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INTERNAL CONTROL AND THE SUPERVISION OF CASH REGISTER SERVICE AS ILLUSTRATED BY FINANCIAL INSTITUTION X

Introduction

At present, the role of internal control depends on the scheme of management that is accepted by an entity as the scheme determines the effectiveness and efficiency of the control. There are several companies that do not take into consideration the issue of internal control, which weakens significantly company's ability to expand properly and reach the desired effectiveness. An internal control that functions properly protects company assets and contributes to the best possible financial results.

The functioning on the market of any business entity, including financial institutions, aims directly at its external and internal development. Nowadays, it is difficult to image a company that – while increasing its operations on the market – neglects internal change as regards the coordination of particular units and its management scheme. Important changes that are planned when managing an entity constitute a necessary factor of its adequate development. A key role in detecting the weaknesses of a company is played by internal control.

The aim of the article is to describe and analyze the process of internal control with a particular consideration of cash register service in financial institution X. The presented in the article considerations on the function and significance of internal control in a business entity, cash register service including, indicate that control of crucial processes in any entity is evidently required and necessary. The operations of an internal control are a crucial impulse that initiates changes in all aspects of the entity's activities and indirectly results in the increase of effectiveness and correctness of the tasks performed.

1. The concept of internal control

Internal control can be defined as a set of systematic activities aiming at the development of standards of effectiveness at estimated objectives, designing information feedbacks, conducting the analysis of the actual effectiveness in reference to standards,

identifying, assessing and measuring irregularities, as well as defining the measures that are necessary to ensure an optimal use of company resources¹. It can be concluded from the definition that the basic objective of the audit is to safeguard such conditions of company operations that its appropriate targets should be reached in the possibly most efficient way. However, one should keep in mind that the significance of an internal control in an entity depends to a large extent on the level of the entity's overall development.

A properly functioning system of internal control informs the management that:

- the targets are reached in an economical and rational way,
- the entity operates in accordance with law,
- the resources are protected appropriately,
- mistakes and irregularities are detected and revealed on regular basis,
- necessary measures are taken to eliminate mistakes,
- reports and statements present the actual state of affairs.

An internal control constitutes a feedback-based system of operations. First, measures and activities are decided on and afterwards they are always followed by the control itself.

The literature on the subject usually lists four stages of the control². The first stage is to establish standards and methods for measuring the effectiveness of the performance. It is obvious that the completion of the first stage is achieved in the course of a planning process. Thus, it is important that the implementation method of measurement should be understood and accepted by the staff. It is crucial that the selection of the effectiveness measurement method guarantees the highest possible precision. This stage should involve all areas of the entity in question.

The next stage is the measurement of performance. In the course of this phase, the assessment of the performance is conducted with regard to time, quality and quantity. In general, at this phase the effectiveness of the activities that have been started is measured. The phase reveals any irregularities in relation to the selected patterns and assumed targets. Consequently, in order to avoid delays in the completion of the targets, it is necessary to establish appropriate frequency of controls.

The third stage includes the analysis of the measurement results and their comparison with the predetermined assumptions. Only then, a precise and detailed determination of the level of anomalies can be conducted.

¹ J.A.F. Stoner, Ch. Wankel, *Kierowanie*, PWE, Warszawa 1996, p. 458.

² Ibidem, pp. 458-459; R. J. Mockler, *The Management Control Process*, Prentice-Hall, Englewood Cliffs, New York 1984.

The fourth and final stage includes corrective action. This phase completes the control cycle. The effects and results obtained lead to undertaking adequate measures. The most important requirement is to remove the anomalies that have been discovered, which involves the modification of the scope of operations. However, due to the fact that almost every set of rules and methods has some flexibility, it is not always necessary to correct the emerging anomalies. However, it is advisable to check thoroughly whether the level of the irregularities does not endanger the completion of the targets. Unfortunately, such anomalies have to be monitored more frequently. In the case when they are substantial, a reorganization of the whole entity may be necessary.

The control can also be defined as an ongoing, thorough analysis of the course and results of operations as regards particular functional areas and the whole organization³. The definition implies that the effectiveness of the controlling operations depends on the methods applied and the complexity of the entity. The relation between control planning and the specific features of the entity is a crucial element that integrates the management process and is decisive with regard to the increase of the performance effectiveness. The selection of a professional controller is also significant.

It should be emphasized that the control is particularly effective when applied selectively in the areas that are crucial to successful performance. In every entity there are evidently three such areas⁴:

- operational – focused on the monitoring of the progress and effects of the conversion processes (conversion of resources into effects),
- financial – concentrated on the accumulation of funds necessary to ensure efficient functioning of the organization and the distribution of funds that ensures the survival and development of the organization,
- human resources – the assurance of the required efficiency and quality of tasks performed by the staff.

A typical feature of every internal control system is its uniqueness as every business has its unique objectives, requirements and expectations that are created by the sector and organizational structure of an entity.

³ R.W. Griffin, *Podstawy zarządzania organizacjami*, PWN, Warszawa 2013, p. 474.

⁴ L.R. Bittel, *Krótki kurs zarządzania*, PWN, Warszawa 2002, p. 180.

2. Control documents

The control documentation can be classified by several basic groups with the consideration of diverse criteria. Before the control is commenced, necessary documents must be prepared and completed. As the control in a given unit is conducted at different work sites, the controller should obtain a written authorization to conduct it. The authorization should be issued immediately at the preparatory stage and approved by the manager of the unit in order to confirm the legality of the control.

The control records are usually developed by the controller in the course of the controlling process. However, it often occurs that the controller uses a model document that has been prepared and developed beforehand.

Two protocols, a general and partial protocol, constitute the basic and fundamental group of records.

The protocols are developed in order to confirm the course of the control at individual work sites or in other areas such as a warehouse or cash desk. They include notes and records made on request of the controller or possibly of the employees that are subject to the control. They may particularly concern ad hoc by-laws, preservation of evidence, statements and explanations.

All documents that are developed in the course of control must be reliable, honest and unquestionable.

A brief and precise description of events is an unquestionable requirement. Only then is an objective assessment possible. The formulation of adequate conclusions from the facts, particularly when their quantification is necessary, requires the development of written justifications of supervisors and the enclosure of evidence. This principle concerns particularly events that are negative in character as such events are the most common reason for dispute and, consequently, they have to be presented in a precise, honest and objective way. Other practically applied documents include regulations and orders of the management of the entity or of the head of control department as regards the conduct of internal audit or follow-up activities. Such documents include information on the schedule of the current control, its object and date as well as the person authorized to conduct the control activities.

The control protocol is the final control document which is executed in two counterparts - one copy for the head of the unit under control and the other for the head of the controlling unit. The control protocol should be written clearly, objectively and on time. It is crucial that it contains the facts determined by the controller and the bases and sources of the findings.

Within 21 days after obtaining the post-control recommendations, the head of the entity that was controlled is obliged to inform in writing the person who ordered the control about the implementation of the recommendations. In the cases when the recommendations are not implemented, an appropriate reason must be given.

In most entities the completion of control records and post-control recommendations is monitored by an internal control section in line with the arranged and accepted standards. Having analyzed the control and post-control records that include irregularities, abuse or violation of work duties, the internal auditor implements measures that are necessary to explain the reasons and circumstances of the events, which is strongly connected with the determination of financial effects.

3. Preparatory and post-control activities

Thanks to the records and post-control protocols, there is a probability that irregularities and operational breaches in a given entity are identified. The elimination of faults results in a significant improvement of the effectiveness in reaching the targets. The preparatory activities determine the beginning of the control stage, while the post-control activities indicate the end of the controlling procedures. The preparatory activities include operations that have to be done by a controller before the control is started in a given entity. Such operations mainly include⁵:

- collection of a possibly wide range of materials and information concerning the entity and the scope of the operations to be controlled,
- preparation of a list of the applicable provisions, standards and models that will serve as the basis for the comparison with the results of the actual state of things,
- determination and verification of the ways and control methods as regards the subject of the control with the cooperation with other controllers,
- development of the sets of controlling questions and other means to support the performance of the control,

⁵ K. Adamiecki, *Kontrola jako zasada naukowej organizacji*, „Przegląd Organizacji” 1927, No. 5.

The preparatory process may be carried out either by the controller or by the employees that are given particular tasks by the controller. However, it is recommended that the whole preparatory process should be conducted personally by the controller unless the deadline for the control is very urgent and the controller is busy with other activities. A preliminary preparation of the controller to commence controlling procedures is beneficial and it significantly facilitates the effectiveness of the process, including the selection of the crucial issues that the controller is obliged to investigate first.

Obviously, a satisfactory control depends to a large degree on the preparatory work. However, one should not think that this will be enough for the controller to be successful in the subsequent stages of the control. There is an ongoing criticism as regards the delays in catching up with the issues regarding the methodology of control as this is a crucial factor that affects control effectiveness or even results in a complete ineffectiveness. Thus, preparatory activities should be obligatory. The main aim of the review and analysis of the whole material concerning the control is to identify potential areas where the irregularities in the functioning of the entity may occur. Such deviations should be treated as priorities in the control process. First, adequate conditions should be ensured for a complex assessment and analysis of the areas under control in order to reach a substantial improvement. The objective is to guarantee the acquisition of comprehensive and complete opinions on the events under investigation and to formulate appropriate conclusions and post-control recommendations. Methodological guidelines are extremely useful to a controller as they facilitate the selection of the best way to achieve the control targets. However, it is not easy to define precisely the method and scope of particular control activities due to the comprehensive and unique nature of the functioning of separate entities and the dynamic changes in the external environment that determine the progress of economic processes. Consequently, methodological guidelines may only take the form of a set of investigation instructions that originate from the control objectives and concern ranking of the key control areas, the analysis methods of the relations between the control objects and subjects and the cause-effect relations⁶. It sometimes happens that methodological guidelines refer to several organizational and technological aspects regarding the order of the investigation, control techniques and methods, relations between control records and control and post-control model documents. A correctly developed set of methodological guidelines should be general and flexible. Only such character of the guidelines will make it possible to implement them in subsequent controls in

⁶ S. Kałużny, *Kontrola w systemie zarządzania*, CPKAP, Warszawa 1989, pp. 39 -

other entities. The other aim of the preparatory phase is to verify the purposefulness and the course of the control activities as well as the scope and time of the control. The verification of the accepted standards and rules is extremely important as they should be continuously updated due to changes in the external environment. This will protect the entity against failures in the fulfillment of the targets and will ensure correct functioning and perfect results.

Post-control activities, which close the control stage, aim at a proper implementation of the results of the control, the preparation of reports and post-control records. Another phase includes meetings with the management of the controlled unit with the aim to check the completion of the post-control activities and recommendations. Through the analysis of the appropriateness of the control findings and the effectiveness of the implemented measurement solutions and techniques, the post-control activities contribute significantly to the development and improvement of the control process itself. Moreover, the awareness that the guidelines are carried out precisely and their implementation result in beneficial effects is a good incentive both for managers and employees. It is not recommended that the control should be finished while the post-control records are still being processed as such procedure results in downgrading the role of the control in an organization and, consequently, does not lead to organizational and procedural changes. Such trends result in the increase in operational costs and restrict the development of the entity. One should also bear in mind that there are situations that an entity may be banned from operating when a significant breach of procedures is revealed.

3. Internal control in financial institution X

Business entity X⁷ is a cooperative financial institution that provides financial services to its members. It plays an important social role as it serves people who – if not for this credit union – would not have the access to certain financial services, credits in particular. The chain of branch offices of the entity in question, which also operates on-line, provides access to credits and loans, it offers accounts where financial means can be deposited, it also facilitates financial settlements and insurance agreements.

The internal control in entity X follows the rules of procedure that define basic organizational and functional principles of the internal control system. The obligatory rules

⁷ Business entity X is a credit union. Due to the lack of agreement of its management to use the actual name in the article, the entity will be referred to as entity X.



of procedure that are in force are a document superior to other detailed internal regulations of the entity and subject to ongoing necessary updating with regard to the changing needs of the external and internal environment. The main objective of the internal control is particularly to support decision-making processes, which play a key role in the successful completion of effective operations. It controls the reliability and truthfulness of the financial statements and the company's compliance with law and internal regulations.

As regards cash register service, the internal control aims at:

- the assessment of the fulfillment and correctness of the target as defined in the instruction,
- the assessment and monitoring of the compliance of the operations with the cash register instructions, internal procedures and prudential methods and regulations,
- the verification of the correctness of all operations that aim at revealing the shortfalls and failures,
- the review and check of the reliability and completeness of cash register documents,
- the organizational supervision, including the separation of contradictory responsibilities and functions,
- the prevention against personal dependences between employees that are in a direct superior-subordinate relation to each other.

An important and crucial condition for reaching the above targets is that control mechanisms should be implemented in the area of cash register services as well as all other levels of company operations. The knowledge and awareness regarding cash handling instructions is the obligation of all the employees that work as cashiers as well as of the managers that they report to. A proper service at a cash register position is also the result of an adequate influence on cashiers through monitoring of their behavior, attitudes and language used. In company X it is unacceptable to tolerate behavior contrary to the standards defined by internal regulations or to neglect the comments of the internal control in this respect. Control activities are conducted at all stages and their aim is to:

- react continually to irregularities and shortcomings,
- monitor the course and effects of work on a regular basis,
- correct mistakes.

Activities that are within the internal control in company X are conducted by an employee who is authorized by the company board. This person is well aware of the problems



concerning each unit. The internal control regarding the cash service staff is based on the standards and regulations on cash service given in the cash register instructions for entity X.

The total control schedule includes:

- control whether the cash in hand balance is consistent with the accounting records,
- a check of the completeness and correctness of cash register records,
- precise counting of banknotes and coins,
- quantitative verification of cash records,
- verification of signatures on cash vouchers.

The control activities are performed by controller X due to his high level of expertise and theoretical knowledge in the area under investigation. One of the crucial objectives of the controller is to check the consistency of the cash in hand balance with the accounting records of employee X that worked at the cash desk on a given day. It should be reminded that before taking up the position, the cashier in financial institution X is obliged to sign a certificate of financial responsibility. Such document is an important safeguard for the employer in cases when the employee's activities incur a financial loss. Controller X checks the balance of cash on hand as well as checks thoroughly the quality and quantity of banknotes and coins.

Having counted the value of all means and coins and completed the specification of cash, the controller compares their consistency with the balance of the generated current cash in hand statement. During the control, on the basis of the specifications and cash statements that were generated on the days preceding the control, a comparative analysis is conducted of the current balance regarding payments and withdrawals. One should not neglect the fact that it is not only controller X who checks the consistency of the cash in hand balance and the cash statement. In company X the value of cash is checked on a daily basis by the cashier, at the beginning and the end of each day when cash service is provided. Moreover, at the end of the day, the control operations are accompanied by the head of the unit. The cash in hand should be consistent with the balance resulting from in-and outgoing vouchers. It is up to the internal controller's decision to conduct a total or sample cash control. A sample control consists in checking a packet of banknotes or rolls of coins selected by the controller. In the course of the cashier's control, the completeness and correctness of the cash records is verified. The control covers:

- substantive control,
- formal control,
- control of the accounts,

- document storage.

The substantive control of the cash register documents in company X consists in a thorough check of the correctness and consistency of cash register receipt and disbursement documents with the actual state. Thus, the operations accounted in the cash statement should be clearly identified with the operations in cash register receipt and disbursement documents. In the course of the formal control, the check includes the correctness and adequacy of the signatures of authorized employees on cash register documents. The control of the accounts deals with the correctness of calculations in cashier's cash specification and with the calculator's printout. The objective of the control is also to check whether the records are protected against the access of unauthorized persons and kept in filing cabinets.

In company X the controller may choose to control all the operations and documents within the scope of the control or select them at random. However, the significance of a document should be taken into consideration. The target of the control activities is to analyze, collect and assess the data obtained in the course of the control. If the internal controller detects circumstances that may result in losses, it is his duty to escalate immediately to the management of the irregularities and to conduct an internal audit with the aim to take measures that would eliminate the risk. The control is completed by signing a post-control protocol by the controlling and the controlled parties. The controlled party has the right to refuse signing the protocol and the reasons for the refusal should be given in writing. The check of the completion of post-control assignments may be conducted by means of a telephone conversation or verification of documents that are selected at random. If the post-control recommendations are not fulfilled, the controller checks again the area where the irregularities originally appeared and investigates the cause of the lack of appropriate reaction. Table 1 presents a sample of a post-control protocol.

Table 1. Post-control protocol for employee X

Entity under control	Financial institution X
Address of the entity under control	Address X
Party under control	Employee X
Position	Cashier
Controlling party	Controller X
Position	Position X
Date of control	dd/mm/yyyy
Subject of control	Control of the cash balance and its consistency with cash register documents. Control of cash register documents.

Source: internal materials of financial institution X

The control process is focused on irregularities that pose a risk to the investigated area of company's operations. In the course of the analysis of the post-control process, the controller assesses and takes into consideration the knowledge, expertise and reliability of the person being controlled.

Conclusion

At present internal, controls are implemented in all entities, including financial institutions, as they are a necessary condition for the introduction of change. A purposeful use of control results in the increase in the effectiveness and accuracy of the recognition and assessment of irregularities and faults. Irregularities are a major cause of the entity's incapability to use optimally the resources that it has access to. It should be emphasized that control operations should be conducted efficiently and on regular basis and not only in the cases when problems appear. Nowadays, controls concern all entities that aim at active functioning on the market. Control operations do not depend on the specific features of an entity, its sector, structure or the volume of its activities. However, some facts indicate that many businesspeople are convinced that control is a kind of phenomenon that is solely related to big companies.

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Abstract

The function and the role of internal control in a business entity, financial institutions including, indicate clearly that control procedures regarding crucial processes in any entity is required and necessary. The operations of an internal control are a crucial impulse that initiates modifications in all aspects of the entity's activities and results in the increase of



effectiveness and correctness of the tasks performed. Regular supervision of the processes that occur in a financial institution, and in the area of cash service in particular, is a preventive measure that aims at the elimination of any serious consequences resulting from the failure to conform to legal regulations and company standards. The basic assumptions and objectives of internal control are: the identification of the weakest links in the processes, an ongoing prevention against the development of abnormal events and the support of decision-making processes.