

# Internal Audit and Fraud Control in Public Institutions in Nigeria: A Survey of Local Government Councils in Osun State

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## Abstract

That fraudulent practices have been canonically accommodated, entertained and celebrated within the local government administration in the country is a statement of fact. Fraud in Public institutions is more easily accomplished in an environment where there is administrative and fiscal laxity. Indeed, it may well be said that a significant proportion of public resource lost each year because of fraud as a result of inefficient internal and external auditing.

This research evaluated the effectiveness of the internal audit unit on fraud control in local government administration in Osun State. In this research, two hypotheses were formulated and tested. The primary data was obtained through the administration of questionnaires, interview and actual observation. This was supplemented with secondary data.

The findings of this research indicate that the Internal Audit unit did not fulfill and in reality does not contribute significantly to fraud prevention and control in local government administration in Osun State. The study thus recommends total overhauling of the internal audit unit in the local government administration in Osun State.

**Keywords:** Internal Audit, Fraud Control, Local Government Council

## Introduction

### 1.1 Background Information

The value of public resource lost each year in Nigeria through fraud and corruption defies precise quantification, but almost certainly runs into many billions of naira. Fraud in public institution in Nigeria, particularly at the Local government level, is ever on the increase and dates back to the ages. This seems to be in an escalating rate as we witness it day-in-day-out through newspapers reportage that public officers and treasury managers entrusted with public treasury manage business to their own advantages.

Fraud which is a major reason for setting up an internal control system has become a great pain in the neck of many internal auditors in Nigeria. It is a fact that any institution with a weak internal control system is dangerously exposed to fraud. Flaws and loopholes may still exist in an organization despite the existence of internal control system, which can easily be circumvented by individuals who are inclined towards fraudulent activities. Therefore, measures have to be put in place to checkmate such fraudsters. One best way of curbing the menace of fraud is through the institutionalization of a vibrant and effective internal audit unit. (Abu-Saeed and Kabir, 2012).

### **1.2 Statement of Research Problem**

Fraudulent practices and corruption have been described as the major causes of comatose state of local government administration in Nigeria, and a major hindrance to good government (Onwemenyi, 2008). It has also been identified by Ali (2008) as one of the problems confronting effective local government administration in Nigeria.

In a nut-shell, the damage which this menace, called fraud has done to our national development is innumerable and needs urgent attention. Therefore, the attempt to put an end to these economic maladies gave rise to this present study.

### **1.3 Research Objectives**

The main objective of this study is to assess the effectiveness of internal audit function in curbing fraudulent practices in the nation local government administration. Specifically the objectives of the study are to:

- i. Examine if existence of functional internal audit unit can curb and prevent incident of fraud in local government administration.
- ii. Examine if fraud detection and prevention will significantly depend on the independence of the internal auditors.

### **1.4 Hypotheses of the Study**

In realization of the objectives of the study, the following hypotheses were tested.

H<sub>1</sub>: Existence of functional Internal audit unit will not significantly prevent instances of fraud in local government administration in Osun State.

H<sub>2</sub>: Fraud detection and prevention in local government administration in Osun State will not significantly depend on the independence of the internal audit.

## **2.0 Review of Literature**

Local government is created to ensure meaningful development of the grassroots through participating approach (Adeyemi, 2012). Regrettably, this is not the case, instead of discharging their functions as development centres, local governments in Nigeria have acquired notoriety for corruption, financial indiscipline and overall irresponsibility (Agbo, 2010). According to Ekawu (2007) local government in Nigeria, has become high temple of corruption and gross mismanagement where combined effect of graft and inefficiency are proudly show cased the officials.

In public institutions like local governments, the internal audit functions hold high potentials for promoting accountability and improving government performance (Md Ali et al, 2009). This is not surprising, several countries of the world have developed policies aimed at strengthening public sector internal audit functions to enhance their capability for contributing these goals (Light, 1993; Newcommer, 1994 & 1998)

Nonetheless, available evidence on the reality of internal audit operations in recent time provides the picture that shows there is much room for improvement. According to Md Ali et al (2009) studies on internal audit operations in public sector in the United States, Canada and Australia reveals a common finding which include: inadequate coverage, particularly of areas of major significance and high risk, a tendency to focus audits on compliance and regularity to the detriment of the performance of audit of economy, efficiency and effectiveness and little attention being given to audit findings within agencies by senior managers. Furthermore in Canada and Australia there exist deficiencies in the professional qualifications of audit staff and in the involvement of senior management in audit planning.

According to Brierley, El-Nafabi, and Gwillam (2001) in a study carried out in the developing country of Sudan, in North Africa, the typical internal audit department is largely engaged in the routine authorization of transactions, is staffed by inexperienced and untrained personnel and has insufficient credibility, independence and authority to act in the manner expected of internal audit personnel. Employing interview and observation research methods, Brierley concludes that in the few places where internal audit may be in operation. It has failed to meet anyone of the five core standards of the Institute of Internal Auditors (IIA 1979) in terms of independence professional proficiency, scope of work, performance and management.

In Nigeria, very little is known on the state of internal audit in the public sector particularly at the local government level. To date there appear to have been very few research studies in that area. In one of the few studies conducted in that area, Achilonu (2013) noted that the problem of corruption and misappropriation of funds affects the internal audit system of local government in Imo State. The study concluded that the prevention of fraud and misappropriation of funds is not solely dependent on the independence of the internal audit. Rather, there are other factors needed to be put in place to enhance the detection and prevention of fraud in local government administration.

On the issue of accountability at the local government, Adeyemi, Akindele, and Agesin (2012) observed that financial accountability in local government will be impossible as long as the internal audit is emasculated by inadequate manpower, poor budgetary provision, lack of official support from the state government and absence of up-to-date annual accounts to work on. In their own submission Barkan, Gboyega, and Stevens (2001) posit that many local governments in Nigeria lack internal capacity to keep good records and ensure that annual audits are carried out on schedule, some willfully resist submitting their accounts for audit.

All in all, it is probably not an exaggeration to say major questions have remained unanswered when it concerns the practice of internal audit in the nation's local government administration. This is simply not conducive to any serious effort to squarely face the challenges of globalization.

### **3.0 Methodology**

This is an exploratory research seeking to determine the effectiveness of the internal audit unit in fraud control and management at the third tier of government in Nigeria. The primary data was obtained through the administration of questionnaires, interviews and actual observation. The population of the study was 290 (made up of 206 Accounting staffs and 84 Internal Audit staffs across all the 30 Local Government Areas Councils in Osun State) out of which a sample of 165 (56.90%) was studied. The chi-square ( $X^2$ ) test statistics was used

to test the two hypotheses. Percentage analysis was used to investigate issues considered relevant to research but were not covered by the hypotheses.

#### **4.0 Results**

Two hypotheses were tested in this research. The findings from the hypotheses are discussed below:

##### **4.1 Hypothesis One**

Hypothesis one sought to find out if the statutory existence of internal audit unit in every local government council in Osun State would significantly prevent instances of fraud in Local government administration in the state. The finding of the study showed that establishment of internal audit unit would not prevent instances of fraud. This is so because the primary function of the internal audit is to evaluate processes that are in place and to identify any weakness in internal controls that might lead to undetected fraud. According to Effiok (2003), the internal audit is expected to anticipate problems, visualize improvements and propose preventive actions. Where such weaknesses are identified and reported to management for corrective actions and nothing is done in that regard on the part of management, and then fraud perpetration is imminent; notwithstanding the existence of internal audit unit. This finding was supported by the work of Abu-Saheed and Kabir (2012) who posit that the internal auditor has the responsibility to appraise the activities of other departments in an organization and provide management with information that is useful in assessing operational effectiveness.

##### **4.2 Hypothesis Two**

Hypothesis two investigated the impact of auditor's independence on fraud detection and prevention in local government administration in Osun State. The finding indicates that fraud prevention and detection in local government administration in Osun State does not significantly depend on the independence of the internal audit. Facts emerging from this research indicate that:

- (a) The internal auditor is usually a career civil servant employed and paid by the executive.
- (b) The internal audit staffs, like other civil servants are expected to be loyal to the government of the day if they want to retain their job.
- (c) Internal Audit is funded like any other units of government.

On the light of the facts listed above, this research found out that internal Audits lacks operational independence to detect or prevent fraud in local government administration in Osun State.

The finding is consistent with that of Maimako (2005) and Atuhire (2013) who posit that prevention of fraud and misappropriation is not solely dependent on the independence of the internal audit. Rather, there are other factors needed to enhance the prevention of fraud. This may be in line with the adage that says "He, who pays the piper, dictates the tune".

#### **Summary And Conclusion**

##### **5.0 Summary of Findings**

This research empirically examined the role of internal audit functions in curbing fraud in local government administration in Osun State.

The summary of the major findings of this research are as follows:

- (a) Existence of internal audit unit did not significantly prevent instances of fraud in local government administration in Osun State.
- (b) Fraud detection and prevention in local government administration in Osun State did not significantly depend on the independence of the internal audit unit.
- (c) Breaches of financial rules and memoranda including expenditure without supporting documents, absence of prepayment audit, expenditure without budgetary provision and refusal to answer audit queries are financial offences that occur quite frequently.
- (d) The internal audit unit as it is presently constituted in Osun State local government administration is highly ineffective to prevent fraud and financial infringement.
- (e) The internal audit lacks the operational independence to carry out its function.
- (f) The internal audit lacks financial autonomy to effectively deploy its weapon of financial watch dog over public funds.
- (i) Because of (e) and (f) above, the internal audit is unable to provide the needed checks and balances in fraud control in Osun State.

### **5.1 Conclusion**

This research empirically investigated the role of the internal audit unit in fraud prevention and detection in Osun State. Based on the findings of this research, the following conclusions are drawn in the context of Osun State of Nigeria. The internal audit unit in local government administration in Osun State is highly ineffective with regards to fraud prevention and detection. It was also concluded that fraud prevention and detection is not solely dependent on the independence of the internal audit.

In a nutshell, internal audit unit of local governments in Osun State did not fulfill and in reality does not contribute to the proper, regulated, economical, efficient and effective management of local governments. In the majority of local governments, internal audit has a systematic attitude, which consistently fails to assess and to develop the effectiveness of the risk management and controlling procedures of local government.

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