

**A STUDY OF THE INTERNAL CONTROL SYSTEMS EVIDENCE FROM
OFFINSO RURAL BANK LIMITED**

RICHARD NSOH ATUGUBA

CYNTHIA MAC – ANDOH

ANTHONY AKWASI BOATENG

ANTHONY OPOKU NUAMAH

ESTHER OWUSU APPIAH

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| NAME/ID | SIGNATURE | DATE |
|----------------------------------|-----------|-------|
| Richard Nsoh Atuguba/10135318 | | |
| Cynthia Mac-Andoh/10135206 | | |
| Anthony Akwasi Boateng /10135218 | | |
| Anthony Opoku Nuamah /10135205 | | |
| Esther Owusu Appiah /10135201 | | |

Supervisor's Declaration

I Hereby Declare that the Preparation and Presentation of the Dissertation Were Supervised
In Accordance With the Guidelines on Supervision Laid down by Christian Service
University College

Supervisor's Name

| | | |
|-------------------------|-------|-------|
| Mr. Eric Atta Appiagyei | | |
|-------------------------|-------|-------|

Head of Department's Name

| | | |
|-----------------------|-------|-------|
| Kwaku Ahenkorah (Dr.) | | |
|-----------------------|-------|-------|

ABSTRACT

This project work seeks to study the internal control systems of Offinso Rural Bank Limited. The Offinso Rural Bank limited was incorporated in as a private limited liability company on 4th day of July 2006 under the Companies Code 1963 (Act 179) and commenced Business on 10th October 2008.

In instances, where companies suddenly collapse, the obvious resounding question is “what went wrong?” a breakdown of the internal control systems are usually the causes.

The wide spread global corporate accounting scandals that assumed near epidemic proportion in recent years and also, taken cognisance of the fact that, the bank is new with a lot financial constraints has informed this study.

The total population of the employees of the bank comprised of twenty-eight of the three branches including head office and ten thousand self-employed and salary workers. The structured interview questionnaires were distributed to twenty staff both at head office and the branches and one hundred self employed, and two hundred salary workers representing seventy-one percent (71%) of the total sample size selected from employees and zero point zero three percent (0.03%) of the total customers’ population of the bank.

Findings: It was found that procurement committee was in place and all transactions were duly authorised and approved by the appropriate Officers. The Bank has instituted an effective mechanism to ensure that, the duties of one person are being checked by another.

However the assets of the bank have not been embossed with its initials and its identification numbers. The researchers recommended that all the fixed assets must be embossed with initials of the bank and its identification numbers and also, all fixed assets must be properly insured against fire, accident, theft, and natural disaster.

DEDICATION

This piece of academic work is dedicated to the almighty God for His guidance and protection throughout the undertaken of this project work.

It is also dedicated to our loved ones especially to our parents, spouses and children for their moral, prayers and financial support.

To our lecturers and all those who contributed in one way or the other to make this work a success.

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CHAPTER ONE

RESEARCH INTRODUCTION AND CONTEXT

1.1 BACKGROUND OF THE STUDY

Internal control systems in banking organisations are managerial tools used in banking operations towards achieving their objectives. These objectives includes efficient and effective operational measures, credit control systems, reliability of financing reporting and compliance with relevant and regulations (COSO 1992). In instances, where companies suddenly collapse, the obvious resounding question is “what went wrong?” a breakdown in the internal control systems are usually the causes. The absence of these variables mentioned above often result in organisation failure.

The wide spread global corporate accounting scandals that assumed near epidemic proportion in recent years inform this study. Notable case includes, Managing Director and chief financing officer of Cadbury Nigeria plc were dismissed in 2006 for inflating the profits of the company for the year before the company’s foreign partner acquired controlling interest. (Amudo and Inanga, 2008), and in South Africa, accounting scandals have been recorded in JCI, and Randgold and Exploration companies. These scandals emphasise the need to test, evaluate, scrutinise and formulate internal control systems of checks and balances to guide corporate executives in decision – making. These executives are legally and morally obliged to produce honest, reliable, accurate and informative corporate financial report periodically, (Amado and Inanga, 2008) so that it will meet the requirements of users globally to decide their investment drive.

The internal control systems seek to ensure that pre-audit function which is considered the most critical element in financial control concept are put in place by management through the internal audit unit to ensure that operations are carried out according to plan in order to achieve the overall objectives of the business enterprise. The pre-audit function in the past used to be concerned only with the vetting and passing of payment vouchers. Today the pre-audit function has moved on to include the operational review of all transactions and offer appropriate technical advice.

The rural banking system in Ghana was established by the Central Bank in 1976. This was in response to the need and the concern to make institutional credit and other formal financial and banking services easily available to the majority of Ghanaians, especially those living in the rural areas, thereby raising incomes and promoting growth generally.

Rural banking in Ghana takes its origins from the early 1970s. Prior to that period, the main operators in the rural financial market comprised branches of the universal banks, credit Unions as well as other entities in the informal sector such as money lenders, traders and 'Susu' collectors. Friends and relations were also important sources of rural finance.

Financial intermediation in rural Ghana was at a very low level compared to the situation in urban areas. Consequently, economic units in the rural areas were starved of financial resources. The banks which operated branches in rural areas mostly served the interest of large and medium-size enterprises and resource-based companies.

The banks were reluctant to modify their operations to suit the needs of the peasant farmers. Whatever they were doing was profitable enough without involving the supposedly high risk peasant farmer and small-scale operator. The small scale operators and peasant farmers were therefore generally neglected and were left to the mercy of informal sector intermediaries like money lenders 'susu' operators, cocoa marketing cooperatives, etc., who charged usurious interest rates. This deterred prospective borrowers and tended to discourage indigenous entrepreneurs. Little credit therefore reached the peasant farmer or artisan in the rural areas, although the banks, to some extent, financed some commercial farming enterprises that were sparsely scattered in the rural areas. This situation created a gap in the provision of institutional credit to the peasant farmer and rural dweller. The absence of institutional credit undoubtedly created a huge problem for rural dwellers. It manifested in the form of low acreages under cultivation, poor farm maintenance practices, inadequate or no fertiliser application, generally poor agronomic and animal husbandry practices.

These negatives resulted in poor yields which translated into poor incomes for the farmer. The problem therefore got exacerbated if after a year, the farmer had to contend with the money lender again for his credit needs. The irony of this scenario is that rural Ghana abounds in wealth. Cocoa, timber, gold, manganese, and diamond, fruits like oranges, bananas, pineapples, pawpaw, pears and food crops generally are all products of rural Ghana. It was quite evident that if economic activities in the rural areas of the country were to be enhanced and sustained, then some kind of institutional arrangement had to be put in place to address the problem of inadequate credit. To do this, the Bank of Ghana carried out a study into the rural credit problems in Ghana in 1971 to ascertain why rural dwellers/operators could not avail themselves

of institutional credit from the existing that had rural branches and agencies. The recommendations gave birth to rural banking in Ghana.

1.2 STATEMENT OF THE PROBLEM

The rural banking system in Ghana was established purposely to bring the business of banking to the door steps of rural folks who were not the target of the commercial banks.

The rural business could not grow because they were obtaining their credit from small scale susu collectors, formally friends and members when the need for credit arise.

Ever since, rural banks have remained at their small scale level due to fraudulent practice on some of their staff who dissipates the banks money for their personal benefits.

Besides that, most credits that are granted end up becoming bad, hence the credit creation businesses of rural banks are facing major default risk.

In view of this many controls have been put in place to safeguard against loss of revenue from credit or misplacement, misappropriation of assets. This study was conducted to test the effectiveness of the controls in place at Offinso Rural Bank Limited.

1.3 OBJECTIVES OF THE STUDY

This seeks to study the internal control systems that are in operation in Offinso Rural Bank to achieve its short term profitability and long term survival.

Specifically the study seeks to:

- i. Identify the internal control systems put in place for risk assessment and whether procurement procedures are being adhered to by Offinso Rural Bank

- ii. Identify whether customers are operating within their credit limits that are set for all customers by credit officer
- iii. Recommend the appropriate policy measure that to improve and strength the internal control systems in Offinso Rural Bank Limited.

1.4 RESEARCH QUESTIONS

This paper seeks to test the internal control systems that are in operation in Offinso rural bank in order to achieve its short term profitability and long run survival. Specifically the paper seeks to find out the follow:

- i. Do customers of the bank operating within their credit limits that are set for all customers by Credit officer?
- ii. Are the procurement procedures put in place adhered to by Offinso Rural Bank Limited.?
- iii. What policy measures had been put in place to improve and strength the internal control systems in Offinso Rural Bank Limited?

1.5 SCOPE OF THE STUDY

The study covered the internal control systems in Offinso Rural Bank between 2008 and 2012. This study had conducted to assist all the staff to assess how they discharge their responsibilities and also to furnish top management with analyses, appraisals, recommendations and pertinent commentary on the activities of the bank.

1.6 SIGNIFICANCE OF THE STUDY

The significances of the study had been that:

- i. The Board of Directors finds appropriate solution to the problems of internal control systems of the bank.

- ii. Findings from the study are expected to help managers to have insight into the internal control systems put in place.
- iv. To other researchers, studying on a related subject, this study serves as a guide to enhance their work. It serves as a source of literature to other researchers, and the limitation of this research may be built on by others studying on the same topic.

1.7 ORGANISATION OF THE STUDY

The project is divided into five main chapters with subdivisions as follows;

Chapter one is divided into the background of the study, statement of the problems, objective of the study, Research questions, scope of the study, significance of the study and organisation of the study.

Chapter two consists of Literature review on internal control systems especially within the banking framework, Offinso Rural Bank as a focus.

Chapter three looks at the methodology of the research the population and sample of the study, and organisational profile of Offinso Rural Bank Limited. Presentation of findings, analysis and discussion of the work is contained in chapter four. Finally, chapter five covers the summary, recommendations and conclusions.

CHAPTER TWO

LITERATURE REVIEW

2.0 STUDIES ON INTERNAL CONTROL

This chapter is the compilation of definitions and nature of internal controls system, classifications of the system as well as the critical areas of such system. It also considers the benefits of internal controls and their limitation to enable the researchers test their effectiveness in Offinso Bank.

The auditing standards define an internal control system as “the whole system of controls, financial and otherwise established by 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”

It is also defined as a systematic measures (such as reviews, checks and balances, methods and procedures) instituted by an organisation to conduct its business in an orderly and efficient manner, safeguard its assets and resources, deter and detect errors, fraud, and theft, ensure accuracy and completeness of its accounting data, produce reliable and timely financial and management information, and ensure adherence to its policies and plans (www.businessdictionary.com).

William F. Messier Jnr; also defined internal controls as the process affected by an entity’s Board of Directors, Management and other personnel designed to provide reasonable assurance regarding the achievement of objective in the following categories.

- i. Operations control- relating to the effective and efficient use of the entity's resources.
- ii. Financial reporting controls- relating to the preparation or reliable published financial statement.
- iii. Compliance controls- relating to the entity compliance with applicable laws and regulations.

Millichamp, A.H: (2002), defines internal control as the whole system of controls, financial or otherwise, established by management in order to carry on the business of an 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.

Internal control is an integral process that is affected by an entity's management and personnel and is designed to address risks and to provide reasonable assurance that in pursuit of the entity's mission, the following general objectives are being achieved:

- i. Executing orderly, ethical, economical, efficient and defective operations;
- ii. Fulfilling accountable obligations;
- iii. Safeguarding resources against loss, misuse and damage from a management's perspective, testing the internal control systems is a way of meeting its (management) stewardship or agency responsibilities.

Management must reconfirm and also provide reasonable assurance that adequate control exists over the entity's assets and records. This can only be accomplished by developing internal controls that required employees to follow corporate policies and procedures such as proper

authorisation for transactions and periodically asking an independent person to check the internal control systems.

In his book auditing and Assurance service, William F Messier Jnr. emphasised the need for an internal control system so as to generate reliable information for decision-making. It further states that if the information system does not generate reliable information, management may be unable to make informed decisions about issues such as product pricing, cost of production and profit information.

2.1 TYPES OF INTERNAL CONTROLS

According to I. T. Okai (1996) Auditing For You, the types on which the Auditor seeks to rely vary widely. The main types of internal control systems which the Auditor may find and on which to seek some degree of release are as follows.

2.1.1 Organisation

Every enterprise ideally should have a plan of their organisation, defining and allocating responsibilities and identifying lines of reporting for all aspects of the enterprise's operations. Authority delegation within the organisation and responsibilities should be clearly specified.

2.1.2 Segregation of duties

It is important to separate those responsibilities or duties if combined enable one individual to record and process a complete transaction. Segregation of duties thus reduces the risks of intentional manipulation or errors and increases the element of checking. The functions which should be separated include authorisation, execution, custody, and recording and in the case of computer-based accounting systems, systems development and daily operations.

2.1.3 Physical

These are concerned mainly with the custody of assets and involve procedures and security measure designed to ensure that access to assets is limited to authorised personnel. This includes both direct and indirect access via documentation. These controls assume importance in the case of valuable, portable, exchangeable or desirable assets.

2.1.4 Authorization and approval

All transaction should require authorisation or approval by an appropriate responsible person. The limits for those authorisations should be specified.

2.1.5 Arithmetic and approval

These are the controls within the recording function which check that the transactions to be recorded and processed have been authorised, that they are all included and that they are correctly recorded and accurately processed.

Such controls include checking the arithmetical accuracy of the records, maintenance and checking for documents.

2.1.6 Personnel

There should be procedures to ensure that personnel have capabilities commensurate with their responsibilities. Inevitably, the proper functioning of any system depends on the competence and integrity of those operating it. The qualifications, selection, and training as well as the innate personal characteristics of the personnel involved are important features to be considered in setting up any control system.

2.1.7 Supervision

Any system of internal control should include the supervision by responsible officials of day-to-day transactions and the recording thereof.

2.1.8 Management

These are controls exercised by management outside the day to day routine of the system. They include the overall supervisory control exercised by management the review of management accounts and comparison thereof with budgets, the internal audit function and any other special review.

The above categories of internal control were extracted from the approved auditing guidelines

2.2 AUDITOR’S USE OF INTERNAL CONTROL

The auditor’s objective in evaluating internal controls is to determine the degree of reliance which may be placed on the information contained in the accounting records. Where he obtains reasonable assurance by means of compliance tests and procedures that the internal controls are effective in ensuring the completeness and accuracy of the accounting records and the accounting records, and the validity of entries therein, he may then limit the extent of his substantive tests or procedure.

2.3 OBJECTIVES OF INTERNAL AUDIT

The objective of internal audit as outlined in ARB Apex Bank, (2004), internal control and internal Audit for Rural and community Banks; Operational Manuel “is to assist members of the

organisation in the effective discharge of their responsibilities by furnishing them with analyses, appraisal, recommendations, counsel, and information concerning the activities.”

2.4 EVIDENCE OF INTERNAL AUDIT TEST

2.4.1 Compliance Test

Before the Auditor can place reliance on internal control system of an organisation, he is expected to carry out compliance tests. These are designed to obtain reasonable but not absolute assurance that those internal control on which the Auditor wishes to rely were functioning both properly and throughout the period. Compliance tests normally involve.

- i. Examination of evidence; the inspection of records, documents, reconciliation, reports etc. for evidence that a specific control appear to have been properly applied (e.g. inspecting signatures or initials on a purchase invoice evidencing that the invoice has been matched with a purchase order or goods received note or inspection exception reports.)
- ii. Re-performance- the repeating, either in whole or in part of the same procedures performed by the employee of firm(e.g. matching a purchase invoice with the corresponding purchase order)
- iii. Observation and enquiry- the observation of a procedure, together with informed enquiry about the procedure at other times. Observation and enquiry is a valid form of compliance testing, the only risk here is that the control may not be performed when the Auditor is absent.
- iv. In carrying out compliance tests or functional test as it is sometime termed the Auditor tests the controls and not transactions involved. Which may be the means/medium used for the test.

- v. As a result all weakness, breakdown, deviations, exceptions revealed by his test are recorded and investigated irrespective of the amount involved.

An exception here means where a control procedure has not operated correctly whether or not a quantitative error has occurred.

The result of compliance tests is a determining factor in assessing the extent of substantive work to be carried out. Thus the Auditor may place reasonable but not absolute reliance on the effective functioning of internal controls tested where the result of compliance tests does not indicate any weakness and/or exceptions. Reliability on internal control means the Auditor will limit the extent of his substantive test on information contained in financial records. If on the other hand the tests disclose exceptions which indicate that;

- i. Virtually controls are non- existent
- ii. Not operated properly or
- iii. Breakdown during the period under consideration

The auditor should ascertain the reasons for such exceptions, in determining the success.

The Auditor then assessed whether each weakness is an isolated departure, or is a representative of others and whether it raises the presumption of possible existence of fraud and/or errors in the accounting records if the explanations received suggest that the exception is only an isolated departure, then there must be a confirmation of the validity of the explanation for example by carrying out further tests. The controls cannot be relied on if there is a confirmation as a result of the further tests that internal control tested was being improperly operated.

Under such a circumstance the Auditor will increase the level of his substantive tests unless there are alternative/compensating controls.

2.4.2 Substantive Test

It is a test designed to obtain evidence as to the completeness, accuracy and validity of the data produced by the accounting system according to I. T. Okai (1996) Auditing For You. When the test is directed towards balance sheet items they are aimed at achieving the following objectives.

- i. Existence of assets and liabilities
- ii. Ownership of assets and responsibilities or obligation for liabilities
- iii. The values attributed to assets and liabilities
- iv. Completeness- that no materials items have been omitted
- v. The presentation of items in the accounts.

Substantive tests when applied to profit and loss items are designed to ensure that all items of income or expenses that have been earned or incurred and which have gone into the calculus of profit or loss are recorded in the appropriate accounts and financial period. The substantive tests directed to both balance sheet and profit and loss items enables the Auditor to ascertain whether the accounting policies of the company are appropriate and have been consistently followed.

Substantive tests are normally carried out:

- i. In noted areas of a firm's internal control where assessment indicates weaknesses,
- ii. In areas of the firm where compliance tests indicate that the system though assessed as strong is not complied with,
- iii. On all items not subject of internal control procedures. These include unusual or one-off transactions,
- iv. On all assets and liabilities,

2.5 INTERNAL AUDIT

Internal Audit constitutes an element of internal control systems established by management. I.T. Okai (1996) states that, internal audit is an independent appraisal activity within an organisation for the review of operations as a service to management. It is a management control which functions by measuring and evaluating the effectiveness of other controls within an enterprise. The appraisal here signifies an impartial assessment of a functional area of activity. It further reviews the procedural controls and various departments to assess whether or not the intended function is being carried out.

2.5.1 Substantive Tools For Carrying Out Tests

The following are some of the tools employed in substantive tests account balance and other relevant information in the account.

- i. Confirmation-
- ii. Inspection-
- iii. Re-performance
- iv. Vouching-
- v. Observation and enquiry

Confirmation

This consists of obtaining evidence on a fact or conditions from a third party with regards to account balance or information contained in the accounts confirmations obtained from persons who are independent of the client provides strong support for the fact or account balance and often serve as the principal substantive test of detail related to that account balance.

Inspection

This involves counting and/or examining physically transactions or items contained in the financial statement. Examples include cash count, examination of share certificate of fixed asset, observation of stock count etc.

Re-Performance of Computations

Where an account balance is derived as a result of certain computations, the substantiation of such balance may be carried out by recalculation that is, re-performance of the computation in order to confirm its accuracy. For example where a firm uses a certain formula to make provision for say bad and doubtful debts or for obsolete and slow moving stock, the Auditor in carrying out substantiate will;

- i. Evaluate the reasonableness of the basis of the computation and
- ii. Mathematically check the calculations.

Vouching

This deals with examination of documentary evidence giving rise to item in the financial Statement of an enterprise with the view to determining their nature and propriety.

Observation And Enquiry

These are used to assess how;

- i. Management compares actual with budgeted performances and
- ii. Exceptions are dealt with.

The assurance obtained by the Auditor in applying the above mentioned tools will in no small way influence his decision on the extent of substantive test to be carried out.

The tools already mentioned are mainly used as direct test of accounts balances and information as contained in management accounts. There are other tools of substantive tests but of a more general nature and these include.

- i. Analytical review procedures
- ii. Reading board and Annual General Meeting Minutes
- iii. Obtaining confirmation from company lawyers regarding pending litigations.
- iv. Security procedures and
- v. Reconciliation

2.5.2. Nature And Extent Of Substantive Tests

This depends on a lot of factors and is to some extent judgmental. The following are some of the factors that are normally taken into consideration

- i. The degree of reliance placed on internal accounting controls by the Auditor. Where through compliance placed test the Auditor obtains reasonable assurance as to satisfactory adherence to control procedures, he will decide to limit the extent of his substantive test work.
- ii. The materiality of the items in relation to the auditor avoids testing immaterial account balance unless it is absolutely necessary.
- iii. The possibility of an account being wrongly stated through fraud and/or error.
- iv. The extent to which exceptions are identified in the course of applying substantive testing procedures.

2.5.3 Internal Check

This is the area of internal control which is exclusively concerned with the prevention and early detection of errors and possibly fraud. It therefore involves the arrangement of book-keeping and other clerical duties in such a way as to ensure that.

- i. No single task is executed by only one person from its beginning to the end.
- ii. The work of each personnel engaged on a task is subject to an independent check in the course of another person's assignment.

This is normally achieved incidentally and yet intentionally within the course of the other clerical function. The purpose of internal check can be summarized as follow:

- i. To pin down to definite persons responsibility of particular acts defaults or omissions by the segregation of tasks.
- ii. To obtain confirmation of facts and entries physical and financial by the creation and preservation of necessary records.
- iii. To facilitate the breakdown of routine procedures so as to avoid bottlenecks and to establish an even flow of work.
- iv. To reduce to a minimum the possibility of fraud and/or errors.

The existence of an efficient and operative system of internal check makes it difficult for any extensive fraud to be perpetrated except as a result of collusion between various members of staff. Even with collusion however, fraud should not go undetected for any length of time provided comprehensive system exist such as ensuring rotation of employee between various jobs at time intervals. It must be noted that internal check does not make all fraud impossible. It is just like the existence of police force yet crime exists.

What internal check does is to make fraud more difficult by reducing temptations, putting obstacles in the way of potential criminals and greatly increasing their risk of detection.

2.6 LIMITATIONS TO INTERNAL CONTROL

According to Amudo, A. and Inanga, L (2008), although internal controls are of paramount importance they have their own limitation. No internal control however, elaborates and comprehensive, can guarantee efficient administration and reliability of records or can be a proof against fraudulent collusion especially on the part of those holding high positions of authority or trust. Authorisations controls can be abused by a person in whom authority is vested.

Other factors likely to undermine effective operation of controls are:

- i. Fatigue
- ii. Distraction; can easily be controlled through experience
- iii. Carelessness
- iv. Misunderstanding
- v. Errors of judgment and/or interpretation.

Making internal control systems effective for internal control system to achieve its desired objective, it must be effective and reliable. The following should be watch dogs.

- i. Procedural Manual must be followed
- ii. Inspection and Audit report must be accessed and act upon
- iii. Leadership inspiration and supervision is paramount important.
- iv. Management should support the process

Features of a successful control environment

A good and successful control environment exhibits certain attributes. These include:

- i. Commitment to trust and fair dealing
- ii. Commitment to quality and competence
- iii. Communication of ethical values
- iv. An appropriate organization structure
- v. Independence, integrity and openness at Board reporting level
- vi. A professional approach to financial reporting (finsec consult, 2008)

2.7 SUMMARY

It can be inferred from the above reviews that for every entity to succeed in achieving its goals and objectives it should not only have an evidence of effective internal control systems, and an effective and efficient internal Auditor but all parties should be committed to the process and periodically have a mechanism to test the system to find out whether they are working well. Thus, the objectives of a company are in away embodied in that of internal control and internal audit unit.

Therefore, the objective of internal control and internal audit unit and for that matter, a company will be defeated if there exist weak and inadequate internal control systems and ineffective internal Auditor as a result of challenges or limitations. Hence, it will be of great importance to ensure that there is some acceptable degrees of perfection in internal control systems and internal auditing unit which will periodical test the systems to find out whether they exist and are working.

CHAPTER THREE

METHODOLOGY AND ORGANIZATION PROFILE

3.1 INTRODUCTION

This chapter consists of Research Design, Population, Sample Size, Instrument used, Data Collection Technique as well as the method for Data Analysis. This chapter describes the research design and procedure employed in obtaining data for the study.

3.3 THE RESEARCH DESIGN

The strategy adopted is based on investigation into the internal control system of Offinso Rural Bank Limited.

The structured interview technique used for the data collection required the internal auditors of the bank, the operation manager, credits managers, the officers in charges (OIC's), and other fifteen employees, and some customers from the bank. These officers and customers had responded to different set of structured interview questionnaires posed by the researchers since they performed unique responsibility in the bank.

The heads of department were included because of their expertise in internal control systems and had the opportunity to give detailed account on whatever goes on in the various areas of the bank so far as internal control systems were concerned.

Also the questionnaires were divided into five sections and respondents responded to their field of specialization or operation.

3.4 POPULATION OF THE STUDY

The total population of the employees of the bank comprised of twenty-eight of the three branches including head office and ten thousand self-employed and salary workers. The structured interview questionnaires were distributed to twenty staff both at head office and the branches and one hundred self employed, and two hundred salary workers representing seventy-one percent of the total population. The bank operates a centralised system with four (4) departments, namely; Administration, Accounting, Credit and Internal Audit. The researchers visited the head office and the entire branches and their departments of the bank.

3.5 THE SAMPLE SIZE OF THE STUDY

The three (3) branches employees were made up of the General Manager, the Accountant, the Credit Manager, Internal Auditor and Head of systems from head office and other fifteen employees were sampled to respond to the structured interview questionnaires. This represents seventy-one percent (71%) of the total sample size selected from employees. The same technique was used to interview about one hundred self-employed and two hundred salary workers representing zero point zero three percent (0.03%) of the total customers' population out of ten thousand in the bank.

3.6 SAMPLING PROCEDURE

The researchers distributed structured interview questionnaires to twenty employees of the bank; that is; both seniors and juniors staff. Two hundred salary workers and one hundred self-employed customers were randomly sampled given these structured interview questionnaires at the premises of the bank. About fifty percent of these customers were assessing loans at the bank during that month.

3.6 THE DATA COLLECTION TECHNIQUE

The main data collection technique had been questionnaire designed in a structured interview form to guide and to ensure uniformity of responses from the interviewees. The three branches managers and all the senior staff members from head office were given the structured interview questionnaires to respond on the same issues. The General Manager, the Accountant, Credit Manager and, Internal Auditor and the System Officer responded to different set of questionnaires that had centered in their area of expertise. Other fifteen employees were given the chance to answer the questionnaires. Customers made up of one hundred self employed, and two hundred salary workers of the bank were also given the opportunity to answer the structured interview questionnaires.

3.7 THE DATA ANALYSIS

Qualitative data were collected from primary and secondary sources and used for the analysis. The primary data had obtained through the use of the structured interview questionnaires. The secondary data source had come from ledger account, payment vouchers and audited financial statement of the bank. These Secondary data were obtained on accounting, credit and audit departments of the bank concerning internal control system and had been analysed. These data collected from respondents are used to generate a table and pie chart with percentages.

3. 9. SUMMARY AND PRESENTATION

This chapter explained the procedures employed to collect the field data for the analysis of the study. A qualitative technique in the data collection was adopted for the study. Due to resource and time constraints the sample size of the population was twenty employees. Principally, structured interview questionnaires were used to collect the field data for the study. The analysis of the field data is presented as:

Section A of the questionnaires related to the back ground of the respondents. This section highlighted the gender, age, educational attainment, marital status, and type of job. Section B identifies the internal control systems of bank. Section C of the questionnaire relates to risk assessment the loans given by the bank. The operations manager and the branch accountants responded to the questionnaires in section D, which relates to the identification of control activities of the bank's transactions. The internal auditor and system administrator responded to questionnaires in section E that has to do with investigating the effectiveness and monitoring the systems of the bank.

The researchers undertook documentary analysis on the records and transaction activities of the bank as to how officers record and maintain the books of accounts ranging from cash transaction (lodgments, payment, and treasury and species movement), inter-agency control, credit control, office account control and general ledger control.

CHAPTER FOUR

RESULTS, FINDINGS AND DISCUSSION

4.0 INTRODUCTION

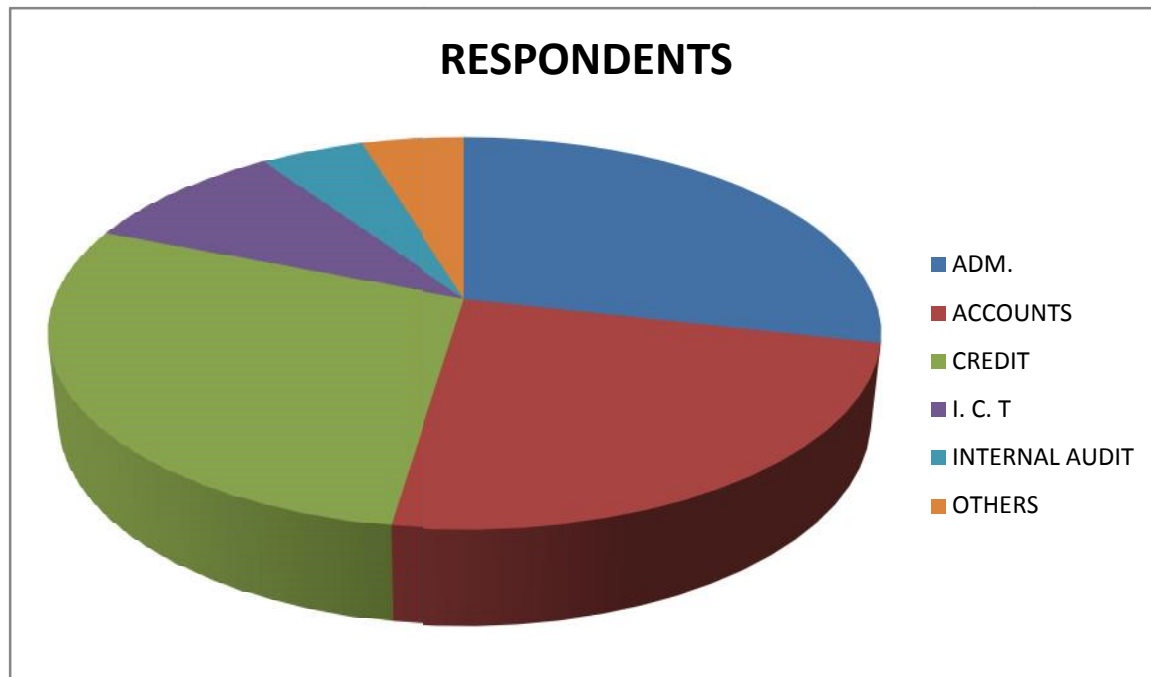
This chapter analysed the field data gathered from Offinso Rural Bank Limited and examined the findings in the light of the objective of the study. The data includes answers to the questionnaires of twenty employees of the bank, two hundred salary workers and one hundred self employed customers from different background. The responses from the respondents are described, analyses, and the inferences made to established relationships.

4.1 FINDINGS

TABLE 1

| DEPARTMENT | <u>NO</u> OF EMPLOYEES | TOTAL <u>NO</u> RESPONDED |
|----------------|------------------------|---------------------------|
| Administration | 8 | 6 |
| Accounting | 4 | 4 |
| Credit/loans | 7 | 6 |
| I. C. T | 3 | 2 |
| Internal Audit | 1 | 1 |
| Others | <u>5</u> | <u>1</u> |
| TOTAL | <u>28</u> | <u>20</u> |

TABLE 2



In findings out the internal control systems, the following methods were employed:

4.1.1. ACCOUNTING AND ARITHMETICAL ACCURACY

There were effective and reliable records of transactions in place at the bank. The accounting procedure ensures that transactions were fully recorded, classified, summarised and reported at any given time.

The accounting procedure includes the following:

- i. Waste sheet
- ii. Ledger Account Sheet
- iii. Non-cash transactions
- iv. Daily Balance Sheet

4.1.2. Waste Sheet

For financial control purposes, the bank has assigned an officer to write up the waste and balance it every day. The waste sheet records all transactions which took place during the day's work and it can also be used to prepare Daily Balance Sheet. The officer who prepares the waste sheet signs it and is cross-checked by the Accountant of the Bank.

4.1.3. Ledger Account Sheet

Ledger Account Sheet is used to record the bank's activities and gives evidence about all transactions routed through the bank. This ledger account sheet is used when a customer opens an account with the bank. The ledger sheet gives information like'

- i. Name of the customer
- ii. House Address/Business Address/contact number
- iii. Occupation
- iv. Specimen signature
- v. Passport size photograph

However the house address and two passport quarter size were not available in most of the customers' files. The above information is expected to be filled by the customer and account number is given. This information should be duplicated to the head office.

4.1.4. Non- Cash Transaction

This Non-Cash Transaction refers to any movement of transaction which does not involve cash. Transactions are executed using the impersonal voucher for debit and credit transfers. These impersonal vouchers are passed by an officer where a brief description of the transaction is stated together with the amount. After these vouchers have been passed, both the accountant and the manager signed to satisfy the control system. It was observed that most at time this is ignored and only one person signs.

4.1.5. Daily Balance Sheet (D.B.S)

This sheet is used by the bank as a summary of the day's work. It is also used by the accountant to affect postings into the general ledger. After this sheet has been prepared and signed by an officer, the accountant counter signs as a check and is filed for future reference. The researchers observed that because the bank operates more on manual than the computer, officers delayed in summarizing the day's work.

4.2 .0 INTER AGENCY CONTROL SYSTEM

The bank has branches where their activities are being controlled by the head office. The bank has established the following control systems in the branches to ensure that defalcations and errors are prevented. It was deduce that

4.2.1 Correspondence

Communication from the branch to the head office is though made by “memo,” it was found out that, there was no separate file for correspondence in order to ensure that no letter is lost in transit. The letters were not numbered serially. All letters addressed from branch to head office should be signed by the officer-in-charge and a register is kept to record all letters and circulars received, and if any is found missing, the branch immediately informed the head office. All correspondence must be acknowledged by the recipient.

4.2.2 Inter Agency Reconciliation

Reconciliation exercise is carried out at regular interval by the bank to ensure that transactions between the branch and the head office are reconciled to address any outstanding matters and prevent defalcation and errors. In so doing the head office has to communicate to the branch by issuing “Advice” indicating the particular transaction which is credited or debited to the branch and the vice versa. This advice is responded by the recipient and accordingly debited or credited as per the transaction. A register must be kept by the head office and the branch, which would be used to record transactions between them.

4.3.0 RISK ASSESSMENT

This is one of the major dependent variable identified in financial controls which emphasised on credit management to ensure that loans granted to customers of the bank are effectively managed to avoid losses.

The various sectors in which the bank concentrated in the disbursement of loans are as follows:

- i. Agriculture
- ii. Cottage Industries
- iii. Transport
- iv. Trading
- v. Others

4.3.1. LOAN FACILITY

Customers were given the structured interview questionnaires especially those who access loan facilities at the bank. It was found out that, the processing of the loan facilities took about two or more months for the Board of Directors to approve them.

The researchers observed that the credit department of the bank ensures monthly loan repayment and interest is updated. The credit officer ensures that the customer personal accounts is debited and transfer to the loan account at the end of the month. The credit officer of the bank then submits the returns to the supervising manager for onward submission to the board of directors to deliberate on the bank credit facilities position.

The advances are then classified in the following categories:

- i. Current (sectored),
- ii. Olem (up to 3 months),

- iii. Sub-standard (above 3 months to 6 months),
- iv. Doubtful (above 6 months to 18 months),
- v. Loss (over 18 months).

This classification of advances schedule is done to show whether or not a loan granted by the bank is repaid according to the agreed repayment period. This can quickly be checked and an immediate action taken to recover the loans. This was a commendable measures put in place by the bank. However, as many as ten customers went on retirement without finishing re-payment of their loans as salary workers. This means retirement of the applicants was not verified.

4.4. PROCUREMENT MANAGEMENT OF CURRENT AND FIXED ASSETS

The questionnaires which were meant for the employees of the bank to find out whether proper procurement of assets and to examine the procurement act in Offinso Rural Banks in its acquisition of fixed assets, the following reports were gathered;

- i. A capital expenditure budget was prepared at the beginning of the year with various departments and branches incorporating their assets that will be needed.
- ii. A procurement committee must review and approve it before board of directors' ratification and purchase requisition could be raised in a form of 'memo' to the procurement committee.
- iii. The procurement committee sort quotations from three different suppliers before one is finally approved, and payment advice is raised by the accountant which counter signed by the manager before the assets is purchased.
- iv. After delivery, an officer inspects the assets together with the delivery note and the assets are then recorded into proper books of accounts.
- v. It was observed that, the procurement committee was adhoc.

CHAPTER FIVE

SUMMARY OF FINDINGS, RECOMMENDATION AND CONCLUTION

5.0 INTRODUCTION

This consists of summary of the findings, recommendations and conclusions of the study.

It was that there were effective and reliable records of transactions in place at the bank. The accounting procedure ensures that transactions were fully recorded, classified, summarised and reported at any given time.

5.1 SUMMARY OF FINDINGS

5.1.1 Findings on Identifying Risk Assessment of the Bank

The analysis on identifying risk assessment of the bank revealed that:

- i. The bank had made it a policy that, in order to maintain its liquidity position and also to remain in the industry, mechanisms must be put in place to manage its credit facilities given to its customers. In so doing, it was realised that the bank had made it a policy that management would exercise due care by ensuring that loans granted to each applicant both self employed and salary worker is monitored right from the day it was granted till it is finally repaid.
- ii. The study further revealed that management had the following unique measures in a form of report, to monitor the loans so that the risk association with them are minimised to keep the bank's liquidity position high at all times.

Considering that loans are the most critical risk areas in banking, management had established special procedures and controls to ensure loans granted to customers were properly monitored and accounted for within a stipulated time. The bank also had a mechanism to recover the overdue loans. It was also realised that management convened meeting periodically for Board of directors to scrutinise and study the returns. Although, there were overdue loans which would not affect the operation of the bank at the moment, management have instituted plans to recover overdue loans. Such plans include:

- i. Enforcement of guarantee security provided by the customer.
- ii. Institute legal actions against the defaulted customer.

It is also revealed that management has recognised the present challenges in banking industry (Operational Risk) and as a result put in place effective plans to meet future challenges.

The management has also strengthened its controls in order to protect their reputation so that they would continue to win the trustworthiness of their customers and attract more customers for the bank.

5.2 FINDINGS ON IDENTIFYING CONTROL ACTIVITIES OF THE BANK

5.2.1 Authorization and Approval

It was realised that transactions ranging from the disbursement of loans, purchase of materials, inter-agency transactions, fixed assets, investment, and other related transactions have duly authorised and approved to ensure checks and balances.

5.2.2 Segregation of Duties

Segregation of duties in Offinso Rural Bank Limited, was seen as an effective mechanism that the bank had instituted to ensure that the duty of one person is been checked by another.. The Daily Balance Sheet shows the General Ledger various account headings.

5.2.3 Periodic Balancing and Checks

In order to ensure that internal control systems in the bank are effectively managed, management had instituted a policy that, both head office and branches must balance their ledgers twice every month and reconciled the differences that might occurred immediately. Inter-agency and head office reconciliation are also done monthly and the necessary entries are passed. It was also realised that the supervising manager occasionally conduct surprised checks on certain sensitive areas particularly the vault, cheque purchase transactions, current account ledger, savings and other subsidiary registers. The books and registers are always called for, for scrutiny by the manager to ensure that balances agreed with the general ledger. All records and vouchers of the bank were signed by the officer-in-charge and the manager to strengthen the controls systems.

5.2.4 Information and Communication

The study further revealed that all transactions between the head office and the branches were put in an advice form rather than verbal where appropriate debit transactions of a branch would be corresponded with credit transactions the head office through inter-agency account.

5.2.5 Internal Audit

There was an internal audit department in the bank. Unfortunately, the personnel needed to beef up the sector were inadequate. This might lead to monitoring problems of the banking operation. Management must employ an internal auditor to exercise oversight control over the internal control systems. Policies must be established by management to ensure that the objectives of the bank are achieved. It was also revealed that management does not have audit committee at the Board of Director structure that would ensure that policies and procedures are adhere to and enforce compliance.

5.3 FINDINGS ON MONITORING SYSTEM PUT IN PLACE FOR EFFECTIVENESS OF THE INTERNAL CONTROL SYSTEMS OF THE BANK

5.3.1 Monitoring

Management was able to submit the prudential reports and complied with the banking regulations of maintaining primary reserves to its maximum. The Bank of Ghana and ARB Apex Bank use these prudential reports to monitor the operations of the bank and where necessary give advice to strengthen the internal control systems.

The following are examples of prudential reports submitted to Bank of Ghana and ARB Apex Bank;

- i. Important Financial Indicators (Appendix 6)
- ii. Statement of Assets and Liabilities (Appendix 7)
- iii. Profit and Loss Account (Appendix 8)
- iv. Dormant Accounts Analysis (Appendix 9)
- v. Capital Adequacy Ratios (Appendix 10).

5.3.2 Incentives Package

It is recommended that the bank should institute incentive packages like scholarship, award scheme and special bonuses for the employees in order to motivate them to work harder to maintain and improve the human capital of the bank.

5.3.3 Safeguarding of Assets

- i. It is recommended that the bank takes up an insurance policy against the cash holdings in the vault against fraud, fire and natural disaster.
- ii. It is also recommended that the bank takes up an insurance cover against the movement of cash, accident and burglary from the head office to the branches and vice versa.
- iii. The provision of communication facilities should be given to the security personnel to safeguard the bank and its staff.
- iv. It is further recommended that all the assets of the bank be embossed with initials of the bank and identification numbers.
- v. All the fixed assets must also be properly insured against fire, accident, theft, and natural disaster.

5.3.4 Stationery

- i. It is recommended that the bank should maintain reasonable level of stationery to avoid waste.
- ii. It is also recommended that different supplies must be considered in selecting process to engage efficient and reasonable pricing for value for money.
- iii. It is further recommended that the head office supplies stationery regularly to the branches.

5.3.5 Dormant Accounts

- i. Dormant ledger at various agencies must be calculated and balanced at the end of every month and any discrepancies noted must be reconciled and reported to the head office immediately for action.
- ii. It is further recommended that the dormant ledgers which have been reactivated from the dormant accounts should be properly authorised by the accountant and entries must be passed to reflect the new dormant account balance in the general ledger.

5.3.6 Computer Networking

It is recommended that the bank should network its operations, by network all the various branches to ensure smooth transactions and effective communication among the branches and the head office. This will enhance the bank activities.

5.3.7 Independence of an Internal Auditor

It is further recommended that the internal auditor exercise his independence in discharge of his duties. Management should treat audit reports as urgency as possible.

5.3.8 Recommended for further studies

During the research, a number of issues came up, that could have impacted on the current findings which were identified in the course of the work. Due to time and resources constraints, these were not considered and could be useful area for future studies. However, future researcher could benefit from the following suggestion:

- i. Like the previous studies, the present study used a relative small sample size to analyse the same date under consideration. A future study could use a large sample size to analyse the same issue under consideration.
- ii. The previous studies have evaluated the financial controls by using case study. A future study could be extended to all the Rural Banks in Ghana by talking sample from all of them.
- iii. Despite the results of the present study, another researcher could take up the topic with appropriate policy and measures that would improve the effectiveness of the internal control and research into by adopting survey or use the multiple samples to draw conclusion for the study.

5.4 CONCLUSION

The investigations of the research revealed the internal control systems in Offinso Rural Bank Limited. However, the effectiveness of the internal control could be described as satisfactory. The study further revealed the following setback.

There is the need to employ additional project officers and auditors to lessen the work load and improved the monitoring systems to ensure effective and efficient internal controls.

There was no immediate policy of training and development programme for the junior staff. Furthermore, the bank needs to motivate its staff to work harder and retain high caliber of staff. The Board of Directors needs to strengthen the control system in the area of stationery, dormant accounts and safeguarding the assets of the bank.

There is no computer networking which makes it difficult for the head office to communicate with the branches effectively. Apart from the above, the management was able to maintain and control the credit department, regular balancing of ledgers, and segregation of duties. Proper authorisation and approval were made to ensure the effectiveness of the bank's operations.

From the researcher observation, the staff of the bank exhibited competencies in their discharge of duties and commitment to work. The Board of Directors also played useful role by ensuring that scrutinisation of reports submitted by supervising manager. There is a policy to meet every month to discuss and sanction any personnel where necessary.

This study is purely for academic exercise, and more of the intended purpose of the research is clearly stated in the introductory chapter. The work will not be achieved if the research does not benefit the bank which provided material for the project.

In conclusion therefore, the existing problems being experienced by the bank can be solved, if the suggestion outlined in the research made available to the Board of Directors and Management of the bank. It is the belief of the researchers that management will put these recommendations into practice.

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APPENDIXES

OFFINSO RURAL BANK

P.O. BOX 295

OFFINSO

.....

Dear Sir/Madam

APPROVAL OF LOAN/OVERDRAFT FACILITY

In response to your application, we are glad to inform you that a loan/overdraft of Has been approved in your favour for..... months under the following conditions:

- (1) The rate interest chargeable on the facility shall be the rate in force during the tenure
of the loan, which at the moment is
.....
- (2) You will be required to provide a suitable guarantor.
- (3) You will be required purchase Worth of the Bank's
- (4) You will be required to maintain minimum sayings balance
of on which the bank will hold lieu for the period of the facility.

Kindly indicate your acceptance of these conditions by signing and returning to us the
attached **MANAGER**

FOLLOW – UP/MONITORING REPORT

Date of Visit;

Contact Person:

1. General Information.

Name of Customer

Nature of Business:

Location of Project/Business:

Purpose of Facility

2. Status of Facility

Amount Approved:

Date Approved:

Period of Facility:

Expiry Date:

Outstanding Balance:

Amount Paid/Promised to pay:

3. Project Performance/Personal Observation:

4. What action needs to be taken by the borrower?.....

5. Recommendation/Conclusion:.....

5. Date of Next Visit:

OFFINSO RURAL BANK LTD.

BRANCH

.....

TREASURY OUT VOUCHER

DateMonth Year.....

CREDIT

(NOTES AND COINS ONLY)

| | | | |
|--------------|--|--|--|
| NOTES | | | |
| GH ¢ 50 | | | |
| GH ¢ 20 | | | |
| GH ¢ 10 | | | |
| GH ¢ 5 | | | |
| GH ¢ 1 | | | |
| COINS | | | |
| GH ¢ 1 | | | |
| 50 Gp | | | |
| 20 Gp | | | |
| 10 Gp | | | |
| 5 Gp | | | |
| 1 Gp | | | |

TOTAL GH ¢

Amount in (word).....

..... GH ¢ Gp

Signature

Accountant Cashier

OFFINSO RURAL BANK LTD.

DAILY BALANCING SHEET

GENERAL LEDGER

Date.....

Checked by:

Call over by:

OFFINSO RURAL BANK LIMITED**IMPORTANT FINANCIAL INDICATORS AS AT 2012**

| | | | MONTHS | |
|-------|---------------------|-------|---------|---------|
| | | MARCH | FEBUARY | JANUARY |
| (a) | Savings | | | |
| (i) | No. of Customers | | | |
| (ii) | Balance | | | |
| (iii) | % of Total Deposits | | | |
| | | | | |
| (b) | Demand Deposits | | | |
| (i) | No. of Customers | | | |
| (ii) | Balance | | | |
| (iii) | % of Total Deposits | | | |
| | | | | |
| (c) | Fixed Deposits | | | |
| (i) | No. of Customers | | | |
| (ii) | Balance | | | |
| (iii) | % of Total Deposits | | | |
| | | | | |

| | | | | |
|-------|--|--|--|--|
| | LIQUID ASSETS | | | |
| (a) | Cash Balance | | | |
| (b) | BOG Clearing Account | | | |
| (c) | ARB APEX Bank Clearing Account | | | |
| (d) | Other Bank Clearing Account | | | |
| (E)d | 5% Deposit placement with Apex Bank Ltd. | | | |
| | | | | |
| | INVESTMENTS | | | |
| (i) | Treasury Bill | | | |
| (ii) | Deposit at Call | | | |
| (iii) | ARB APEX ACOD | | | |
| (iv) | Inter Banks Lending | | | |
| | | | | |
| 3 | RESERVE ASSETS RATIO | | | |
| (a) | Primary Reserve: | | | |
| | Surplus | | | |
| | | | | |
| (b) | Secondary Reserves: | | | |
| | Surplus | | | |
| | | | | |
| (4) | LOANS AND OVERDRAFTS | | | |
| | LOANS | | | |
| (a) | LOANS | | | |

| | | | | |
|-------|---|--|--|--|
| (i) | No. of Customers | | | |
| (ii) | Outstanding Balance | | | |
| (iii) | Overdue Balance | | | |
| | | | | |
| (b) | OVERDRAFTS | | | |
| (i) | No. of Customers | | | |
| (ii) | Outstanding Balance | | | |
| (iii) | Overdue Balance | | | |
| (c) | % of loans and overdrafts to Total Deposits | | | |

APPENDIX II

QUESTIONNAIRE

This questionnaire is intended for the collection of data to help the researchers to investigate into the internal control systems of Offinso Rural Bank Limited. The exercise is purely for academic purposes. Whatever information provided will be kept confidential.

Please complete this questionnaire as appropriate with brief reasons or tick where necessary.

SETION A

BACKGROUND OF INTERVIEWWEE

- | | |
|-----------------------------------|---------------------------|
| 1. GENDER: Male () Female () | 3. Educational Attainment |
| 2. Age: | |
| i) 20-30 years () | i Basic () |
| ii 31-40 years () | ii. Secondary () |
| iii. 41-50 years () | iii. Tertiary () |
| iv. 51- 60 years () | |
| v. Above 60 years () | |
| 4. Designation / position / Grade | 5. Marital Status |
| i) Accountant | Married () |
| ii) Internal Auditor | Single () |
| iii) Project Officer | |

SETION B

IDENTIFYING TYPES OF FINANCIAL CONTROL SYSTEM

6. Who is responsible for setting up internal control systems and why?

7. How many types of internal control systems do you have in Offinso Rural Bank Limited?

.....

SECTION C

IDENTIFYING RISK ASSESMENT OF THE BANK

8. How many projects Officer do you have in Offinso Rural Bank Limited?

.....

9. Who is supposed to approve loans on behalf of the bank to customers?

.....

10. Mention the number of sector the bank is interested to grant loan facilities and why?

.....

11. State any mechanisms the bank used to monitor the life of a loan granted to a customer?

.....

SECTION D

IDENTIFYING CONTROL ACTIVITIES OF THE BANK

12. Do the bank has procurement policy in place

Yes () No ()

DO the bank has procurement committee

Yes () No ()

If yes, what are the responsibilities of procurement committee?

.....

13. Who authorize payment on behalf of the Bank?

14. How do you ensure that branch and the head office communicate effectively on business transactions?

SECTION E

INVESTIGATION EFFECTIVE MONITORING SYSTEM OF THE BANK

16. Does the bank have audit committee as part of their board?

- a. Yes () b. No. ()

17. In what circumstances will internal auditor be considered as an independent in performance of your duties?

.....

18. Is the bank regularly submits returns to supervising bodies like Apex and Bank of Ghana as required by law?

- a. Yes () b. No ()

19. How will you rate the internal control policies and procedures of the bank?

- i) Strong ()
ii) Satisfactory ()
iii) Weak ()