

E-contents for Bcom, part-1
Vaniya Mahavidyalaya, Patna
University

Subject: AUDITING

Topic: INTERNAL CONTROL

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INTRODUCTION

It refers to all policies and procedures that are adopted by the management to ensure -

- Smooth and efficient operation of the business.**
- Optimum utilisation of resources.**
- Prevention of errors and frauds.**

Internal control may be defined as comprising the plan of the organisation and all the coordinate systems established by the management of an enterprise to achieve management objectives of ensuring as far as is practical the orderly and efficient conduct of its business including the safeguarding of the assets, the reliability of accounting records and the timely preparation of reliable financial information.

In a good system of internal control, the work of an auditor becomes very easy. The auditor makes a review of the system of internal control and evaluates its effectiveness for the determination of the extent of reliance that he can place on it and

the extent of tests and procedures that he can restrict.

OBJECTIVES OF INTERNAL CONTROL

- **To follow the policies and procedures**
- **Safeguarding of assets**
- **Prevent and detect the frauds and errors**
- **Accuracy and completeness of records**
- **To ensure that the business transactions are recorded as per the administrative Authorization**
- **To provide security to the assets from unauthorised use**
- **To evaluate the system of accounting for complete authorization of the transaction**
- **To insure there is the proper utilisation of business resources**

TYPES OF INTERNAL CONTROL

- **Detective internal control- To find error after they occur eg. Surprise cash counting, internal audit.**

- **Preventing internal control- Backup computer data, segregation of duties.**
- **Corrective internal control**

ESSENTIAL ELEMENTS OF INTERNAL CONTROL

- **Work should be divided among different employees.**
- **Relation among various departments should be clear.**
- **Work done by employees should be examined.**
- **Communication system of the institution should be analysed.**
- **Administrative level of the institution should be evaluated.**
- **Actual work should be compared with work standard.**

OBJECTIVES OF INTERNAL CONTROL SYSTEM

- **Verifying the assets of company**
- **Verifying the liability of company**

- **Reviewing the system of internal check**
- **Detection of errors and frauds**
- **Verifying the accuracy of accounts**
- **To follow the policies and procedures laid down by management**
- **Timely preparation of reliable financial information**
- **Completeness of records**

LIMITATIONS OF INTERNAL CONTROL SYSTEM

- **High cost of implementation**
- **Potential of human errors**
- **Possibility of collusion**
- **Misuse of authority**
- **Inadequacy**
- **Manipulation by management**

INTERNAL CHECK

It is a method of organising system of business in such a manner that work of one person is checked automatically by the work of others.

IMPORTANT ELEMENTS OF INTERNAL CHECK

- **Apply check day to day transaction**
- **Work continuously done automatically**
- **Work of one person is complementary to the work of another person**

BASIC PRINCIPLES OF INTERNAL CHECK SYSTEM

- **The authority and responsibility of the staff should be clearly defined**
- **There should not be any duplication of authority or responsibility at any level**
- **Division of work should be according to the skill, experience and ability of the employee**
- **All the cheques, drafts and etc received should be crossed and deposited in the bank**
- **All bad debts, claims of defective goods should be sanctioned by responsible officials**

- **All cash, cheques, drafts and etc received should be kept in safe custody with some responsible officials and deposited in the banks**
- **All the letters and other mails should be entered in a register and from there it should be sent to the department concerned under acknowledgement**

CHARACTERISTICS OF INTERNAL CHECK SYSTEM

- **Proper distribution of work**
- **Priority to machine work for accounting**
- **Change in work of employees**
- **Correspondence with debtors and creditors**
- **Self balancing system of ledger**
- **Prompt deposit of receipt in the bank**
- **Receipt and payment should be dealt by different person**

OBJECTIVES OF INTERNAL CHECK SYSTEM

- **Early detection of errors and frauds**

- **Efficiency of employees**
- **To reduce auditor's burden**
- **Promptness in work**
- **Simplify the audit work**

ADVANTAGES OF INTERNAL CHECK SYSTEM

- **Prevention of errors and frauds**
- **Fixation of responsibility**
- **Economical activity**
- **Motivate the employee**
- **It increases the profit of the business**
- **It reduces the workload of auditor**
- **Quick preparation of final accounts**
- **Proper performance of work**
- **No need of extensive checking**
- **Easy approach towards test checking**
- **It increases the efficiency of the clerk's**
- **Moral influence on the employee**
