</td>
<td>66.3 (12.65)</td>
</tr>
</tbody>
</table>

Findings pertaining to the first research question show that workers believe that strict adherence to various control measures installed in the local government does not lead to fraud (54%). Although, this is not an overt majority but, it does appear that local government workers are of the view that adherence to the various control measures does not lead to fraud rather it helps to curb fraud and promote accountability which are the main purpose of government accounting.

Furthermore, taking an acceptable mean criteria of 2.5, it recorded an overall mean rate of 2.04 and SD = 4.70. However, mean is quite below the acceptable criteria and this proves that strict adherence does not lead to fraud.

Result shows that local government employees do believe that non-adherence to various control measures can lead to fraud (51%) only 30% of them feel that it cannot lead to fraud. An overall mean of the fourteen questions used to
measure this shows a mean rate of 7.65 and SD = 12.52 indicating that non-adherence to the various control measures leads to fraud.

For research question tree, findings from Table 1 show that 61% of local government workers believe that partial adherence to the control measures leads to fraud. A look at the mean 2.7 and standard deviation 8.73 of all the questions used in measuring views on partial adherence reveal that partial adherence does not help in checking fraud as half measure yields no result.

The study went further to find out, if workers believe that account reconciliation helps to check fraud. Findings appear to show that they believe it will help (60%) Also with a mean of 3.1 and SD of 11.6 from all the six questions used to measure reconciliation of accounts, it does appear that accounts reconciliation, if probably carried out, may reveal many irregularities and errors that may lead to fraud. If workers are aware that accounts reconciliation takes place every quarter or annually, then it may discourage them from participating in embezzlement and misappropriation.

Furthermore, an analysis of variance (ANOVA) was performed to determine if the mean differed significantly. The dependent variable used in the ANOVA was the total internal control evaluation score and the independent variable was local government size. The result of the ANOVA revealed that local governments do not adhere to the policies governing the general questions on internal control. The F calculated value for the differences among the different local governments are (5, 2.455) = .027, P > .05, (5, 4.447) = .001 P > .05, (5, 2.455) = .033, P
>.05 and (5, 2.817) = .016 P > .05. This means that they are all significant at .05 indicating that local governments in the southeastern zones do not adhere to the levels of internal control installed in the system. This shows that the different local government systems although they do not adhere to the four groups of questionnaires on internal control differed significantly. This suggests that controls in place may differ in any of the two local governments. The result revealed that, although, the differential effect of internal control general in reducing fraud in Nkanu and Nsukka local governments are not significant at .05 but it tends towards significant (sig. .081 and .075) in favor of Nsukka local government. An inspection of the mean difference indicates that the mean between Enugu-North and Nkanu is the highest (52.125) and this is the highest among the multiple comparison of local government indicating that the effect of internal control, cash on reduction of fraud, in Nkanu is the least while the effect in Enugu north is the highest. The other local government comparisons are not significant. Enugu – North and Nkanu are two extremes. In addition, the differential effect of internal control, cash receipt on fraud reduction in Nkanu is significant in favor of Enugu-North. Other comparisons of pair of Local governments are not significant. It does appear from the analysis, that the levels of internal control may have a better effect in Enugu North and no effect in Nkanu. It also shows that Local governments in the southeastern zone do not adhere to the levels of internal control installed in the s
ystem hence, it has no effect on fraud reduction.

The results of the study generally show that not all the control measures installed in the local governments in Nigeria are adhered to. Some of the important control measures are not religiously adhered to. For instance item 3 - non-adherence recorded the highest frequency indicating that accounting records and the underlying records are not audited annually. Local government workers confirmed this. They also admit that an audit committee is not effectively operational in the local governments in Enugu- State. The result also revealed that local government workers are afraid of the chief executives, that is, the chairmen of the local governments. Even the internal auditors have this perception that if audit queries are issued and you force them to answer, it could lead to termination of their job or transfer to remote areas. This notion is true, because, there are many cases where internal auditors are victimized, as a result of audit queries issued to Chairmen. Internal Auditors are employees of the local governments in Nigeria and are therefore, answerable to the chief executives.

Moreover, respondents overwhelmingly agree that revenue collectors are encouraged to use government official booklet and simultaneously answer that revenue collectors print their own receipts and issue same to the market women.. This they agree is one of the major ways of defrauding local governments in Nigeria. Furthermore, employees of local governments are of the view that mails are not handled by those who are responsible for the accounting records, accounting records not maintained and shown regularly to members before audit
exercise. This may result in a situation whereby workers in the accounting departments connive with the Chief Executive and misappropriate local governments’ resources. This agrees with Nwoko’s (1993) assertion that workers in the accounting department, due to longevity in a particular office, connive with the Chief Executives and embezzle local governments’ resources.

Workers also believed that accounts reconciliation, if properly carried out will assist in checking fraud. During the exercise, many errors and irregularities will be revealed and fraud will be detected. Local government workers interviewed, confessed that there is nothing like effective accountability in Enugu State local governments as the accountants work hand in hand with the Chief executive. Majority of the respondents are of the view that most of these measures installed in the system are just there without any practical recognition and application. This has practical implication. It suggests that if these important measures are not adhered to, there is every likelihood that fraudulent practices in Nigeria local governments could lead to total crippling of local governments activities. It is evident therefore, that there is need for strict adherence of these measures so as to reduce fraud in Nigeria local councils. One of the ways, is by supervising the activities of local government staff on a regular basis, ensuring that all the levels of internal control are strictly adhered to with particular emphasis to cash receipts, cash disbursement and accounts reconciliation.
References


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