

## **EVALUATION OF ROLES OF INTERNAL CONTROLS IN PREVENTING AND DETECTING FRAUDS: A STUDY OF GUARANTY TRUST BANK PLC, LAGOS.(2005 -2017)**

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### **ABSTRACT**

*The study evaluated the roles of Internal Controls in preventing and detecting fraud; in essence, the study assess the impact of internal control system as a means to maximize and prevent the occurrence of fraudulent practices in any form in the banking sectors. The researchers used two sources of data collection, the primary source which enable researchers to get first class information and the secondary method of data collection. In this research work, questionnaires were administered for collecting data using random sampling techniques. Results of this study shown that the major causes of fraud and actors that contributed to the incidence of fraud and forgery in commercial banks is job insecurity, and also revealed that overriding of control system in the banks by top management has also significantly contributed to the collapses of some banks in the past couple with poor or weak management control, monitoring and lack of supervision of internal control system and procedures which also caused fraud to be perpetrated. It has been established in this study that internal control system is paramount in ensuring effective operation of banks, and it has impact on prevention and detection of fraud and enhances the overall profitability of banks. From the study, it was cleared that Guaranty Trust Bank Plc, there control procedures and monitoring activities have shown conformity with good internal control system and staff job being highly secured.*

**KEYWORDS:** *Internal Controls, Fraudulent practices, Management control, Commercial Bank*

## **INTRODUCTION**

Banks occupy a critical position in a complex financial system that supplies the money and credit needs of the economy. The unique characteristic of a commercial bank is that it also creates money, and it is this particular feature of the commercial banks which distinguishes them from non-banking financial institutions. However, all take part in the process of financial intermediation whereby such intermediaries also provide considerable benefits to borrowers in so far as there may be difficulties in locating potential savers who are willing to lend appropriate amount of funds at relevant interest rate.

Banks' ability to promote growth and development depends on the extent to which financial transactions are conducted with trust and least risk. The foundation on which banks is built is on confidence and trust, and where banks indulge in unsafe and unsound confidence, such banks may collapse. So, for banks to achieve objectives and as well as generating overall confidence, the Introduction and Establishment of Internal Control must come in to promote efficient operation. Internal control system therefore serves as a sine-qanoon for Fraud Prevention. Internal control is a creation of management, thus, the management retains sole responsibility for the establishment and maintenance of adequate and functional internal control.

Banks play very important roles in the economic development of any country. As an important component of the financial system, banks channel scarce resources from surplus economic units to deficit units. Thus, to an appreciable and reasonable extent, they exert a lot of influence on the pattern and trend of economic development through their lending and deposit mobilization activities. The efficient mobilization of savings and its allocation of productive investment by financial institution, thereby promote economic growth and development as well as achieving their objectivities, profitability and solvency. All the aforementioned benefits that banks can exert on the economy as a whole can be achieved through an effective internal control system and fraud prevention in the banking industry. "Internal Control system is an independent appraisal function within an organization for the review of system of control and the quality of performance as a service in the organization. It as a review of operations and records, sometime continuous undertaken with a business by a

specially assigned staff. Internal control, therefore is a whole system of controls, financial or otherwise, established by the management in order to carry out the business of an enterprise in an orderly and efficient manner, ensure adherence to management policies, safeguard the assets and secure as far as possible the completeness and accuracy of record. Fraud, on the other hand is defined as an act of deception deliberately practiced to gain unlawful or unfair advantage to the detriment of another. Fraud is an intentional act by one or more individuals among management, those charged with governance, employees or third parties involving the use of deception to obtain an unjust or illegal advantage. Fraud may include: manipulation, falsification or alteration of documents and records; recording transaction without substances, intentional misapplication of accounting policies etc. just to mention a few. Therefore, the menace called fraud has been a deadly disease that has infected many financial corporate body particularly the banks which led to reformation in the banking industry in Nigeria in the past, thus, involving the process of business combination in the industry such as merger and acquisition whereby the infected banks are being merged to and/or acquired by the financially healthy and sound one. The enormous damage that fraud has done to the banks, thus, the dilution in the financial strength of Nigeria banks. To combat this syndrome of fraudulent practices, several measures have been identified as the way out to minimize this act. Internal control system is one of the many measures that are to be discuss in of this journal. Internal Control System has been the most single trusted and effective measures that can combat this act of malpractices to the barest minimum. In fact, the Central Bank of Nigeria (CBN) reported that the backward development in Nigeria was attributable to the weakness in the Internal Control System of the banks. Therefore, an attempt to bring to barest minimum, if not completely eradicated, the spate of fraud by the measure of internal control system gave rise to this paper.

## **CONCEPTUAL AND EMPIRICAL REVIEW**

This paper presents the literature reviewed on evaluation of roles of internal controls in preventing and detecting fraud in banking sector studying Guarantee Trust Bank Plc. It is divided into Conceptual, and Empirical.

It begins with an overview of the conceptual framework of internal control in the Banking Industry and how fraud is preventing and detecting and the need for improvement.

The institute of chartered accountants of England and wales define internal control as the whole system of controls, financial or otherwise established by management in order to carry out the business of an enterprise in orderly and efficient manner, ensure adherence to management policies, safeguard the assets and secure as far as possible the completeness and accuracy of records.

Internal Controls as the measure taken by an organization for the purpose of protecting its resources against waste, fraud, inefficiency; ensuring accuracy and reliability in accounting and operating data; securing compliance with organization policies and evaluating the level of performance in the division of the organization.

Internal control system of an independent appraisal function within an organization for the review of system of control and the quantity of performance as a service in the organization. Also following the need to restore public confidence and trust in the financial statement of companies, both financial and non-financial institutions, as it emphasizes the importance of effective internal control, and thus, internal control also seen as the procedures and processes used by a company to safeguard the assets, process information accurately and ensure compliance with laws and regulation. It requires companies to maintain strong and effective internal control over the recording of transactions and the preparing of financial statement. Such controls are important because they detect fraud and prevent misleading financial statements. From these definitions, it can be deduced that internal control comprises the plan of an organization and all of the co-ordinate methods and measures adopted within it, to safeguard its assets, check the accuracy and reliability of its accounting data, promote operational efficiency and encourage adherence to prescribed managerial policies. Internal control objectives are channels towards ensuring adherence to managerial policies and achieving organizational goals in general. It also embraces internal checks, internal audit and the whole system of control, checks and balance established by the management.

Fraud has been widely defined in literature by scholars and experts. Fraud as an action or an instance of checking somebody in order to make money or obtain goods illegally. The same dictionary defines the perpetrators of frauds as fraudsters. According to the Institute of Chartered Accountants of Nigeria study Pack, Fraud consists of both the use of deception to obtain an unjust or illegal financial advantage and intentional misrepresentations, affecting the financial statements by the one or more individuals among management, employees, or third parties.

Fraud is an act of deception deliberately practiced to gain unlawful or unfair advantage to the detriment of another, also refer to fraud as the misrepresentation by a person of a material fact known. Fraud is also referred to as intentional misrepresentation of financial record by one or more individuals or by management or employee or third parties. It is also a type of irregularities involving the use of criminal deception to obtain an unjust or illegal advantage. Fraud is a predetermined and well planned tricky process or device usually undertaken by a person or group of persons, with the sole aim of checking another person or organization, to gain ill-gotten advantages, be it monetary or otherwise, which would not have accrued in the absence of such deceitful procedure. From the above, the term fraud may be said to be as an intentional misrepresentation of financial information by one or more individuals among management, employees or third parties. Fraud may involve;

- (a) Manipulation, falsification or alternation of documents and records
- (b) Recording transaction without substances
- (c) Mis-appropriate of assets or theft
- (d) Intentional mis-application of accounting policies
- (e) Suppressing of transactions or omitting such transaction from records
- (f) Wilful misrepresentation of transactions of the entity's state of affairs

Involves taking a property unlawfully from its owner, without his/her knowledge, permission or consent, or to misstate a situation knowingly or by negligence.

## **INTERNAL CONTROL ELEMENTS**

These elements are also refers to as the component of internal control. The internal control systems therefore consist of five closely related components and interrelated elements. They are:

1. Management oversight and the control culture
2. Bank recognition and assessment
3. Control activities and segregation of duties
4. Information and communication
5. Monitoring activities and correcting deficiencies

The problems observed in recent large losses at banks can be aligned with these five elements. The effective functioning of these elements is essential to achieving a bank's performance, information, and compliance objectives Principles for the assessment of internal control system under each of the elements.

### **The Need for Internal Control Department/ Unit**

The aftermath of fraud, , causes an embarrassment to the nation and on bank owners, customers and their family members, as most bank failures are associated with large scale frauds.

In his conclusion, the internal control department/unit of any organization is very important in detection and prevention of fraud and cannot be undermined especially by banks, since lack of an effective internal control system, according to the he findings is the major cause of bank frauds. It is then concluded that the management of every bank should create and establish a standard internal control system, strong enough to stand against the wiles of fraud in order to promote continuity of operations and to ensure the liquidity, solvency and going concern concept of the bank.

## **METHODOLOGY**

The methods and procedures that were employed in this journal is discussed. It is also covered research design, sources of data, determination of sample size, procedures employed in the data collection, and the techniques used in analysing the data collected.

The method used in this paper was the exploratory research design. This design method was chosen so as to enable gathering of information relating to Evaluation of roles of internal controls in preventing and detecting fraud as it applies to the activities of Guaranty Trust Bank Plc. in Nigeria. Furthermore, applications internal controls by bank officials is not widespread, thus the reason for this design method.

The researchers examined an evaluation of roles of internal controls in preventing and detecting fraud impact of the application on Guaranty Trust Bank Plc. It also examined the degree to which Guaranty Trust Bank Plc understand and appreciate the value of internal controls in relation to on Guaranty Trust Bank Plc to reduce fraud through internal control. It also examined the extent to which internal controls has been employed by the Guaranty Trust Bank Plc over the past seven years and the major challenges that have militated towards the maximal applications of internal control by Guaranty Trust Bank Plc in fulfilling its mandate.

The data required for this paper was therefore obtained by studying Guaranty Trust Bank Plc operations over the study period and responses of Guaranty Trust Bank officials to trends that they have observed over the years.

The total population of GTB officials within the selected offices within Lagos State, used for the study is 1,250. This gives a sample size of 120. (Confidence level used is 95%, and the standard deviation was 8.5).

## **METHOD OF DATA COLLECTION**

Primary and secondary data collection methods were adopted for this paper. The primary source involved the administration of questionnaires directly to the respondents. The questionnaires were designed to generate concise and precise answers using close-ended questions comparing of responses such strongly agreed, agreed, undecided, strongly

disagreed and disagreed. The respondents were given one week to respond to all the questions.

Secondary sources of data includes published documents obtained from Guarantee Trust Bank; this includes annual report and account journals, magazines, seminars papers, textbooks, periodic and circulars. Data were also obtained from CentralBank of Nigeria, journals (relevant to study), as well as court proceedings and judgement records.

### **METHOD OF DATA ANALYSIS**

The distribution of the response to the questionnaire was done using simple percentages. The responses to the questionnaires were analysed using electronic statistical package (SPSS) using regression analysis as a parameter to determine the effects on the variables under study. Furthermore, a summary was done using descriptive statistics of mean, standard deviations and coefficient of variations. The two hypothesis of the study were tested with the aid of student's t-statistics as the inferential statistic. With the degree of freedom of (n-1) for a sample size n and level of significance set at 0.1 (10%).

#### **Data Analysis**

$$\text{Expected Mean} = \frac{(5+4+3+2+1)}{5}$$

5

$$\text{Expected Mean} = 3$$

#### **Decision Rule**

The null hypothesis (Ho) was rejected if the calculated t value exceeded the tabulated/ critical t value. Otherwise, the null hypothesis was not rejected.

#### **Scope of Research and Coverage Area**

The research was designed to cover the activities of the Guaranty Trust Bank over a period of 12 years (2005-2017), using the Lagos offices as case study. The study was conducted in the selected offices of Guaranty Trust Bank in Lagos state. This is because Lagos State is the hub of business activities in Nigeria and it accounts for the largest portion of the income

generated by the Guaranty Trust Bank in the country. It has the largest population of customers.

## RESULT AND DISCUSSION OF FINDINGS

Data was gathered as well as evaluated centred on the research objectives and questions. The questionnaires were also distributed to the 120 staff of Guarantee Trust Bank PLC in 14 Branches in Lagos State.

The data collected were analysed as follows: One hundred and twenty (120) questionnaires were administered to respondents in Guaranty Trust Bank Plc, One hundred and seventeen (117) were returned, and as such, One hundred and seventeen (117) were available for analysis.

Respondents were assessed on their awareness of the principles of internal control system and its potential in contributing to income generation by the Guaranty Trust Bank. The result is shown in table below.

### Internal Control System as a Tool to Increase Revenue Generation

Expected Mean = 3	Percentage of Responses					Mean Scores of Responses		
	5	4	3	2	1	Mean	SD	Coefficient of Variation
Questions	%	%	%	%	%			%
3. (Q3) I am familiar with Internal control and I know it can be used by GTB to minimize/reduce its fraud,	58.12	35.90	5.12	0.8	0	4.51	0.64	14.14
4 (Q12) I am aware that GTB have certified system auditors to curb	27.35	39.32	24.79	7.69	0	3.87	0.91	23.49

internal fraud in the  
Bank

5	(Q13) I do not know if all the internal control officers of the Bank are certified system auditors to curb the fraud	0.8	9.40	11.97	62.39	11.11	2.23	0.91	23.49
6	(Q10) If GTB internal control system more seriously, its profit will increase greatly	48.72	41.88	5.98	1.71	0.8	4.37	0.75	17.21
7	(Q11) If GTB applies Internal control system more seriously, the fraud cases will greatly reduce	47.01	45.30	4.27	2.56	0	4.38	0.69	15.84
8	(Q14) Internal control system put in place by the bank help to prevent all the attempted fraud case	50.43	42.74	5.13	0	0.8	4.43	0.68	15.24
9	(Q17) Recruitment of competent/ experience staff will facilitate the act of fraud prevention and detection	46.15	47.86	0.8	3.42	0	4.39	0.68	15.58

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**Source: Field Work, 2017.**

Response on awareness of the potentials of Forensic accounting 94% of respondents are familiar with Internal control and they agree that it can be used by Guaranty Trust Bank to boost its revenue 67% of respondents indicated that they are aware of five or more Certify System Auditor who work within the GTB. This is for the confirmed by the fact that about 21% are not certain that they know of any Certify system auditor in Bank.

**Response on the contribution of Internal Control System to the increased revenue generated by Guaranty Trust Bank over the past 12 years.**

In assessing the contribution of Internal Control System to the increase in revenue generated by Guaranty Trust Bank over the last twelve years, the response of the respondents is summarized in Table below:

**Contribution of Internal Control System to the increased revenue generated**

Questions	Expected Mean = 3	Percentage of Responses					Mean Scores of Responses		
		5	4	3	2	1	Mean	SD	Coefficient of Variation
		%	%	%	%	%			%
10. (Q4) Over the last 12 years, Certify Internal Control has not been fully employed and maximized by GTB as it should		35.90	36.75	16.24	8.55	0	4.03	0.95	23.47
11. (Q6) Internal Control is a major tool that has been used by GTB in its operations		4.27	16.24	21.37	53.85	3.42	2.64	0.95	35.84
12. (Q7) Internal Control officers have never been		3.42	13.67	56.41	25.64	0.8	2.93	0.75	25.62

called upon in fraud  
litigations involving GTB

- |     |   |      |       |       |       |      |      |      |       |
|-----|---|------|-------|-------|-------|------|------|------|-------|
| 13. | (Q8) GTB does not have Certified Accountants Internal Control as part of its Management                     | 0.8  | 6.84  | 22.22 | 63.25 | 5.13 | 2.34 | 0.72 | 30.96 |
| 14. | (Q9) Internal Control System has contributed to increased income generated by the GTB over the last 12years | 6.00 | 17.95 | 26.50 | 47.01 | 1.71 | 2.79 | 0.97 | 34.54 |

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**Source: Field Work, 2018.**

### **Response on the Contribution of Internal Control to the Increased Income Generated by GTB over the Study Period.**

73% of respondents agree that internal control has not been fully employed by the Guaranty Trust Bank during the study period. This is further confirmed by the fact that majority (57%) are of the opinion that Internal Control is not one of the major tools that GTB employs in its day to day operation. 56% of respondents are not certain as to whether internal control officer have been involved in fraud litigations involving GTB. 69% of respondents are of the opinion that the GTB has certify internal control officer as part of its officials. 49% of respondents believe that internal control has not made any significant contribution to the increased revenue/ income generated by the Bank over the last twelve years.

### **CONCLUSIONS AND RECOMMENDATIONS**

Detailed examination of internal control system and fraud prevention in Commercial Banks was looked into in this paper because of the rate of fraud and forgery that has negatively affected the profitability and growth of financial institutions. This work specifically examined

the role of internal control system on fraud prevention in Guarantee Trust Bank. In gathering information, both primary and secondary sources of data were used and properly analyzed.

Mobilization of savings and lending being an important activities in commercial banks business and which Santomero, and lending, accounts for a sizeable portion of the risk assets of banks. Thus, both has associated problem of fraud and forgery in ensuring effective mobilization of such savings and collections of the amount lent out. From the findings, it is obviously depicted that the major causes of, and actor that contributed to the incidence of fraud and forgery in commercial banks is job insecurity. Furthermore, the findings vividly revealed that overriding of control system in the bank by top management has also significantly contributed to the collapses of some large banks, coupled with poor or weak management control, monitoring and supervision of internal control system and procedures which also causes fraud to be perpetrated. However, general principles for the assessment of internal control system as sub-divided under each of the elements of internal control system were examined. During the course of this study, the primary data reveals that strong and effective system of internal control reduces the risks of fraud and forgery being perpetrated and also ensures the continuous existence (going concern) of the bank.

It has been established in this study that internal control system is paramount in ensuring effective operation of banks, and it has impact on prevention and detection of fraud and enhances the overall profitability of banks. As such, it is an important factor that ensures the going concern of corporate body especially financial institution. Most commercial banks, though has internal control system in place, but are being threatened due to weak and ineffective monitoring of the controls in place, and the overriding of such control by management.

Having studied the situation in Guaranty Trust Bank Plc., it is imperative at this point to make some recommendations as to ways of prevent further occurrence of fraud and forgery and to improve monitoring activities and procedures on internal control system in commercial banks. In order to achieve these, the following suggestions are advanced:

1. Bank staff should be guaranteed of job security.
2. Proper evaluation of the system of internal control and the various control procedures relating to control objectives should be constantly monitored, supervised and improved where any lapses is noticed or found. This can be achieved by establishing an internal control unit/department.
3. External control system as discussed in the conclusion paragraph above should be strictly, constantly and continuously adhere to or followed in order to make internal control system effective and sufficient enough to reveal lapses and inadequacies open to fraudsters and forgers within and outside the bank.

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