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UDC:
005.584.1:352.07
657.633

TYPE OF WORK:
REVIEWED PAPER

RECEIVED: 26. 4. 2022. ✓

ACCEPTED: 19. 5. 2022. ✓



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THE EFFECTIVENESS OF INTERNAL CONTROL IN LOCAL GOVERNMENT UNITS

Abstract: There are many definitions of control, which shows its various functions, however the essence of control always remains one – the control is aimed at comparing the existing actual state of affairs with the desired state. All differences between these states should be detected by the controlling authority and the methods, guidelines being supposed to eliminate these shortcomings must be indicated in the recommendations and conclusions. It should be pointed out that each individual unit is aspiring to the realization of defined goals. These goals can be differently defined. They express themselves in the pursuit of full compliance actions with the law, ensuring that the data presented in financial statement are reliable, preventing the uncontrolled outflow of information from the unit. The effective internal control is helpful in achieving these goals.

Aim-determining the meaning of the terms: internal control, management control and presenting the relationship between these concepts. Research methodology – direct questionnaire surveys (PAPI). The attempt was made to identify supporting factors and limit the effectiveness of internal control in local government units.

Keywords: SYSTEM OF INTERNAL CONTROL, MANAGEMENT CONTROL, EFFECTIVENESS.

Introduction

The concept of the internal control system in local government units is probably the most important for the entire practice of auditing and control. The internal control system, as it results from the conducted research, is a commonly used method to ensure due care for the proper course of processes and protection of the interests of the public administration body.

The concept of the internal control system in local government units is not a new concept, and the control system itself, in a more or less formalized way, functions in each of the analyzed units.

Internal control is the basic mechanism that enables financial management to be conducted in a manner consistent with the principles of purpose limitation, effectiveness and efficiency (Bananuka, Nkundabanyanga, Nalukenge & Kaawaase, 2018). It is also important that the control finalizes the management process of the enterprise and each activity within it.

It should also be pointed out that control in management science was and is perceived as an element which supports management (Hellich, 2010, p. 25).

Therefore, the entire control process allows managers to monitor the progress of work of lower-level employees (Khan, Khalid, Anjum, Khan, Cho, & Park, 2022, p.136). Tag and IoT based safety hook monitoring for prevention of falls from height. *Automation in Construction*, 136, 104153), without the need to limit both the creativity and skills of employees and without interfering with its course. Thus, the face of control changes from a tool that accounts a given employee into a tool that controls his actions.

The aim of the article is to define the meaning of the terms: internal control, management control and to present the relationship between these terms. Additionally, the article attempts to indicate factors supporting and limiting the effectiveness of internal control functioning in local government units.

Research methodology - the research results were obtained thanks to the conducted direct questionnaire research (PAPI), limited to local government units located in the Żagań powiat. Additionally, the literature, legal acts and internal documents of the surveyed entities were analyzed.

On the basis of the case study, a list of factors has been formulated that have an impact on the conduct of effective and rational internal control in units, in terms of the factors indicated in the article that cause its limitations.

Internal control system in communes and management control

The relationship between internal control and management is reflected in the draft amendment to the Public Finance Act, where the term “management control” is introduced instead of the word “internal control”.

The Public Finance Act of 2009 [Public Finance Act, 2009, Article 272 (1)] introduced the concept of management control, defining in it both the tasks and obligations of managers of public sector units, including local governments, related to the need to implement it. Management control covers all activities undertaken to ensure the implementation of objectives and tasks in a legal, effective, economical and timely manner.

Currently, the provisions on management control depart from the need to create procedures and perceive the entity as an institution collecting and spending public funds. Management control focuses on the goals and tasks that the entity is to accomplish. However, there is a noticeable trend that the functioning of public finance sector units is assessed through the prism of the tasks performed and the degree of achievement of objectives while the proper functioning of the unit is an element of the system, not the overriding purpose of its operation.

The control system in a commune or public administration body in the public finance sector consists of:

- internal and external orders, instructions and procedures,
- authorizations, formal replacements, etc.,
- scope of activities and duties,
- formal limitations of rights,
- no entry and restriction of access to rooms, the presence of two people required to perform certain activities,
- hierarchical organizational structure,
- transaction authorization procedures (Jędrzejewski, Nowicki, 1995, pp. 32-56).

The use of the above-mentioned means makes all activities performed in the units a coordinated and orderly operation. All the mentioned measures form a coherent whole called the internal control system, and the means that make up the control system are called control mechanisms.

A properly functioning control system must have arrangements in place:

1. preventing problems and errors,
2. detecting and reporting problems,
3. correcting detected errors and minimizing their effects.

These mechanisms are known as: preventive, detection and corrective control

mechanisms, respectively. Although it is commonly believed that risk prevention is the most effective action, it is difficult to imagine a well-functioning system without solutions that detect errors and minimize their effects (Jagielski, 2018, pp. 47-73).

Pursuant to Art. 68 sec. 2, the purpose of management control is to ensure, in particular:

- compliance of operations with legal regulations and internal procedures,
- effectiveness and efficiency of activities and information flow,
- credibility of reports,
- resource protection,
- compliance and promotion of the principles of ethical conduct,
- risk management (Paczuła: 2004, No. 4 (11)).

Ensuring the functioning of adequate, effective and efficient management control belongs to the duties of:

- a minister by the government administration departments he manages,
- commune head, mayor, city president, chairman of the management board of a local government unit,
- the entity's manager (Public Finance Act, 2009, Article 69 (1)).

Pursuant to these regulations, a catalog of persons responsible for the proper functioning of the management control system has been defined and the features of the system itself have been defined. The legislator indicated that the management control system should meet the following features:

- adequacy,
- efficiency,
- effectiveness (Płękka, 2005, No. 12).

Adequacy should be characterized by whether the designed system is optimal for the purposes and tasks carried out by units of the public finance sector. Thus, the adequacy should take into account the specific nature of the entity's activity.

On the other hand, efficiency answers the question of whether the assumed goals and tasks are carried out with the use of optimal financial outlays (Wu & Zhang, 2019, p. 586-590).

The last feature, effectiveness, means that the implementation of goals and objectives is carried out in a reasonable manner. It is the responsibility of each unit manager to implement the management control system in the unit he supervises, i.e. in all its organizational units.

According to K. Winiarska (Winiarska, 2005, p. 83), internal control should be an efficiently operating system consisting of the organization, methods and procedures of each area of the entity's activity in order to ensure its functioning.

According to M. Klimas (Klimas, 1997, p. 237), internal control, as a management function, includes the following control phases:

1. determining the actual state,
2. determining the applicable, designated state,
3. comparing the actual state with the state designated in order to establish their compliance or non-compliance,
4. explaining the reasons and effects of stating the compliance or non-compliance of the actual state with the designated state (Dobbin & Fencel, 2021, No 73).

The above phases of the concept of control should be applied cumulatively, none of them taken separately can be considered internal control.

When analyzing international standards of internal control, one can notice common elements for management control in the developed COSO report or INTOSAI standards (Yilmaz & Karakaya, 2020, p. 753-769).

In accordance with the INTOSAI Guidelines on Internal Control Standards, internal control is a management tool used to obtain reasonable assurance that management objectives have been achieved. Therefore, the responsibility for the suitability and effectiveness of internal control structures rests with business unit management. The manager of each organization should ensure an appropriate internal control structure as well as its verification and improvement so that it is effective (Czerwieński, 2004, p. 156).

In the COSO report, internal control, which also applies to municipalities, is defined as a process carried out by the company's management and other employees (Frazer, 2020, p.28-38). This process is designed to achieve reasonable assurance that the goals are achieved in the following terms:

1. Operational efficiency.
2. Reliability of financial statements.
3. Compliance with laws and regulations.

The first category relates to the commune's core goals of achieving profitability and securing resources. The second is related to the preparation of reliable financial statements to be made public. The third one is compliance with the law and other regulations in force in a given organization.

According to the concept presented in the COSO report, the internal control system in the commune consists of five elements, closely related to each other and to the management process in local governments. They are as follows:

1. Control environment.
2. Risk assessment.
3. Control activities.
4. Information and communication.
5. Monitoring (Kałużny, 2008, p. 74-112).

K. Czerwieński additionally includes internal audit as an element of the internal control system. Internal audit, apart from being an element of this system, monitors

its functioning and evaluates it (Czerwiński, 2004, p. 162).

The internal control system should effectively combine the controllers, the subject of control and control activities, taking into account the environment in which the above-mentioned activities are carried out. Therefore, the internal control system should be considered in terms of the subject, object and function.

Factors supporting and limiting the effectiveness of internal control in local government units

As a result of the study on the effectiveness of internal control, direct questionnaire surveys (PAPI) were conducted on November 15-19, 2021. Eight local government units from the Żagań powiat participated in the study, i.e. 100%. As a result, factors contributing to the achievement of effectiveness in the control systems as well as the factor causing its reduction have been identified.

Internal control in a commune can help the organization achieve its goals. According to the definition presented at the beginning of the article, it is supposed to give the management a reasonable assurance about the achievement of goals, while not guaranteeing their achievement.

The results of the conducted research became the basis for formulating a list of factors for achieving high efficiency. Thus, the quality of internal control in the surveyed communes is influenced by the following factors:

- internal control regulations, serving as a formal definition of the scope of the controls performed,
 - work regulations and job cards should be precisely defined as to the scope of tasks, duties and responsibilities required of employees working in specific positions,
 - document circulation instruction, allowing to indicate the correct system of circulation, records and control of documentation in the unit,
 - in the accounting policy, the rules for the use, storage and inventory of assets should be defined
 - high qualifications of inspectors and ethical behavior of the entity's employees.
- Limitations of internal control in a commune may result mainly from:
- making wrong decisions based on control findings,
 - oversight, distraction or carelessness of employees,
 - disregard of the institution of control by superiors or management,
 - collusion of persons acting jointly to commit or conceal a tort.

Among the irregularities related to the functioning of the applicable internal control standards in the surveyed communes, the following were indicated, inter alia,

on insufficient professional competences of employees, including: non-compliance with recruitment procedures (14%), lack of periodic employee appraisal (30%) and lack of periodic training plans (55%).

It was observed that although internal control should be exercised at all levels of the entity's functioning, taking into account the activities of both the management and employees of the entity, as many as (45%) employees were not trained in this area.

Despite the fact that the internal control system enforces the use of procedures allowing for very accurate and timely recording of economic events, errors were found in 50% of respondents. It is often explained by ignorance of the regulations (in the case of employees with short work experience), misinterpretation of the applicable regulations and excessive work duties.

The applicable legal provisions and standards were often not taken into account in the procedures in place (23%). It also indicated numerous deficiencies in defining the accounting principles in the entity and updating the accounting policy in force (18%).

There was also a lack of identification of regular employees with the set goals of the unit and the tasks performed by them (25%).

There was also a lack of management action to identify appropriate remedial measures to limit the occurrence of adverse events (20%).

In communes, there was also an incorrect definition of the scope of duties and responsibilities for individual positions (14%).

The obtained data allowed for the determination and indication of factors that support and limit the effective application of management control in units. It should be pointed out that initiating, modifying and remedial actions are necessary in each of the examined communes.

The analysis of the collected data proves that the effectiveness and quality of the internal control system depend to a large extent on people. The management has the greatest responsibility for the operation of the system and therefore should identify with it. In fact, the attitude of management towards an internal control institution influences the way it is treated by other employees. The role of management is to set directions for action, control the achievement of goals and enforce their implementation.

The analysis of the collected data proves that the effectiveness and quality of the internal control system depends to a large extent on people. The management has the greatest responsibility for the operation of the system and therefore should identify with it. In fact, the attitude of management towards an internal control institution influences the way it is treated by other employees. The role of management is to set directions for action, control the achievement of goals and enforce their implementation.

It should also be emphasized that internal control provides information for the

self-assessment of management's conduct. Errors or shortcomings of individual employees may result from the way of acting and wrong decisions made by the management.

The analysis also showed that in 45% of units, the processes were improved on an ongoing basis, the efficiency and effectiveness of internal control systems were improved, and the internal procedures were updated and detailed. Moreover, the compliance of actions taken by communes with the law and internal regulations was ensured.

Undoubtedly, the existence of internal control is necessary due to its key role in improving the functioning of local government units.

Conclusions

It should be noted that management control, unlike internal audit, which is obligatory only in some units of the local government subsector, is carried out in all audited units.

As the analysis shows, internal control in a commune is the sum of systems and procedures aimed at:

- ensuring an orderly, efficient and effective activity consistent with the tasks of a given unit,
- securing resources against possible losses resulting from waste, abuse, mismanagement, errors or other irregularities,
- compliance with laws, regulations and legal regulations as well as issued internal regulations,
- timely recording of financial and management data and their reliable disclosure in obligatory reports.

Summing up, it should be stated that both the knowledge of the management staff and the skilful selection of supporting factors lead to the proper and reliable functioning of the control in a given unit. Despite the fact that in each of the audited units there are a number of ordinances and resolutions regarding the efficient functioning, without the implementation of efficient and effective internal control, the proper functioning of the unit would be impossible.

To be effective, control activities should be useful, linked to the entity's responsibilities, goal-oriented, objective, reliable and credible, and implemented with the desired detail and flexibility. Thus, the above features and the factor should be taken into account when building an internal control system in local government units.



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ЕФЕКТИВНОСТ УНУТРАШЊЕ КОНТРОЛЕ У ЈЕДИНИЦАМА ЛОКАЛНЕ САМОУПРАВЕ

Апстракт: Постоји много дефиниција контроле које показују њене различите функције, међутим суштина контроле увек остаје једна – контрола је усмерена на упоређивање постојећег стварног стања ствари са жељеним стањем. Све разлике између ових стања треба да открије контролни орган, а методе, смернице које треба да отклоне ове недостатке морају бити назначене у препорукама и закључцима. Треба истаћи да свака појединачна јединица тежи остварењу дефинисаних циљева. Ови циљеви се могу различито дефинисати. Изражавају се у тежњи за потпуним поштовањем закона, обезбеђујући да подаци приказани у финансијским извештајима буду поуздани, спречавајући неконтролисани одлив информација из јединице. Ефикасна интерна контрола помаже у постизању ових циљева.

Циљ – утврђивање значења појмова: интерна контрола, управљачка контрола и представљање односа између ових појмова. Методологија истраживања – директна анкета (ПАПИ). Покушај да се идентификују пратећи фактори и ограничи ефективност интерне контроле у јединицама локалне самоуправе.

Кључне речи: СИСТЕМ УНУТРАШЊЕ КОНТРОЛЕ, УПРАВЉАЧКА КОНТРОЛА, ЕФЕКТИВНОСТ.