



INTERNATIONAL JOURNAL OF ADVANCE RESEARCH, IDEAS AND INNOVATIONS IN TECHNOLOGY

ISSN: 2454-132X

Impact factor: 4.295

(Volume 3, Issue 6)

Available online at www.ijariit.com

An Empirical Study of Internal Control System Impact on Co-operative Banks Employees

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Abstract: Internal controls are defined as the plans of an organization, including management's attitude, methods, procedures, and measures that provide reasonable assurance that the objectives are being achieved. The study set out to investigate the role of internal control system in the performance of co-operative banks in India. Specifically, the study sought to establish the effect of control environment on the performance of co-operative banks. To achieve the objective of the study an empirical study has been applied. For the collection of data, a questionnaire has been designed and circulated among 217 respondents. The study found a significant relationship between control environment, control activities, monitoring, and performance of co-operative banks. The study recommended that control environment, control activities, and monitoring should be enhanced in order to further improve the performance of co-operative banks.

Keywords: Internal Control System, Internal Audit, Internal Audit.

INTRODUCTION

A system of internal control refers to the process by which organizations maintain environments that encourage incorruptibility and deter fraudulent activities by management and employees. An organization's components of internal control are evaluated during the planning phase of an independent financial statement audit. Internal control as defined in accounting and auditing is a process for assuring achievement of an organization's objectives in operational effectiveness and efficiency reliable financial reporting and compliance with laws regulations and policies. A broad concept internal control involves everything that controls risks to an organization. It is the integration of the activities, plans, attitudes, policies, and efforts of the employees of a department working together to provide reasonable assurance that the department will achieve its mission.

Internal control being one of the five main functions of management, is a process of monitoring operations so as to detect whether the operations fulfil their functions as planned or not, and if there is a deviation, the control process determines the reasons for this deviation and takes the necessary steps to eliminate it (Ozten et al. 2012, p.1). The main purpose of control is to raise concern over errors and detect the points of failure in order to prevent their re-emergence. The internal control system can be generally defined as a system which has the features of maintaining the assets of a company, ensuring accuracy and reliability of information and reports related to accounting and other operations, and increasing the effectiveness of the operations. Additionally, the system also covers all assessment and methods that are adopted in order to detect the suitability of operations in accordance with policies determined by management, implementing a chart of accounts and reporting system, specifying the duties, authority and responsibilities, and organization plan of the cooperation (Cook et al. 1980, p.198). In other words, an internal control system which is created by management and implemented by management and employees is a process which is designed to ensure reasonable assurance to achieve pre-specified objectives (Doyrangöl, 2002). According to the definition by COSO in 1992, an internal control system is defined as a set of methods, designed and controlled by senior management and board of directors to provide a limited assurance regarding the reliability of financial reporting, effectiveness, and efficiency of operations and their compliance with laws and regulations (Aksoy, 2007). W.W. Bigg explains internal control in clear terms, "Internal control is best regarded as indicating the whole system of controls, financial or otherwise established for the conduct of business including internal check, internal audit and other forms of control.

REVIEWS

Etengu R.O & Amony M. (2016) investigated the role of internal control system in the financial performance of non-governmental organizations in Uganda. They found a significant relationship between control environment, control activities, monitoring, and financial performance. They recommended that control environment, control activities, and monitoring should be enhanced in order to further improve the financial performance of International Union for Conservation of Nature. Additionally, performance standards should be established and communicated to employees of International Union for Conservation of Nature in a bid to improve financial performance. Kiumars N.A. et al. (2016) evaluated the relationship between internal control systems with the financial performance of Medical Sciences University of Golestan. They found that from the view of financial employees of University, there has a positive and significant association between the internal control system and financial performance in Medical Sciences University of Golestan and dimensions of internal control had an association with control environment, control activities and internal audit with financial performance. Michael O.O. (2016) investigated the issue of controls and frauds by assessing whether churches have effective internal controls and if such can prevent fraud. They concluded that the trace of internal control in place, churches need to work particularly on the authorization and personnel controls to avoid the incidence of fraud. Magu J.K. & Kibati P. (2016) aimed to establish the influence of internal control system on the financial performance of KFA Ltd. They revealed that the staffs have been not trained to implement the accounting and financial management systems; and that the security systems do not identify and safeguard organizational assets. They also found that there is a positive relationship between internal control systems and financial performance of KFA Ltd. Okechukwu, E. O. Umehali, E.E & Ugeh Scholastica (2016) evaluated the performance of co-operative societies in Delta State focusing on the degree of adoption and application of internal control systems. They revealed that internal control system has a significant influence on the performance of co-operatives, the internal control system being used by co-operatives are majorly physical control, financial authorization, arithmetic, and accounting. Adagye I.D. (2015) assessed the effectiveness of internal control system in tertiary educational institutions in Nasarawa State, Nigeria with a specific focus on the Nasarawa State Polytechnic, Lafia. They recommended that transparency should be seen as significant, as the institution work toward meeting its objectives, it, therefore, means that the right staff is assigned the right job and regular checking of the subordinates by their superiors ensue. Channar Z.A., Khan M. & Shakri I.H. (2015) investigated the functionality of each of the five internal control components, the effectiveness of the control system and its relationship with financial performance. Results showed that internal control effectiveness is strongest in private banks, followed by public banks and weakest in Islamic banks, although the difference is not statistically large, slight variation exists. Dimitrijevic D., Milovanovic V. & Stancic V. (2015) aimed of this work is to show how the overall quality of control and company performance is improved through implementation of preventive methods by internal controls, and to indicate that a developed system of internal control represents a protective barrier against various kinds of data manipulation and fraud inside the companies. They recommended that companies should be treated with much attention because their adequate implementation increases the quality of business performance and control. Internal control should gradually implement new methods for fraud prevention. Nevertheless, internal control should at least consult other controls while handling fraud in order to increase the quality of a company's defense mechanisms. Joseph O.N., Albert O. & Byaruhanga J. (2015) aimed to ascertain the effect of internal controls on fraud prevention and detection in district treasuries of Kakamega County. They recommended that effective and efficient internal control policies and procedures should be put in place to prevent and detect fraud within district treasuries and other institutions. Kinyua J.K. (2015) determined the effect of internal control systems on the financial performance of companies quoted in the Nairobi Securities Exchange (NSE). To achieve the objective of this study, they analyzed control environment, internal audit, risk management, internal control activities and role of corporate governance controls on the financial performance of quoted companies in Kenya. They concluded that there has a significant association between internal control environment and financial performance recommends that internal control environment should be enhanced to further improve the financial performance of companies quoted in Nairobi Securities Exchange.

OBJECTIVES OF THE STUDY

The proposed research work has been undertaken it meets the following objectives:

1. To undertake an in depth study of literature on the internal control system in co-operative banks.
2. To examine the impact of the internal control system on performance of the co-operative bank.

Hypotheses

The following hypothesis will be developed to significant the research work:

H₀: There is a no significant relationship between the internal control system and employee performance.

Research Methodology

In order to perform proposed study research methodology has been followed:

1. **Sampling:** for the collection of data we used the convenient sampling method for this research work.
2. **Data Collection:** for the collection of data questionnaire has been made. The questionnaire has been distributed to 217 respondents of Udaipur district of Rajasthan.
3. **Data analysis:** for the analysis of collected data, descriptive statistics, Z-test has been applied.

Demographic Profile of Respondents

Table 1 Demographic Profile

(A) Gender of Respondents	Count	Percentage
Male	133	61.3%
Female	84	38.7%
(B) Age of Respondents	Count	Percentage
Less than 25 Years	28	12.9%
25 years to 30 years	14	6.5%
30 years to 35 Years	49	22.6%
More than 35 Years	126	58.1%
(C) Education Level of Respondents	Count	Percentage
Under graduate	7	3.2%
Post-Graduate	140	64.5%
Chartered Accountant	49	22.6%
Professional	21	9.7%
(D) Type of Respondents	Count	Percentage
Bank Employee	84	38.7%
Manager	14	6.5%
Chartered Account	49	22.6%
Academic	56	25.8%
Others	14	6.5%

Table 1 shows the demographic profile of respondents. It has been classified into various sections. Section A describes gender of respondents. Out of 217 respondents, 133 (61.30%) respondents were male and 84 (38.70%) respondents were female. In this study, male respondents were more than female respondents. Section B describes the age of respondents. Out of 217 respondents, 28 (12.90%) respondents age were less than 25 years, 14 (6.50%) respondents age were between 25 years to 30 years, 49 (22.60%) respondents age were between 30 years to 35 years and 126 (58.10%) respondents age was more than 35 years. Maximum respondents were belonged more than 35 years age group. Section C describes education level of respondents. Out of 217 respondents 7 (3.20%) respondents were graduates, 140 (64.50%) respondents were post-graduate, 49 (22.60%) respondents were chartered accountant and 21 (9.70%) respondents were professionals. Maximum respondents of the study were highly educated. Section D describes the type of respondents. 84 (38.70%) respondents were bank employees, 14 (6.50%) respondents were managers, 49 (22.60%) respondents were chartered accounted and 56 (25.80%) respondents were academicians.

S No	Statements	Z-Value	Mean	STDVE	C.V.
1	It increases co-ordination between employees and management	-11.10*	2.13	0.49	23.13%
2	It provides reasonable assurance that the department will achieve its mission	-16.95*	1.84	0.57	31.26%
3	It increases ethical values in employees	-22.50*	1.90	0.39	20.53%
4	It increases corporate governance	-6.51*	2.19	0.69	31.61%
5	It increases Integrity of employees	-20.46*	2.00	0.36	18.00%
6	It increases Objectivity of employees	-12.94*	2.00	0.57	28.46%
7	It increases Professional Competence and Due Care in employees	-11.14*	2.16	0.45	20.73%
8	It increases Confidence of employees	-11.14*	2.16	0.45	20.73%
9	It increases Professional Behaviour of employees	-13.41*	1.94	0.62	32.05%
10	It identifies the areas in which the greatest threat or risk of inaccuracies or loss exist	-12.94*	2.00	0.57	28.46%
11	It increases the accuracy of the employees	-14.50*	2.03	0.48	23.38%
12	It increases the reliability of the employees	-12.78*	2.03	0.54	26.53%

13	It increases efficiency of employees	-14.50*	2.03	0.48	23.38%
14	It reduces mismanagement of employees	-29.67*	1.90	0.30	15.57%
15	It reduces irregularities between employees	-5.71*	2.23	0.71	31.76%
16	It helps in the economical and efficient use of resources	-28.93*	2.00	0.25	12.73%
17	It encourages adherence to prescribed managerial policies.	0.23	2.52	1.01	40.31%
18	Sound personnel policies and practices	-1.51	2.39	1.10	46.09%
19	It helps in separation of duties between employees	-5.38*	2.23	0.75	33.76%
20	It increase in monitoring performance	-8.07*	2.10	0.74	35.10%
21	It increases motivation of employees	-16.95*	1.84	0.57	31.26%
22	It provides better direction to employees	-16.50*	1.97	0.48	24.15%
23	It helps in better training to employees	-21.98*	1.87	0.42	22.53%
24	It increases performances of employees	-69.76*	1.10	0.30	27.02%

Table 2 shows opinions of respondents regarding “What is the impact of the internal control system on co-operative banks?” Z-test has been applied to test significant difference between the overall opinion of respondents and neutral opinion of respondents at 5% level of significance. It has been found that there is a significant difference in 19 statements out of 20 statements.

Respondents’ opinion on whether

1. “Internal control system plays important role in ensuring objective achievement of banks” z-score (-18.82) shows that there is a significant difference between opinions of respondents. The average score of opinion shows the agreement of respondents. Internal control plays important role in ensuring objective achievement of banks.
2. “Internal control system helps co-operative banks to reduce their operational risk” z-score (-17.24) shows that there is a significant difference between opinions of respondents. Average score (1.81) of opinion shows the agreement of respondents. Internal control system helps co-operative banks to reduce their operational risk.
3. “Internal control system helps in improve the reliability of financial reporting” z-score (-22.33) shows that there is a significant difference between opinions of respondents. Average score (1.71) of opinion shows the agreement of respondents. Internal control helps in improve the reliability of financial reporting.
4. “Internal control system influences the effectiveness of internal audit” z-score (-8.43) shows that there is a significant difference between opinions of respondents. Average score (2.19) of opinion shows the agreement of respondents. Internal control influences the effectiveness of internal audit.
5. “Internal control system encourages incorruptibility” z-score (-18.82) shows that there is a significant difference between opinions of respondents. Average score (1.84) of opinion shows the agreement of respondents. Internal control encourages incorruptibility.
6. “Internal control system helps deter fraudulent activities” z-score (-16.71) shows that there is a significant difference between opinions of respondents. Average score (1.87) of opinion shows the agreement of respondents. It helps deter fraudulent activities.
7. “Internal control system helps in Risk measurement” z-score (-14.00) shows that there is a significant difference between opinions of respondents. Average score (2.03) of opinion shows the agreement of respondents. Internal control helps in Risk measurement.
8. “Internal control system provides helps in independent financial statement audit” z-score (-3.04) shows that there is a significant difference between opinions of respondents. Average score (2.32) of opinion shows the agreement of respondents. The internal control provides helps in independent financial statement audit.
9. “Internal control system reduce detailed testing” z-score (-0.89) shows that there is no significant difference between opinions of respondents.
10. “Internal control system reduce audit fee” z-score (-14.00) shows that there is a significant difference between opinions of respondents. The average score of opinion (2.03) shows the agreement of respondents. Internal control reduces audit fee.
11. “Internal control system increases operational effectiveness and efficiency” z-score (-18.85) shows that there is a significant difference between opinions of respondents. Average score (1.90) of opinion shows the agreement of respondents. Internal control increases operational effectiveness and efficiency.
12. “Internal control system improves compliance with laws regulations and policies” z-score (-14.70) shows that there is a significant difference between opinions of respondents. Average score (1.94) of opinion shows the agreement of respondents. Internal control system improves compliance with laws regulations and policies.

13. "Internal control system increases efforts of the employees of a department" z-score (-7.31) shows that there is a significant difference between opinions of respondents. Average score (2.23) of opinion shows the agreement of respondents. Internal control increases efforts of the employees of a department.
14. "Internal control system increases effective use of assets" z-score (-19.06) shows that there is a significant difference between opinions of respondents. Average score (1.94) of opinion shows the agreement of respondents. Internal control increases effective use of assets.
15. "Internal control system assure the reliability and integrity of information" z-score (-11.10) shows that there is a significant difference between opinions of respondents. Average score (2.13) of opinion shows the agreement of respondents. Internal control assures the reliability and integrity of information.
16. "Internal control system helps in the economical and efficient use of resources" z-score (-11.18) shows that there is a significant difference between opinions of respondents. Average score (2.10) of opinion shows the agreement of respondents. Internal control helps in the economical and efficient use of resources.
17. "Internal control system encourages adherence to prescribed managerial policies" Z -score (-11.18) shows that there is a significant difference between opinions of respondents. Average score (2.10) of opinion shows the agreement of respondents. Internal control plays important role in ensuring objective achievement of banks.
18. "Internal control system increase in monitoring performance" z-score (-20.46) shows that there is a significant difference between opinions of respondents. Average score (2.00) of opinion shows the agreement of respondents. Internal control increase in monitoring performance.
19. "Internal control system helps in taking corrective action" z-score (-20.46) shows that there is a significant difference between opinions of respondents. Average score (2.00) of opinion shows the agreement of respondents. Internal control helps in taking corrective action.
20. "Reviewing compliance with existing financial regulations, instructions, procedures" Z -score (-25.80) shows that, there is a significant difference between opinions of respondents. Average score (1.81) of opinion shows the agreement of respondents. Internal control plays important role in ensuring objective achievement of banks.

CONCLUSION

Under internal control, we incorporate those activities in which the work of one person is tested and tested by another person. For any development in any organization, it is necessary that all the work was done by him be done at the initial level. Internal control is necessary for all organizations. It can be applied to all types of individuals and properties in internal control. Therefore it provides significant support for the development of all employees. The internal control provides the knowledge of motivating direct coordination to the employees and the knowledge necessary for their development. In this research, we have studied the effect of the internal control system on the employees of the co-operative banks in Udaipur city of Rajasthan State. To achieve the objective the current study questionnaire has been made and circulated among the respondents of Udaipur city on convenient bases. In this questionnaire total, 20 questions have been included. These 20 questions clarify the effect of internal control on the employees. We tested the views of these respondents and found that meaningful differences were found in the opinion of the respondents on these questions. To calculate the significant difference between opinions of respondents, z-test has been applied at the 5% level of signification and found that a significant difference was found in 19 of the 20 questions. Further, the average score of the respondents' opinion indicated agreements of the respondents. It shows that internal control has a meaningful and important effect on the employees and it also helps in the development of the employees. Therefore, it can say that internal control has a positive effect on the employees. The co-operative bank in which the internal control was implemented effectively, the employees of that co-operative bank are energized and provide significant support in the development of the banks.