INTERNAL CONTROL SYSTEMS AND CORPORATE SURVIVAL IN THE NIGERIAN BANKING INDUSTRY: A STUDY OF SOME SELECTED BANKS

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BEING A THESIS SUBMITTED TO THE POST GRADUATE SCHOOL, AHMADU BELLO UNIVERSITY, ZARIA, IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF MASTER OF SCIENCE (M.Sc.) DEGREE IN ACCOUNTING AND FINANCE.

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DECLARATION

I, Kabir Tahir Hamid, hereby declare that this research work is original and is the result of my personal research effort. To the best of my knowledge and belief this work has never been submitted nor accepted in any institution for the award of any degree or certificate of any kind.

All contributions and borrowed materials are duly and properly acknowledged in the bibliography. Any error, either of omission or commission is not with intent, and is highly regretted.

Considering the facts that complete accuracy is not always possible due to human weaknesses, I personally accept responsibility for any shortcomings and inadequacies herein.

Kabir Tahir Hamid

CERTIFICATION

This thesis entitled: **INTERNAL CONTROL SYSTEMS AND CORPORATE SURVIVAL IN THE NIGERIAN BANKING INDUSTRY: A STUDY OF SOME SELECTED BANKS**, by Kabir Tahir Hamid, meets the regulation governing the award of Master of Science (M. Sc.) Degree in Accounting and Finance of the Ahmadu Bello University, and is approved for its contribution to knowledge and literary presentation.

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DEDICATION

This research work is dedicated to my first son Abdul-Jalal Kabir Tahir (Late) who died during my course work, two weeks after he was born. May him save us in the hereafter. Amin.

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The successful completion of this research project is made possible by the help and assistance received from many people and institutions to whom I owe a duty to express my profound gratitude and appreciation.

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ABSTRACT

This research thesis investigates the problem of corporate failures as a result of weak internal controls system, which brings about distressness, collapse and withdrawal of licences of banks by regulatory authorities in Nigeria, thereby bringing untold hardship to all stakeholders.

The researcher used a sample of seven banks, systematically selected from a population of twenty-eight banks whose shares were traded on the floor of the Nigerian Stock exchange as at 22nd August 2003. Questionnaires were administered on 420 respondents, 60 from each of the seven banks, made-up of 20 from the management staff, 20 from audit staff and 20 from operation/banking staff. Out of this number, only 303 questionnaires were completed and returned. The primary data collected through the

administration of questionnaires was analyzed using simple percentages and chi-square test (x^2), while the secondary data collected from the annual report and accounts of some of the sample banks was analyzed using spearman rank order correlation and t statistics.

Thus it was found that effectiveness or otherwise of internal control system can make or mar corporate survival of banks in Nigeria.

The research work concluded that internal control system is the responsibility of every body in an organization and as such every staff must be aware of his role in its process and fully engaged in it.

Finally it recommends that banks managements must put in place a sound approach to the selection of appropriate internal control practices and procedures, governed by a process of risk analysis and continuously monitor the overall effectiveness

of the internal control system to ensure that it is in conformity with the nature, complexity and risk run by the banks.

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CHAPTER ONE: INTRODUCTION

1.1 BACKGROUND OF THE STUDY

An organization's internal control system is comprised of the control environment, risk assessment, control procedures, monitoring, and information & communication system. It includes all the policies and procedures adopted by the directors and management of an entity to assist in achieving their objectives, ensuring, as far as practicable, the orderly and efficient conduct of their business, including adherence to internal policies, the safeguarding of assets, the prevention and detection of fraud and error, the accuracy and completeness of the accounting records, and the timely preparation of reliable financial information.

The control environment is an organization's overall attitude toward controls. It is the tone at the top. Risk assessment is the process of identifying the risks faced by an organization. Once these risks have been identified then specific control procedures can be designed and implemented to address them. Monitoring is important to ensure that controls are functioning as designed. And Management uses an organization's information and communication system to maintain the system of internal controls.

Every good system of internal control must be able to assist an organization carry on its business in an effective and efficient manner. It must be capable of sustaining credible adherence to management's policies, safeguard its assets, and be able to guarantee complete recording of all its

business transactions. A good system must exist to correlate responsibility with authority regarding the whole process of financial reporting and other spheres of the organization's activity (Hamid, 2004:6).

Internal control systems must be effective, particularly in banking organizations where their stock-in-trade is cash. Ineffective internal control systems can results to high financial losses to banking organizations and their customers, the depletion of shareholders' fund, as well as loss of confidence by the public. Similarly, fraud, which may result from ineffective internal control system, could in extreme cases lead to closure of banks as had happened in the country (Tanko, 2003:186). Owoh (2003:6) contends that weak internal control system renders an organization very soluble to fraud and corrupt practices. It encourages non-productive pursuits such as embezzlement, falsification of records and accounts, insider dealing, betrayal of fiduciary relationships, etc. The management of an organization has a duty to institute a system of internal control that will be appropriate to the enterprise. This will assist in preventing, or at least, substantially reducing the incidence, not only of mistakes, but also of irregularities and intentional errors, including fraud.

A system of effective controls is a critical component of a bank management and a foundation for safe and sound operation of banking organization. A system of strong internal controls can help to ensure that the goals and objectives of a banking organization will be met, that the bank will achieve long-term profitability targets, and maintain reliable financial and

managerial reporting. Such a system can also help to ensure that the bank will comply with laws and regulations as well as policies, plans, internal rules and procedures, and decrease the risk of unexpected losses or damage to the bank's reputation (Hamid, 2004:7).

This heightened interest in internal controls is, in part, a result of significant losses incurred by several banking organizations. An analysis of the problems related to these losses indicates that they could probably have been avoided had the banks maintained effective internal control systems. Such systems would have prevented or enabled earlier detection of the problems that led to the losses, thereby limiting damage to the banking organization (Hamid, 2004:6). Sound internal controls are therefore essential to the prudent operation of banks and to promoting stability in the financial system as a whole and ensuring corporate survival of banking organizations.

Internal control is a process effected by the board of directors, senior management and all levels of personnel. It is not solely a procedure or policy that is performed at a certain point in time, but rather it is continually operating at all levels within the bank. The board of directors and senior management are responsible for establishing the appropriate culture to facilitate an effective internal control process and for continuously monitoring its effectiveness: however, each individual within an organization must participate in the system. The exact application of internal control systems depends on the nature, complexity and risks of a bank's operations. The

main objective of internal control in banking organizations is to attain, operational, information and compliance objectives (Hamid, 2004:7).

Operational objectives of internal control pertain to the effectiveness and efficiency of the bank in using its assets and other resources in protecting the bank from loss. The internal control process seeks to ensure that personnel throughout the organization are working to achieve its objectives in a straight forward manner, without unintended or excessive cost or placing other interests (such as an employee's, vendor's or customer's interest before those of the bank).

Information objective of internal control address the preparation of timely, reliable reports needed for decision making within the banking organization. They also address the need for reliable annual accounts, other financial statements and other financial related disclosures, including those for regulatory reporting and other external uses. The information received by management, the board of directors, shareholders and supervisors should be of sufficient quality and integrity that recipient can rely on it in making decisions.

Compliance objectives of internal control ensure that all banking business is conducted in compliance with applicable laws and regulations, supervisory requirements and internal policies and procedures. This objective must be met in order to protect the bank's franchise and reputation, which are necessary for its survival.

In varying degrees, internal control is the responsibility of everyone in a bank. Almost all employees produce information used in the internal control system or take other actions needed to effect control. An essential element of a strong internal control system is the recognition by every employee of the need to carry out his responsibilities effectively and to communicate to the appropriate level of management any problems that may arise in operations, instances of non-compliance with the code of conduct, or other policy violations or illegal actions that are noticed.

Many internal control failures that resulted in significant losses for banks could have been substantially lessened or even avoided if the board and senior management of organizations had established strong control culture. Adamu (2004:3) contends that good internal control is necessary in ensuring the healthy survival and growth of any organization especially financial institution. Internal control is being put in place to achieve accountability, prudence and completeness. One common feature of all strong banks in the country is their common passion for controls. They do not compromise on them (Adamu, 2004:3). Adamu (2004:3) reported that available statistics has shown that all banks that have at one time or the other gone under have a weak internal control system in place. He argues that without weak internal control system there is no way that accounts could illegally be overdrawn, or be overdrawn with inadequate collaterals, or even be extended to a sector that is clearly under threat due to socio economic or other factors.

Banking is a dynamic, rapidly evolving industry. Banks must continually monitor and evaluate their internal control systems in light of changing internal and external conditions, and must enhance these systems as necessary to maintain their effectiveness and ensue their survival.

1.2 STATEMENT OF THE PROBLEM

The prevalence of fraudulent practices in the Nigerian banking industry has affected the franchise and reputation of many banking organizations over the years. During the period, February 1951 and May 1952, 18 indigenous banks were registered. All of them failed without any exception within a short period. The failure of these indigenous banks was as a result of lack of banking expertise and non-prudent lending policies (Olalusi, 1997:145). History has it that by 1952, a total of 25 banks closed their doors to depositors in Nigeria with consequent untold hardship for customers. There is a story of a customer of Farmers' Bank Limited who on finding that his bank had closed it doors indefinitely, suffered a heart attack and dropped dead by the bank premises (Abdullahi, 2002: 10).

Abdul Mutallab (2003:14) also reported that the operating licenses of thirty-six (36) banks were withdrawn between 1994 and March 2003, and many banks that were involved in foreign exchange malpractices were sanctioned. Abdullahi (2002:7) explained that in the year 2001, 723 cases of fraud and forgeries were reported in the Nigerian banking industry, out of which 388 were successfully executed representing 53.7%. The amount involved was ₦2.185 billion, while the actual loss totaled ₦1.07 billion, mainly

through defalcation of customers' cash lodgments by bank employees, substitution and depression of clearing cheques and manipulation of customers' accounts. NDIC reported that the banking sector recorded ₦12.9 billion fraud-related cases in 2002/2003 financial year, and CBN was reported to have said that there were 981 reported cases of fraud and forgery involving ₦5 billion, $5.25 million and 1,701.17 million Pound sterling respectively in 2002 (The New Age, 2003:29). Out of this number however, CBN said 428 cases resulted in losses of ₦1.40 billion and $153,000 to the banks while the other cases were nipped in the bud.

NDIC reported in its 2002 annual report that 16 out of the 90 licenced banks in operation failed to insure the deposits kept in their banks in violation of section 32 of the NDIC Act. No. 22 of 1988 (as amended) as at December 2002. NDIC also stated in its 2002 annual report that the level of compliance with the requirement of fidelity insurance coverage by the 74 insured banks was 82.2% as against 90% in 2001(The New Age, 2003:29). CBN annual report for 2002 also indicated that the December 2002 deadline fixed for meeting the new minimum paid-up capital for existing banks of ₦1 billion has expired with only 39 banks representing 43% of the 90 licenced banks meeting the requirement (Abdullahi 2002:8). Pressures to deliver reasonable returns to shareholders has pushed some bank's to take above normal risks, which has resulted in portfolio problems. Between 2001 and 2002, the Nigerian banking industry non-performing loans increased by 57% to ₦77 billion. Losses from fraud in the banking industry have remained high, and

are likely to increase further as merchant banks converting to commercial banks have limited experience in commercial banking and are vulnerable to operational errors and frauds. These trends and the growth of unsound banks in 2002 were indeed worrisome and made many Nigerians to fear the survival of the industry.

Is it that the internal control measures put in place by banks in Nigeria are not effective or the role of managements in ensuring strict compliance to internal control system is below expectation? To what extent does in-effective Internal control systems threatens corporate survival in the Nigerian banking industry? Can corporate survival be ensured by good internal control system? What are the implications of non-compliance by banks with statutory regulations (CAMA'90, BOFIA' 91, the Money Laundering Act of 1995, the Advance Fee Fraud & other fraud related offences Act 1995) and monetary circulars issued by the CBN on their internal control systems and corporate survival?

1.3 OBJECTIVES OF THE STUDY

One of the objectives of this research work is to determine the degree of relationship between ineffective internal controls system and fraud/forgeries of banks in Nigeria.

Another objective of the research work is to review the control environment in the Nigerian banking industry with a view to ascertain the overall attitude of the top-level management toward controls, the implications

of such attitude on fraud/forgeries and performing and non-performing loans/advances, with a view to make recommendations that will bring about enhanced control and ensure survival of banks in Nigeria.

The research work equally intends to examine the relationship between internal control systems and corporate survival in the Nigerian banking industry and the extent to which internal control systems can make or mar corporate survival.

It is also an objective of this research to examine the implications of non-compliance by banks with laid down procedures and the extent to which such can affect corporate survival.

Lastly, the causes and implications of fraudulent and unethical practices, breach of procedures and legislations, and collapse of banks in the Nigerian banking industry, will be examined. The research also intends to make appropriate recommendations, in an attempt to make a modest contribution to knowledge.

1.4 STATEMENT OF HYPOTHESES

The following hypotheses have been formulated for testing in this research work with a view to propounding possible explanations for the causes of the research problems or give some perceived relationships between certain variables or factors surrounding the problems. It is hoped that the result to be obtain from the testing of these hypotheses will help to

make appreciable contributions to the existing body of knowledge by providing solutions to the research problems.

HYPOTHESIS ONE

***H_0*:** There is no relationship between fraud/forgeries and ineffective internal control system of banks in Nigeria.

***H_A*:** There is relationship between fraud/forgeries and ineffective internal control system of banks in Nigeria.

HYPOTHESIS TWO

***H_0*:** Effective Internal control system does not help in the detection of fraud and other abuses in the banking industry.

***H_A*:** Effective Internal control system helps in the detection of fraud and other abuses in the banking industry.

HYPOTHESIS THREE

***H_0*:** Effective internal control system does not ensure compliance with laid down procedures in the banking industry.

***H_A*:** Effective internal control system ensures compliance with laid down procedures in the banking industry.

HYPOTHESIS FOUR

***H_0*:** Effective Internal control system does not ensure corporate survival of banks in Nigeria.

***H_A*:** Effective Internal control system ensures corporate survival of banks in Nigeria.

1.5 SIGNIFICANCE OF THE STUDY

This study is significant because of the immense contribution it will make to knowledge by examining and evaluating the internal controls system in the Nigerian Banking Industry with a view to determine whether or not the system is effective and the extent to which its effectiveness or otherwise can determine corporate survival of Banking Organizations in Nigeria.

This study would be of enormous benefit to banks Board of Directors, managements & employees, Shareholders & Depositors, Auditors (both external and internal), and the regulatory authorities in Nigeria.

Board of Directors of banks that have the responsibility for the preparation of financial statements, which give a true and fair view of the state of affairs of their Banks at the end of the financial year; that have to ensure that adequate internal control procedures are instituted to safeguard assets, prevent and detect frauds and other irregularities; that have to ensure that proper accounting records are maintained; that have to ensure that applicable accounting standards are adhered to; that have to ensure that suitable accounting policies are adopted and consistently applied; that have to ensure that judgments and estimates made in the financial statements are reasonable and prudent; that have to ensure that financial statements are prepared on the going concern basis (unless it is inappropriate to presume that the bank will continue in business); stand to benefit from the findings of this research. The Boards will benefit especially in the areas of knowing the effectiveness or otherwise of the internal controls system being operated by

them, and the degree to which those controls are adequate or inadequate to check excesses and frauds and ensure the attainment of desired objectives. It will also help them to know the correlation between internal control systems and corporate survival in the Nigerian Banking Industry. This will help them to ascertain the changes that are necessary to safe themselves and their Banks from being ruined and collapsed, ensuring the safety of depositors money and shareholders funds, and the corporate survival of their Banks.

Management & employees, who are involved in the day-to-day management of banks in Nigeria, would also benefit from the findings of this study; especially on knowing fully the roles expected of them in the internal controls system, as the Basel committee report of 1998, recommends for the involvement of all and sundry.

Shareholders and Depositors, who have interest, would also benefit from the findings of this research; especially on knowing the safety of their shareholdings and deposits in the Nigerian banking industry. The findings of the research will also help shareholders in deciding the caliber of people to be elected as their representatives in Boards of banks, as directors, who will ensure effective internal controls system that would guarantee the safety of their investments.

Auditors (both external and internal) would also benefit from this study, especially by knowing the extent of effectiveness or otherwise of the internal controls system in the Nigerian banking industry. This could help

them in determining the level of audit work expected of them in the discharge of their responsibilities in the industry.

The regulatory authorities like the Central Bank of Nigeria, Nigerian Deposit Insurance Corporation, the Securities and Exchange Commission, the Nigerian Stock Exchange and the Nigerian Capital Market, would all benefit from this study. There is no doubt that the findings of this research will assist them in their regulatory activities of the Nigerian Banking Industry.

The result of the study would make a good library material for researchers on internal control systems in corporate organizations.

1.6 SCOPE OF THE STUDY

This study is meant to examine the correlation between internal control systems and corporate survival in the Nigerian Banking industry. The study attempted an analytical review of the current internal control practices in the Nigerian Banking Industry. In this regard focus was made on all the various aspects of an internal controls system, and other conceptual framework for internal control systems and corporate survival.

The scope of this study is restricted to seven out of 28 banks that are quoted on the floor of the Nigeria Stock Exchange (as 1st Tier Securities) - as at 22/08/2003. The seven banks were selected using a systematic sampling technique from the 28 banks. These banks are: Access Bank Nigeria PLC., Co-operative Development Bank PLC., First Bank of Nigeria PLC., Hallmark

Bank PLC., Liberty Bank PLC., Omega Bank PLC and United Bank For Africa PLC. Our respondents were therefore drawn from these banks.

The study covered a period of ten years, from 1994 to 2003.

1.7 LIMITATIONS OF THE STUDY

The following are some of the limitations encountered in this research work:

(i) The researcher was unable to collect all the questionnaires administered on the respondents. This was as a result of the inability of some of the respondents to complete and return their questionnaires due to their numerous banking schedules.

(ii) Some of the targeted respondents do not seem to have understood the essence of the study, thus they suspected it to be a sort of spying by the regulatory authorities. This scares some of them away from completing and returning the questionnaires administered on them.

The researcher took appropriate measures to motivate the respondents to accept the reasons why questionnaires were administered on them. This encouraged some of them to complete and return their questionnaires. Enough time was also given to them to enable them complete the questionnaires at their own convenience. The researcher is therefore of the opinion that these limitations would not in any way affect the validity of the research findings.

1.8 DEFINITION OF KEY TERMS

Below are the definitions of the major terms as used in this research work:

[a] Bank: A bank is a company incorporated by the corporate Affairs Commission and licensed by the central bank of Nigeria to carry on the business of collecting and repaying deposits into various types of accounts and the granting of money loans and overdrafts to its customers. With the inception of Universal Banking in Nigeria, banks now act as financial supermarkets by offering wide range of financial services.

[b] Basel Committee: The Basle Committee on Banking Supervision is a committee of banking supervisory authorities, which was established by the central bank Governors of the group of ten countries in 1975, consisting of senior representatives of bank supervisory authorities and central banks from Belgium, Canada, France, Germany, Italy, Japan, Luxembourg, Netherlands, Sweden, Switzerland, United Kingdom and the United States.

[c] Corporation: This refers to limited liability companies, which are artificial beings, intangible, invisible, that can own property, enter in to a contract, and sue and be sued. This includes both private limited liability companies (LTD.) and public limited liability companies (PLC).

[d] COSO Reports: These are reports issued by the National Commission on Fraudulent Financial Reporting (better known as the Tread way Commission) to guard against financial reporting scandals which started during the 1980s.

[e] Customer: to be a customer of a bank, the law has it that one has to have an account opened in his own name and money lodged into it.

[f] Distress: This refers to financial difficulties facing a corporate entity and its subsequent inability to transact business as expected.

[g] Information Technology: The term "information technology" or IT, encompasses hardware and software products, information system operations and management processes, and the skills required to apply those products and processes to the task of information production and information system development, management and control.

[h]Internal Control System: Internal control is defined as a process, affected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories: effectiveness and efficiency of operations, reliability of financial reporting, and compliance with laws and regulations.

[i] Investors: These are individuals, institutions or corporate entities who have subscribed to the share capital of a company with a view to getting returns in the form of dividend (cash or stock or both), or with a view to capital appreciation of their investment.

[j] Management information System (MIS): This is a system using standardized procedures to provide management at all levels and in all functions with relevant information to enable management take timely and effective decisions.

[k]Nigerian capital Market: This is the market that allows companies, government and other institutions to raise capital and debt in Nigeria.

[l]Nigerian Deposit Insurance Corporation (NDIC): This is the authority that insures small deposits up to a maximum of N50, 000.0 in the Nigerian banking industry. It also issues and withdraws license of banking organizations in Nigeria.

[m]Nigerian Stock Exchange (NSE): This is the place for the actual trading of shares and Securities. It regulates and over see all share and securities deals in the country.

[n]Non-performing Loan: A credit facility is referred to non-performing, when the principal and interest is due and remain unpaid for ninety (90) days or more.

[o]Performing Loan: A credit facility is deemed to be performing if payment of both the principal and interest are up to date in accordance with the agreed terms.

[p] Publicly Quoted Banks: These are banks whose shares are quoted (traded) on the floor of the Nigerian stock exchange.

[q] Shares: This can be defined as interest in a company expressed in monetary terms.

[r] Shareholder: This refers to someone who holds shares in a company.

[s] Securities and Exchange Commission (SEC): This is the apex institution in the Nigerian capital market. It regulates activities in the entire capital market.

[t] Stock Exchange Market: This is the primary capital market in which companies, government and other institutions raise funds by issuing either shares, debentures or other securities like geld edge. But it is more important as a secondary market for buying and selling existing securities.

[u] Survival: This is the ability to achieve desired objectives and continue as a going concern.

[v] System: A system is an assembly of components connected in an organized way. The components are affected by being in the system and the behavior of the system is changed if they leave it. This organized assembly does something and has been identified as of particular interest.

[w] Winding Up: This refers to the legal termination of a business.

1.9 PLAN OF THE STUDY

This work is made up of five chapters as follows:

Chapter One: Chapter one, which is this chapter, warms up the topic as clearly and precisely as possible. It explained the background of the study, problems statement, objectives(s) settings, scope description, hypotheses, justifications statement, limitations and delimitations of the study and definition of unfamiliar terms used in the study.

Chapter Two: This chapter is about the literature review. Here all relevant works would be tactfully reviewed, concentrating on the findings and recommendations of the authors of the works and expressing opinion(s) more especially, the recommendations. Relevant textbooks, journals, magazines and newspapers will be reviewed here.

Chapter Three: The method used in conducting the research will be clearly and honestly explained here. The population of the study, the sampling technique, sample size, methods of data collection, method of editing and tabulation of data, method of data analysis and interpretation will all be explained here.

Chapter Four: This chapter is about analysis and interpretation of data collected through the administration of research instruments and secondary data collected from the annual report and accounts of the selected banks. Hypotheses of the study will also be tested using the results obtained from the data analysis to confirm or disconfirm them.

Chapter Five: The study is to be concluded here by highlighting the major findings of the work. Conclusions will be drawn based on the findings and recommendations for improvement/betterment or correction of lapses shall be made accordingly.

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CHAPTER TWO: LITERATURE REVIEW

2.1 INTRODUCTION

This chapter deals with the review of related literature on internal controls system and the correlation between effectiveness of internal controls system and corporate survival in the Nigerian banking industry. This chapter serves as the bedrock for the final analysis and conclusions that are to be drawn from the study. The chapter reviews literature on the concept of internal control system, framework for the evaluation of internal controls system in the banking industry, the objectives of internal control framework, internal control and the role of the auditors, corporate survival in the Nigerian Banking industry, the Banking industry in Nigeria and the Nigerian Stock Exchange.

2.2 THE CONCEPT OF INTERNAL CONTROL

A system of internal control consists of policies and procedures designed to provide management with reasonable assurance that the company would achieve its goals and objectives. These policies and procedures are often called controls, and collectively they comprise the entity's internal control. The operational standard practices committee of the UK defined internal control as the whole system of controls, financial and otherwise, established by the management in order to carry on the business of the 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 the records (IAG6). Dandago (2003) observes that the Internal Auditing Guidelines' (IAG6) definition can be summarized briefly as the entire control measures which the management puts in place to make sure that all aspects of the organization: finance, assets, records, etc. are effectively monitored and managed for the achievement of organizational objectives. He went further to say that these controls are set up to ensure that the possibility of fraud or error and all kinds of material defects and irregularities are prevented or substantially reduced. Hence, the overview of internal control centers around the various procedures to be followed in order to make an organization effective and put it on course for the achievement of its immediate and remote objectives.

Similarly, Woolf (1985) observes that the striking thing about the definition is it's all- embracing nature and it is clear that internal control is concerned with the control operative in every area of corporate activity, as well as with the way in which individual controls inter-relate. Extending the comment further, one can posit that internal control in organization should comprise of all types of control measures i.e. both financial and non-financial, record and non-record related, which must be working harmoniously to ensure the attainment of organizational objectives and the safeguarding of resources.

Agbelusi (1986) defines internal control as a plan of organization with methods and measures adopted within a business to: safeguard the assets of the organization; check the accuracy and reliability of the accounting data;

encourage employees to adhere to procedures set up by employers. Awoyemi (1989) defines internal control as the plan of an organization procedure and equipment used in a business to protect its assets from improper use and to promote efficiency in operations. He outlined some strategies, which are involved in the internal control system of an organization. They include: Segregation of duties; authorization; personnel; organization/management; arithmetical and accounting; and supervision. Oshisami (1992) observes that internal control involves the whole system of controls, financial and otherwise, established by the management to assist it in carrying out its functions in an orderly manner, safeguard its assets, secure as far as possible the accuracy and reliability of its records, promote operational efficiency and encourage adherence to policies.

The Coso Report (1992) defines internal control as a process effected by the entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories: effectiveness and efficiency of operations; reliability of financial reporting; and compliance with applicable laws and regulations.

From the diversity of these definitions, the term internal control refers to any combination of measures, policies and procedures that the management of an organization adopts in order to ensure that the assets of such organization are duly protected and that all operations are carried out in the

most efficient manner. These measures are adopted to enhance the realization of organizational objectives.

2.2.1 Components Of Internal Control

Various studies in the literature have discussed extensively what are believed to be components of internal control systems. Woolf (1985), for instance, identifies the following three essential components of internal control systems:

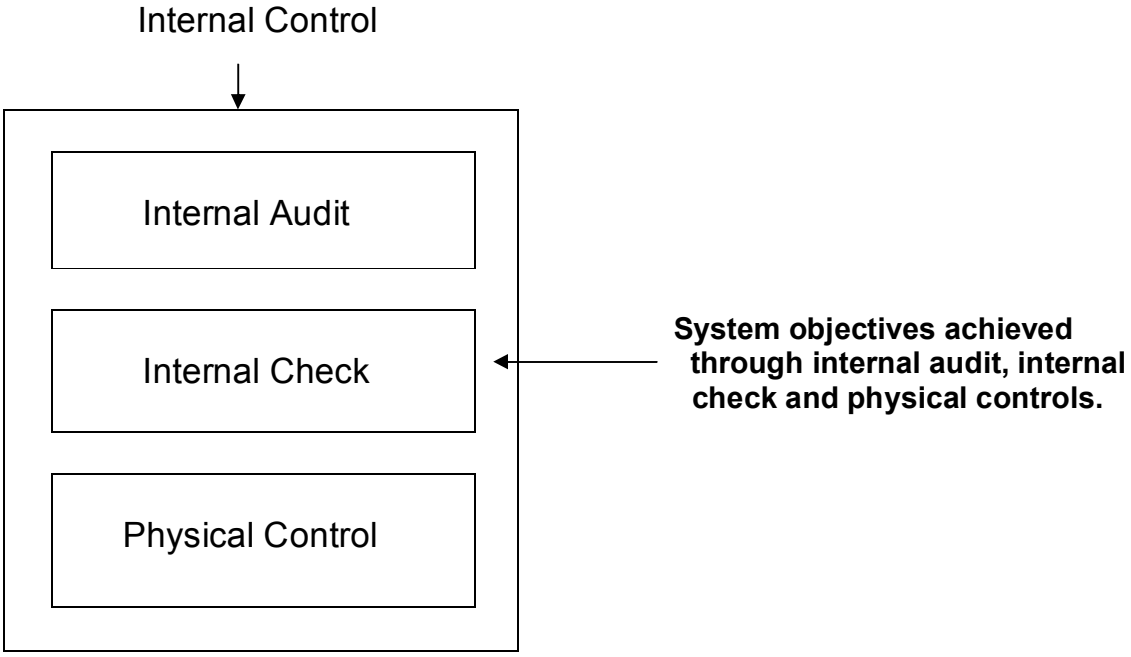
(i) Internal Audit

(ii) Internal Check, and

(iii) Physical Controls

This suggest that the overall objective of achieving good internal control is obtainable through **(a)** regular and effective internal audit **(b)** provision of good internal checks or simply the use of checks and balances in all functions and operations; and **(c)** the use of physical measures such as lucks and safes where necessary to guarantee the safeguard of assets. Fig. 2.1 is used to depict the relationship between internal control, internal audit, internal check and physical controls.

Fig. 2.1 ***Composition of Internal Control System***



Source: *Damagum (2003:6)*

On the other hand Arens *et al* (1999) identify five inter-related components of internal control that are integrated within the management process: Control environment; risk assessment; control activities; Information and communication; and monitoring.

2.2.2 The Internal Control Environment

Internal control covers all methods, procedures and arrangements adopted within an organization to ensure as far as possible the safeguarding of assets, the completeness, accuracy and reliability of accounting records and the promotion of operational efficiency and adherence to management policies. Management should introduce appropriate controls to prevents, or at least substantially reduce the incidence, not only of mistakes but also of irregularities and intentional errors, including frauds.

Helmkamp *et al* (1985) observe that there are two types of internal control measures that are used by a business: administrative controls and accounting controls. Administrative controls are used to maintain an efficient operation and ensure adherence to prescribed company policies. Accounting controls on the other hand, are the methods used to protect assets and ensure that accounting information is reliable. They include procedures used to authorize various business transactions to separate record keeping duties from the custody of a firm's assets. Ouch (1989) is of the view that controls are basically two, behavioral controls and output controls, thus controls relates to ability to measure results. Hence accounting controls means perfect knowledge of the transformation process with high propensity to measure outputs. Dandago (2003) contends that the following are the types of control that are to be put in place in any organization (public or private):

(i) Organizational Control

Every organization should have an organization chart, which should adequately define and allocate responsibilities; each function specified by the chart must be under a specific person who is to be seen as the responsible officer. When authorities are delegated, responsibilities must be clearly specified.

(ii) Segregation of Duties

This is a general term, which means separation of duties. Duties normally segregated are those of custody, recording, authorization/approval and execution.

(iii) Physical Control

This is about custody of assets and it involves procedures and security measures designed to ensure that access to assets (both current and fixed) is limited to authorize persons only. This control is specifically important in the case of valuable, portable, exchangeable or desirable assets.

(iv) Personnel Control

Procedures should be designed to ensure that personnel operating a system are competent and motivated to carry out tasks assigned to them. The recruitment system must give premium to skills, qualification and competence. Good remuneration system should be put in place and provision for training and retraining of personnel should be made. All these would make this control effective, he describes personnel control as the most important control in terms of prevention of fraud and irregularities.

(v) Supervision Control

There should be an upward reporting and downward supervision. The span of control should be clearly defined for effective supervision.

(vi) Management Control

These are controls exercised by the management, which are outside the day-to-day activities of the organization. Cost and management accounting systems, auditing systems, etc. are part of this control.

(vii) Authorization and Approval

This requires that all transactions should be authorized or approved by an appropriate person. The maximum amount of expenditure to be incurred by officers and bodies/committees at various levels should be clearly spelt- out.

(viii) Arithmetical and Accounting Control

This control requires that an effective bookkeeping and accounting system needs to be put in place.

Millichamp (2000) describes control environment to mean the overall attitude, awareness and actions of directors and management regarding internal controls and their importance in the entity. The control environment encompasses the management style, and corporate culture and values shared by all employees. Aren et al (1999) explain that because economic, industry, regulatory, and operating conditions constantly change, management is challenged with developing mechanisms to identify and deal with risks associated with change bearing in mind that internal control under ones set of conditions will not necessarily be effective under another.

Sabari (2003) contends that control activities (also called control procedures) are those policies and procedures in addition to the control environment and the information system that management establishes to provide reasonable assurance that their objectives are achieved. They include in particular procedures designed to prevent or detect and correct errors. John *et al* (1987) opine that control activities are generally established

over: authorization and execution of transactions; segregation of duties; the design and use of documents and records; access to assets and records; and, independent checks on performance.

Sabari (2003) found that to operate effectively and efficiently, an entity needs to identify, capture, and communicate both external and internal information in a form and time frame that enables people to discharge their assigned responsibilities. Information and Communication has to do with identifying, assembling, classifying, analyzing, recording, and reporting the entity's transactions and maintaining accountability for related assets. Arens et al (1999) observe that for accounting system to be effective, it should: Include methods and records that will identify all valid transactions; record transactions in the proper accounting period; and, describe transactions on a timely basis and in sufficient detail to permit proper classification, to measure the transaction properly, and present summarized transactions and related disclosures accurately in the financial statements.

According to Ricchiute (2002), the auditor's objective in considering an entity's accounting system is to obtain an understanding of: major classes of transactions; how transactions are initiated; the records, documents, and accounts used in the processing and reporting transactions; the processing of transactions; and, financial reporting procedures. Monitoring activities deal with on going or periodic assessment of the quality of internal control performance by management to determine that controls are operating as intended and that they are modified as appropriate for change in conditions.

Information for assessment and modification comes from a variety of sources, including, studies of existing internal controls, internal audit reports, reports by regulators such as regulatory agencies, complaints from customers etc.

Millichamp (2000) argues that the controls must not operate in isolation but in absolute harmony if the overall corporate objective is to be achieved. By way of examples the same author provided a good number of internal control measures in various areas of business operation. Over cash balances he suggested the following;

(i) Appointment of officials responsible for each cash balance

(ii) Establishment of cash floats of specified amounts and locations.

(iii) Arrangement of security measures including the use of safes and restriction of access.

(iv) Imprest with rules on re-imbursement only against authorized vouchers.

(v) Strict rules on the authorization of cash payments.

(vi) Independent cash counts on regular and surprised basis.

(vii) Insurance arrangements e.g. for cash balances and fidelity guarantee.

(viii) Special rules for IOUs, preferably these should not be permitted.

2.2.3 Designing of Internal Control

It has been observed that internal control can differ from one organization to another and even within different sections of same

organization. In view of this, the designing of any internal control system will inter-alia depend on the size and nature of an organization, operations, the geographical spread of its coverage and the financial significance of recorded transactions. Towards a good guide to internal control designing, some authors provides that good internal control should possess the following characteristics (Damagum: 2003):

(i) Well-defined areas of responsibility and authority adapted to the organization's operations and the qualifications of the operatives.

(ii) Well-established work routine.

(iii) Division of responsibilities and duties in such a way that significant errors or irregularities cannot go undetected without at least two people acting incorrectly; and

(iv) A systematically built-up accounting system, specifically adapted to the organization's operations and structure as well as the existing external auditing requirements in general.

What seems to emanate from these provisions is that good internal controls are only tenable where organizations have well defined structures with clear lines of responsibility, control and authority fully stated. Similarly, an adequate number of personnel with requisite qualifications (not only academic but personal) must be on ground and also a well-structured accounting or record keeping system. In terms of the actual internal control structure, it is required to provide checks and balances whereby one

individual in the normal course of his duties automatically checks the work of one individual.

2.2.4 Characteristics of a Good Internal Control System

The system controls is integrative the whole system being more than the parts. Controls are sustained through the financial process by the use of control accounts and/or through the other mediums, which could relate to physical restriction of access to the organization's assets or liabilities (Owoh, 2003). Internal controls could be a creation of management by its own accounting personnel, or through the use of external consultants or external auditors who may be required to act as financial and administrative advisers.

Every system of internal control must be able to assist the organization carry on its business in an effective and efficient manner, it must be capable of sustaining credible adherence to management's polices, safeguard its assets, and be able to guarantee complete recording of all transactions. In doing this, the transactions thus recorded must have the potency of substantial reliability. A good system must exist to correlate responsibility with authority regarding the whole process of financial reporting and other spheres of the organization's activity. For effectiveness and efficiency, there must be a well-defined concept of the organization. Each human resource component of the organization must operate within a defined reporting framework in manner that clearly specifies the due lines of delegation of authority and responsibility. Owoh (2003) suggests that the organization structure must be constructed in such a manner that guarantees that no one person conceives,

initiates, processes, analyses, and takes custody *(CIPAC)* of a complete transaction. Financial transactions would operate within a continuum having a considerable chain of executing persons, each well trained and skilled enough to execute only a fragment of the entire *CIPAC* cycle. The *CIPAC* cycle is known as the segregation of duties constituents of internal controls.

The *CIPAC* cycle complements the ubiquitous roles that ensures physical security of the assets, authorizations, adequacy of arithmetic and accounting procedures, due personnel operating system, completeness of supervision and consistent promotion of the management idea, *SAAPSM*. There must be a competitive process of acknowledgement of responsibility by ensuring that all persons involved in the execution of accounting operations attest to the operations executed by them by appending their signatures, initials, rubbers stamps, statements of commitments to input and output particulars containing such operations. In resource allocation, due diligence and budget discipline and budgetary controls must be emphasized. This internal control component, acknowledgement of performance of an operation and budget *(PB),* thus provides a comprehensive framework of structures that helps to stabilize uncertainties.

Thus, a simple model for a good internal control system is specified as follows:

IC=CIPAC + SAAPSM + PB

Where:

IC=**I**nternal **C**ontrol

CIPAC= Conceive, **I**nitiate, **P**rocessed, **A**nalyzed, and take **C**ustody

SAAPSM= Physical **s**ecurity of the assets, **A**uthorizations, **A**dequacy of arithmetic and accounting procedures, due **P**ersonnel operating system, completeness of **S**upervision and consistent promotion of the **M**anagement ideas.

PB= acknowledgement of **P**erformance of an operation *(P)* and **B**udget *(B)*

Owoh (2003) argues that this simple model accords with the proposition of eminent scholars of management and accounting processes. For instance, the classic definition of Anthony (1985) insists that 'controls' should be understood as management driven. Thus, controls refer to the efficient utilization of the organization's resources towards achieving its objectives. Though Anthony (1985), did not explain the sense in which organization establish objectives and procedures they employ in classifying them. According to Machin (1993), accounting controls are the hallmark of management controls. In the words of Otlet and Berry (1980), control is dynamic, therefore requiring the existence of cybernetic model that must correlate with predictive model to properly situate relative control phenomena in context. Control is central to organizations "threat-avoiding" quest, (Vickers: 1987).

2.2.5 Elements of Internal Control Systems

To ensure effectiveness of internal control systems, the following elements have to be provided for (Damagum, 2003):

(i) Proper documentation and classification

(ii) Recording of transactions

(iii) Authorization

(iv) Separation of duties

(v) Supervision

(vi) Restrictions of access to resources and records

Proper Documentation and classification: is necessary to provide reasonable assurance that all transactions and significant events are properly recorded. By this token, it is another way of suggesting that to have good internal control in place, there has to be an evidence of good accounting system. The existence of good accounting systems guarantees the tracing of events or transactions from inception to completion. Proper Recording of Procedures is also necessary if transactions and events are to be fully accounted for. For this reason, all good internal control systems must provide for proper, accurate and timely recording of transactions.

Authorization Procedure is another element, which is provided to guarantee that only valid transactions are processed through a given system. It is equally required that authorization procedures be fully communicated to all appropriate personnel to avoid possible mistakes of judgments. Separation of duties: this is usually provided in all sensitive areas to prevent any significant errors or irregularities going undetected.

Supervision; this is equally necessary to ensure prompt checking of employees on the job, particularly those that have to do with key aspects of an internal control system. It is for this reason that cahiers are always supervised or checked by senior officers possibly on regular basis.

Restriction of access: is equally necessary to guarantee that access to documents and resources is restricted to authorized personnel only. This goes to strengthen internal control system and provide proper safeguard over assets. Restriction of access to documents and records can best be achieved through the following (Damagum: 2003):

(i) Keeping them locked in safes.

(ii) Assigning a sequential number to each document: and

(iii) Assigning custodial accountability to responsible individuals.

The elements of control are essential in every organization, although the emphasis may depend upon the size of the organization.

Tanko (2003) in his own part opines that the following are the elements of control that are essential in every organization:

(a) Responsibilities Of Board Of Directors

The directors of any bank are responsible for the preparation of financial statements, which give a true and fair view of the state of affairs of the bank at the year end of each financial year and of the profit or loss for that year and comply with the provisions of the Companies And Allied Matters Act 1990 and Banks And Other Financial Institutions Act, 1991, in doing so they ensure that:

[i] Adequate internal control procedures are instituted to safeguard the assets, prevent and detect frauds and other irregularities'

[ii] Proper accounting records are maintained;

[iii] Applicable accounting standards are adhered to;

[iv] Suitable accounting policies are adopted and consistently applied;

[v] Judgments and estimates made are reasonable and prudent;

[vi] The financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

(b) Organizational Structure

Defines areas of responsibility, limits of authority, lines of reporting. Centralized versus decentralized organizational structure. Designed to support the goals of the organization by establishing relationships amongst people and activities in order to facilitate decision-making and preserve accountability.

(c) Management Attitudes, Philosophy and Operating Style

(i) Exert a great deal of influence on internal control.

(ii) Attitudes of top management permeate the organizational culture

(iii) Management's view of the importance of business ethics

(iv) Management's expectation of quality of work and performance.

(d) Management Control Mechanism

Methods adopted for controlling organizational activities and assessing performance of employees can have an important impact on the achievements of a strong control environment. This include budgeting, standards, responsibility accounting etc.

(e) Personnel Policies And Practices

(i) Ensuring compliance with organizational policies.

(ii) Corporate codes of conduct (general principles and specific practices e.g. behaviour towards other employees).

(iii) Enforcement Mechanisms.

(f) Audit Committee

This is the communication link between internal and external auditors and the Board of Directors. Responsibilities include ensuring that effective internal control structure is maintained for investigating fraud.

(g) Internal Audit Responsibilities

Internal audit assist management to discharge its responsibilities. It also ensures: the adequacy and effectiveness of the internal control structure, the reliability and integrity of the financial and operating data, the efficient use of the organization's resource, the prevention and detection fraud.

2.2.6 Benefits of Good Internal Control System

Owoh (2003) argues that good internal control system helps the organization to ensure adequate custody of its assets, proper measurement of liability, maximization of gains/profits or minimization of losses, and sustenance of an output driven work force.

Adequate custody of assets is achieved by:

i. Ensuring the physical existence of the asset;

ii. Confirming and ensuring adequate security of legal and other evidence of existence of the asset(s);

iii. Evidence that processes were concluded to ensure that the valuation of the asset is reliable and complete;

iv. Evidence that the asset is well protected from unauthorized removals or expropriations; and evidence that the non-cash assets are kept and maintained in a manner that makes it market- receptive through competitiveness.

Proper measurement of liabilities are maintained by:

i. Creating a system that serves to promote a process that ensures that the initiation of the commitment of the liability is properly authorized and in line with management policy;

ii. Monitoring a system that ensures that the value for which the liability is incurred, was actually received;

iii. Monitoring system that would sustain evidence that valuation of the liability is competitive and least-cost based;

iv. That neither of the parties could alter the terms of a subsisting liability without due mutual process; that

v. Legally acceptable evidence exists to sustain all levels of liability as measured (statutory compliance in reporting).

A system of profit maximization and loss minimization according to Owoh (2003) relates to the process of maintaining a system that ensures that:

ii. All procurement are carried out in the most transparent manner e.g. buying at least cost possible given a level of quality and quantity;

iii. Attempts are encouraged to ensure prompt compliance with statutory provisions, accounting standards and pronouncement of relevant government agencies, regulatory and professional bodies, etc.

iv. Decision-accounting process are integrated into the management information system so as to make the organization enjoy the benefit of on-line assessment of its policies and decisions;

v. Rewards cost-savings, ingenuity, and innovations in production, marketing, and systems documentation.

Out-put driven work force is maintained by the system that satisfies itself that:

I. Adequate organization assessment is made to discover the areas and caliber of human resources needs within the organization;

II. The gaps so identified are sourced with great tact with respect to cost and sustainability;

III. A viable system exists for the purpose of measuring the output of each employee.

IV. Reward system is based on productivity and honesty; and that

V. There is a well-defined mode of entry, operation and exit.

2.2.7 **Characteristics of an Effective Internal Control System**

Owoh (2003) contends that effective internal control system that should be able to prevent and detect fraud must posses the following characteristics:

i. Character of Human Resources:

Even though the primary audit objective is no longer that of detection of fraud, fraud is detected if the auditor applies full professional skill and detail in discharging his assignment. Conscientious application of technical audit procedures of depth checks, substantive testing, compliance testing for instance, are equipped to detect fraud when they have occurred. The knowledge that auditors would apply these techniques serves as a moral check on the organization. To achieve this, auditors must be men of integrity, independent and objective. Their interests must not conflict with that of the organization. They must not be prone to accepting gifts from clients or clients' employees, and must not engage in trade union activities. Information obtained from clients' office must not be used for personal gains, and all published information about the client must conform to the minimum standards. It is also suggested that for effective internal control purposes, that auditors should not engage in share dealings in their client company. On the part of management, there must be present in them, the professional will to be of high integrity to avoid management induced collusion and false control.

ii. According to Vickers (1987), any control tool whether internal or external, must be **time-compliant,** internal control systems and procedures must target at the financial operating system without excessive time slippages. Fraud is time-sensitive. Almost all forms of fraud are detectable over time, but not all fraud could be prevented without swift

and timely internal control system intervention. Time is critical in ensuring the effectiveness of internal control in fraud prevention and detection. Between the time for internal control and its implementation, adequate space horizon must exist to forestall due feasible region so that implementation would permit reaction. This scenario has the potency of activating proactive operations.

iii. Reliability of Control Mechanism

Management must ensure that its internal control procedures are concrete, with inbuilt impersonal systems approach. Internal controls must be contingent on both internal and external pressures that might infest an organization. The controls so established must be able to feel the pulse of the environment.

iv. Measurability of Internal Controls Variables

It is advised that internal control system must have the potency of being measurable to ensure its constant review. Ouch (1989), views measurability as very critical to the efficiency of internal control. Constant measurement and evaluation of internal control system serves to check management' disposition towards "biasing" Lowe & Shaw (1988) 'smoothing', Birnberg & Turopolec (1992), " focusing", Kaplan (1996), "gaming" Birnberg & Turopolec (1992), "filtering", Feldman & March (1981) "illegal acts", Dalton (1959). Measurability of internal control process makes it possible for early isolation of deviating constituents and output of the mechanism.

v. Structure Based Accounting System

There must be a well-defined organization structure with chains of command and authority levels clearly delineated. A consistent and organization based communication system would enable the system sustain a reliable information and feedback system, eliminating systems' noise completely, or at least monitoring the lowest level of its impact on the organization. The system of accounting must be clear, consistent and sustainable. Since accounting controls connotes the entire control system of the organization, (financial or otherwise), the accounting system must be all embracing, cutting through all strata of the organization.

All accounting and allied-roles within the organization must work through a chain of integrated operation. All operations, be it administrative or accounting, must be well documented, (either electronic or manual), and must of essence, be traceable from the beginning to the end. Trail of activities and operations must be achieved without any break of flow and sequence.

2.2.8 The Effects of Weak Internal Control System

Weak or ineffective internal control system as argues by Owoh (2003) lead to the falsification of financial information, concealing fraud and defalcations. Tam (2002) explains that internal control failures could be disastrous. In 1995, Baring Bank (in England) suffered from $1.3 billion loss and collapsed subsequently. The bank's downfall was brought about by its trader- Nick Leeson- who committed the Bank to highly speculative derivative

transactions. Apparently, there was no internal control to monitor Lesson's activities. Baring's management was unaware of Leeson persistently acting beyond his authority. In its investigation of Baring's collapse, the Bank of England attributed Leeson's unauthorized trading activities to the absence of effective internal controls. A satisfactory level of internal control could have mitigated such an opportunity.

Basel Committee Report as reported by Collins (2000) and Dimistris (2002) describes the following lessons that can be learned from internal control failures in a banking organization.

[A] <u>Management Oversight and the Control Culture</u>

1. Many internal control failures that resulted in significant losses for banks could have been substantially lessened or even avoided if the board and senior management of the organizations had established strong control cultures. Weak control cultures often had two common elements. First, senior management failed to emphasize the importance of a strong system of internal control through their words and actions, and most importantly, through the criteria used to determine compensation and promotion. Second, senior management failed to ensure that the organizational structure and managerial accountabilities were well defined. For example, senior management failed to require adequate supervision of key decision-makers and reporting of the nature and conduct of business activities in a timely manner.

2. Senior management may weaken the control culture by promoting and rewarding managers who are successful in generating profits but fail to implement internal control policies or address problems identified by internal audit. Such actions send a message to others in the organization that internal control is considered secondary to other goals in the organization, and thus diminish the commitment to and quality of the control culture.

3. Some banks with control problems had organizational structures in which accountabilities were not clearly defined. As a result, a division of the bank was not directly accountable to anyone in senior management. This meant that no senior manager monitored the performance of these activities closely enough to notice unusual activities, financial and otherwise, and no senior manager had a comprehensive understanding of the operations and how profits were being generated. If management had understood the operations of the division, they may have been able to recognize warning signs (such as an unusual relationship of profit to levels of risk), investigate the operations and take steps to reduce the eventual losses. These problems could also have been avoided if line management had reviewed transactions and management information reports and held discussions with appropriate personnel about the nature of business transacted. Such approaches provide line management with an objective look at how decisions are being made and ensure that key personnel are operating within the parameters set by the bank and within the internal control framework.

[B] Risk Assessment

4. In the recent past, inadequate risk assessment has contributed to some organizations' internal control problems and related losses. In some cases, the potential high yields associated with certain loans, investments, and derivative instruments distracted management from the need to thoroughly assess the risks associated with the transactions and devote sufficient resources to the continual monitoring and review of risk exposures. Losses have also been caused when management has failed to update the risk assessment process as the organization's operating environment changed. For example, as more complex or sophisticated products within a business line are developed, internal controls may not be enhanced to address the more complex products. A second example involves entry into a new business activity without a full, objective assessment of the risks involved. Without this reassessment of risks, the system of internal control may not appropriately address the risks in the new business.

5. As discussed above, banking organizations will set objectives for operational efficiency and effectiveness, reliability in financial reporting and compliance with laws and regulations. Risk assessment entails the identification and evaluation of the risks involved in meeting those objectives. This process helps to ensure that the bank's internal controls are consistent with the nature, complexity and risk of the bank's on- and off-balance sheet activities.

[C]. Control Activities

6. In reviewing major banking losses caused by poor internal control, supervisors typically find that these banks failed to observe certain key internal control principles. Banks that experienced significant losses from internal control problems, most frequently overlooked one of the pillars of sound internal controls system that is segregation of duties. Often, senior management assigned a highly regarded individual responsibility for supervising two or more areas with conflicting interests. For example, in several cases, one individual supervised both the front and back offices of a trading desk. This permitted the individual to control transaction initiation (e.g., buying and selling securities or derivatives) as well as the related bookkeeping function. Assigning such conflicting duties to one individual gives that person the ability to manipulate financial data for personal gain or to conceal losses.

7. Segregation of duties is not limited to situations involving simultaneous front and back office control by one individual. It can also result in serious problems when an individual has responsibility for:

- Approval of the disbursement of funds and the actual disbursement;
- Customer and proprietary accounts;
- Transactions in both the "banking" and "trading" books;
- Informally providing information to customers about their positions while marketing to the same customers;

- Assessing the adequacy of loan documentation and monitoring the borrower after loan origination; and
- Any other areas where significant conflicts of interest emerge and are not mitigated by other factors.

8. Shortcomings in control activities, however, reflect the failure of a variety of efforts to determine that business is being conducted in the expected manner, from high-level reviews to maintenance of specific checks and balances in a business process. For example, in several cases management did not appropriately respond to information they were receiving. This information took the form of periodic reports on the results of operations for all divisions of the organization that informed management of each division's progress in meeting objectives, and allowed them to ask questions if the results were different from their expectations. Often, the divisions that later reported significant losses at first reported profits--far in excess of expectations for the apparent level of risk--that should have concerned senior management. Had thorough top level reviews occurred, senior management may have investigated the anomalous results and found and addressed some of the problems, thus limiting or preventing the losses that occurred. However, because the deviations from their expectations were positive (i.e., profits), questions were not asked and investigations were not started until the problems had grown to unmanageable proportions.

D. Information and Communication

9. Some banks have experienced losses because information in the organization was not reliable or complete and because communication within the organization was not effective. Financial information may be misreported internally; incorrect data series from outside sources may be used to value financial positions; and small, but high-risk activities may not be reflected in management reports. In some cases, banks failed to adequately communicate employees' duties and control responsibilities or disseminated policies through channels, such as electronic mail, that did not ensure that the policy was read and retained. As a result, for long periods of time, major management policies were not carried out. In other cases, adequate lines of communication did not exist for the reporting of suspected improprieties by employees. If channels had been established for communication of problems upward through the organizational levels, management would have been able to identify and correct the improprieties much sooner.

E. Monitoring

10. Many banks that have experienced losses from internal control problems did not effectively monitor their internal control systems. Often the systems did not have the necessary built-in ongoing monitoring processes and the separate evaluations performed were either not adequate or were not acted upon appropriately by management.

11. In some cases, the absence of monitoring began with a failure to consider and react to day-to-day information provided to line management and other personnel indicating unusual activity, such as exceeded exposure limits, customer accounts in proprietary business activities, or lack of current financial statements from borrowers. In one bank, losses associated with trading activities were being concealed in a fictitious customer account. If the organization had a procedure in place that required statements of accounts to be mailed to customers on a monthly basis and that customer accounts be periodically confirmed, the concealed losses would likely have been noticed long before they were large enough to cause the failure of the bank.

12. In several other cases, the organization's division or activity that caused massive losses had numerous characteristics indicating a heightened level of risk such as unusual profitability for the perceived level of risk and rapid growth in a new business activity that was geographically distant from the parent organization. However, due to inadequate risk assessment, the organizations did not provide sufficient additional resources to control or monitor the high-risk activities. In fact in some instances, the high risk activities were operating with less oversight than activities with much lower risk profiles--several warnings from the internal and external auditors regarding the activities of the division were not acted upon by management.

13. While internal audit can be an effective source of separate evaluations, it was not effective in many problem-banking organizations. A combination of

three factors contributed to these inadequacies: the performance of piecemeal audits, the lack of a thorough understanding of the business processes, and inadequate follow-up when problems were noted. The fragmented audit approach resulted primarily because the internal audit programs were structured as a series of discrete audits of specific activities within the same division or department, within geographic areas, or within legal entities. Because the audit process was fragmented, the business processes were not fully understood by internal audit personnel. An audit approach that would have allowed the auditors to follow processes and functions through from beginning to end (i.e., follow a single transaction through from the point of transaction initiation to financial reporting phase) would have enabled them to gain a better understanding. Moreover, it would have provided the opportunity to verify and test the adequacy of controls at every step of the process.

14. In some cases, inadequate knowledge and training of internal audit staff in trading products and markets, electronic information systems, and other highly sophisticated areas also contributed to internal audit problems. Because the staff did not have the necessary expertise, they were often hesitant to ask questions when they suspected problems, and when questions were asked, they were more likely to accept an answer than to challenge it.

15. Internal audit may also be rendered ineffective when management does not appropriately follow-up on problems identified by auditors. The delays may have occurred because of a lack of acceptance by management of the role and importance of internal audit. In addition, the effectiveness of internal audit is impaired when senior management and members of the board of directors (or audit committee, as appropriate) failed to receive timely and regular tracking reports that indicate critical issues and the subsequent corrective actions taken by management. This type of periodic tracking device can help senior management confront important issues in a timely manner.

2.2.9 Limitations of Internal Control

Despite the benefits derivable from installing a good internal control system, the system can never be regarded as completely effective, regardless of the care followed in their design and implementation. Even if system personnel could design an ideal system, its effectiveness depends on the competency and dependability, of the people using it. Dunn (1998) as cited in Sabari (2003) highlights some of the internal control inherent limitations. He said that most internal controls are designed to prevent fraud or error by relatively junior staff it would usually be relatively easy for management to override the controls, which they have established; segregation of duties can be circumvented by fraudulent collusion. If one member of staff has access to assets and the other maintains the related records it would be possible for them to work together to defraud the

organization and share the proceeds; controls can break down because of human error, poor training or under qualified staff; Compliance test can also prove misleading. The auditor can examine the document to ensure that it has been signed correct. This signature says nothing about the care with which the person responsible checked the item. Similarly, observation could be misleading if staff modified their behavior in the auditor's presence.

2.3 FRAMEWORK FOR THE EVALUATION OF INTERNAL CONTROL SYSTEMS IN BANKING INDUSTRY

The Basel Committee, along with banking supervisors throughout the world, focused on the importance of sound internal controls. This heightened interest in internal controls is, in part, a result of significant losses incurred by several banking organizations. Collins (2000) and Dimistris (2002) report that according to the Basle Committee publication No. 40 of 1998 an analysis of the problems related to these losses indicates that they could probably have been avoided had the banks maintained effective internal control systems. Such systems would have prevented or enabled earlier detection of the problems that led to the losses, thereby limiting damage to the banking organization.

As part of its effort to encourage sound risk management practices, the Basel Committee on Banking Supervision as reported by Collins (2000) and Dimistris (2002) issued a framework intended to be used by supervisory authorities throughout the world in evaluating banks' internal control systems. This is in recognition of the fact that effective internal controls are critical

components of bank management and foundation for the safe and sound operation of banking organizations. A system of strong internal controls can help to ensure that the goals and objectives of a banking organization will be met, that the bank will achieve long-term profitability targets, and maintain reliable financial and managerial reporting.

In developing those principles, the committee has drawn on lessons learned from problem banks situations in various countries of the world. The committee accordingly developed fourteen principles. These principles are to be used in assessing banks' internal control systems. According to the Basel Committee the exact application of the principles depends on the nature, complexity and risks of the bank's operations. These principles are grouped under six major headings: management oversight and the control culture, risk assessment, control activities, Information and communication, monitoring and evaluation by supervisory authorities (Collins: 2000 and Dimistris: 2002).

2.3.1 Management oversight and the control culture

Principle 1: The board of directors should have responsibility for approving strategies and policies; understanding the risks run by the bank, setting acceptable levels for these risks and ensuring that senior management takes the steps necessary to identify, monitor and control these risks; approving the organizational structure; and ensuring that senior management is monitoring the effectiveness of the internal control system.

Principle 2: Senior management should have responsibility for implementing strategies approved by the board; setting appropriate internal control policies; and monitoring the effectiveness of the internal control system.

Principle 3: The board of directors and senior management are responsible for promoting high ethical and integrity standards, and for establishing a culture within the organization that emphasizes and demonstrates to all levels of personnel the importance of internal controls. All levels of personnel at a banking organization need to understand their role in the internal controls process and be fully engaged in the process.

2.3.2 ***Risk Assessment***

Principle 4: Senior management should ensure that the internal and external factors that could adversely affect the achievement of the bank's objectives are being identified and evaluated. This assessment should cover all the various risks facing the bank (for example, credit risk, country and transfer risk, market risk, interest rate risk, liquidity risk, operational risk, legal risk and reputational risk).

Principle 5: Senior management should ensure that the risks affecting the achievement of the bank's strategies and objectives are continually being evaluated. Internal controls may need to be revised to appropriately address any new or previously uncontrolled risks.

2.3.3 Control Activities

Principle 6: Control activities should be an integral part of the daily operations of a bank. Senior management must set up an appropriate control structure to ensure effective internal controls, defining the control activities at every business level. These should include: top level reviews; appropriate activity controls for different departments or divisions; physical controls; periodic checking for compliance with exposure limits; a system of approvals and authorizations; and, a system of verification and reconciliation. Senior management must periodically ensure that all areas of the bank are in compliance with established policies and procedures.

Principle 7: Senior management should ensure that there is appropriate segregation of duties and that personnel are not assigned conflicting responsibilities. Areas of potential conflicts of interest should be identified, minimized, and carefully monitored.

2.3.4 *Information and communication*

Principle 8: Senior management should ensure that there are adequate and comprehensive internal financial, operational and compliance data, as well as external market information about events and conditions that are relevant to decision making. Information should be reliable, timely, accessible, and provided in a consistent format.

Principle 9: Senior management should establish effective channels of communication to ensure that all staff are fully aware of policies and procedures affecting their duties and responsibilities and that other relevant information is reaching the appropriate personnel.

Principle 10: Senior management must ensure that there are appropriate information systems in place that cover all activities of the bank. These systems, including those that hold and use data in an electronic form, must be secure and periodically tested.

2.3.5 ***Monitoring***

Principle 11: Senior management should continually monitor the overall effectiveness of the bank's internal controls in helping to achieve the organization's objectives. Monitoring of key risks should be part of the daily operations of the bank and should include separate evaluations as required.

Principle 12: There should be an effective and comprehensive internal audit of the internal control system carried out by appropriately trained and competent staff. The internal audit function, as part of the monitoring of the system of internal controls, should report directly to the board of directors or its audit committee, and to senior management.

Principle 13: Identified internal control deficiencies should be reported in a timely manner to the appropriate management level and addressed promptly.

Material internal control deficiencies should be reported to senior management and the board of directors.

2.3.6 *Evaluation by Supervisory Authorities*

Principle 14: Supervisors should require that all banks, regardless of size, have an effective system of internal controls that is consistent with the nature, complexity, and risk of their on-and-off-balance-sheet activities and that responds to changes in the bank's environment and conditions. In those instances where supervisors determine that a bank's internal control system is not adequate (for example, does not cover all of the principles contained in this document), they should take action against the bank to ensure that the internal control system is improved immediately.

2.4 OBJECTIVES AND ROLES OF INTERNAL CONTROL FRAMEWORK

Internal control is a process affected by the board of directors, senior management and all levels of personnel. It is not solely a procedure or policy that is performed at a certain point in time, but rather it is continually operating at all levels within the bank. The board of directors and senior management are responsible for establishing the appropriate culture to facilitate an effective internal control process and for continuously monitoring its effectiveness; however, each individual within an organization must participate in the process. Collins (2000), and Dimistris (2002) report that the following are the main objectives of internal control framework developed by the Basle Committee:

[i] Efficiency and effectiveness of operations (operational objectives);

[ii] Reliability and completeness of financial and management information (information objectives); and

[iii] Compliance with applicable laws and regulations (compliance objectives).

Operational objectives for internal control pertain to the effectiveness and efficiency of the bank in using its assets and other resources and protecting the bank from loss. The internal control process seeks to ensure that personnel throughout the organization are working to achieve its objectives in a straightforward manner, without unintended or excessive cost or placing other interests (such as an employee's, vendor's or customer's interest) before those of the bank.

Information objectives address the preparation of timely, reliable reports needed for decision-making within the banking organization. They also address the need for reliable annual accounts, other financial statements and other financial-related disclosures, including those for regulatory reporting and other external uses. The information received by management, the board of directors, shareholders and supervisors should be of sufficient quality and integrity that recipients can rely on the information in making decisions. The term reliable, as it relates to financial statements, refers to the preparation of statements that are presented fairly and based on comprehensive and well-defined accounting principles and rules.

Compliance objectives ensure that all banking business is conducted in compliance with applicable laws and regulations, supervisory requirements, and internal policies and procedures. This objective must be met in order to protect the bank's franchise and reputation.

2.5 INTERNAL CONTROL AND THE ROLE OF AUDITORS

Although external auditors are not, by definition, part of a banking organization and therefore, are not part of its internal control system, they have an important impact on the quality of internal controls through their audit activities, including discussions with management and recommendations for improvement to internal controls. The external auditors provide important feedback on the effectiveness of the internal control system. While the primary purpose of the external audit function is to give an opinion on, or to certify, the annual accounts of a bank, the external auditor must choose whether to rely on the effectiveness of the bank's internal control system. For this reason, the external auditors have to conduct an evaluation of the internal control system in order to assess the extent to which they can rely on the system in determining the nature, timing and scope of their own audit procedures (Dandago: 1999). Basle Committee as reported by Aina (2001) explained that the exact role of external auditors and the processes they use vary from country to country. Professional auditing standards in many countries require that audits be planned and performed to obtain reasonable assurance that financial statements are free of material misstatement. Auditors also examine, on a test basis, underlying transactions and records

supporting financial statement balances and disclosures. An auditor assesses the accounting principles used and significant estimates made by management and evaluate the overall financial statement presentation. In some countries, external auditors are required by the supervisory authorities to provide a specific assessment of the scope, adequacy and effectiveness of a bank's internal control system, including the internal audit system (Aina: 2001, Collins: 2000 and Dimistris: 2002).

One consistency among countries, however, is the expectation that external auditors will gain an understanding of a bank's internal control process. The extent of attention given to the internal control system varies by auditor and by bank; however, it is generally expected that the auditor would identify significant weaknesses that exist at a bank and report material weaknesses to management orally or in confidential management letters and, in many countries, to the supervisory authority. Furthermore, external auditors may be subject to special supervisory requirements that specify the way that they evaluate and report on internal controls.

The internal Auditor on the other hand also plays an important role in the internal control system. He objectively examines, evaluates and reports on the adequacy of internal control as a contribution to the proper, economic, efficient and effective use of resources. Tijjani (2003) observes that the objective of internal auditing is to assist members of the organization in the effective discharge of their responsibilities. In its standards for professional practice on internal auditing, the Institute of Internal Auditors (1991) define

the scope of internal auditing as the examination and evaluation of the adequacy and effectiveness of the organization's system of internal control and the quality of performance in carrying out assigned responsibilities. Thus, internal audit is concerned with an evaluation of both internal controls as well as the quality of actual performance. This according to the Institute of Internal Auditors as reported by Tijjani (2003) involves the following five areas of operations:

[I] Reliability and Integrity of information
[ii] Compliance with policies, plans, procedures, laws and regulations
[iii] Safeguarding assets
[iv] Economical and efficient use of resources
[v] Accomplishment of established objectives and goals for operations or programmes.

It can be seen that the modern concept of internal auditing covers not only the traditional functions dealing with a review of custodianship and safeguarding of assets, compliance with policies and reliability of accounting information, but it also emphasizes new areas like reviewing the economical and efficient use of resources and organizational performance.

Sabari (2003) contends that many organizations have internal auditors who are responsible for a continuous review and analysis of the internal control system. Both administrative controls and accounting controls are studied by the internal auditors to identify weaknesses in internal control that can improve over time. Thus, internal auditors are not simply one of the organization's controls – they are a control over all other controls. For this reason, while internal auditors can recommend control, they should not

design and implement the controls. Rather, to maximize their objectivity, internal auditors should serve the organization as independent appraisers of existing controls as emphasize by the standards for professional practice of internal Auditing (2001).

The major roles of internal auditor generally fall into the following specific control activities (Sabari: 2003): adequate separation of duties; proper authorization of transactions and activities; adequate documentations and records; physical control over assets and records; and, independent checks on performance.

2.5.1 Adequate Separation of Duties

There are four general guidelines that are of special significance to the auditor for both fraud and errors prevention under adequate separation of duties and these are; **(a)** Separation of the custody of assets from accounting. **(b)** Separation of the authorization of transaction from the custody of the related assets. **(c)** Separation of operational responsibility from record-keeping responsibility, and **(d)** Separation of Information technology duties from duties of key users outside information technology (Dimistris: 2002).

2.5.2 Proper Authorization of Transactions and Activities

Responsible personnel acting within the scope of their prescribed authority and responsibility should authorize all transactions. Without a formal system of transaction authorization, any employee could commit resources

without regard to the entity's objectives. The authorization could be specific or general depending on the nature, scope, and frequency of occurrence. Specific authorization means authorization is required each time the transaction is proposed and is typically used for usual, material, or infrequent projects. In contrast general authorization means the entity has policies and procedures that personnel should follow to determine if a proposed transaction or project is authorized in general. It should also be noted that authorization is not the same as approval. Authorization simply means authority has been given to acquire or expend resources. Approval in contrast, means the condition for authorization has been met and the resources may therefore be acquired or expended.

2.5.3 Adequate Documents and Records

Documents and records are the physical objects upon which transactions are entered and summarized. To obtain accurate and reliable accounting data, auditor must ensure that transactions are recorded promptly in the accounting periods and in Naira amounts actually executed, and classified properly in subsidiary and control accounts.

In computer systems, though, audit trails can be eliminated or otherwise distorted, the auditor rather than focus on audit trail when auditing in computer systems, he should focus on management's controls over the system, testing whether the controls are adequate and, therefore, whether the system is likely to be effective.

Certain relevant principles dictate the proper design and use of documents and records. Documents and records should be: Prenumbered consecutively to facilitate control over missing documents and as an aid in locating documents when they are needed at a later date; prepare at the time a transaction takes place, or as soon as possible thereafter; sufficiently simple to ensure that they are clearly understood; designed for multiple use, when possible, to minimize the number of different forms; and, constructed in a manner that encourages correct preparation.

2.5.4 Physical Control over Assets and Records

To maintain internal control, it is essential for the auditor to ensure that assets and records are protected. If assets are left unprotected, they can be stolen. If records are not adequately protected, they can be damage, or lost. The most important type of protective measure for safeguarding assets and records is the use of physical precautions. An example is the use of storerooms for inventory to guard against theft. Fireproof safes and deposit vaults for the protection of assets such as currency and securities are other important physical safeguards.

In the case of information technology, only authorized personnel should have an access to assets and records and several means can be used to limit access. These include protection devices, online recording, and access codes. Protection devices restrict unauthorized personnel from gaining direct access to assets. Online recording limits access to assets records by limiting the number of employees involved in recording and posting transactions.

Access codes, such as employee identification and personal identification numbers, restrict access to data that could be used to alter records or to misappropriate assets.

2.5.5 Independent Checks on Performance

The need for independent checks or internal verification by the auditor arises because internal control tends to change over time unless there is a mechanism for frequent review. Personnel are likely to forget or intentionally fail to follow procedures, or they may become careless unless someone observes and evaluates their performance. An essential characteristic of the person performing internal verification procedures is independence. An internal auditor's effectiveness depends crucially on his or her independence from the personnel and the activities of an organization. Otherwise, the integrity of an internal auditor's conclusions and recommendations would lack credibility.

2.6 CORPORATE SURVIVAL IN THE NIGERIAN BANKING INDUSTRY

Corporate survival can be defined as the ability of a company to remain a going concern without threat to its franchise or existence by regulatory authorities, shareholders or creditors (Hamid: 2004). It can also be defined as the state of continuing to live or exist by a corporate entity without closing down its doors to customers as a result of withdrawal of its licence by regulatory authorities, liquidation by creditors, or by any other means of liquidation (Garba: 2002). He opines that frequent interference in the

management of a bank by influential members of the society, high operating cost, lack of controls, huge bad debt portfolio, breach of procedures, non-compliance with statutory requirements, poor credit risk management and loss of public confidence, are some of the factors that constitute threat to the survival of a banking organization.

2.6.1 Components of Corporate Survival

Garba (2002) explains that for a banking organization to ensure its survival, it must ensure the achievement of the following:

[i] Compliance with relevant statutes, laws and circulars by regulatory authorities.

[ii] Implementation of a good control system that would prevent wastages and fraud and ensure enhanced performance.

[iii] Maintaining sufficient turnover and profitability.

[iv] Ensuring cost effectiveness in operations.

[v]Sustaining the confidence of depositors and shareholders through enhancing the safety and security of their deposits and investments.

[vi] Response to the increasingly hostile banking environment through improved liquidity to meet the demand of depositors at all times.

[vii] Making a bank more attractive to depositors and shareholders by ensuring the attainment of effectiveness and efficiency in operations.

[viii] Achieving operational excellence by minimizing overhead cost and reduction of other frictions cost.

2.7 THE BANKING INDUSTRY IN NIGERIA

The genesis of banking can be traced back to as early as 2000 BC in Babylon, when a functional system of banking was still in the neophytic stage (Olalusi, 1997). Bankers and banks were given different names in different places. It is speculated that the word 'bank' must have been coined from, **Banco san Giorgio,** which was established in Genoa in 1407. The bank of Amsterdam, basically established in 1609 to carter for the banking needs of Amsterdam businessmen, was a pioneer of modern banking by its introduction of a certificate of deposit and receiving of all forms of coins. The roles of the goldsmiths in Britain and the effect of the gold rush of 1848 in the United States were significant in the evolution of modern banking.

In the late nineteenth century, there were a lot of trading activities along the Nigerian Coastal areas. Therefore, banking evolved to support these trading activities (Ndekwu: 1994, Olalusi: 1997). It was initially foreign base. In August 1891, the chairman of ELDER DEMPSTER COMPANY initiated the setting up of a branch of African Banking Corporation. The purpose of this was to boost the British shipping business operated by the company. The bank was accorded the privilege of importing silver coins from Britain for use in Nigeria as from January 1892. Elder Dempster Company took over the bank on payment of E1000 (one thousand pounds sterling) and the bank became incorporated on 31st March 1893 as the Bank of British West Africa (B. B. W. A.). The bank was biased in favour of Elder Dempster Company, so there were a lot of agitations by British traders. This development led to the establishment of a second bank

in 1899 known as Anglo African Bank, which later became bank of Nigeria. The B.B.W.A. Was merged with the new bank (i.e. the Bank of Nigeria) in 1912.

In 1917, another bank known as the Colonial Bank was set-up. This bank, which later became Barclays Bank Nig. Ltd, is now known as the Union Bank (Nig) Plc. It posed a formidable competition for B.B.W.A. In 1948, the British and French bank was established. Later in 1961, it changes its name to the United Bank for Africa Ltd, now Plc. In fact, the First Bank, Union Bank and United Bank for Africa (UBA) are the three largest banks in Nigeria today.

During the period 1929 and 1952, numerous indigenous banks were established. The Agbonmagbe Bank Ltd (Currently known as Wema Bank) was set-up in 1938, followed by African Continental Bank (ACB), which was set-up in 1948. During the period, February 1951 and May 1952, 18 indigenous banks were registered. All of them failed without any exception within a short period. The failure of these indigenous banks was as a result of lack of banking expertise and non-prudent lending policies (Olalusi, 1997).

From independence in 1960 to 1985, there were a total of 40 banks in the country made up of 12 Merchant Banks and 28 Commercial Banks. Due to … deregulation, however, the number of operating banks in the country increased phenomenally from 40 in 1985 to 66 in 1988, 100 in 1990 and 120 in 1992. Equally, the bank branches increased from 1316 in 1985 to 1698 in 1988, 1944 in 1990 and 2027 in 1992! Thus within a period of seven years (1985 – 1992)

the banking industry witnessed a growth that it had not witnessed in the first 25 years of the country as an independent nation… (Bulama, 1999).

At present, most players are undergoing changes in their operations. Some of these changes include conversions from merchant to commercial banks, expansion of branch network (to enhance market position), significant investment in information technology and injecting capital to expand operations (Sanusi, 2002). To date, eleven banks have swapped their merchant-banking license for commercial banking licences, as commercial banks are better positioned to mobilize deposits and therefore grow. Due to the inability of merchant banks to access the Clearing House its cost of funds has remained high. Low cost producers of funds can profitably accommodate low risks and more stable transaction lines. Banks that control deposits control profit, due to the fact that the bulk of liabilities are non-interest liabilities or low interest bearing deposits, which finance themselves in the ordinary course of business (Ogunleye, 2000). Therefore banks with a good market share of deposits have low cost of funds that they are able to profitably invest in treasury bills or credit worthy names (Oduyemi: 2000).

In Nigeria banking products are generic, and efforts at product differentiation have not been very successful. Competition in the industry has been based largely on pricing and service delivery. Therefore banks need to distinguish themselves through service delivery in order to have a competitive

advantage over others. A successful information technology strategy is key to meeting expectations of customers. Bank's that have not made investment in information technology employ more people and the implicit costs of carrying these people is significant (Ogunleye: 2000). The New Age (2003) reported that by December 2002 there were a total of 90 licenced banks, 282 community banks, 74 primary mortgage institutions and 6 development banks.

Banking survey (1999/2000) by the CBN reveals that Losses from fraud in the banking industry have remained high, and are likely to increase further as merchant banks converting to commercial banks have limited experience in commercial banking and are vulnerable to operational errors and frauds. In its 1999 annual accounts, the Nigerian Deposit Insurance indicated that fraud losses totalled ₦2.7 billion. Banks need to strengthen their internal control systems to mitigate risks in their business process and invest more in staff training to prepare them for the increased challenges of the industry (sanusi, 2002).

2.7.1 Functions and Nature of Business of Commercial Banks

Banks are the custodians of the general public's money, which they accept in the form of deposits and pay out on the clients' instructions. The most distinguishing feature of banks is that their liabilities are generally accepted as a means of payment. In the past, banks were functionally subdivided into commercial, merchant and general banks. This distinction is

no longer valid since many banks offer the entire spectrum of services under one roof. Although a number of highly specialized institutions (catering for specific groups of clients and niche markets) remain in the financial sector the discussion below outlines the whole spectrum of functions performed by commercial banks.

According to First Bank of Nig. Plc., Graduate Employees Orientation Course Documents (1999), commercial banks render the following services:

(1) Acceptance of deposits into various types of accounts;

(a) Current Accounts: These are demand deposit accounts withdrawable with the use of cheque. Interest is payable/charged on the balance of the deposit.

(b) Savings Accounts: These are also demand deposit accounts withdrawable in person. The accounts attract monthly interest.

(c) Short Deposit: This is a time deposit account, which attracts interest. It requires 7 days notice before withdrawal can be made or the customer forfeits interest on the amount withdrawn in lieu of notice.

(d) Fixed Deposit: It is a time deposit account of a fixed amount for a period ranging from 3 – 12 calendar months at a fixed rate of interest payable on specified date. It attracts high rate of interest depending on the duration of the deposits. No interest is paid on deposits withdrawn before maturity.

(2) Lending Facilities: The banks are required to lend certain proportion of their deposits to their customers. Banks lend by way of:

(a) Loan: A loan account is opened with the authorized advance amount immediately debited to it and transferred to the Current Account. Interest is charged on the whole amount advanced.

(b) Overdraft: An overdraft is an authority granted to a customer to overdraw his current account to an agreed limit and the balance usually varies from day-to-day transactions. Interest is charged on the amount actually utilized.

(c) Bills Discounting

(d) Opening letters of credit

(e) Issuance of Bonds, Guarantees and indemnities

(3) Transfer of funds: Transfers are effected through:

(a) Telegraphic Transfers

(b) Mail Transfers

(c) Issue of Bank Cheques and Bank Drafts

(d) Issue of Cheque cashing facilities

(e) Automated Teller machine

(4) Issue of status Report and Enquiries

This is the means by which a bank asks for or gives information on the financial position of its customers. This plays an important role in enhancing meaningful commercial transactions both locally and internationally.

(5) Safe Custody (Bailment)

Banks receive and take charge of customers' valuables like boxes of trinkets, bonds and shares certificates, title deed for real property etc. for safekeeping. Receipts are usually issued when these items are deposited and such receipts are surrendered before the collection of such items. The bank can either be a gratuitous bailee or a paid bailee.

(6) Foreign Exchange Transaction

All licensed banks act as authorized dealers to the Central Bank of Nigeria in buying and selling currencies, travelers' cheques, etc.

(7) International Trade Services to Importer And Exporter

(a) <u>Trade Services</u>: An Importer can be issued with letters of introduction addressed to overseas correspondent banks requesting them to give assistance by way of information and advise about possible sellers of the goods the importer wants to buy.

(b) <u>Traveler's Cheques</u>: They are denominated in foreign currencies. The holder signs the cheques as soon as they are issued. They are counter-signed by the holder in the presence of the cashier when being cashed. The signature must agree.

(c) Foreign Currency: Banks generally keep some limited quantities of foreign Currencies to be sold to travelers for minor expenses before their travelers' cheques are cashed.

(d) Bills for Collection: When an exporter is shipping his goods on collection basis, he draws a bill of exchange on the importer. The exporter gives the bill of exchange to his banker to collect the proceeds to the credit of his account. The collecting bank sends the bill to a correspondent bank in the country of the importer to be presented to the drawee for payment. When the proceeds are received the exporter's account is credited. In some cases, the exporter may send the bill direct to the importer for acceptance. When the bill is accepted it is returned to the exporter who now presents it to his bankers who forward it to their correspondent bank for payment.

(e) Bill for Negotiation: The exporter may be in need of money. He can therefore negotiate the bill with his bank. In a nutshell he is selling the bill to the bank that now pays the face value of the bill less discount. Generally, banks discount bills with recourse. In other words, if the bill is not accepted by the drawee, the bank will claim from the customer the amount that was paid to him. A bill is normally negotiated against deposit of security except if it is a documentary bill when the documents will form part of the security.

(f) Documentary Letter of credit: It may be revocable or non-revocable. While revocable, credit does not constitute a legally binding undertaking.

Irrevocable credit on the other hand constitutes a legally binding undertaking between the bank and all other parties.

(8) Other services:

(a) <u>Counter-manding cheques</u>: A customer may wish the payment of a cheque issued, stolen or lost, to be stopped. The customer must quote the cheque number, amount, date and payee's name on the cheque. Once such countermand is received the bank will check and make sure that the cheque has not been paid. When such cheque is presented, it will be returned with the answer "refer to drawer".

(b) <u>Standing Order</u>: A customer may instruct his bank to deduct specified amount from his account to the account of another or any of his account such as savings account. In some cases it may be in respect of monthly premium on insurance to customers, etc.

(c) Collection of Cheques issued by customers.

(d) Executorships and Trusteeship Services.

In addition to these functions given by the First Bank training programme, The South African Financial Sector forum (1997) gave the following functions of banks:

(9) ***Money creators*****:** i.e. banks create money by way of deposit liabilities. In contrast to the liabilities of other institutions, bank liabilities (cheques) are generally accepted as a means of payment.

(10) ***Managers of the payments system*****:** i.e. banks provide a sound and stable mechanism to effect payments. This task not only involves the payment of cheques, but also of credit and debit cards, ATMs, EFTs, and the like.

(11) ***Creators of indirect financial securities*****:** i.e. banks operate as financial intermediaries placing themselves between ultimate lender and ultimate borrower and transforming primary securities (i.e. liabilities of firms) into indirect securities (i.e. liabilities of financial intermediaries that are desired by investors). Accordingly, banks hold assets that are subject to specific risks, while issuing claims against them in which these risks are largely eliminated through diversification. In essence, banks are similar to other financial intermediaries in performing this function, but have a competitive advantage because they enjoy economies of scale and scope and have better information.

(12) ***Information agents*****:** i.e. owing to an asymmetric supply of information (i.e. information not available to all) borrowers choose, often for competitive reasons, not to make relevant information publicly available (i.e. in the capital market), but are willing to share it with a bank in order to obtain the necessary funding. Moreover, firms do not always wish to be subjected to the

discipline of continuous public scrutiny, as would happen when funds are obtained through the capital markets.

(13) ***Financial "spectrum fillers":*** i.e. in a (theoretically) perfect market - with zero transaction costs, complete and symmetrically available information (i.e. information available to all) - there would be no role for banks as financial intermediaries. Banks exist because the capital market is not perfect and cannot supply the full range of instruments required by borrowers. Banks fill this gap in the spectrum of financial services and are often able to supply specific instruments, tailor-made on request.

(14) ***Investors for depositors*****:** i.e. banks accept an investment function for their depositors by assessing investment opportunities and monitoring subsequent investment strategies. By accepting this monitoring task banks help to overcome the inability of lenders (depositors) to exercise control over the behaviour of borrowers. Since much of the information is not public knowledge, a banking firm enables lenders to select better investments and to monitor their performance at lower costs than would be the case if lenders did so themselves.

(15) ***Dealers in foreign currency*****:** i.e. considering the increasing degree of interaction between South Africa and the rest of the world this function is growing in importance. Not only do banks arrange various forms of transfer, but they also handle foreign financing and provide advice on exchange rates and foreign financial market conditions.

2.7.2 Universal Banking

The guidelines issued by CBN subtly define Universal Banking as "The Business of receiving deposits on current, savings or other accounts; paying or collecting cheques drawn or paid in by customers; provision of finance, consultancy and advisory services relating to corporate and investment matters; making or managing investment on behalf of any person; and the provision of insurance marketing services and capital market business or such other services as the Governor of the Central Bank of Nigeria, may, by regulation, designate as Banking business" (Oduyemi: 2000).

Furthermore, the guidelines clearly state the activities that banks can undertake as: -

- Clearing House Activities
- Underwriting/Issuing House activities
- Insurance services

From the above scenario, Universal Banking in Nigeria will be the freedom of licensed banks to operate retail and investment banking representing as at now, commercial and merchant banking, and a restricted entry into the pie of insurance business.

In a loose sense, Universal Banking will be official permission for banks to indulge in multi- purpose functions in banking and related banking products of securities and insurance (Ogunleye: 2000).

Again, the guidelines specified six areas in insurance business that banks can undertake (Ogunleye: 2000), namely: -

- Agency services
- Brokerage services

} Marketing services only

- Underwriting services
- Loss Adjustment services

} Underwriting services only

- Re-Insurance Services
- Retrocessionaire services

} Re- insurance services

While banks may provide both marketing and underwriting services directly, the re-insurance service is expected to be provided either through a subsidiary or an associated company (Ogunleye: 2000). Oduyemi (2000) reported that the guidelines went further to itemise fifteen conditions banks must comply with. The highlight of these guidelines is as follows:

- All insurance subsidiaries of banks must comply with the capitalization requirements under the Insurance Decree No. 2 of 1997 and any subsequent amendments.
- All insurance activities shall be licensed and regulated by National Insurance Commission NAICOM in accordance with the Insurance Decree of 1997 or such other insurance laws as may be enacted.
- Banks shall be required to keep distinct records relating to their insurance transactions

The innovation will not necessarily be a compulsion to any licensed bank. A bank will be free to determine from its core competency areas, a

service mix from the three areas of operation specified and design appropriate products to achieve and retain a slice of the consuming market.

2.7.3 Bank Distress and Its Causes

Government's interest in the banking sector is usually aimed at ensuring a safe and sound system where depositors are protected. This is usually done by careful and selective choice of financial institutions. Having licensed them, Government would appoint its agents to continually monitor the operations of the institution to ensure that their operations are in accordance with their enabling laws and above all, that the institutions are operated in a safe and sound manner (Abdullahi, 2002). These supervisory activities of government are designed to protect depositors' consumers, and the financial system and to ensure monetary stability (Spong, 1995). Also banks are extensively regulated to minimize risk and cost of failure (Dale, 1984).

It is on record that in spite of government's efforts to protect the financial system, failures do occur. According to Abdullahi (2002) endogenous factors such as bad management and weak internal control system or exogenous ones such as economic recession usually precipitate such failures. Sometimes both factors combine to bring distress to financial institutions especially banks and when that happens, depositors are the most affected.

Several attempts have been made in the past to define “distress” in the financial services industry. In ordinary parlance the word “distress” connotes “ unhealthy situation” or a state of inability or weakness, which prevents the achievement of desired or set goals and aspirations (Smith and Wall, 1992, Ologun, 1994). Benston *at al* (1986) on the other hand describe distress as a situation of complete or near complete loss of shareholders fund. Banking distress occurs when a bank or some banks in the system experience inliquidity or insolvency resulting in a situation where depositors fear the loss of their deposits and a consequent break down of contractual obligations (Abdullahi, 2002).

History has it that by 1952, a total of 25 banks closed their doors to depositors in Nigeria with consequent untold hardship for customers. There is a story of a customer of Farmers’ Bank Limited who on finding that his bank had closed it doors indefinitely, suffered a heart attack and dropped dead by the bank premises (Abdullahi, 2002). Unfortunately, those were the days when no formal banking regulations existed in the country. It was after the crises that the banking Act was enacted in 1952 and CBN was established much later in 1959. By 1989, seven banks, mostly owned by state governments, were technically insolvent. The situation has since deteriorated as a second generation of distressed banks emerged. With the exception of the slight decline from 9 in 1990 to 8 in 1991, the number of distressed banks had been on the increase (Abdullahi: 2002). For instance, the number of distressed banks increased from 7 in 1989 to 28 in 1993, representing an

increase of 300%. The number peaked to an alarming rate of 60 as at the end of 1995 out of which 31 were not only insolvent but also terminally distressed. The total number of the distressed banks however decline to 52 at the end of the third quarter of 1996. Moreover, these distressed banks as at the end of 1996, had ₦70.8 billion deposits or 33.6% of the total deposit in the entire system. While the total assets stood at ₦95.6 billion or 19.8 % of the assets of all the banks. It has also been estimated that an injection of about ₦24.3 billion would be required as at the end of 1996 to adequately recapitalised these banks. The situation has become worrisome especially when one compares the level of the insurance fund risk exposure ₦36.4 billion with the deposit insurance fund of NDIC which was just about ₦6 billion as at the end of 1996 (Abdullah, 2002). However in the year 2000, 11 distressed banks were identified, 3 were terminally distressed and their licences revoked, while the remaining 8 were recapitalised and their Boards/ Managements reconstituted. In recent times, instability in the financial system and the banking sector in particularly has arisen from institutional failures of the past (Abdullahi, 2003).

Regulators and researchers in response to the concern for distressness in the banking industry have over the years been engaged in the attempt to evolve reliable set of determinants for the banks failure. One of such analysis was carried out by the office of United States Controller of currency in 1988. The composite CAMEL rating emerged from the studies (Abdullahi, 2002). The categorization of a financial organization as a

"problem" or "distressed" institution is usually based on CAMEL rating system (Sinkey, 1980: Ebhodaghe, 1993: and Nyong, 1994).

2.7.4 Fraud/Forgery in Nigerian Banks

Common classification has shown that frauds vary widely in nature, character and methodology or methods of perpetration, thus making the classification a very difficult exercise. Ahmad (2004) observed that classification of fraud and forgeries can be made on the basis of:

[i] Perpetrators: This can sub divided into three types,

[a] Internal perpetrators: This relate to fraud committed by members of staff.

[b] External perpetrators: This relate to fraud committed by outsiders.

[c] Mixed Perpetrators: This involves collusion between outsiders and insiders.

[ii] By method used: On the basis of method used the list is inexhaustible, as the perpetrators continue to develop and evolve new methods every day. Thompson (2004) and Ahmad (2004) argue that an analysis of the type of fraud/forgery cases perpetrated in the Nigerian banking industry shows the commonest types as:

i. Presentation of forged cheques.
ii. Granting of unauthorized loan.
iii. Positing of fictitious credits.
iv. Suppression of cheques.
v. Fraudulent transfer and withdrawals.
vi. Forgeries on savings and deposits accounts.

vii. Forgeries on current account by use of forged cheques.

viii. Forgeries of transfer instruments such as drafts, mail/ telegraphic transfers etc.

ix. Opening and operating fictitious accounts together with the creation of false credit balance.

x. Over invoicing of services to the bank.

xi. Diversion of bank's funds.

xii. Embezzlement or outright theft of cash.

xiii. Cross firing or kite flying, sometimes with suppression of cheques.

xiv. Foreign exchange malpractices.

xv. Payment against uncleared effects and suppression of entries.

xvi. Advances to non-existing customers.

xvii. Misuse of various suspense accounts.

xviii. Suppression of cash lodgements.

xix. Operation of specie movement of their own with instructions from one bank branch to other to obtain cash.

xx. Printing of chequebooks to agree with the chequebooks of the bank intended to be defrauded.

xxi. Use of forged CBN credit advice.

xxii. Substitution of CBN presentation from clearing house.

xxiii. Interception and switching of telex messages for transfer of funds.

To enable us have a good understanding of the extent of fraud in the banking industry we shall consider the NDIC annual reports.

TABLE 2.7.4a: **SUMMARY OF RETURNS OF COMMERCIAL BANKS ON FRAUDS AND FORGERIES.**

YEAR	Average No. Of Bank Rendering Returns	Total No. of Fraud Cases	Total Amount Involved (₦'m)	Actual Expected Total Loss (₦'m)	Proportion of Actual/ Expected Loss To Amount (%)
2000	46	400	2,844.20	1,077.89	37.90
1999	43	182	6,369.69	2,713.40	42.73
1998	37	564	3,129.26	673.50	21.52
1997	39	741	3,590.31	224.54	6.25
1996	43	587	1,542.91	371.08	24.07
1995	43	127	1,006.28	226.38	22.49

Source: NDIC Annual Report 1995 – 2000.

TABLE 2.7.4b: **SUMMARY OF RETURNS OF MERCHANT BANKS ON FRAUDS AND FORGERIES.**

YEAR	Average No. Of Bank Rendering Returns	Total No. of Fraud Cases	Total Amount Involved (₦'m)	Actual Expected Total Loss (₦'m)	Proportion of Actual/ Expected Loss To Amount (%)
2000	20	3	6.91	2.68	38.78
1999	31	13	1,036.59	16.66	1.61
1998	25	9	67.65	18.75	27.84
1997	29	16	187.59	2.90	1.54
1996	4	19	57.77	4.16	7.21
1995	25	14	5.08	2.75	54.13

Source: NDIC Annual Report 1995 – 2000

During the period under study, the average number of total reporting banks stood at about 32 per annum. The number of reported cases of fraud

increased significantly by 119.8% from 182 in 1999 to 400 in 2000, and the total amount involved for commercial banks in 2000 was ₦2, 844.20 million. On the average, about 37.90% of the total amount involved was lost by commercial banks during the year, whilst, the actual/expected loss for merchant banks stood at ₦2.68 million, with a proportion of 38.80% as at December 2000 compared to a very low level of 1.61% in 1999.

The highest reported incidence of frauds and forgeries occurred in ten banks. Together the banks were responsible for about 88.9%, 93.47% and 93.35% of the total amount of fraud in the banking industry, amounting to ₦11, 481.06 million in 2002, ₦10, 509.27 million In 2001 and ₦2, 661.45 million in 2000 respectively. The amount in 2000 is in relative proportion higher than 64.90% for 1999 but lower than 97.11% in 1998. In 1997, the amount involved was ₦3, 649.10 million, which represents 96.60% of the total amount involved as compared with 65.76% 1996 and 62.34% in 1995.

TABLE 2.7.4c: **SUMMARY OF TEN BANKS WITH HIGHEST FRAUD CASES**

Years	Total For Ten Banks		Total For All Banks	
	Amount Involve (₦.m)	% Share	Amount Involve (₦.m)	% Share
1995	630.49	62.34	1,011.36	100.00
1996	1,052.62	65.76	1,600.68	100.00
1997	3,649.10	96.60	3,777.92	100.00
1998	3,104.30	97.11	3,196.52	100.00
1999	4,793.62	64.90	7,356.26	100.00
2000	2,661.45	93.35	2,851.11	100.00
2001	10509.27	93.47	11,243.94	100.00
2002	11,481.06	88.9	12,919.55	100.00

Source: NDIC Annual Reports 1995 – 2002

A study of the type of fraud and forgery cases perpetrated involves "fraudulent transfer and withdrawals" this constituted the largest proportion in both amount involved and actual/expected loss during the period under review. "Presentation of forged cheques" occupied the second position in terms of the amounts involved (24.03%) and actual/expected loss (14.78%), followed by "Outright theft" (13.24%) in third position "Granting of unauthorized loans" (10.36%) and "Posting of fictitious credits" (10.03%) were fourth the and fifth respectively. Also on the increase was reported cases of loss of money to armed robbers (10.76%).

A total of 152 and 85 staff were involved in frauds and forgeries in 2002 and 2001 respectively. A total of 493 staff of banks were involved in frauds and forgeries in 2000, a decrease of about 17.30% when compared with the previous years level. In 1997, 566 staff were involved compared with 625 and 552 in 1995 and 1996 respectively. Of the total, core operational staff such as supervisors, officer, accounts managers, executive assistants, clerks and cashiers accounted for about 75.10%, an increase of 5.60% relative to 1999 and 1998 levels. In the period 1995 to 1997 they accounted for about 84.99%. The staff involved were dismissed, retired or terminated. The table 2.7.4d below expantciates further.

TABLE 2.7.4d: **BANKS' STAFF INVOLVED IN FRAUDS & FORGERIES.**

Year	1995		1996		1997		1998		1999		2000		2001		2002	
Rank	No.	%	No.	%	No.	%	No.	No.	%	%	No.	%	No.	%	No.	%
Supervisors and Managers	151	24.16	218	39.49	203	35.90	112	36.01	178	29.90	132	26.80	55	36.18	16	18.80
Officers, Accountants and Executive Assistants	142	22.72	96	17.39	154	27.20	72	23.15	144	24.20	101	20.50	60	39.47	48	56.50
Clerks and Cashiers	172	27.52	145	26.27	124	21.90	82	26.37	92	15.40	137	27.80	30	19.74	13	15.30
Typists, Technicians and Stenographers	18	2.88	19	3.44	20	3.50	12	3.86	37	6.20	20	4.10	----	----	----	----
Messengers, Drivers Cleaners, Security Guards And Stewards	123	19.68	66	11.96	57	10.10	26	8.36	127	21.30	81	16.40	5	3.29	4	4.70
Temporary Staff	16	2.56	5	0.91	5	0.90	5	1.61	15	2.50	8	1.60	2	1.32	4	4.70
Uncategorized Staff	3	0.48	3	0.54	3	0.50	2	0.64	3	0.50	14	2.80	----	----	-----	----
Total	625	100	552	100	566	100	311	100	596	100	493	100	152	100	85	100

Source: NDIC Annual Report 1995 – 2002.

2.7.5 Computer Based Accounting System and Internal Controls

Computer systems are widespread in the Nigerian banking industry. Most banks have embraced information technology, recognizing it as part of the requirements for survival. As computer system eliminates intermediate records (Glynne, 1995), the possibility of fraud occurring in the industry is likely going to be higher, with very less chances of detection (Dandago, 1999). There is, therefore the need to establish a sound system of internal control in order to ensure maximum protection of assets, and completeness and accuracy of records.

Rapid adoption of information technology (IT) by banks has not change the basic need for internal controls. However, the integration of IT into banking business processes extends the role of IT systems and IT-based internal controls (Tam, 2001). Clients' use of IT affects internal controls. For instance, an increasing amount of information supporting significant financial statement assertions is electronically initiated, recorded, processed, and reported by IT systems and programs. There is therefore the need for in-built internal controls (e.g. an edit test or a check digit control procedure during data entry to reject invalid input).

2.7.5.1 Effects of Computer on Internal Control

The computer, despite its importance and indispensability, posed a considerable threat to the banking industry. The level of fraud in the Nigerian banking industry has continued to rise. For example in 2002 financial year NDIC reported ₦12.9 billion fraud related-cases, as against ₦11.2 billion in 2001. This may not be unconnected with increase in computer fraud, where information technology equipment is used to manipulate programmes or data dishonestly (i.e. by opening and operating fictitious accounts together with the creation of false credit balance, forgeries of telegraphic transfer, posting of fictitious credits, payment against uncleared effects, fraudulent transfer and withdrawal, altering, substituting or destroying or creating spurious records).

2.7.5.2 Internal Controls Within Computer Systems

Glynne (1995) and Dandago (1999) classify the main controls within a computer system into: Systems Development and Control; Organizational Controls; and Procedural Controls.

[i] Systems Development and Control: As a computer system develops, all stages of the development must be fully recorded; the accounting processes analyzed would be tabulated in the form of a flow chart, as a permanent record. Programmes must be standardized as much as possible; they must be carefully stored— preferably in a special "library" under lock and key. Amendments to programmes should be written out, on pre-determined forms, fully authorized and verified by the use of test packs, before put into actual operation.

[ii] Organizational Controls: As in any other section of the business, organizational internal control within the computer section is achieved by staff rotation, segregation of duties and responsibilities, use of control totals to check upon output, and carefully logging of activities both of personnel and machines. The computer files require particular control—by the use of special storage library and a system of identity numbers for each file coupled with a file register. The organization must also provide for fire and standby arrangements.

[iii] Procedural Controls: These are controls related to the actual processing of information within the system- i.e., to ensure that the correct file is processed, with substantial accuracy, based upon the right information,

and that the output is correctly used. They comprise of input controls, output controls and processing controls.

There is therefore the need for a more sound internal control system, made up of in-built controls, in the computer system, to be able to control the level of fraud in the banking industry. Tam (2001) argues that internal controls can be implemented electronically as constraints (including assertion and triggers). Constraints define the conditions under which data is valid. Expressing internal accounting controls as constraints allow desired business rules (i.e. internal controls) to be specified. Improving internal controls is an inexpensive way to reduce losses from errors and fraud. Likewise, today's IT based internal controls cannot be neglected as the integration of IT into banking business processes continues. For example the authorization function (such as the decision whether or not to accept a particular cheque or funds transfer, to open an account and post a credit into it, to allow withdrawal, to give overdraft or loan etc) must be built into the computer programme, as part of the organizational and procedural controls (Tam, 1995). Through this, the level of risk associated with computer operations will be minimized, performance improved and fraud-related cases brought to minimum.

2.8 THE NIGERIAN STOCK EXCHANGE

The Nigerian Stock Exchange was established in 1960 as the Lagos Stock Exchange. In December 1977 it became The Nigerian Stock Exchange, with branches established in some of the major commercial cities

of the country. As at the end of December 2002 there are six branches of The Nigerian Stock Exchange. Each branch has a trading floor. The branch in Lagos was opened in 1961; Kaduna, June 1978; Port Harcourt, April 1980; Kano, May 1989; Onitsha, February 1990; and Ibadan August 1990; Abuja Area office, October 1999 and Yola, April 2002 (Kurfi: 2003).

2.8.1 Listing Requirements in the Nigerian Stock Exchange

As reported by Kurfi (2003) the Exchange started operations in 1961 with 19 securities listed for trading. As at the end of December 2002, there were 257 securities listed on the Exchange, made up of 11 Government Stocks, 52 Industrial Loans (Debenture/Preference) stocks and 194 Equity/Ordinary shares of companies, with a total market capitalization of ₦730.0 billion. Many of the listed companies have foreign/multinational affiliations and represent a cross-section of the economy ranging from agriculture through manufacturing to services.

The market has in place a tested network of Stockbrokerage Firms, Issuing Houses (Merchant Banks), practicing corporate law firms and over 50 quality firms of auditors and reporting accountants (most with international links). The Stock Exchange and most of the nation's stock broking firms and issuing houses are staffed with creative financial engineers that can compete anywhere in the World. Therefore, the market has in place a network of intermediating organizations that can effectively and creditably meet the challenges and growing needs of investors in Nigerian (SEC: 2000).

2.8.1.1 First-Tier Securities Market (FSM)

As reported by Kurfi (2003) for a company's shares to be listed in the first-tier securities market of the NSE, the company must meet the following requirements:

[i] The company must be registered as a public limited company under the Companies And Allied Matters Act (CAMA ' 90).

[ii]All restrictive clauses on transfer of shares in memorandum and articles of association of the company must be expunged.

[iii] The company must submit to the Exchange audited financial statements and business records of the past five years, and the date of the last of such financial statements must not exceed nine months.

[iv] The company will be subjected to payments of annual listing fees, which is based on market capitalization.

[v] The amount of money that can be raised is unlimited depending on the financial strength of the company.

[vi] The number of shareholders of the company must not be less than 300.

[vii] At least 25% of the nominal value of the shares of the company must be offered to the public.

[viii] After listing, the company must submit quarterly, semi-annual and annual accounts to the Exchange for presentation to market operators.

[ix] Securities must be fully paid up at the time of allotment.

[x] Securities not allowed must be warehoused and sold on the floor of the Exchange.

The stringent listing requirements of the first-tier securities market could not be met by small and medium scale enterprises (SMEs) that are mostly indigenous companies. Therefore, in April 1985, the Exchange launched the Second-tier Securities Market (SSM) to allow SMEs enjoy the benefits of listing in the stock market.

2.8.1.2 Second-Tier Securities Market (SSM)

For a company's shares to be listed in the second-tier securities market of the NSE, the company must meet the following requirements (Kurfi 2003):

[i] The company must be registered as a public limited company under the Companies and Allied Matters Act (CAMA, 1990).

[ii] All restrictive clauses on transfer of shares in the memorandum and articles of association of the company must be expunged.

[iii] The company must submit to the Exchange audited financial statements and business records of the past three years, and the date of the last of such financial statements must not exceed nine months.

[iv] The company will be subjected to payments of a flat N50, 000.00 annual listing fees.

[v] The amount of money that can be raised is limited to N20 million subject to the financial strength of the company.

[vi[At least 10% of the nominal value of the shares of the company must be offered to the public.

[vii] The number of shareholders of the company must not be less than 100.

[viii] After listing, the company must submit semi-annual and annual accounts to the Exchange for presentation to market operators.

[ix] Securities must be fully paid up at the time of allotment.

[x] Securities not allotted must be warehoused and sold on the floor of the Exchange.

However, as for municipal and corporate bonds, some of the listing requirements in the Exchange include: a feasibility study report on the proposed project must be submitted to the Exchange; an annual listing fee will be payable based on the market value of the bonds outstanding; and the stock must be commercially attractive, that is, the yield should not be less than the Minimum Rediscount Rate (MRR) issued by the Central Bank of Nigeria (CBN).

2.8.1.3 Transaction In The Nigerian Stock Exchange

The Nigerian Stock Exchange has been operating an Automated Trading System (ATS) since April 27, 1999' with dealers trading through a network of computers connected to a server. And the clearing, settlement and delivery of transactions on the Exchange are done electronically by the Central Securities Clearing System Limited (CSCS), a subsidiary of the Nigerian Stock Exchange (Kurfi: 2003).

The Central Securities Clearing System Limited Commences operation on April 1997 providing automated clearing, settlement, delivery and custodian services. According to Kurfi (2003) the CSCS serves as:

[i] Central depository for share certificates of companies listed on the Nigerian Stock exchange.

[ii] Sub-registry for all quoted securities (in conjunction with registrars of quoted companies).

[iii] Issuer of central securities identification numbers to stockbrokers and investors.

[iv] Clearing and settlement of transactions.

[v] Custodian/Safe keeping for local and foreign instruments (in conjunction with custodian members).

Kurfi (2003) points out that before the establishment of the CSCS in the stock market, it took between 3-12 months to receive a share certificate. And there were a lot of manipulation due to long transaction circle, with minimum transparency and general lack of confidence in the system. However, with the establishment of the CSCS the efficiency in delivery and settlement system of the Nigerian capital market has been enhanced.

2.9 SUMMARY OF THE CHAPTER

From the foregoing discussions it can be seen that current state of the art on literature relevant to the area of study has been reviewed, to provide adequate and comprehensive analysis of the subject, as seen by other authors, with a view to properly ground this research topic in to it. This will go along way in ensuring the success of this research. This is in recognition of the fact that the success of any research effort largely depends upon the

extent to which the researcher capitalizes on the empirical and theoretical advances made by previous researches.

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CHAPTER THREE: RESEARCH METHODOLOGY

3.1 INTRODUCTION

This chapter explains the methods, techniques and instruments used in this research work. It also explains the method used in collecting and analyzing data. Items explained herein under include the research design, population of the study, sample size and sampling technique, administration of data collection instruments, procedures for processing collected data and a complete references for all works consulted.

3.2 RESEARCH DESIGN

A researcher uses research design to serve as a scheme or a blueprint for data collection, and to help him know how the variables will be observed, controlled or manipulated to generate necessary primary data for the study (Asika, 2001:27).

This research work uses exploratory cross-sectional survey research design for the purpose of obtaining data to enable the researcher test the research hypotheses. This method explores the relationship between variables in the population by selecting an unbiased sample and generalizing the findings on the entire population. The method is quite suitable for our study, because the study seeks to discover the relationship between internal controls system and corporate survival in the Nigerian Banking Industry. As explained by Asika (2001:29) one major characteristics of all survey designs is lack of control. The researcher is interested in observing what is happening to sample subjects or variables without any attempt to manipulate or control

them. Descriptive research design, which is a variant of survey design, involves one-time observation of independent and non-manipulated variables. Here the variable is corporate survival, which will be observed in relation to effectiveness or otherwise of the internal control system. It is worthy to mention that the exploratory design is a variant of descriptive design that is geared towards the collection of data for hypotheses testing with a view to discover and explained certain relationship between variables that creat a particular state of affairs (Asika, 2001:30).

3.3 POPULATION OF THE STUDY

This research work has as its population of study the entire banks that are quoted on the floor of the Nigerian Stock Exchange (NSE) as first-tier securities as at 28th March 2003. As indicated by the table in appendix v, there are a total of 28 of such banks as at 28th March 2003.

3.4 SAMPLE SIZE AND SAMPLING TECHNIQUES

The sample size of this study comprises of seven banks (representing 25 per cent) of the entire subjects of the population. This is done with a view to ensure that the sample estimate, as accurately as possible, the population characteristics, and serves as an accurate representative of the population from which it was drawn. In order to ensure an unbiased sample, every subject of the population was given an equal and independent chance of being selected in the sample. This was made possible by the use of systematic sampling techniques, which is a variant of probability sampling method.

The population of the study was serially listed in alphabetical order as shown below. To obtain the sample interval, the population of the study –28, was divided by the sample size - 7. After the division, 4, was arrived at as the sample interval. The 1st subject was randomly selected from the first 4 units, to serve as the starting point on the population list. Then the researcher selects every 4th unit after the first. This gave the sample list comprising of the 1st, 5th, 9th, 13th, 17th, 21st and 25th subjects on the population list. These are: Access Bank Nigeria PLC., Co-operative Development Bank PLC., First Bank of Nigeria PLC., Hallmark Bank PLC., Liberty Bank PLC., Omega Bank PLC. and United Bank For Africa PLC.

Systematic sampling technique was used with a view to ensure randomness and to eliminate the problems of imprecision and biasness that may arise if judgement/ non-probability sampling technique was used. The researcher was also of the opinion that since the sample subjects have similar characteristics, there is n question of typical cases, which may need to be represented in the sample. Therefore any sample drawn at random can serve as accurate representative of the population.

3.5 ADMINISTRATION OF DATA COLLECTION INSTRUMENTS

Asika (2001:105) opined that a data collection instrument is a device for collecting the data or measuring the variables, which are used for answering research questions and or testing study hypotheses. Questionnaires were administered on 420 respondents who have at least 5 years working

experience in the banking industry, 60 respondents from each bank. All the questions contained on the research instrument were closed ended questions, which provided options, to enable the respondents to answer and return the questionnaires in good time, and without much affecting their numerous banking commitments. The choice of the questionnaire as the research instrument was made due to the recognition that: it is cost effective, it places less pressure on the respondents for immediate response, and the respondents may have greater confidence on their anonymity and thus feel freer to express their views.

3.6 METHOD OF EDITING AND TABULATION OF DATA

Editing and tabulation of data is necessary in research work in order to make data meaningful and easy for analysis. Another reason, which calls for data editing and tabulation, is the issue of incomplete information supplied by respondents. Incompetence on the side of research assistants (if any) may call for data editing in order to remove errors that may cause inconsistencies if used in their original form.

In view of the above, the method adopted by the researcher in data editing is the use of both field editing and pre-coding (central) editing.

The method used in tabulation of data is one, which observes the following rules for tabular presentation:

i. **Title**: The tables have titles, which are brief, yet explanatory clearly stating the nature, classification and time reference of the information given. This is written on top of the table.

ii. **Number**: The tables in this research work are numbered to show their position in the series.

iii. **Captions and stubs**: 'Captions' are the designation placed over the vertical columns while 'stubs' are those at the left, opposite the horizontal lines of figures.

iv. **Units of measurement**: The unit of measurement is stated in the caption. But where it is self evident, it is not stated in the caption. Example of self-evident unit of measurement is expenditure (in millions of Naira).

v. **Ruling**: Vertical and horizontal ruling or lines are used to set figures apart in the tables used in presenting data in the research work.

vi. **Totals**: The totals are shown at the bottom of the table. Where two (2) or more significant sub-classifications are involved, subtotals may be shown before arriving at the grand totals.

3.7 DATA ANALYSIS TECHNIQUES

There are various forms of data analysis that can be used or employed by a researcher. For the purpose of this study, descriptive statistics, simple percentage, chi-square (x^2), spearman's rank order correlation (r_s) and t-statistics were used in analyzing collected data. This is with a view to enable the researcher to find whether or not there is relationship between internal controls system and corporate survival in the Nigerian banking industry.

In order to test the study hypotheses (which are of statistical nature) chi-square (x^2), spearman's rank order correlation (r_s) and t-statistics will be used. The decision rule for each of these techniques is as follows:

3.7.1 Chi-square Test

Formula: $x^2 = \Sigma \frac{(oi - ei)^2}{ei}$

Where: x^2 = chi – square

Σ = summation

oi = observed frequency

ei = expected frequency

The conditions precedent in the use of this statistical test of hypothesis are that, the number of respondents or observations must be sufficiently large (i.e.) not less than 20) and the expected frequency should not be less than 10.

The decision rule for this test is that, if the calculated x^2 value is less or equal to critical x^2 (i.e. from chi-square table) value for (r-1)(c-1) degrees of freedom at X level of significance, then the null hypothesis (H_O) is accepted while the alternative hypothesis (H_A) is rejected. Conversely, if the calculated x^2 value is greater than x^2 critical value for (r-1)(c-1) degrees of freedom at X level of significance, the null hypothesis (H_O) is rejected while the alternative hypothesis (H_A) is accepted (Asika, 2001:138).

3.7.2 spearman's rank order correlation (r_s) and t-statistics

Formula: $r_s = 1 - 6 \frac{\Sigma d^2}{n(n^2-1)}$

Where: r_S (rho) = spearman's rank order correlation

$\Sigma d^2 = \Sigma R(X_I) - R(Y_I)^2$

n=Number of observations.

The decision rule requires that for two-sided hypothesis, H_O should be rejected at the appropriate oc level, if the computed r_s is greater than the critical oc value corresponding to 1 – oc /2. Even by inspection one can conclude whether the correlation is positive, negative, high or low (Asika, 2001:143).

If, however, we want to know the strength of the relationship between X and Y variables, we may convert the Spearman rank correlation statistics to t statistics using the following formulae.

$$t=r_s \frac{\sqrt{n-2}}{1-r_s^2}$$

and use the result to test the hypothesis. The t statistic can only be used when the number of sample pairs is equal to or greater than 10. Otherwise only spearman rank order correlation is used (Asika, 2001:143).

Where: t=t statistic

$r_{s=}$ Spearman rank order correlation

n= Number of observations

√ = Square root

3.8 SUMMARY OF THE CHAPTER

In this chapter effort was made to explain the methodology adopted for the study. The chapter pointed out clearly the research design and the reasons for using such a design. Other things explained included the population of the study, sample size (and why in the opinion of the researcher the sample size is adequate to generalized findings), the sampling technique (and why such a technique is the most appropriate in this circumstance), administration of data collection instrument (and why the research instrument in question was used) and method used in analyzing collected data.

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CHAPTER FOUR
DATA PRESENTATION, ANALYSIS AND INTERPRETATION

4.1 INTRODUCTION

This chapter presents the analysis and interpretation of data collected through questionnaires administered on 420 respondents from the sample banks under investigation, and secondary data collected from NDIC reports and annual reports and accounts of some of the sample banks. The data was analyzed using both descriptive and statistical techniques. Thereafter the hypotheses of the study were tested to confirm or disconfirm them.

4.2 RELATIONSHIP BETWEEN FRAUD/FORGERIES AND IN-EFFECTIVE INTERNAL CONTROL

The table 4.2 below shows the number of reported cases of fraud in the Nigerian banking industry by NDIC from 1995 to 2002.

Table 4.2

Year	Total Amount Involved (₦'m)	Actual Expected Total Loss (₦'m)	R (Yi)	R (xi)	Di	di^2
***2002	12,919.55	1299.69	14	13	1	1
***2001	11,243.94	906.3	13	11	2	4
**2000	2,844.20	1,077.89	9	12	-3	9
*2000	6.91	2.68	2	1	1	1
**1999	6,369.69	2,713.50	12	14	-2	4

*1999	1,036.59	16.60	7	5	2	4
**1998	3,129.26	673.50	10	10	0	0
*1998	67.65	18.75	4	6	-2	4
**1997	3,590.31	224.54	11	7	4	16
*1997	187.59	2.90	5	3	2	4
**1996	1,542.91	371.08	8	9	-1	1
*1996	57.77	4.16	3	4	-1	1
**1995	1,006.28	226.38	6	8	-2	4
*1995	5.08	2.75	1	2	-1	1
					$\Sigma di^2=$	54

Sources: Computed from NDIC Annual Report 1995 – 2002.

Note:

*Merchant Banks

**Commercial Banks

*** Merchant and Commercial Banks Combined

To determine r_s, we apply the formula $r_s = 1 - \frac{6\Sigma d^2}{n(n^2-1)} = 0.8813$

Hence, $r_s = 0.8813$. To test the strength of the positive correlation (0.8813), we shall convert the "r_s" value to "t" scores. Thus, applying another formula:

$$t = r_s \frac{\sqrt{n-2}}{1-r_s^2} = 6.46$$ at degrees of freedom (df) =n-2=14-2= 12.

The critical value of "t" for significance level (α) 0.05 at 12df is 1.782. Therefore we reject the null hypothesis H_O at the 0.05 level of significance; that there is no relationship between fraud/forgeries and ineffective internal control systems of banks in Nigeria, and accept the alternate hypothesis H_A; that there is relationship between fraud/forgeries and ineffective internal control systems of banks in Nigeria.

4.3 RESPONDENTS CLASSIFICATIONS

The table below shows the number of respondents drawn from each bank in the sample list.

Table 4.3

Respondents classification	Number of Respondents from each Bank							
	Access Bank	Co-operative Development Bank	First Bank	Hallmark Bank	Liberty Bank	Omega Bank	United Bank For Africa	TOTAL
Management Staff	20	20	20	20	20	20	20	**140**
Operational Staff	20	20	20	20	20	20	20	**140**
Audit Staff	20	20	20	20	20	20	20	**140**
TOTAL	**60**	**60**	**60**	**60**	**60**	**60**	**60**	**420**

Source: Field Survey, 2004

From the table above it can be seen that a total of 420 questionnaires were administered on the respondents comprising of 60 from each bank. Out of the 60 respondents 20 comes from Management Staff, 20 from Operational/Banking Staff, and 20 from Audit staff. It should be noted however that the questionnaires were administered on different group of respondents to enable the researcher to generate requisite responses from the right people to enable him test his study hypotheses.

4.4 RESPONSES GENERATED

The table below shows the number of responses actually generated from the respondents drawn from each bank in the sample list.

Table 4.4

Respondents	Number of Respondents from each Bank

classification	Access Bank	Co-operative Development Bank	First Bank	Hallmark Bank	Liberty Bank	Omega Bank	United Bank For Africa	TOTAL
Management Staff	12	10	15	11	10	9	16	**83**
Operational Staff	17	17	17	16	16	15	18	**116**
Audit Staff	16	14	18	13	14	12	17	**104**
TOTAL	**45**	**41**	**50**	**40**	**40**	**36**	**51**	**303**

Source: Field Survey, 2004

From the table above it can be seen that out of the total of 420 questionnaires that were administered, only 303 were completed and returned. This number comprises of 83 from management staff, 116 from banking/operations staff and 104 from audit staff. From the table it can be seen that, while, united bank for Africa PLC. has the highest number of questionnaires returned (51), Omega bank PLC. has the lowest number of 36 questionnaires returned.

4.5 THE ROLE OF EFFECTIVE INTERNAL CONTROL SYSTEM IN PREVENTING FRAUD AND OTHER ABUSES IN THE BANKING INDUSTRY

In order to determine the role of effective internal control system in preventing fraud and other abuses in the banking industry, 140 questionnaires were administered on the operation/banking staff of the selected banks. Out of this number only 116 (representing 82.86%) were completed and returned. The table below shows the analysis of the responses generated from the 116 respondents.

Table 4.5.1

S/No. of Question	Question Frame	Yes	No	Total
1.	Are you fully aware of policies and procedures affecting your duties and responsibilities?	85	31	116
		73.28	26.72	100%
2.	Do you take into account relevant internal and	90	26	116

	external market information about events and conditions before granting a credit facility to a customer?	77.59	22.41	100%
3.	Do you belief that adequate measures are put in place to ensure effectiveness and efficiency in your bank operations to protect the bank from loss.	106	10	116
		91.38	8.62	100%
4.	Can you say that your activities conducted in compliance with applicable laws and regulations, supervisory requirements and internal policies and procedures?	107	9	116
		92.24	7.76	100%
5.	In your opinion, do you think the staff of your Bank possessed the cognate experience and technical capabilities to discharge their responsibilities effectively?	90	26	116
		77.59	22.41	100%
6.	Can you say that your bank is properly compensating you and your training and skills periodically updated?	80	36	116
		68.97	31.03	100%
7.	Are you satisfied with the ethical values of your bank management displays in their business dealings, both inside and outside the organization?	96	20	116
		82.76	17.24	100%
8.	Are your bank operational procedures contained in clearly written documentation that is made available to all relevant personnel?	83	33	116
		71.55	28.45	100%
9.	Are there well-established limit of transactions for all categories of staff in your Bank?	108	8	116
		93.10	6.90	100%
10.	If your answer in question (9) above is "Yes", are approvals and authorizations required for transactions over certain limits to ensure that an appropriate level of management is aware of the transaction or situation in order to establish accountability?	108	8	116
		93.10	6.90	100%
11.	Are control activities an integral part of the daily functions of all-relevant personnel in your Bank?	102	14	116
		87.93	12.07	100%
12.	Can you say that internal control system can help in detection of errors /fraud and other abuses in the banking industry?	102	14	116
		87.93	12.07	100%

Source: Field Survey, 2004

Table 4.5.2 Analysis of Positive Responses

Serial Number of Question	Number of Respondents from each Bank that answered "Yes"							
	Access Bank	Co-operative Development Bank	First Bank	Hallmark Bank	Liberty Bank	Omega Bank	United Bank For Africa	TOTAL
1.	14	11	10	12	13	11	14	85
2.	15	12	11	12	13	12	15	90
3.	17	14	16	15	15	12	17	106
4.	17	14	17	15	14	13	17	107
5.	14	12	14	12	13	11	14	90
6.	13	10	12	11	13	9	12	80
7.	15	12	15	13	14	11	16	96
8.	13	11	13	11	13	9	13	83

9.	17	14	17	15	14	13	18	108
10.	17	14	17	15	14	13	18	108
11.	16	13	17	14	13	12	17	102
12.	15	14	17	14	13	13	16	102
TOTAL	183	151	176	159	162	139	187	1,157

Source: Field Survey, 2004

From table 4.5.2 above, it can be seen that out of (12x116=1392) 1392 responses on questions that borders that borders on the role of effective internal control system in preventing/detecting fraud and other abuses in the Nigerian banking industry, 1157 responses (representing 83.12%) are in affirmative.

Table 4.5.3 Chi-square Test Computation $X^2 = \frac{(Oi - ei)^2}{ei}$

O	**E**	**O – e**	**$(Oi - ei)^2$**	**$\frac{(Oi - ei)^2}{ei}$**
15	$\frac{20 \times 102}{140}$ 14.57	0.43	0.1849	0.0127
14	$\frac{20 \times 102}{140}$ 14.57	-0.57	0.3249	0.0223
17	$\frac{20 \times 102}{140}$ 14.57	2.43	5.9049	0.4053
14	$\frac{20 \times 102}{140}$ 14.57	-0.57	0.3249	0.0223
13	$\frac{20 \times 102}{140}$ 14.57	-1.57	2.4649	0.1692
13	$\frac{20 \times 102}{140}$ 14.57	-1.57	2.4649	0.1692
16	$\frac{20 \times 102}{140}$ 14.57	1.43	2.0449	0.1404
X^2				**0.9414**
Degrees of freedom = (r-1)(c-1)=(7-1)(2-1)= 6 degrees of freedom				

Source: Field Survey, 2004

Analyzing the data, we realize that the value from the chi-square table at 99% confidence level is 0.872, while from our computation using the table above X^2 = 0.9414. From the observed frequency, we can see that the

computed chi-square X^2 is 0.9414 which is greater than X^2 using 99% confidence level at 6 degrees of freedom = 0.872. Since the computed value of the chi-square X^2 is greater, we reject the Ho (of hypothesis two) and accept the alternate hypothesis H_A that effective Internal control system helps in the detection of fraud and other abuses in the banking industry.

4.6 THE ROLE OF EFFECTIVE INTERNAL CONTROL SYSTEM IN ENSURING COMPLIANCE WITH LAID DOWN PROCEDURES IN THE BANKING INDUSTRY

In an attempt to determine the role of effective internal control system in ensuring compliance with laid down procedures in the Nigerian banking industry, 140 questionnaires were administered on internal audit staff of the selected banks. Out of this number, only 104 questionnaires (representing 74.29%) were completed and returned. The analyses of the responses are shown in tables 4.6.1 and 4.6.2 below.

Table 4.6.1

S/No. of Question	Question Frame	Yes	No	Total
1.	Are you aware of your role in internal control process and fully engaged in it?	**54**	**50**	**104**
		51.92%	**48.08%**	**100%**
2.	Are there adequate checks and balances and control in the activities and operations of your bank?	**94**	**10**	**104**
		90.39%	**09.61%**	**100%**
3.	Are you satisfied with the CIPAC (conception, initiation, processing, authorization and custody) circle of your operation? Can you say that there is adequate segregation of duties?	**96**	**08**	**104**
		92.31%	**07.69%**	**100%**
4.	Are the information systems in your bank secured and periodically tested to ensure to ensure maximum protection of funds?	**80**	**24**	**104**
		76.92%	**23.08%**	**100%**
5.	Can you say that you are satisfied with the level of effectiveness of your bank's internal audit and your activities are carried out in accordance with management policies?	**94**	**10**	**104**
		90.39%	**09.61%**	**100%**
6.	Are internal audit reports given adequate attention by	**100**	**04**	**104**

	your bank's Board of Directors or its audit committee and senior management?	**96.15%**	**03.85%**	**100%**
7.	Are identified internal control deficiencies reported in a timely manner to the appropriate management level and addressed promptly?	**100**	**04**	**104**
		96.15%	**03.85%**	**100%**
8.	Can you say that your bank internal control system is consistent with the nature, complexity and risk of your activities and responds to changes in the bank's environment and conditions?	**86**	**18**	**104**
		82.69%	**17.31%**	**100%**
9.	Are your Bank assets and other resources adequately safeguarded against unauthorized acquisition, use or disposition, or loss?	**96**	**08**	**104**
		92.31%	**07.69%**	**100%**
10.	Can you say that your annual accounts and other financial-related disclosures, including those for regulatory reporting and other external uses are reliably and the recipients can rely on it for making decisions?	**80**	**24**	**104**
		76.92%	**23.08%**	**100%**
11.	Can you say that there are no communication gaps in reporting lines and that an effective level of management control is extended to all levels of your Bank and its activities?	**68**	**36**	**104**
		65.39%	**34.61%**	**100%**
12.	Can you say that relevant duties within your bank are adequately splitted among various individuals in order to reduce the risk of manipulation of financial data or misappropriation of assets?	**100**	**04**	**104**
		96.15%	**03.85%**	**100%**
13.	Are there adequate safeguard to risk associated to electronic information systems and the use of information technology to avoid disruptions to business and potential losses in your Bank?	**90**	**14**	**104**
		86.54%	**13.46%**	**100%**
14.	Can you say that your bank's internal control system is effective and its plays a role in ensuring compliance with statutory regulations?	**91**	**13**	**104**
		87.50%	**12.50%**	**100%**

Source: Field Survey, 2004

Table 4.6.2

Serial Number of Question	Number of Respondents from each Bank that answered "Yes"							
	Access Bank	Co-operative Development Bank	First Bank	Hallmark Bank	Liberty Bank	Omega Bank	United Bank For Africa	TOTAL
1.	8	7	10	7	7	6	9	54
2.	14	13	16	12	13	11	15	94
3.	15	13	17	12	13	11	15	96
4.	12	11	14	10	11	9	13	80
5.	14	13	16	12	13	11	15	94
6.	15	14	17	13	13	12	16	100
7.	15	14	17	13	13	12	16	100
8.	13	16	15	11	12	10	9	86
9.	15	13	17	12	13	11	15	96
10.	12	11	14	10	11	9	13	80
11.	10	9	12	9	9	8	11	68
12.	15	14	17	13	13	12	16	100

13.	13	12	15	12	12	11	15	90
14.	13	11	15	12	13	11	16	91
TOTAL	184	171	212	158	166	144	194	1229

Source: Field Survey, 2004

From table 4.6.2 above, it can be seen that out of (14x104=1456) 1,456 responses on questions that borders on the role of effective internal control system in ensuring compliance with laid down procedures in the Nigerian Banking industry, 1229 responses (representing 84.41%) were in affirmative.

Table 4.6.3 Chi-square Test Computation $X^2 = \frac{(Oi - ei)^2}{ei}$

O	E	O – e	$(Oi - ei)^2$	$\frac{(Oi - ei)^2}{ei}$
13	$\frac{20 \times 91}{140}$ 13	0	0	0
11	$\frac{20 \times 91}{140}$ 13	-2	4	0.3077
15	$\frac{20 \times 91}{140}$ 13	2	4	0.3077
12	$\frac{20 \times 91}{140}$ 13	-1	1	0.0769
13	$\frac{20 \times 91}{140}$ 13	0	0	0
11	$\frac{20 \times 91}{140}$ 13	-2	4	0.3077
16	$\frac{20 \times 91}{140}$ 13	3	9	0.6963
X^2				**1.6963**
Degrees of freedom = (r-1)(c-1)=(7-1)(2-1)= 6 degrees of freedom				

Source: Field Survey, 2004

Analyzing the data, we realize that the value from the chi-square table at 99% confidence level is 0.872, while from our computation using the table above X^2 = 1.6963. From the observed frequency, we can see that the computed chi-square X^2 is 1.6963 which is greater than X^2 using 99% confidence level at 6 degrees of freedom = 0.872. Since the computed value of the chi-square X^2 is greater, we reject the Ho (of hypothesis three) and

accept the alternate hypothesis H_A that effective internal control system ensures compliance with laid down procedures in the banking industry. The level of confidence was varied to 98% and 95% with a view to determine the effects of each of the variations on the conclusion reached. It was observed from the chi-square table that X^2 =1.134 and 1.635 respectively. Both the two values are below the computed X^2 value of 1.6963.This means that the conclusion still holds using 98% and 95% level of confidence.

4.7 RELATIONSHIP BETWEEN INTERNAL CONTROLS SYSTEM AND CORPORATE SURVIVAL

In order to determine the relationship between internal controls system and corporate survival of banks in Nigeria, 140 questionnaires were administered on the management staff of the selected banks. Out of this number only 83 (representing 82.86%) were completed and returned. The table below shows the analysis of the responses generated from the 116 respondents.

Table 4.7.1 Classification Of Responses

S/No. of Question	Question Frame	Satisfied	More Satisfied	Strongly Satisfied	TOTAL
1.	Are you satisfied with the responsibility of your bank's Board of Directors in terms of approving strategies and policies, understanding and setting acceptable levels for the risk run by the bank, ensuring that senior management takes steps to monitor and control the bank's risks and effectiveness of internal control system?	**13**	**20**	**50**	**83**
		15.66	24.10	60.24	100%
2.	Are you satisfied with the responsibility of your bank senior management in terms of implementing strategies approve by the	15	16	52	**83**

	board, setting appropriate internal control policies, and monitoring the effectiveness of the internal control system?	18.07	19.28	62.65	100%
3.	How would you explain the attitude of your Board of Directors and senior management in promoting high ethical and integrity standards in your bank?	12	13	58	**83**
		14.46	15.66	69.88	100%
4.	Are you satisfied with the way your bank, either at head office or branch level, identify and evaluate factors that could adversely affect the attainment of your objectives?	18	20	45	**83**
		21.69	24.10	54.21	100%
5.	Are you satisfied with the way your bank internal control systems is revised to appropriately address any new or previously uncontrolled risks?	11	18	54	**83**
		13.25	21.69	65.06	100%
6.	How would you describe the way your bank senior management continuously monitors the overall effectiveness of the bank's internal controls in helping to achieve the bank's objectives?	14	15	54	**83**
		16.87	18.07	65.06	100%
7.	Are you satisfied with the way the management of your bank follow up on recommendations and concerns expressed by auditors and supervisory authorities on internal control weaknesses?	5	8	70	**83**
		6.02	9.64	84.34	100%
8.	Are you satisfied with the role of the internal control system in establishing prudent limits on risk exposure in your Bank?	11	12	60	**83**
		13.25	14.46	72.29	100%
9.	Are you satisfied with the role of your bank's internal control system in ensuring cost effectiveness in operations, sustaining the confidence of depositors and shareholders, response to the increasingly hostile banking environment, making your bank more attractive to depositors and shareholders and achieving operational excellence by minimizing overhead cost?	8	9	66	**83**
		9.64	10.84	79.52	100%
10.	How would you describe the role of your internal control system to the attainment of your bank's objectives and prevention/detection of fraud?	0	24	59	**83**
		0	28.92	71.08	100%
11.	If your answer in question (10) above is either "satisfied" or "highly satisfied " can you say that you are satisfied with the profit and other performance indices of your bank in the last 3 years?	0	20	63	**83**
		0	24.10	75.90	100%
12.	Are you satisfied with the role of your bank internal control system in ensuring the corporate survival of the bank?	11	7	65	**83**
		13.25	8.44	78.31	100%

Source: Field Survey, 2004

Table 4.7.2 Analysis Of Responses On Bank Basis

S/No. of Question	Opinion of Respondents	NUMBER OF RESPONDENTS FROM EACH BANK								
		Access Bank	Co-operative Development Bank	First Bank	Hallmark Bank	Liberty Bank	Omega Bank	United Bank For Africa	SUB TOTAL	TOTAL
1	Satisfied	2	1	2	2	1	2	3	13	
	More Satisfied	3	2	3	3	3	3	3	20	
	Highly Satisfied	7	7	10	6	6	4	10	50	83
2	Satisfied	2	2	2	1	2	3	3	15	
	More Satisfied	1	2	3	2	3	2	3	16	
	Highly Satisfied	9	6	10	8	5	4	10	52	83
3	Satisfied	2	1	2	1	1	2	3	12	
	More Satisfied	2	2	1	2	2	1	3	13	
	Highly Satisfied	8	7	12	8	7	6	10	58	83
4	Satisfied	2	2	3	1	2	3	5	18	
	More Satisfied	3	2	3	3	3	3	3	20	
	Highly Satisfied	7	6	9	7	5	3	9	45	83
5	Satisfied	2	1	2	3	0	2	1	11	
	More Satisfied	2	2	3	3	2	2	4	18	
	Highly Satisfied	8	7	10	5	8	5	11	54	83
6	Satisfied	2	2	2	2	1	3	2	14	
	More Satisfied	3	2	2	2	1	3	2	15	
	Highly Satisfied	7	6	11	7	8	3	12	54	83
7	Satisfied	0	1	0	2	0	1	1	5	
	More Satisfied	1	1	1	1	1	1	2	8	
	Highly Satisfied	11	8	14	8	9	7	13	70	83
8	Satisfied	2	1	2	1	2	2	1	11	
	More Satisfied	2	2	1	2	1	2	2	12	
	Highly Satisfied	8	7	12	8	7	5	13	60	83
9	Satisfied	1	1	1	1	1	1	2	8	

	More Satisfied	0	2	2	1	2	0	2	**9**	
	Highly Satisfied	11	7	12	9	7	8	12	**66**	**83**
10	Satisfied	0	0	0	0	0	0	0	**0**	
	More Satisfied	3	3	4	4	4	3	3	**24**	
	Highly Satisfied	9	7	11	7	6	6	13	**59**	**83**
11	Satisfied	0	0	0	0	0	0	0	**0**	
	More Satisfied	2	3	3	2	4	4	2	**20**	
	Highly Satisfied	10	7	12	9	6	5	14	**63**	**83**
12	Satisfied	3	1	1	1	1	1	3	**11**	
	More Satisfied	0	1	2	1	1	2	0	**7**	
	Highly Satisfied	9	7	12	9	8	6	14	**65**	**83**
TOTAL		144	**119**	**180**	**132**	**120**	**108**	**194**	**996**	**996**

Source: Field Survey, 2004

From table 4.7.2 above, it can be seen that a total of (12x83=996) 996 responses on questions that borders on the relationship between internal control system and corporate survival of banks in Nigeria were received. All of these responses expressed satisfaction at various levels on the relationship between internal control system and corporate survival.

Table 4.7.3 Chi-square Test Computation $X2 = \frac{(Oi - ei)^2}{ei}$

Opinion of Respondents	**Access Bank**	**Co-operative Development Bank**	**First Bank**	**Hallmark Bank**	**Liberty Bank**	**Omega Bank**	**United Bank For Africa**	**TOTAL**
Satisfied	3	1	1	1	1	1	3	**11**
More Satisfied	0	1	2	1	1	2	0	**7**
Highly Satisfied	9	7	12	9	8	6	14	**65**
TOTAL	**12**	**9**	**15**	**11**	**10**	**9**	**17**	**83**

Source: Field Survey, 2004

4.7.3.1 Calculations Of Expected Cell Frequencies using the equation,

$Eij = \frac{ni \times nj}{n}$ (n=83)

Opinion of Respondents	**Access Bank**	**Co-operative Development Bank**	**First Bank**	**Hallmark Bank**	**Liberty Bank**	**Omega Bank**	**United Bank For Africa**
Satisfied	$\frac{11 \times 12}{}$	$\frac{11 \times 9}{}$	$\frac{11 \times 15}{}$	$\frac{11x11}{}$	$\frac{11x 10}{}$	$\frac{11 \times 9}{}$	$\frac{11x 17}{}$

	83	83	83	83	83	83	83
More Satisfied	$\frac{7 \times 12}{83}$	$\frac{7 \times 9}{83}$	$\frac{7 \times 15}{83}$	$\frac{7 \times 11}{83}$	$\frac{7x10}{83}$	$\frac{7 \times 9}{83}$	$\frac{7 \times 17}{83}$
Highly Satisfied	$\frac{65 \times 12}{83}$	$\frac{65 \times 9}{83}$	$\frac{65 \times 15}{83}$	$\frac{65x11}{83}$	$\frac{65x10}{83}$	$\frac{65 \times 9}{83}$	$\frac{65 x17}{83}$

4.7.3.2 Expected Frequency Table

Opinion of Respondents	Access Bank	Co-operative Development Bank	First Bank	Hallmark Bank	Liberty Bank	Omega Bank	United Bank For Africa	TOTAL
Satisfied	1.59	1.19	1.99	1.46	1.33	1.19	2.25	**11**
More Satisfied	1.01	0.76	1.26	0.93	0.84	0.76	1.44	**7**
Highly Satisfied	9.40	7.05	11.75	8.61	7.83	7.05	13.31	**65**
TOTAL	**12**	**9**	**15**	**11**	**10**	**9**	**17**	**83**
Degrees of freedom = (r-1)(c-1)=(3-1)(7-1)= (2)(6)=12 degrees of freedom								

Using the equation, $X^2 = \frac{(Oi - ei)^2}{ei}$

Values for $X^2 = \frac{(Oi - ei)^2}{ei}$

For n11 – n17 = $\frac{(3-1.59)^2}{1.59} + \frac{(1-1.19)^2}{1.19} + \frac{(1-1.99)^2}{1.99} + \frac{(1-1.46)^2}{1.46} + \frac{(1-1.33)^2}{1.33} + \frac{(1-1.19)^2}{1.19} + \frac{(3-2.25)^2}{2.25} +$

For n21- n27 = $\frac{(0-1.01)^2}{1.01} + \frac{(1-0.76)^2}{0.76} + \frac{(2-1.26)^2}{1.26} + \frac{(1-0.93)^2}{0.93} + \frac{(1-0.84)^2}{0.84} + \frac{(2-0.76)^2}{0.76} + \frac{(0-1.44)^2}{1.44} +$

For n 31- n37= $\frac{(9-9.40)^2}{9.40} + \frac{(7-7.05)^2}{7.05} + \frac{(12-11.75)^2}{11.75} + \frac{(9-8.61)^2}{8.61} + \frac{(8-7.83)^2}{7.83} + \frac{(6-7.05)^2}{7.05} + \frac{(14-13.31)^2}{13.31}$

The summation of Values for $X^2 = \frac{(Oi - ei)^2}{ei}$ gives us

1.250+0.030+0.824+0.145+0.082+0.030+0.250+

1.010+0.076+0.435+0.005+0.030+1.316+1.440+

0.017+0.000+0.005+0.018+0.004+0.156+0.036= 7.16

Analyzing the data, we realize that the value from the chi-square table at 99% confidence level is 3.571, while from our computation using the table above X^2 = 7.16. From the observed frequency, we can see that the computed chi-square X^2 is 7.16 which is greater than X^2 using 99% confidence level at 12 degrees of freedom = 3.571. Since the computed

value of the chi-square X^2 is greater, we reject the Ho (of hypothesis four) and accept the alternate hypothesis H_A, that effective internal control system ensures corporate survival of banks in Nigeria. The level of confidence was varied to 95% with a view to determine the effects of such variation on the conclusion reached. It was observed from the chi-square table that X^2 =5.266 using 95 level of confidence. This value is also below the computed X^2 value of 7.16. This means that the conclusion still holds using 95% level of confidence.

4.7.4 RELATIONSHIP BETWEEN PERFORMING LOANS/ADVANCES AND GROSS EARNINGS OF BANKS IN NIGERIA

The tables 4.7.4.1 and 4.7.4.2 below show the relationship between performing loans/advances (a measure of good internal control system, which is considered as an independent variable) and gross earnings (a measure of corporate survival, which is considered as a dependent variable). The tables 4.7.4.1 and 4.7.4.2 are computed from various years' results of First Bank Plc. and United Bank for Africa Plc. respectively (which are among the seven selected banks for this study).

Table 4.7.4.1

Financial Year	Gross Earnings Y (₦'m)	Performing Loans/Advances X (₦'m)	R (Yi)	R (xi)	di	di^2
2003	45,055	55,038	10	9	1	1
2002	41,717	59,778	9	10	-1	1
2001	29,098	45,111	8	8	0	0
2000	26,855	32,981	7	7	0	0
1999	17,767	31,150	6	6	0	0
1998	13,808	25,831	5	5	0	0
1997	--------	---------	1	1	0	0
1996	10,030	16,020	4	4	0	0

1995	8,271	11,818	3	3	0	0
1994	5,355	5,980	2	2	0	0
					$\Sigma di^2=$	2

Sources: Computed from First Bank Annual Reports 1994 – 2003.

To determine r_s, we apply the formula: $r_s = 1 - \frac{6\Sigma d^2}{n(n^2-1)} = 0.9897$

Hence, $r_s = 0.9897$. To test the strength of the almost perfect positive correlation (0.9897), we shall convert the "r_s" value to "t" scores. Thus, applying another formula:

$$t = r_s \frac{\sqrt{n-2}}{1-r_s^2} = 17.99$$ at degrees of freedom (df) =n-2=10-2= 8.

The critical value of "t" for significance level ( ) 0.05 at 8df is 1.860. Therefore it can be concluded that there is a direct positive relationship between gross earnings and performing loans/advances of banks in Nigeria. We reject the Ho (of hypothesis four) at 0.05 level of significance: that effective internal controls system cannot ensure corporate survival of banks in Nigeria and accept the alternate hypothesis H_A: that effective internal controls system can ensure corporate survival of banks in Nigeria. Change in the level of significance to 0.100,0.025,0.010 and 0.005 at 8df will give 1.397, 2.306, 2.896 and 3.355 respectively, thus holding the above conclusion.

Table 4.7.4.2

Financial Year	Gross Earnings Y (₦'m)	Performing Loans/Advances X (₦'m)	R (Yi)	R (xi)	di	di^2
2003	23,720	45,932	10	10	0	0

2002	22,112	39,764	9	9	0	0
2001	19,148	22,846	8	7	1	1
2000	18,701	16,811	7	6	1	1
1999	10,650	24,331	6	8	-2	4
1998	7,850	16,608	5	5	0	0
1997	7,276	10,749	4	4	0	0
1996	6,976	8,819	3	3	0	0
1995	4,640	6,077	2	2	0	0
1994	3,629	5,012	1	1	0	0
					$\Sigma di^2=$	6

Sources: Computed from UBA Plc. Annual Reports 1994 – 2003.

To determine r_s, we apply the formula: $r_s = 1 - \frac{6\Sigma d^2}{n(n^2-1)} = 0.9963$

Hence, $r_s = 0.9963$. To test the strength of the almost perfect positive correlation (0.9963), we shall convert the "r_s" value to "t" scores. Thus, applying another formula:

$$t = r_s \frac{\sqrt{n-2}}{1-r_s^2} = 32.76$$ at degrees of freedom (df) =n-2=10-2= 8.

The critical value of "t" for significance level ( ) 0.05 at 8df is 1.860. Therefore it can be concluded that there is a direct positive relationship between gross earnings and performing loans/advances of banks in Nigeria. We reject the Ho (of hypothesis four) at 0.05 level of significance: that effective internal controls system cannot ensure corporate survival of banks in Nigeria and accept the alternate hypothesis H_A: that effective internal controls system can ensure corporate survival of banks in Nigeria. Change in the level of significance to 0.100,0.025,0.010 and 0.005 at 8df will give 1.397, 2.306, 2.896 and 3.355 respectively, thus holding the above conclusion true.

4.7.5 RELATIONSHIP BETWEEN NON-PERFORMING LOANS/ADVANCES AND GROSS EARNINGS OF BANKS IN NIGERIA

The table 4.7.5.1 below shows the relationship between non-performing loans/advances (a measure of weak internal control system, which is considered as an independent variable) and gross earnings (a measure of corporate survival, which is considered as a dependent variable). The table is computed from various years' results of United Bank for Africa Plc. (which is among the seven selected banks for this study).

Table 4.7.5.1

Financial Year	Gross Earnings Y (₦'m)	Non-Performing Loans/Advances X (₦'m)	R (Yi)	R (xi)	di	di^2
2003	23,720	3,398	10	8	2	4
2002	22,112	1,230	9	1	8	64
2001	19,148	3,890	8	10	-2	4
2000	18,701	3,858	7	9	-2	4
1999	10,650	2,761	6	6	0	0
1998	7,850	2,046	5	2	-3	9
1997	7,276	2,382	4	3	1	1
1996	6,976	2,684	3	4	-1	1
1995	4,640	2,719	2	5	-3	9
1994	3,629	2,825	1	7	-3	36
					Σdi^2=	132

Sources: Computed from UBA Plc. Annual Reports 1994 – 2003.

To determine r_s, we apply the formula: $r_s = 1 - \frac{6\Sigma d^2}{n(n^2-1)} = 0.2$

Hence, $r_s = 0.2$. To test the strength of the correlation (0.2), we shall convert the "r_s" value to "t" scores. Thus, applying another formula:

$$t = r_s \frac{\sqrt{n-2}}{1-r_s^2} = 1.66$$ at degrees of freedom (df) =n-2=10-2= 8.

The critical value of "t" for significance level (α) 0.05 at 8df is 1.860. Therefore it can be concluded that there is no direct positive relationship between gross earnings and performing loans/advances of banks in Nigeria. We reject the Ho (of hypothesis four) at 0.05 level of significance: that effective internal controls system does not ensure corporate survival of banks in Nigeria and accept the alternate hypothesis H_A: that effective internal controls system ensures corporate survival of banks in Nigeria. Change in the level of significance to 0.025,0.010 and 0.005 at 8df will give 2.306, 2.896 and 3.355 respectively, thus holding the above conclusion true.

4.8 SUMMARY OF THE CHAPTER

This chapter presented and analyzed the data collected through questionnaires administered on respondents, and secondary data collected from NDIC annual reports and annual reports and accounts of two of the case studies of this research. The result of the analysis made rejected all the null hypotheses in the study and accepted the alternate hypotheses. Thus, it was found that there is relationship between ineffective internal controls system and fraud/forgeries of banks in Nigeria, and that effective internal controls system helps in the detection of fraud and other abuses in the banking industry; effective internal control system ensures compliance with laid down procedures; and ensures corporate survival of banks in Nigeria.

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CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

From the review of related literature and the results of data analysis presented in chapter two and four of this research work, the following summary, conclusion and recommendations are presented.

5.1 SUMMARY

5.1.1 Summary of the Work Done

Chapter one of this research work introduces the topic under investigation. It discussed the Background of the study, problems statement, objectives(s) settings, scope description, hypotheses, significance of the study, limitations and definition of key terms.

Chapter two dealt with the literature review. Here all relevant works were reviewed, concentrating on the findings and recommendations of the authors of the works and expressing opinion(s) more especially, the recommendations. Relevant textbooks, journals, magazines and newspapers, websites were reviewed.

Chapter three explained the methodology used in conducting the research. It discussed the population of the study, the sampling technique, sample size, methods of data collection, methods of data editing, and techniques of data analysis.

Chapter four discussed the method of data presentation, analysis and interpretation. It also shows the real data analysis made, the techniques that were involved, the results obtained, and the conclusions reached.

Chapter five concluded the study by highlighting the major work done and the major findings of the work. Conclusions were drawn based on the findings and recommendations for improvement/betterment or correction of lapses were made accordingly.

5.1.2 Summary of The Major Findings

The following are the summary of the major findings of this research work

[1] The study has established that there is direct positive relationship between ineffective internal control system and fraud/forgeries of banks in Nigeria. It has also been found that there is an almost perfect positive relationship between performing loans/advances and gross earnings/profitability of banks in Nigeria.

[2] Evidence from the NDIC report regarding fraud in the banking industry reveals that the phenomenon has been on the upward trend despite the control measures put in place by the individual banks.

[3] Evidence abound to show that Internal control is not solely a procedure or policy that is performed at a certain point in time, but rather a process that should be continually operating at all levels within a bank. However, each individual within an organization must participate in the process. The board of directors and senior management are responsible for establishing the appropriate culture to facilitate an effective internal control process.

[4] Every good system of internal control must be able to assist the organization carry on its business in an effective and efficient manner. It must be capable of sustaining credible adherence to management's policies, safeguard its assets, and be able to guarantee complete recording of all its business transactions. A good system must exist to correlate responsibility with authority regarding the whole process of financial reporting and other spheres of the organization's activity.

[5] A system of effective controls is a critical component of a bank management and a foundation for safe and sound operation of banking organization. A system of strong internal controls can help to ensure that the goals and objectives of a banking organization will be met, that the bank will achieve long-term profitability targets, and maintain reliable financial and managerial reporting. Such a system can also help to ensure that the bank will comply with laws and regulations as well as policies, plans, internal rules and procedures, and decrease the risk of unexpected losses or damage to the bank's reputation.

[6] The internal control process seeks to ensure that personnel throughout the organization are working to achieve its objectives in a straight forward manner, without unintended or excessive cost or placing other interests (such as an employee's, vendor's or customer's interest before those of the bank).

[7] Effective Internal Control System ensures corporate survival of banks, helps in the detection of fraud and other abuses, and ensures compliance with statutory regulations.

[8] Many internal control failures that resulted in significant losses for banks could have been substantially lessened or even avoided if the board and senior management of the organizations had established strong control cultures. Senior management may weaken the control culture by promoting and rewarding managers who are successful in generating profits but fail to implement internal control policies or address problems identified by internal audit. Such actions send a message to others in the organization that internal control is considered secondary to other goals in the organization, and thus diminish the commitment to and quality of the control culture.

5.2 CONCLUSION

On the basis of the findings of this study, the following conclusions are hereby made.

[1] Management has the ultimate responsibility for an organization's internal control structure. Without their support, the internal control structure is unlikely to achieve its purpose.

[2] Designing an effective internal control system is an art not a science. Combinations of the following can be used in designing an internal control system: Organization, Policies, Procedures, Personnel, Accounting, Budgeting, Reporting and Internal Review.

[3] An effective internal control system in a banking organization ensures cost effectiveness in operations, sustains the confidence of depositors and shareholders thereby making the bank more attractive to them.

[4] Many banks that have experienced losses from internal control problems did not effectively monitor their internal control systems. Often the systems did not have the necessary built-in ongoing monitoring processes and the separate evaluations performed were either not adequate or were not acted upon appropriately by management.

5.3 RECOMMENDATIONS

On the basis of the findings of this study, the following recommendations are hereby made:

[1] All banking business should be conducted in compliance with applicable laws and regulations, supervisory requirements and internal policies and procedures, so as to protect the bank's franchise and reputation, which are necessary for its survival.

[2] Detection and prevention of fraud should be a collaborative effort between the bank, its shareholders, the public and the government.

[3] Management should institute an appropriate and properly integrated system of accounts and records. In addition, there should be frequent internal audit to monitor every transaction in a bank.

[4] Emphasis on maintaining effective internal control system should first start with the management, which is the first line of defence, next by independent auditors who provide the second defence and of course the regulatory authorities who provides the last defence layer. All banks should be instructed by the CBN to open internal control compliance section in their branches to monitor and ensure strict adherence and report any breach in the internal control system. To ensure adequate coverage of all banks branches nationwide, compliance officers have to be deployed to regional offices to co-ordinate the compliance activities in each region, whilst the Accountant, Assistant manager in each branch should acts as the compliance officers.

[5] Anti-money Laundering Policies and procedures should be put in place by all banks and necessary arrangements made to produce new account opening forms for customers in line with the requirements of the CBN's "know your customer" manual for banks and other financial institutions in Nigeria.

[6] All banks' managements should established prudent limits on risk exposure in their banks to prevent banks from huge losses that could result in their collapsed. In the recent past, inadequate risk assessment has contributed to some organizations' internal control problems and related losses. In some cases, the potential high yields associated with certain loans, investments, and derivative instruments distracted management from the

need to thoroughly assess the risks associated with the transactions and devote sufficient resources to the continual monitoring and review of risk exposures. Losses have also been caused when management has failed to update the risk assessment process as the organization's operating environment changed.

[7] Banks management should continuously identify and evaluate factors that could adversely affect the attainment of their objectives. They should ensure that internal control system is consistent with the nature, complexity and risk of their activities and responds to changes in the banks' environments and conditions.

[8] Banks should invest more in staff training to enable them possessed the cognate experience and technical capabilities to discharge their responsibilities effectively and to prepare them for the increased challenges of the industry.

[9] Operational procedures contained in clearly written documentation should be made available to every bank staff to enable him to be aware of his role in internal control process and fully engaged in it. This can also help to reduce communication gaps in all levels of banks' activities.

[10] In this information age, banks managements should ensure adequate safeguard to risk associated to electronic information systems and the use of information technology to avoid disruptions to business and potential losses to banks in Nigeria. The system should also be periodically tested to ensure maximum protection of funds.

[11] There should be an effective and comprehensive internal audit of the internal control system carried out by appropriately trained and competent staff. The internal audit function, as part of the monitoring of the system of internal controls, should report directly to the board of directors or its audit committee, and to senior management.

[12] Senior management should ensure that there are adequate and comprehensive internal financial, operational and compliance data, as well as external market information about events and conditions that are relevant to decision making. Information should be reliable, timely, accessible, and provided in a consistent format.

[13] Banks managements should ensure that the internal and external factors that could adversely affect the achievement of their objectives are being identified and evaluated. This assessment should cover all the various risks facing the banks (for example, credit risk, country and transfer risk, market risk, interest rate risk, liquidity risk, operational risk, legal risk and reputational risk).

[14] Banks managements should ensure that the risks affecting the achievement of their banks strategies and objectives are continually being evaluated. Internal controls may need to be revised to appropriately address any new or previously uncontrolled risks.

[15] Banks managements should ensure that there is appropriate segregation of duties and that personnel are not assigned conflicting responsibilities.

Areas of potential conflicts of interest should be identified, minimized, and carefully monitored.

[16] Banks structure should include appropriate consideration of the form and nature of its departments/units, the data processing organization, and related management functions and reporting relationships. In addition,

authority and responsibility within the bank should be assigned in an appropriate manner.

[17] An effective audit committee, or its equivalent, should take an active role in overseeing a bank's accounting and financial reporting policies and practices. The committee should assist management and the board of directors in fulfilling their fiduciary and accountability responsibilities, and it should help maintain a direct line of communication between the board and the bank's external and internal auditors.

[18] There should be an effective personnel management method, which should include a bank's policies and procedures for hiring, training, evaluating, promoting, and compensating employees, and providing them with the resources necessary to discharge their assigned responsibilities.

[19] Controls should be established and exercised by parties outside the banks (i.e. by NDIC, SEC, CBN); on areas that affects banks operations and practices. They should monitor compliance requirements imposed by legislative and regulatory bodies.

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APPENDIX I

QUESTIONNAIRE

FOR INTERNAL AUDIT STAFF OF THE SELECTED BANKS

TOPIC: **INTERNAL CONTROL SYSTEMS AND CORPORATE SURVIVAL IN THE NIGERIAN BANKING INDUSTRY: A STUDY OF SOME SELECTED BANKS**

Dear Respondent,

I am a Post Graduate Student of Ahmadu Bello University (ABU), Zaria, presently conducting a research on the above mentioned topic, as part of the requirements for the award of a Master of Science Degree in Accounting and Finance. It is In view of the above, that I humbly wish to request you to answer the questions raised on the attached questionnaire. All the questions have options from which you are required to tick. We will appreciate it if you give us the benefit of having your true feeling, as the success or otherwise of this study depend squarely on your response. All information supplied will be used for the purpose of the said research only and will be treated in the strictest confidence.

Thank you for sparing time to participate in the research work.

Signed
Kabir Tahir Hamid
M.Sc. / Admin. /32224/2001-2002

QUESTION 1

Are you aware of your role in internal control process and fully engaged in it?

[a] Yes [ ]
[b] No [ ]

QUESTION 2

Are there adequate checks and balances and control in the activities and operations of your bank?

[a] Yes [ ]
[b] No [ ]

QUESTION 3

Are you satisfied with the CIPAC (conception, initiation, processing, authorization and custody) circle of your operation? Can you say that there is adequate segregation of duties?

[a] Yes [ ]
[b] No [ ]

QUESTION 4

Are the information systems in your bank secured and periodically tested to ensure to ensure maximum protection of funds?

[a] Yes [ ]
[b] No [ ]

QUESTION 5

Can you say that you are satisfied with the level of effectiveness of your bank's internal audit and your activities are carried out in accordance with management policies?
[a] Yes [ ]
[b] No [ ]

QUESTION 6

Are internal audit reports given adequate attention by your bank's Board of Directors or its audit committee and senior management?
[a] Yes [ ]
[b] No [ ]

QUESTION 7

Are identified internal control deficiencies reported in a timely manner to the appropriate management level and addressed promptly?
[a] Yes [ ]
[b] No [ ]

QUESTION 8

Can you say that your bank internal control system is consistent with the nature, complexity and risk of your activities and responds to changes in the bank's environment and conditions?
[a] Yes [ ]
[b] No [ ]

QUESTION 9

Are your Bank assets and other resources adequately safeguarded against unauthorized acquisition, use or disposition, or loss?
[a] Yes [ ]
[b] No [ ]

QUESTION 10

Can you say that your annual accounts and other financial-related disclosures, including those for regulatory reporting and other external uses are reliably and the recipients can rely on it for making decisions?
[a] Yes [ ]
[b] No [ ]

QUESTION 11

Can you say that there are no communication gaps in reporting lines and that an effective level of management control is extended to all levels of your Bank and its activities?
[a] Yes [ ]
[b] No [ ]

QUESTION 12

Can you say that relevant duties within your bank are adequately splitted among various individuals in order to reduce the risk of manipulation of financial data or misappropriation of assets?
[a] Yes [ ]
[b] No [ ]

QUESTION 13

Are there adequate safeguard to risk associated to electronic information systems and the use of information technology to avoid disruptions to business and potential losses in your Bank?
[a] Yes [ ]
[b] No [ ]

QUESTION 14

Can you say that your bank's internal control system is effective and its plays a role in ensuring compliance with statutory regulations?

[a] Yes [ ]
[b] No [ ]

APPENDIX II

QUESTIONNAIRE

FOR OPERATIONS STAFF OF THE SELECTED BANKS

TOPIC: **INTERNAL CONTROL SYSTEMS AND CORPORATE SURVIVAL IN THE NIGERIAN BANKING INDUSTRY: A STUDY OF SOME SELECTED BANKS**

Dear Respondent,

I am a Post Graduate Student of Ahmadu Bello University (ABU), Zaria, presently conducting a research on the above mentioned topic, as part of the requirements for the award of a Master of Science Degree in Accounting and Finance. It is In view of the above, that I humbly wish to request you to answer the questions raised on the attached questionnaire. All the questions have options from which you are required to tick. We will appreciate it if you give us the benefit of having your true feeling, as the success or otherwise of this study depend squarely on your response. All information supplied will be used for the purpose of the said research only and will be treated in the strictest confidence.

Thank you for sparing time to participate in the research work.

Signed
Kabir Tahir Hamid
M.Sc. / Admin. /32224/2001-2002

QUESTION ONE

Are you fully aware of policies and procedures affecting your duties and responsibilities?

[a] Yes [ ]
[b] No [ ]

QUESTION 2

Do you take into account relevant internal and external market information about events and conditions before granting a credit facility to a customer?

[a] Yes [ ]
[b] No [ ]

QUESTION 3

Do you belief that adequate measures are put in place to ensure effectiveness and efficiency in your bank operations to protect the bank from loss?

[a] Yes [ ]
[b] No [ ]

QUESTION 4

Can you say that your activities conducted in compliance with applicable laws and regulations, supervisory requirements and internal policies and procedures?

[a] Yes [ ]
[b] No [ ]

QUESTION 5
In your opinion, do you think the staff of your Bank possessed the cognate experience and technical capabilities to discharge their responsibilities effectively?
[a] Yes [ ]
[b] No [ ]

QUESTION 6
Can you say that your bank is properly compensating you and your training and skills periodically updated?
[a] Yes [ ]
[b] No [ ]

QUESTION 7
Are you satisfied with the ethical values of your bank management displays in their business dealings, both inside and outside the organization?
[a] Yes [ ]
[b] No [ ]

QUESTION 8
Are your bank operational procedures contained in clearly written documentation that is made available to all relevant personnel?
[a] Yes [ ]
[b] No [ ]

QUESTION 9
Are there well-established limit of transactions for all categories of staff in your Bank?
[a] Yes [ ]
[b] No [ ]

QUESTION 10
If your answer in question (9) above is “Yes”, are approvals and authorizations required for transactions over certain limits to ensure that an appropriate level of management is aware of the transaction or situation in order to establish accountability?
[a] Yes [ ]
[b] No [ ]

QUESTION 11
Is there an established system of periodic reconciliation of accounts in your Bank?
[a] Yes [ ]
[b] No [ ]

QUESTION 12
Are control activities an integral part of the daily functions of all-relevant personnel in your Bank?
[a] Yes [ ]
[b] No [ ]

APPENDIX III

QUESTIONNAIRE

FOR MANAGEMENT STAFF OF THE SELECTED BANKS

TOPIC: **INTERNAL CONTROL SYSTEMS AND CORPORATE SURVIVAL IN THE NIGERIAN BANKING INDUSTRY: A STUDY OF SOME SELECTED BANKS**

Dear Respondent,

I am a Post Graduate Student of Ahmadu Bello University (ABU), Zaria, presently conducting a research on the above mentioned topic, as part of the requirements for the award of a Master of Science Degree in Accounting and Finance. It is In view of the above, that I humbly wish to request you to answer the questions raised on the attached questionnaire. All the questions have options from which you are required to tick. We will appreciate it if you give us the benefit of having your true feeling, as the success or otherwise of this study depend squarely on your response. All information supplied will be used for the purpose of the said research only and will be treated in the strictest confidence.

Thank you for sparing time to participate in the research work.

Signed
Kabir Tahir Hamid
M.Sc. / Admin. /32224/2001-2002

QUESTION 1

Are you satisfied with the responsibility of your bank's Board of Directors in terms of approving strategies and policies, understanding and setting acceptable levels for the risk run by the bank, ensuring that senior management takes steps to monitor and control the bank's risks and effectiveness of internal control system?

[a] Satisfied [ ]
[b] More Satisfied [ ]
[c] Highly Satisfied [ ]

QUESTION 2

Are you satisfied with the responsibility of your bank senior management in terms of implementing strategies approve by the board, setting appropriate internal control policies, and monitoring the effectiveness of the internal control system?

[a] Satisfied [ ]
[b] More Satisfied [ ]
[c] Highly Satisfied [ ]

QUESTION 3

How would you explain the attitude of your Board of Directors and senior management in promoting high ethical and integrity standards in your bank?

[a] Satisfied [ ]
[b] More Satisfied [ ]
[c] Highly Satisfied [ ]

QUESTION 4

Are you satisfied with the way your bank, either at head office or branch level, identify and evaluate factors that could adversely affect the attainment of your objectives?

[a] Satisfied [ ]
[b] More Satisfied [
[c] Highly Satisfied [ ]

QUESTION 5

Are you satisfied with the way your bank internal control systems is revised to appropriately address any new or previously uncontrolled risks?

[a] Satisfied [ ]
[b] More Satisfied [ ]
[c] Highly Satisfied [ ]

QUESTION 6

How would you describe the way your bank senior management continuously monitors the overall effectiveness of the bank's internal controls in helping to achieve the bank's objectives?

[a] Satisfied [ ]
[b] More Satisfied [ ]
[c] Highly Satisfied [ ]

QUESTION 7

Are you satisfied with the way the management of your bank follow up on recommendations and concerns expressed by auditors and supervisory authorities on internal control weaknesses?

[a] Satisfied [ ]
[b] More Satisfied [ ]
[c] Highly Satisfied [ ]

QUESTION 8

Are you satisfied with the role of the internal control system in establishing prudent limits on risk exposure in your Bank?

[a] Satisfied [ ]
[b] More Satisfied [ ]
[c] Highly Satisfied [ ]

QUESTION 9

Are you satisfied with the role of your bank's internal control system in ensuring cost effectiveness in operations, sustaining the confidence of depositors and shareholders, response to the increasingly hostile banking environment, making your bank more attractive to depositors and shareholders and achieving operational excellence by minimizing overhead cost?

[a] Satisfied [ ]
[b] More Satisfied [ ]
[c] Highly Satisfied [ ]

QUESTION 10

How would you describe the role of your internal control system to the attainment of your bank's objectives and prevention/detection of fraud?

[a] Satisfied [ ]
[b] More Satisfied [ ]
[c] Highly Satisfied [ ]

QUESTION 11

If your answer in question (10) above is either "satisfied" or "highly satisfied " can you say that you are satisfied with the profit and other performance indices of your bank in the last 3 years?

[a] Satisfied [ ]
[b] More Satisfied [ ]
[c] Highly Satisfied [ ]

QUESTION 12

Are you satisfied with the role of your bank internal control system in ensuring the corporate survival of the bank?

[a] Satisfied [ ]
[b] More Satisfied [ ]
[c] Highly Satisfied [ ]

APPENDIX IV

LIST OF ABBREVIATIONS

ATA – AUTOMATED TRADING SYSTEM

CAC- CORPORATE AFFAIRS COMMISSION

CBN- CENTRAL BANK OF NIGERIA

COSO- COMMITTEE FOR SPONSORING ORGANIZATION

CSCS – CENTRAL SECURITIES CLEARING SYSTEM LIMITED

FSM – FIRST-TIER SECURITIES MARKET

MRR – MINIMUM REDISCOUNT RATE

SMEs- SMALL AND MEDIUM SCALE ENTERPRISES

SRO- SELF-REGULATORY ORGANIZATIONS

SSM – SECOND-TIER SECURITIES MARKET

UB- UNIVERSAL BANK

NAICOM- NATIONAL INSURANCE COMMISSION

FSRCC- FINANCIAL SERVICES REGULATION COORDINATING COMMITTEE

NDIC- NIGERIAN DEPOSIT INSURANCE CORPORATION

SEC- SECURITIES AND EXCHANGE COMMISSION

NCM-NIGERIAN CAPITAL MARKET

NSE- NIGERIAN STOCK EXCHANGE

LTD- LIMITED [PRIVATE LIMITED LIABILITY COMPANY]

PLC- PUBLIC LIMITED LIABILITY COMPANY

CAMA- COMPANIES AND ALLIED MATTERS ACT

BOFIA- BANKS AND OTHER FINANCIAL INSTITUTIONS ACT

APPENDIX V

Banks Quoted On The Nigerian Stock Exchange

The following are the Banks that were quoted on the Nigerian Stock Exchange as First Tier Securities, as at 22/08/2003, as published by the authority of the Council of the Exchange.

S/No.	NAME OF BANK
1.	Access Bank Nigeria PLC.
2.	Afribank Nigeria PLC.
3.	African Express Bank Plc.
4.	Chartered Bank PLC.
5.	Co-operative Development Bank PLC.
6.	Co-operative Bank PLC.
7.	EIB International Bank PLC.
8.	First Atlantic Bank PLC.
9.	First Bank of Nigeria PLC.
10.	FSB International Bank PLC.
11.	Guaranty Trust Bank PLC.
12.	Gulf Bank Of Nigeria PLC.
13.	Hallmark Bank PLC.
14.	IMB International Bank PLC.
15.	Inland Bank (Nigeria) PLC.
16.	Intercontinental Bank PLC.
17.	Liberty Bank PLC.
18.	Lion Bank of Nigeria PLC.
19.	Manny Bank PLC.
20.	NAL Bank PLC.
21.	Omega Bank PLC.
22.	Savannah Bank PLC. **
23.	Trade Bank PLC.
24.	Trans International Bank PLC.
25.	United Bank For Africa PLC.
26.	Union Bank Nigeria PLC.
27.	Universal Trust Bank PLC.
28.	Wema Bank PLC.

SOURCE: Publication of the NSE dated 22/08/2003

**** Savannah Bank Nigeria PLC.**

Savannah Bank Nigeria PLC. Last transacted business on the floor of the NSE on 15/02/2002 and dividend was last paid to the shareholders on 12/10/99. Even though NDIC has sealed the Bank following the revocation of its licence, the matter is still lingering in the court, as the management of the Bank is challenging the revocation of the lecence arguing that it was politically inclined.

APPENDIX VI

NIGERIAN BANKING INDUSTRY IN YEAR 2002/03: AT A GLANCE

- 90 Licenced Banks
- 282 Community Banks
- 74 Primary Mortgage Institutions
- 6 Development Banks
- 10 Banks Dominate The Industry
- 39 Banks (43 per cent) met N1 billion Minimum Capital
- Savannah and Peak Merchant Banks Delicenced
- 21 Banks Indicted by CBN for forex Offences
- Total Penalty for the 21 banks amounted to $1.4 billion
- NDIC Reported N12.9 billion fraud-related cases
- Unsound banks total assets rose by 134 per cent (N170.93 billion by December 2003); 5.75 per cent of industry total
- Insider credit facility of unsound banks rose to N665 million to 13.65 billion
- CBN introduce direct sales of Traveler's Cheque
- Industry Profitability dropped from N95.12 billion to N93.20 billion
- 16 Out Of 90 Banks Failed To Insure Deposits

Source: The New Age, www.newage-online.com Monday, Dec. 8, 2003 p B29