Internal Controls Organization: A Methodology Approach

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Abstract: Internal controls is one of the main organization systems established to achieve business goals. Also, internal control lays in the area of audit committees and internal audit function.

Key words: Internal Control System • Internal Audit • Audit Committee

INTRODUCTION

As businesses grow, a need in internal control and audit is increasing [1]. Internal controls systems can be viewed as one of the criteria for a successful business; often they are concerned with many organization goals and not only pure controls [2, 3].

Also, these functions are gaining popularity among government sectors as well. Internal audit can be viewed as a voluntary controls system within a business established by its owners and instructed by its internal documents which overview accounting and internal controls functions.

Internal audit system can contain individual internal auditors, internal audit function, audit committees [4, 5].

Also, the terms of 'internal audit' and 'internal controls' are relatively new to a Russian company in contrast with developed countries as the latter have more experience in a relative field of controls and audit [6, 7].

Main Part: Internal control definition is not new; it originated in the beginning of 18th century and was formed by the start of the 20th century as a combination of three elements: delegation of duties, personnel rotation and accounting.

Afterwards, internal control systems were developing dramatically, transformed into organization and co-ordination of activities, aimed at the assets safeguard, accounting reviews, efficiency and effectiveness of operation, fulfillment of established policies and procedures.

Therefore, new functions increased the definition of internal control beyond the normal accounting problems. After its evolution, internal control has arrived as a risk control instrument and a risk management approach by the end of 20th century.

Internal control is a process aimed at the fulfillment of organization goals and is a result of business actions of planning, organization, activity monitoring as a whole and its divisions. Managers should establish business goals and build an appropriate structure. Also, they should provide effective document and reporting workflow system, segregation of duties, authorization, monitoring in order to fulfill the necessary goals [3, 4].

Internal audit is affected by the following factors:

- Management attitude to internal controls;
- Organization environment, its size, structure, scope and activities;
- Strategy, aim and goals;
- Technological and other resources;
- Personnel competencies.

Internal controls and audit is the main part of the modern management system trying to achieve established goals with minimum expenses [8, 9].

But many Russian companies may have struggles with establishing its internal controls. In Russian practice, three following organization internal controls are used:

- Internal audit function;
- Audit committees function;

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Structural and functional control.

These forms can be used both individually and in combination. It should be noted that owners and directors should decide its needs in the number of controls and their goals.

Audit committees are concerned with the safeguard of assets, operating effectiveness and fraud investigation.

Internal audit function goals are concerned within consultation on the internal controls, risk management and corporate governance.

Structural and functional controls are frequently used on a small and medium-sized businesses. They presume a development of internal documents and regulations, identification of discrepancies and solving the necessary problems.

But practice shows that this form is not effective enough on the planning and monitoring phases. Internal audit function is most effective when subdued to the audit committee and not to the general director.

Also, internal audit function organization can cause a significant increase to the general overheads. Internal auditor should have degree in economics or law, special audit training, experience and relevant skills. Internal audit is linked with accounting, analytical, production and managerial processes.

It should be noted, however, that structural and functional internal control function does not require serious additional costs on its start-up and maintenance. This form presumes that company specialists along with external auditors and consultants create internal documentation regulating its structural units, managers, control activities, solving of found discrepancies and their monitoring.

As practice shows, a combination of internal audit with the structural and functional control form in a cost-effective approach. In this case, a small internal audit group plays a role of control organizators and work is carried out by control personnel employed in the other divisions.

In this case, internal audit service fulfils the following organization functions:

- Choosing the audit objects and their preliminary examination;
- Development of general plans and audit programmes;
- Internal audit and control team building;
- Communication with the customers about the audit goals;
- Finalization of audit work;
- Establishing of a feedback controls and its monitoring and information.

Internal audit system is therefore concerned with operation within an entity, recorded in a management and financial accounting, non-financial documents, due diligence and effectiveness of operations and rationalization of decisions made.

It should be noted, that among internal auditors these problems are solved by audit committees and one should keep in mind the differences between these forms of control.

Audit committee in Russian entities is a constant elected body of a company which controls their financial and operating activities. Audit committee carries out the internal activities of a company. Members of a Board of Directors, executive bodies, or General Director, can not be a member of an Audit Committee.

Audit Committee's three members are elected by Shareholders' General Meeting, for 1 year and can be re-elected indefinitely. Audit Committee can examine internal documents, including financial reporting; and can receive responds from any company officers.

Audit Committee should reports any discrepancies found to a General Meeting and Board of Directors.

Internal audit function performs operating control over economic activity. When making decision of internal controls organization form, we should note the internal control environment in the organization.

Start-up and further maintenance of internal control is an expense of organization and, as per, Tax Code of Russia, external audit fees can be recognized as other expenses (par. 264.1.17) [5].

Internal audit expenses can also decrease the profit tax base, as per Ministry of Finance Letter of 23.05.2005 # 03-03-01-04/1/281. Internal audit salary are included in the salary expenses as per par. 255 of the Tax Code.

**CONCLUSION**

Internal controls system can be defined as a combination of specific methodic and procedures. Internal controls is deemed effective, if it warns about operating deficiencies in a timely manner.

If we compare internal audit in Russia and abroad, we may outline the significant differences; however we should state that internal controls should be established as an integrated system in a business entity.
Summary: Internal control methodologies can be outlined to specific recommendations and used in Russian companies practice.

REFERENCES