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The Role of Internal Control in Fraud Prevention and Detection in Non-Governmental Organisations (NGOs) in Jordan

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This study was conducted to identify the role of internal control in fraud prevention and detection in non-governmental organisations (NGOs). A six random sample of NGOs sector was selected and the sample consisted of (73) NGOs employees who are working in the managerial control and financial positions, had been randomly recruited to fill the questionnaire (which consisted of three axes for measuring the questions of the study). The results indicated that internal control in NGOs plays a significant role in fraud prevention and detection and ensures that all transactions comply with the internal guidelines and manuals. In addition to that, the study recommends the researchers pay more attention towards internal control in NGOs in Jordan since NGOs have an important role in the Jordanian society, and the researchers of this study will conduct more research on this topic in the future due to the importance of this sector in Jordan.

Keywords: *Internal Control, Fraud Prevention, Fraud Detection.*

1. Introduction

The Committee of Sponsoring Organisations of the Treadway Commission:

Internal control was defined by The Committee of Sponsoring Organisations ('COSO') as internal control being a process that is influenced by the entity's board of directors, management, and other employees and is designed to provide reasonable assurance regarding the objectives achievement in the following categories: effectiveness and efficiency of

operations, financial reporting reliability, and compliance with applicable laws and regulations. (COSO's, 2013).

Internal control helps to ensure the compliance with applicable regulations, rules and laws, and at the same time can improve operational efficiency and effectiveness (Bongani, 2013).

However, the success of any entity refers to the contribution of effective internal control through the financial, operational and administrative systems (Ayom, 2013). If the internal control system is weak and not effective, the organisation will be more vulnerable to irregularities and errors, and more prone to fraud and fraudulent activities (Ndungu, 2013).

Fraud is a global phenomenon and is a broad term that affects all sectors of economy. It is defined by The Australian Standard for Fraud and Corruption Control as: "Dishonest activity causing actual or potential financial loss to any person or entity including theft of moneys or other property by employees or persons external to the entity and where deception is used at the time, immediately before or immediately following the activity. This also includes the deliberate falsification, concealment, destruction or use of falsified documentation used or intended for use for a normal business purpose or the improper use of information or position for personal financial benefit" (Australian Standard for Fraud and Corruption Control, 2008). Cressey, in the 1950s, highlighted that fraud occurrence is caused by three essential elements: opportunity, pressure and rationalisations. Moreover ethical values play a significant role in the occurrence of fraud as Tunggle in 2008 reported that fraud is a distortion in moral perceptions called truth, justice of law and equality.

Fraud can be classified into two classes: institutional and external. While the former is caused by work volume, ineffective supervision of employees, exposure to cash, poor employee training, lack of segregation of duties, employee negligence, maintenance of incomplete records, and management lapses, the latter is caused by societal/peer pressure and poor legal systems (Ehbodaghe,2014; Myer,2012).

According to KPMG in 2013, most organisational fraud is related to misrepresentation of financial statements, thefts of funds, misappropriation of assets and corruption. In the same line, three primary categories of fraud were identified by the Association of Certified Fraud Examiners (ACFE) 1. Asset misappropriations, 2. Corruption schemes, 3. Fraud schemes of financial statements.

1.1 Study Problem

Fraud and misuse of funds that results from lacking ethical values are creating fear and anxiety for the donors in non-profit organisations. Internal control systems play a significant role in such organisations since the income is obtained from donors, and the right use of such funds will attract more donors and will increase the grants, so poor internal control will decrease the

funds for these organisations. In Jordan there was a lake of investigation of the role of ethics and internal control in fraud detection and prevention. In addition to that the researchers of this study will answer the following questions:

1. What is the role of internal control in fraud prevention in NGOs?

2. What is the role of internal control in fraud detection in NGOs?

1.2 Study Importance

The study importance comes from lack of such studies in Jordan that present and discuss the role of internal control in fraud prevention and detection in NGOS. Internal control is very important building the trust between NGOs and donors, since the donors are looking for partners who have the capacity to spend the funds in a good way and to achieve the objectives of the projects without any irregularities or misuse.

1.3 Study Objectives

The aim of this study is to examine the role of internal control in the prevention and detection of fraud in non-governmental organisations, in addition to providing NGOs with reliable recommendations to enhance their internal control which will attract more donors.

1.4 Study Hypotheses

From the above problem and objectives of research, the following hypotheses were formulated by the researchers:

H01: There is no statistically important role for internal control in fraud prevention in NGOs.

H02: There is no statistically important role for internal control in fraud detection in NGOs.

2. Theoretical framework and previous studies

Internal control as defined by COSO is "a process, affected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting, and compliance".

There are five internal control components identified by COSO:

1) The control environment is a set of standards and processes that provide the bases for carrying out internal control in the organisation and are considered the most important components of internal control (COSO, 2013). Several studies have highlighted the link between control environment and fraud prevention and have reported that control environment is the basis for the continuation in internal control and that it plays the principle role in reducing fraud. (Amado & Niangua, 2009), (Yurniwati & Rizaldi, 2015).

2) The risk assessment is a dynamic process for identifying risk that negatively affects the achievement of objectives. Also, in determining how risk will be managed, COSO highlighted the importance of performing a fraud risk assessment in each organisation to reduce fraudulent activities (COSO, 2013).

3) Control activities are establishment actions through policies and procedures to assist in decreasing risks in the achievement of objectives (COSO, 2013). Control activities can be categorised into detection and prevention control activities. Prevention activities are for prediction of undesirable events, and detection activities are identified as undesirable events that have already occurred and alert the management (COSO, 2013).

4) Information and communication is important to carry out internal control that help in objective achievements, communication is a continuity process for sharing and exchanging information to support in coordinating activities (COSO, 2013).

5) Monitoring activities assessment of the quality of internal control system performance is necessary, it can be assessed by ongoing monitoring or by separate evaluation (COSO, 2013).

A study was conducted in 2016 to examine the effect of internal control on fraud prevention in banking industries by using primary data to test internal control and secondary data to test fraud prevention. The results of multiple regressions found that internal control is effective against fraud (Adetiloye et al, 2016). In addition, a study was conducted in Nigeria to examine the effect of internal control on fraud prevention and a significant relationship was found between internal control and fraud prevention, the researcher highlighted on the importance of internal control as a safeguard (Ozigbo, 2015).

A descriptive study conducted in 2015 aimed to ascertain the effect of internal control on fraud prevention and detection in Kenya. Simple random method and purposive sampling methods were used, the questionnaire used was closed ended questions, inferential and descriptive statistical analysis were used, and the results revealed a significant positive relationship between effective internal control and fraud prevention and detection (Oguda et al, 2015).

3. Methodology

The methodology of the study was designed to assess the relationship among the variables of the study: internal control, fraud prevention and detection in NGOs.

3.1 Study Population

Six NGOs in Jordan were randomly selected to be in the study. A self-administered questionnaire was distributed to NGOs employees working in managerial and finance positions.

3.2 Study Sample

The researchers selected six NGOs in Jordan randomly and distributed 80 questionnaires to the study sample (administrator managers, finance managers, internal control managers and accountants). After retrieving the questionnaires, 7 were excluded as non-suitabile for the purposes of statistical analysis. The study sample was therefore 73 questionnaires. Table (1) shows the demographic distribution of the study sample.

Table (1) Demographic data of the study sample

Variable	Repetition	percentage
Sex		
Male	63	86%
Female	10	14%
Age		
18 – 25	14	19%
26 – 35	33	45%
36 – 45	19	26%
46 & above	7	9%
Academic Qualification		
High School	***	***
Diploma	3	4%
Bachelor	51	70%
Master	16	22%
PHD	3	4%
Total	73	100%

3.3 Study Tool

The study consisted of two parts:

First part: Demographic variables, including gender, age, academic qualification).

Second part: including:

1. First Axis: internal control.

2. Second Axis: fraud prevention.

3. Third Axis: fraud detection.

3.4 Reliability of Study Tool

The questionnaire was submitted to the referee (the research supervisor) to verify the veracity of its paragraphs, take his opinion, reformulate some paragraphs, and make the required adjustments and to carefully multiply the weight scores between the content. From the decision in the paragraphs, as well as around it, which confirms the truth of the tool.

3.5 Stability of Study Tool

To calculate the stability of the study tool, the researchers used the equation of internal consistency using Cronbach's test alpha shown in Table (2). The results of the test for all variables of the study and identification of generally where higher (60%) which is acceptable in the scientific research and studies.

3.6 Statistical Processing:

To answer the questions of the study, the researchers used descriptive and analytical methods, using the package of statistical (SPSS), which includes standard descriptive statistics (Descriptive Statistic Measure), to describe the characteristics of the sample depending on the frequencies and percentages and in order to answer the questions of the study, means and standard deviations, as well as the Cronbach Alpha Test were used to ensure the stability of the study tool.

4. Testing the Hypotheses:

H01: There is no statistically important role for internal control in fraud prevention in NGOs.

To answer the first hypothesis averages and standard deviations were extracted to identify the responses of the sample of the study on the importance of internal control. Table (2) illustrates this.

Table (2): The means, standard deviations and rank for the first axis (Internal control).

No.	Paragraph	Means	Standard deviation	Rank
1	ERP system in all department within the organisation.	4.22	0.86	1
3	Bank accounts should be reconciled monthly.	4.16	1.02	2
2	Separate Bank account for each project is important.	4.04	1.24	3
5	The accounting system identifies receipts and expenditures separately for each project.	4.00	1.32	4
4	Information can be retrieved accurately in the event of loss	3.94	1.7	5
7	Adequate records of fixed assets costs and depreciation are important.	3.7	1.6	6
6	The formal written procedures for performing a physical inventory.	3.6	1.54	7
8	Fixed assets are tagged when procured	3.56	1.52	8
10	The cash box should be limited with ceiling	3.09	1.42	9
9	A petty cash fund is utilized and reconciled periodically.	2.61	1.47	10
11	Code of conduct signed by employees	2.58	1.48	11
	General average	3.59	1.38	

The above table shows that the averages for this axis (Internal control) ranged between 4.22 and 2.58, where he earned axis on the arithmetic average total (3.59), a high level, and has received Paragraph No. (1) the highest average account where the (4.22), and the standard deviation (0.86), a high level, which stipulates paragraph (the ERP system in all department within the organisation). In second place came paragraph 3 with a mean of 4.16 and standard deviation of 1.02, a high level, which stipulates that “Bank accounts should be reconciled monthly”. In third place came paragraph 2 with a mean of 4.04 and standard deviation of 1.24), a high level, which stipulates that “A separate bank account for each project is important. In fourth place came paragraph 5 with a mean of 4.00 and standard deviation of 1.32, a high level, which stipulates that “The accounting system identifies receipts and expenditures separately for each project”. In fifth place came paragraph 4 with a mean of 3.94 and standard deviation of 1.7, a high level, which stipulates that “Information can be retrieved accurately in the event of loss”. In sixth place came paragraph 7)with a mean of 3.7 and standard deviation of 1.6, a high level, which stipulates that “Adequate records of fixed assets costs and depreciation are important”. In seventh place came paragraph 6 with a mean of 3.6 and standard deviation of 1.54, a high level, which stipulates that “Adequate records of fixed assets costs and depreciation are important”. In eight place came paragraph 8 with a mean of 3.56 and standard deviation of 1.52, a high level, which stipulates that “Fixed assets are tagged when procured”. On the contrary, paragraph 10 has an arithmetic average of 3.09, and a standard deviation of 1.42), a mid-level, stipulates that “The cash box should be limited with ceiling”. Paragraph 9 has an arithmetic average of 2.61 and a standard deviation of 1.47, a mid-level, stipulates that “A petty cash fund is utilised and reconciled periodically. Paragraph 11 has an arithmetic average of

2.58 and a standard deviation of 1.48, a mid-level, stipulates that "Code of conduct signed by employees". This explains that the internal control has an important role in fraud prevention

Table (3): The means, standard deviations and the rank for the second axis (Fraud prevention).

No.	Paragraph	Means	Standard deviation	Rank
17	Training courses to help solve problems with accountants	4.40	0.88	1
15	All transactions comply with the organisation manual.	3.94	1.70	2
18	Segregation of duties principle between the employees	3.92	1.12	3
13	Suppliers and Vendors are reviewed to identify potential conflict of interest.	3.81	1.16	4
12	Responsibilities are clearly defined in writing and communicated.	3.75	1.20	5
16	Awareness sessions for employees about fraud actions and how to report such acts	3.6	1.54	6
14	Written Conflict of Interest Policy in place that is adopted by the Board of Directors.	3.57	1.29	7
	General average	3.86	1.27	

Table (3) show that the averages for this axis (fraud prevention), ranged between 4.40 and 3.57. where he earned axis on the arithmetic average total (3.86), a high level, and has received Paragraph (17) on top arithmetic average reaching (4.40), and the standard deviation (0.88), a high level, which stipulates "Training courses to help solve problems with accountants". In second place came paragraph 15 with a mean of 3.94 and deviation standard of 1.70, a high level also, which stipulates that "All transactions comply with the organisation manual". In third place came paragraph 18 with a mean of 3.92 and a standard deviation of 1.12, a high level also, which stipulates that "Segregation of duties principle between the employees. In fourth place came paragraph 13 with a mean of 3.81 and a standard deviation of 1.16, a high level also, which stipulates that "Suppliers and Vendors are reviewed to identify potential conflict of interest" In fifth place came paragraph 12 with a mean of 3.75 and a standard deviation of 1.20, a high level also, which stipulates that "Responsibilities are clearly defined in writing and communicated". In sixth place came paragraph 16 with a mean of 3.6 and standard deviation of 1.54, a high level also, which stipulates "Awareness sessions for employees about fraud actions and how to report such acts". In lowest ranked plasce was paragraph 14 with a mean of 3.57 and a standard deviation of 1.29, stipulating "Written Conflict of Interest Policy in place that is adopted by the Board of Directors". This explains that internal control plays a role in fraud prevention.

H02: There is no statistically important role for internal control in fraud detection in NGOs.

To answer the second hypothesis averages and standard deviations were extacted to identify the responses of the sample of the study about the role of internal control on fraud detection in NGOs in Jordan. Table 3 illustrates this.

Table (4): The means, standard deviations and the rank for the third axis (Fraud detection).

No.	Paragraph	Means	Standard deviation	Rank
25	All payments through bank transfer	4.44	0.70	1
19	Spot check to count the cash box.	3.96	1.09	2
20	Regular internal audit on the organisation departments.	3.92	1.12	3
23	Audit general journal entries	3.81	1.16	4
26	Matching the salaries sheet with the bank transfer.	3.75	1.20	5
27	Spot check to count the inventory	3.57	1.29	6
22	Examine procurement documents, where applicable.	3.56	1.52	7
21	Examine cancelled checks/bank statement s	3.56	1.52	8
24	Easy to deal with accounting systems	2.61	1.47	9
	General average	3.69	1.23	

Table (4) shows that the averages for this axis (fraud detection) ranges between 4.44 and 3.57, where he earned axis on the arithmetic average total (2.61), a high level, and has received Paragraph (25) on top arithmetic average reaching 4.44, and the standard deviation 0.70, a high level, which stipulates “All payments through bank transfer. In second place came paragraph 19 with a mean of 3.96) and deviation standard (1.09), a high level also, which stipulates that paragraph (Spot check to count the cash box) , and in third place came paragraph (20) with a mean (3.92) and deviation standard (1.12), a high level also, which stipulates that paragraph (Regular internal audit on the organisation departments.), and in fourth place came paragraph (23) with a mean (3.81) and deviation standard (1.16), a high level also, which stipulates that paragraph (Audit general journal entries), and in fifth place came paragraph (23) with a mean (3.75) and deviation standard (1.20), a high level also, which stipulates that paragraph (Matching the salaries sheet with the bank transfer), and in six place came paragraph (27) with a mean (3.57) and deviation standard (1.29), a high level also, which stipulates that paragraph (Spot check to count the inventory), and in seven place came paragraph (22) with a mean (3.56) and deviation standard (1.52), a high level also, which stipulates that paragraph (Examine procurement documents, where applicable), and in eight place came paragraph (21) with a mean (3.56) and deviation standard (1.52), a high level also, which stipulates that paragraph (Examine cancelled checks/bank statements), Came in ranked last paragraph (24) reached a mean (2.61), and a standard deviation (1.47), where the Paragraph (Easy to deal with accounting systems). This explains that the internal control has important role in the fraud detection.

5. Conclusion & Suggestions

This study aimed to identify the role of internal control in fraud prevention and detection in NGOs in Jordan. Usually fraud is associated with large business. Since NGOs have a higher level of trust in the eyes of the public, it normally doesn't come to mind when discussing the topic of fraud. However, through this study it is made clear that many people are deceived by NGOs fraud. Many times these cases have gone to uncovered for years. Therefore, the risk that is faced by profit businesses is the same for NGOs. In fact, there may be a higher risk associated with NGOs due to a lower amount of internal control. In addition to that the NGOs should apply well designed internal control systems by using the ERP system, ensuring the segregation of duties between the employees, make monthly bank and cash reconciliations, review the journal vouchers and in training staff on the problem solving.

By testing the hypotheses, the study highlighted the following results:

1. There is a statistically important role for internal control in fraud prevention in NGOs in Jordan.

2. There is a statistically important role for internal control in fraud detection in the NGOs in Jordan.

3. By implementing internal control in NGOs they can prevent and detect fraud in a timely manner due to the important role of internal control.

These are the recommendations for the purpose of improving internal control in the NGOs. The successful implementation of these must help all NGOs to protect their assets and ensure that all financial resources used to achieve the planned goals without any misuse which will be more attractive for the donors. The suggestions are provided below:

1. Implementation of internal control within NGOs in Jordan. These are the controls that relate to using the ERP system in all departments within the organisation: making sure that the bank accounts are reconciled monthly in addition to maintaining a separate bank account for each project, ensuring that the information can be retrieved accurately in the event of loss of adequate records of fixed assets costs and depreciation are important.
2. Implementation of internal control activities are designed in such way that ensure the input is authorised, accurate, complete and timely.

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