



University of Fort Hare
Together in Excellence



Excellence in Public Administration & Community Service

School of Public Administration

(SPA)

Faculty of Management and Commerce

**THE EFFECTIVENESS OF INTERNAL FINANCIAL CONTROLS WITH
SPECIFIC REFERENCE TO THE EASTERN CAPE PROVINCIAL
DEPARTMENT OF BASIC EDUCATION.**

BY

SABELO TINI

9757899

**A MINI-DISSERTATION SUBMITTED TO THE FACULTY OF
MANAGEMENT AND COMMERCE IN FULFILLMENT OF THE
REQUIREMENTS FOR THE DEGREE OF MASTER OF PUBLIC
ADMINISTRATION**

SUPERVISOR: PROFESSOR MOHAMED SAHEED BAYAT

Declaration

I the undersigned, Sabelo Tini hereby declare that this dissertation is my original work and that it has not been submitted, and will not be presented in any other university for a similar or any other degree award.

Signature

Date

ACRONYMS

INTOSAI	:	International Organisation of supreme Audit Institutions
COSO	:	Committee of Sponsoring Organisations of Treadway Commission
AGSA	:	Auditor General South Africa
PFMA	:	Public Finance Management Act
ECDoE	:	Eastern Cape Department of Education
MEC	:	Member of the Executive Council
EU	:	European Union
AGSA	:	Auditor General South Africa

ACKNOWLEDGEMENTS

I would like to thank my supervisor for his patience during my project and the entire staff of the University of Fort Hare Bhishe campus for their support, also I would like to thank family and friends for their encouragement and support they have shown during my studies.

Abstract

The purpose of this study was to assess the effectiveness of internal financial controls with specific reference to the Eastern Cape provincial department of basic education. A self-administered questionnaire was used to collect data. The questionnaire was filled by the respondents who are directly involved in processing payments and procuring for the departments.

The findings have shown that Internal control system does exist within the department however the implementation and monitoring of its effectiveness needs to be strengthened.

The findings show that the internal control system has an important role to play in attaining desired positive results within the department.

Internal control effectiveness is one of the most important aspects in any organisation, whether in a private sector or in the public sector. It determines the stewardship of an entity's management. The PFMA states that the accounting officer of a department must ensure that that department has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

If public officials could strictly adhere to the stipulated internal controls, there will be a positive response to accountability and also in service delivery as expected by the citizens.

Public accountability gives a reflection on how does the entity conduct its business affairs in terms of adhering to the norms and standards as prescribed by the law and whether there are any strong controls to prevent acts of fraud and corruption.

Contents

CHAPTER 1.....	
INTRODUCTION AND BACKGROUND OF THE STUDY	
1.1 INTRODUCTION	4
1.2 Background of the Eastern Cape Province.....	6
1.3 Statement of the problem	7
1.4 Research Questions	8
1.5 Objectives of the study	8
1.6 Significance of the Study.....	8
1.7 Research Methodology.....	9
1.7.1 Target population	9
1.7.2 Qualitative Research Method.....	9
1.7.3 Quantitative Research Method	10
1.7.4 Sampling.....	11
1.7.5 Data collection	11
1.8 Method of Data Analysis.....	11
1.9 Delimitation of the study	11
1.10 Ethical Consideration	12
1.11 Summary	13
CHAPTER 2.....	
LITERATURE REVIEW	
2.1 Introduction	14
2.2 Concepts and Integrated Framework on Internal Control	17
2.2.1 Legislative provisions on internal control in the public service.....	20
2.2.2 An integral process	20
2.2.3 Effected by management and other personnel	20
2.2.4 In pursuit of the entity’s mission	20
2.2.5 To address risks	21
2.2.6 Provides reasonable assurance	21
2.3 Components on internal control	21
2.3.1 Control Environment	21

2.3.2	Risk Assessment.....	24
2.3.3	Control Activities	25
2.3.4	Information and Communication	27
2.3.5	Monitoring Activities	28
2.4	Roles and Responsibilities in Internal Controls	29
2.5	Characteristics of internal controls	30
2.6	Limitations on Internal Control Effectiveness	31
2.7	Internal Control and the Management Process	33
2.8	Summary	37
CHAPTER 3.....		
RESEARCH METHODOLOGY.....		
3.1	Introduction	38
3.2	Research Methodology for this study.....	38
3.3	Research Design	39
3.4	Units of analysis.....	40
3.5	Data Collection	40
3.6	Sampling process and sampling procedure	41
3.7	Variables	41
3.7.1	Dependant variables	41
3.7.2	Independent variables	41
3.8	Method of Data Analysis.....	42
3.9	Delimitation of the study	42
3.10	Ethical considerations.....	43
3.11	Demographic characteristics of the study sample	43
3.12	Summary	44
CHAPTER FOUR.....		
RESEARCH FINDINGS AND RESULTS.....		
4.1	Introduction	45
4.2	The existence of the internal control system within the Eastern Cape Provincial Department of Basic Education	45
4.3	Conceptualising the effectiveness of internal control with the Eastern Cape Provincial Department of Basic Education	46

4.4	Understanding of the internal control system by the employees.....	48
4.5	The implementation of Internal Controls	49
	SUMMARY	51
	CHAPTER FIVE	
	RECOMMENDATIONS AND CONCLUSION	
5.1	INTRODUCTION	52
5.2	Discussion of findings.	52
5.2.1	Internal control systems in the Eastern Cape Department of Basic Education.....	52
5.2.2	Assessing Control environment component	52
5.2.3	Assessing Risk assessment component.....	53
5.2.4	Assessing Control activities component.....	53
5.2.5	Assessing Information and communication component	53
5.2.6	Assessing Monitoring component	54
5.3	Recommendations.....	54
5.4	Conclusion.....	56
5.4	REFERENCES	58

CHAPTER 1

INTRODUCTION AND BACKGROUND OF THE STUDY

1.1 INTRODUCTION

The government sector in South Africa comprises the national and provincial governments, municipalities, constitutional institutions, public entities and higher education institutions. The primary activity of these government units is the provision of goods and services to the community or to individual households free of charge or at prices that are not economically significant and to redistribute income and wealth by means of transfers.

The Constitution of the Republic of South Africa states that the national legislation must establish a national treasury and prescribe measures to ensure both transparency and expenditure control in each sphere of government by introducing uniform treasury norms and standards. It stipulates a framework for the division of responsibilities between national, provincial and local government. It prescribes an equitable division of revenue between the spheres of government, taking into account their respective functions. It has also created an independent Auditor General and an independent central bank, and sets out the principles governing financial accountability to parliament, as well as the annual budget process.

The concept of internal control and all its concomitant principles apply to both the private sector world of business and to the government sector. The INTOSA describes internal control one of the primary functions of all managers in government: The head of each government organisation must ensure that proper internal control structure is instituted, reviewed and updated.

The importance of internal control in the South African Government sector was brought to the fore and re-emphasised with the issue in 1999 of the Public Finance Management Act (Act1/1999 as amended by Act 29/1999). The objective of the PFMA is to secure accountability and sound management of revenue, expenditure, assets and liabilities of the institutions to which to which the act applies.

A guide for accounting officers in respect of the PFMA, issued by the National Treasury (2000), makes it clear that all members in government have a responsibility for the operation and ownership of the system of internal control for their departments/sections, at their appropriate levels. In short, internal control is deemed to be fundamental to achieving successful financial management in the South African government sector ó the concept pervades all areas of government, involving officials and other formal structures at all levels of government. (Botha, 200: 51-52)

The Internal Control-Integrated Framework published by COSO (committee of Sponsoring Organisations of the Treadway Commission) defines Internal control as a process, effected by an entity ñs board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- É Effective and efficiency of operations
- É Reliability of reporting
- É Compliance with applicable laws and regulations

Guidelines for internal control standards for the public sector defines internal control as an integral process that is effected by an entityø's management and personnel and is designed to address risks and to provide reasonable assurance that in pursuit of the entityø's mission, the following general objectives are being achieved.

- Executing orderly, ethical, economical, efficient and effective operations
- Fulfilling accountability obligations
- Complying with applicable laws and regulations
- Safeguarding resources against loss, misuse and damage.

National treasury plays a role in managing government expenditure and draws its mandate from the Public Finance Management Act, 1999. One of the major aims of national treasury is to regulate financial controls, by granting accounting officers of spending agencies more autonomy in financial decision-making within the ambit of impending financial legislation.

The consolidated financial information for national departments for the 2010/11 financial year showed a deficit of R133 billion. This shows that national departments overspent their budgets.

During his budget speech for 2010/11, the Provincial MEC for Finance Mr Mcebisi Jonas stated that one of the challenges in the province of the Eastern Cape was the potential overspending against budgets in the 2009/10 financial year by the two large departments: Department of Health and the Department of Basic Education.

The audit outcomes for the 2010/11 financial year showed that out of 14 departments 8 received unqualified audit opinions, 6 received qualified audit opinions and one department received a disclaimer of opinion.

1.2 Background of the Eastern Cape Province

This study focus in one of the country's poorest provinces both in economy and poor service delivery. The Eastern Cape is home to 6.7 million people, equivalent to 12.8% of the national population. The following are some of the salient demographic characteristics of the province: the Eastern Cape is comprised of relatively young population; a declining but higher than national average fertility rate; a working age population that is increasingly female; and below-average life expectancy rate.

The province faces significant social challenges: namely, addressing poverty, income inequality, food insecurity, and unemployment. The Eastern Cape is frequently measured as the poorest province in South Africa. Within the Eastern Cape, poverty is widespread, but is most prevalent within Alfred Nzo District Municipality, followed by OR Tambo District Municipality. On the positive side the Eastern Cape has managed to reduce poverty levels between 2007 and 2011, particularly, in the OR Tambo DM. In addition, average deprivation levels are examined by DM so that further reductions in poverty can be achieved through proper targeting of interventions.

The economy of the Eastern Cape is strongly driven by the tertiary sector. The tertiary sector accounted for approximately 77% of the provincial Gross domestic Product (GDP) in 2011, a 1.7

percentage point increase compared with its 2002 level. On the flip side, the secondary and primary sectors, registered a 1.2 and 0.5 percentage point decline respectively. In 2011, 60% of the 1.3 million unemployed people were employed in three sectors, namely, community services (26.1%), trade (23.5%) and manufacturing (12.2%).

1.3 Statement of the problem

During the 2010/11 audit the Auditor General could not express an opinion on the financial statements because of lack of documentation to support the expenditure incurred by the department this problem was a result of internal control measures not being implemented by senior management.

The accounting officer did not submit all the required monthly reports to the relevant treasury and the executive authority on actual revenue and expenditure for the year.

- The departmental environment is not conducive to accountability and service delivery through positive attitude, integrity, competence and ethical behaviour.
- The lack of oversight and accountability of senior management has perpetuated the negative outcomes over the past five years.
- The department does not have adequate processes in place to identify and record irregular and fruitless expenditures, as there is lack of monitoring by senior management. (Auditor General, 2010-11)

During 2013/14 financial year the Auditor General expressed a qualified opinion citing the weakness and deficiencies that have been prolific in undermining the internal control environment over the past number of years not being adequately addressed and as a result the sustainability of the audit outcome was seriously questioned.

This clearly shows weakness in the internal controls of the department and hence an overhaul of these internal controls is of necessity and needs to be treated as a priority in improving accountability by the Eastern Cape Department of Education.

1.4 Research Questions

- What is the commitment of the Department of Education to Internal Controls with regards to the provision of services that is not questionable?
- What is the role of the Department of Education to the implementation of Internal Controls in turning service delivery into service excellence that will bring about clean audit report?
- How well is the Department committed in transforming the public service through Internal Controls?

1.5 Objectives of the study

- To investigate the effectiveness and functionality of the existing financial internal controls in the Eastern Cape Provincial Department of Basic Education.
- To ascertain the extent to which management assess the effectiveness of the department's internal control and also to ascertain the understanding of internal control by staff members.
- To assess the strategies of the Department in implementation of Internal Controls.
- To evaluate the core business of Internal Controls in the transformation of service delivery.

1.6 Significance of the Study

This study is of significance to the department as it seeks to find a solution to the problem of financial reporting within the Department of Basic Education; the study will recommend mechanism by which the department can enhance its internal controls

1.7 Research Methodology

According to Leedy and Ormond (2005: 2) research is a systematic process of collecting, analyzing, and interpreting information (data) in order to increase our understanding of the phenomenon about which we are interested or concerned.

Research methodology is a way to systematically solve the research problem. It may be understood as a science of studying how research is done scientifically. In it we study the various steps that are generally adopted by a researcher in studying his research problem along with the logic behind them. (Kothari. 2004: 8)

The study seeks to investigate the impact of internal controls in financial management in the Eastern Cape Provincial Department of Education. There are two methods that can be used when undertaking a research proposal quantitative and qualitative method. The research method that will be used in this study is the quantitative method because it provides a broader scope, allows one to look at the broader scale of the society. Quantitative research also uses personal administered questionnaires where one provides the explanation that would give a broader understanding.

1.7.1 Target population

The targeted population will be officials across the financial spectrum within the department specifically on supply chain management, payments section and salary administration. These will include, Directors, Deputy Directors, Assistant Directors, and other staff members at head office.

1.7.2 Qualitative Research Method

According to Schostak, (2002:230) there are different forms of qualitative research such as ethnography, case study, action research and evaluation which often combine and overlap. There are also many perspectives or schools of thought who interpret qualitative research in different ways, for example Marxism, empiricism and others. Qualitative research typically focuses on compiling a selection of micro level case studies which are investigated using informal interviews. Qualitative researchers are interested in giving answers to the questionable processes

which do not simply accept the quantitative answers. As the case may be it does not mean that quantitative data is not important but researchers need more than that. Qualitative research is the major form of educational research that is used at the present moment (Schostak, 2006:231).

1.7.3 Quantitative Research Method

In development research quantitative methods have typically been the main focus. Quantitative methods are commonly conceived as those methods which initiates from experimental and statistical methods in natural science. Quantitative research relies on statistics. Quantitative research employs questionnaires and sampling procedures that attempt to get rid of the individual the particular and the subjective. The research is based on deductive method which starts with generalisation. Quantitative research method follows the step of natural science which starts with theory (Schostak, 2006:231).

The research method that will be used in this study is the qualitative method. Qualitative research method seeks to answer to the questions. Qualitative research method systematically uses predefined set of procedures to answer the question. The qualitative research method produces collective evidence, produces procedures findings that were not determined in advance. This method produces findings that are applicable beyond the immediate boundaries of the study. Qualitative research method is also effective in identifying intangible factors such as social norms (Bernard, 2005).

Qualitative and Quantitative research methods primarily differ in:

- Analytical objectives
- Types of questions posed
- Type of data collection
- Forms of data they produce, and
- Degree of flexibility built into the study design

The key difference between these two methods is their flexibility. Qualitative methods are typically more flexible, they allow the researcher to do a desktop research. This study will be

conducted through a desktop research. Information will be accessed through internet, books, including online journals, data from news clippings, from national, provincial and local government sources.

1.7.4 Sampling

Sampling is a statistical practice concerned with the selection of a subset of individuals from within a population to yield some knowledge about the whole population for the purposes of making predictions based on statistical inference. The sampling for this research will not cover the whole population as it is not possible to survey the entire population. Adèr, Mellenbergh, & Hand, 2008: suggests that there are two reasons that population cannot be whole studied, the cost of conducting a research might be too high, and the population might be dynamic in that the individuals making up the population may change over time

1.7.5 Data collection

Data will be collected from the officials across the financial spectrum within the department. These will include, Chief Directors, Directors, Deputy Directors, Assistant Directors and other staff members at the head office

1.8 Method of Data Analysis

Data collected becomes meaningless if it is not analysed, interpreted and deduction are not made on it. A collected data will require a comprehensive analysis for a researcher to be able to attach value to the data.

1.9 Delimitation of the study

Although the study will be carefully prepared there will be limitations to it. First because the study will be conducted mainly from the head office because the districts are responsible mainly for education management. Second, since the questionnaire will be designed to measure the officials' responsibility in applying the internal controls they might be reluctant in giving the correct information or might be discouraged to provide a feedback. Third, since the researcher

will mainly focus on three units within the department and will not go to other units such as budget, accounting services, internal audit and other financial related units the population might be small.

Managers in the public service have a key role to play in creating an environment for their staff to become effective in the way they interact with their work. This requires the motivation of employees to have the necessary tools to do their work. Public officials are less interested in acquiring knowledge of what Internal Controls entail

1.10 Ethical Consideration

According to Struwing and Stead, 2006, ethics in research refers to the system of morals, rules, behaviour and code of good morals on how to conduct research in a morally acceptable way. Brynard and Hanekom, 2006, are of the same view with the latter; that research ethics relate to what is right and wrong when conducting research. This right and wrong of scientific research should conform to generally accepted norms and values.

1.11 Summary

This chapter has briefly outlined the introduction and background of the study and has presented the significance of the undertaking of the study. The objectives, purpose and statement of the problem that speaks to how the Internal Controls are managed by the Department of Education and the research questions have been described. The need of a sound public service through Internal Controls by the Department of Education was identified as critical towards service delivery.

Chapter two deals with the Literature Review.

CHAPTER 2

LITERATURE REVIEW

2.1 Introduction

This chapter will give a theoretical description on the concept of internal control and will also outline the organisational structure of the department specifically on the units of the department that are directly involved with the internal control function of the department.

Internal control Unit

This unit ensures the stability of financial management across the organisation through proper budgeting, control and reporting. Its strategic goal is the efficient administration through good corporate governance and management.

The key activities of this unit are as follows:

- Pre/post audit of source documents for payments of goods and services and compensation of employees.
- Enforcement of all relevant delegations.
- Application of consequence management.
- Review of financial and supply chain management annual delegations.
- Analyse and review financial policies.
- Compile annual internal control procedure documents.
- Review and compile asset management policies and loss control and recovery measures.
- Communicate the internal control procedures to the department and the district offices.

Internal audit and Risk management Unit

This unit ensures that management systems for performance, information and risk mitigation are in place.

The key activities of this unit are as follows:

- Co-sourcing of internal audit.
- Organising audit committee meetings and implementation of audit committee outcomes.
- Performance of internal audits in house
- Risk assessment sessions
- Fraud risk assessment workshops
- Fraud awareness campaigns.

Supply chain management

This unit stabilises financial management by implementing supply chain management framework.

The key activities of this unit are as follows:

- To ensure compliance with the supply chain management policies.
- To manage expenditure on facilities to be within the set budget limits.
- Ensuring acquisitions are endorsed by the relevant units before orders are placed.
- Ensuring availability of payment vouchers after payment run in order perform monthly reconciliations.

Chief Directorate Financial Management

This chief directorate consist of the Budgeting, Payments and salary administration units.

Their key activities include the following:

- Coordination and facilitation of budget.
- Management and monitoring of budget.
- Monitoring of budget and expenditure and reporting on in-year monitoring.
- Management and reporting of revenue.

- Payment of transfers to schools.
- Payment of goods and services.
- Monitoring of implementation of financial management policies.
- Payroll management.

There is an Integrated Framework that was formulated by COSO in 2011 to best articulate how internal controls can be used effectively. The Public Finance Management Act, 1999 and the Treasury Regulations have provisions and give guidance on the importance of internal controls in the public service.

PFMA Section 38 (i) states that the accounting officer for a department, trading entity or constitutional institution-

- (a) Must ensure that that department, trading entity or constitutional institution has and maintains-
 - (i) Effective, efficient and transparent system of financial and risk management and internal control;
 - (ii) A system of internal audit under the control and direction of an audit committee complying with and operating in accordance with regulations and instructions prescribed by the PFMA. (Public Finance Management Act, 1999:45)

Treasury regulation 3.1.10 states that the audit committee must amongst others review following:

- (a) The effectiveness of the internal control system
- (b) The effectiveness of internal audit function
- (c) The risk areas of the institution's operations to be covered in the scope of internal and external audits. (Treasury Regulations,)

The above provisions clearly show that the government is committed in ensuring that transparency and accountability is promoted and that those that are entrusted with the state resources are accountable for them. The accounting officer's role in ensuring the effective system of internal control demands a due diligence to those that have been delegated to perform in those

areas and also the combination of the Internal audit and the accounting officer is a very crucial one as the audit committee is an independent body it can pick up other risks that the accounting officer might not have picked up and also the recommendations of the audit committee can assist the accounting officer in executing his or her duties as per the PFMA

National Treasury states that the responsibility of internal control is to identify, mitigate and manage control risks which may hamper achievement of the Department's objective to effectively, efficiently and economically manage its financial and related resources.

The main functions performed by internal control cover the following areas:-

- Manage effective, efficient and transparent financial (internal) control / inspectorate measures.
- Manage Loss control
- Manage financial and financial related systems
- Support with the management of Fraud prevention
- Maintain financial information and knowledge management
- Maintain governance frameworks
- Facilitate and participate in committees, forums and oversight bodies.

2.2 Concepts and Integrated Framework on Internal Control

The internal control system is intended to allow management to stay focused on the organisation's or department's pursuit of its operation and financial performance goals. This system enables an organisation or a department to deal more effectively with changing economic and competitive environments, leadership, priorities and evolving effective models. It promotes effectiveness and efficiency of operations and supports reliable reporting and compliance with laws and regulations. The study seeks to ascertain the extent to which management assess the

effectiveness of the department's internal controls and also ascertain the understanding of internal controls by the government officials who are entrusted with this system.

National Treasury defines Internal Control as a process put in place by management and other stakeholders, which is designed to do the following:

- To provide reasonable assurances that the organisation's objectives are achieved effectively and efficiently, in compliance with applicable laws and regulations, and
- To ensure reliable financial reporting. Effective Internal Control ensures that an organisation delivers services efficiently and effectively based on its strategic objectives. Effective Internal Controls also support accountability by assisting in providing reliable financial information through effective accounting standards (National Treasury, 2002).

The government also sees the need for the organisation to be able to identify risks and the most important way of doing that is to quickly attend to any weakening aspects regarding internal controls.

According to the International Organization of Supreme Audit Institutions (INTOSAI), internal control helps to provide reasonable assurance to the following:

- Adheres to the laws, regulations and management directives
- Promotes orderly, economical, efficient and effective operations and achieves planned outcomes
- Safe guard resources against fraud, waste, abuse and mismanagement
- Provides quality products and services consistent with the organisation's mission and
- Develops and maintains reliable financial management information and fairly discloses data through timely reporting (INTOSAI, 2005).

For the year ended 31 March 2014 the report of the audit committee for the Eastern Cape Department of Education indicated that the system of internal control, governance and risk management was ineffective for the financial year 2013/14. Several deficiencies in the system of internal control were reported by the internal audit and confirmed by the AGSA in the prior year

audit. Certain deficiencies raised by the Auditor General South Africa (AGSA) in the report of the 2012/13 financial year were not resolved.

The audit management reports of the AGSA for the year ended 31 March 2013, presented to the audit committee for review, also indicated further material deficiencies in the system of internal control and/or deviations detected in controls tested, and substantive errors. (Report of the Auditor General, 2013)

The United States (US) is one of the countries that champions internal control in local government. With the help of its greatly decentralised public sector structure, the US has adopted an understanding of modern internal control practices, particularly in local agencies (World Bank: 2007: 209)

In Europe there is a public internal financial control for an integrated internal control system for the entire public sector. A basic feature of the EU model of an effective public internal financial control system is the clear demarcation between financial management and control on the one hand and internal audit on the other (World Bank: 2007: 180)

According to Mikesell (2011: 204) Program managers are obviously concerned with the delivery of services according to plan. Financial managers are simultaneously concerned with maintaining internal control, defined as the methods and procedures within the agency established to safeguard assets; check the accuracy and reliability of financial and other data; promote operational efficiency and encourage adherence to the prescribed policies and procedures of the agency.

Erasmus & Visser (2012: 277) argue that, internal control is critical in almost every facet of managing, however, attention tends to be diverted to finances, as there is a perception internal control is mainly a financial function requiring management by financial managers and internal auditors.

Hightower (2008: 27) states that internal controls are more than rules; they embody a company's principles, trust, values and culture. Internal control activities are more than walking a process to see if it matches to the documentation. Internal control is much more than standardising process; it includes demonstrating that decisions are made based on applying principles and documenting the assumptions, criteria and evidence used to make decisions.

2.2.1 Legislative provisions on internal control in the public service

According to the Guidelines for Internal Control Standards for the Public Sector that were formulated in 1992, following are the basics of Internal Control.

2.2.2 An integral process

Internal control is not one event or circumstance, but a series of actions that permeate an entity's activities. These actions occur throughout an entity's operations on an ongoing basis. They are pervasive and inherent in the way management runs the organisation. Internal control is therefore different from perspective of some observers who view it as something added on to an entity's activities or as a necessary burden. The internal control system is intertwined with an entity's activities and is most effective when it is built into the entity's infrastructure and is an integral part of the essence of the organisation.

2.2.3 Effected by management and other personnel

People are what make internal control work. It is accomplished by individuals within an organisation, by what they do and say. Consequently, internal control is effected by people. People must understand their roles and responsibilities, and limits of authority.

This concept is important to the extent that an organisation's people include management and other personnel. Although management primarily provides oversight, it also sets the entity's objectives and has overall responsibility for the internal control system.

2.2.4 In pursuit of the entity's mission

Any organisation is primarily concerned with the achievement of its mission. Entities exist for a purpose ó the public sector is generally concerned with the delivery of a service and a beneficial outcome in the public interest.

2.2.5 To address risks

Whatever the mission may be, its achievement will face all kinds of risks. The task of management is to identify and respond to these risks in order to maximize the likelihood of achieving the entity's mission. Internal control can help to address these risks; however it can only provide reasonable assurance about the achievement of the mission and the general objectives.

2.2.6 Provides reasonable assurance

No matter how well designed and operated, internal control cannot provide management absolute assurance regarding the achievement of the general objectives.

Reasonable assurance equates to a satisfactory level of confidence under given considerations of costs, benefits, and risks. Determining how much assurance is reasonable requires judgment. In exercising that judgment, managers should identify the risks inherent in their operations and the acceptable levels of risk under varying circumstances, and assess risk both quantitatively and qualitatively.

2.3 Components on internal control

The Internal Control-Integrated Framework published by COSO (committee of Sponsoring Organisations of the Treadway Commission) sets out five components of internal control. It also sets out seventeen principles representing the fundamental concepts of objective, as well as to individual objectives within a category.

Below is a summary of each of the five components of internal control and the principles relating to each other.

2.3.1 Control Environment

The control environment is the foundation for all other components of internal control. The board and senior management establish the tone from the top regarding the importance of internal control and expected standards of conduct. This component is influenced by entity's history and its values. It is defined by the standards, processes and structures that guide people at various levels in carrying out their responsibilities for internal control and making decisions in the pursuit

of the department's objectives (Integrated Framework, 2011). The framework further states that, an organization or department that establishes and maintains a strong environment positions itself to be more resilient in the face of internal and external pressures. It does this by demonstrating behaviours of integrity and ethical values, adequate oversight processes and structures, designs that enables the achievement of the department's objectives with appropriate assignment of authority and responsibility and a strong sense of accountability for achievement of objectives.

Following are the elements that displays integrity and ethical values

- Mission and value statements
- Standards or codes of conduct
- Policies and practices
- Directives, guidelines and other supporting communications
- Actions and decisions of management at various levels and the board of directors
- Attitudes and responses to deviations from expected standards of conduct and
- Informal and routine actions and communication of leaders at all levels of the department.

These elements articulate and reinforce the commitment of doing what is right and not just complying with laws and regulations, so that these elements are well understood and well embraced by the board of directors, management and all officials.

Commitment versus Competence

According to INTOSAI (2005), commitment to competence includes the level of knowledge and skills needed to help in ensuring order, economy, efficient and effective performance as well as good understanding of individual responsibilities with respect to Internal Control. Managers and employees are to maintain a level of competency that allows them to understand the importance of developing, implementing and maintaining good Internal Control and to perform their duties in order to accomplish the general Internal Control objectives and the entity's mission.

In order for the officials of the Eastern Cape Department of Education to be competent and committed to their responsibilities, there should be provision of training sessions that will talk to different challenges that are faced by each district. Commitment talks to everyone in the team not

just the Chief Directors and Directors but also the sub-ordinates they lead. Top managers should also display supportive attitude to their sub-ordinates as it is a critical aspect in maintaining positive attitudes on employees.

Adherence and Deviations affect the Department in various ways.

The lack of adherence to standards of conduct often stems from situations such as:

- Top managers not effectively conveying expectations with regards to adherence of standards
- The board of directors not providing impartial oversight of senior management's adherence to standards
- High decentralization that leaves senior managers unaware of action that are taken at lower levels
- Inadequate platforms where employees can air their questions and concerns
- Failure to address nonexistence or ineffective controls, which allow opportunities to conceal poor performances
- Inadequate process for the investigation and resolution of alleged misconduct
- A weak internal audit function that does not have the ability to detect and report improper conduct
- Penalties for improper conduct that are insignificant and thus lose their deterrent value (Integral Framework, 2011).

There are five principles relating to control environment.

- The organisation demonstrates a commitment to integrity and ethical values.
- The board of directors demonstrates independence of management and exercises oversight for the development and performance and performance of internal control.
- Management establishes, with board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives.
- The organisation demonstrates a commitment to attract, develop and retain competent individuals in alignment with objectives.

- The organisation holds individuals accountable for their internal control responsibilities in the pursuit of objectives.

2.3.2 Risk Assessment

Every entity faces a risk from both external and internal sources. Risk is defined as a possibility that an event will occur and adversely affect the achievement of objectives. A precondition to risk assessment is establishment of objectives, linked at different levels and internally consistent.

Risk assessment involves a dynamic and iterative process for identifying and analyzing risks to achieving the entity's objectives, forming a basis for determining how risk should be managed. Management considers possible changes in the external environment and within its own business model that may impede its ability to achieve its objectives (Integral Framework, 2011).

There are four principles relating to Risk Assessment:

- The organisation specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.
- The organisation identifies risks to the achievement of its objectives across the entity and analyses risks as a basis for determining how the risks should be managed.
- The organisation considers the potential for fraud in assessing risks to achievement of objectives.
- The organisation identifies and assesses changes that could significantly impact the system of internal control (Integral Framework, 2011).

INTOSAI, 2005, states that as governmental, economic, industry, regulatory and operating conditions are in constant change, risk assessment should be an ongoing iterative process. It further states that, it implies identifying and analyzing altered conditions and opportunities and risks and modifying Internal Control to address changing risk.

Risk assessment as a crucial component of Internal Control plays a crucial role in the selection of the appropriate control activities to undertake. It is the process of identifying and analyzing relevant risks to the achievement of the entity's objectives and determining the appropriate response (INTOSAI, 2005).

2.3.3 Control Activities

Control activities are the actions established by policies and procedures to help ensure that management's directives to mitigate risks to the achievement of objectives are carried out. In order for control activities to be effective, they must be appropriate, function consistently according to plan throughout and be cost effective, comprehensive, reasonable and directly relate to control objectives.

There are three principles relating to Control Activities:

- The organisation selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.
- The organisation selects and develops general control activities over technology to support the achievement of objectives.
- The organisation deploys control activities as manifested in policies that establish what is expected and in relevant procedures into effect the policies.

According to INTOSAI (2005), control activities include the following range of policies and procedures:

- Authorization and approval procedures ó authorizing and executing transactions and events are only done by persons acting within the scope of their authority. Authorization is the principal means of ensuring that only valid transactions and events are initiated as intended by the management. Authorization procedures which should be documented and clearly communicated to managers and employees should include specific conditions and terms under which authorizations are to be made. Conforming to the terms of an authorization means that employees act in accordance within directives and within the limitations established by management or legislation.
- Segregation of duties ó to reduce risk error, waste or wrongful act and the risk of not detecting such problems, no single individual should control all key stages of a transaction or event. Duties should rather be systematically assigned to a number of individuals to ensure that effective checks and balances are put into effect.

- Controls over access to resource and records ó access to resources and records is limited to authorized individuals who are accountable for the custody of use of resources. Accountability for custody is evidenced by the existence of receipts, inventories, or any other records assigning custody and recording the transfer of custody. Restricting access to resources reduces the risk of unauthorized use or loss to the government and helps achieve management directives. The degree of restriction depends on the level of vulnerability of resources and the perceived risk of loss or improper use and should be periodically assessed.
- Verifications ó transactions and significant events are verified before and after processing. Afterwards, the number of goods invoiced is verified with the number of goods received. The inventory is verified as well by performing stock takes.
- Reconciliations ó records are reconciled with the appropriate documents on a regular basis.
- Reviews of operating performance - operating performance are reviewed against a set of standards on a regular basis, assessing effectiveness and efficiency. If performance reviews determine that actual accomplishments do not meet established objectives and standards. The processes and activities established to achieve the objectives should be reviewed to determine if improvements are needed.
- Reviews of operations, processes and activities ó operations, processes and activities should be periodically reviewed to ensure that they are in compliance with current regulation, policies, procedures or other stipulated requirements. This type or review of the actual operations of an organisation should be clearly distinguished from the monitoring of Internal Control.
- Supervision ó competent supervision helps to ensure that Internal Control objectives are achieved. Assigning, reviewing and approving an employees work encompasses the following:
 - Clearly communicating the duties, responsibilities and accountabilities assigned to each employee
 - Systematically reviewing each employees work to the necessary extent
 - Approving work at critical points to ensure that it flows as intended (INTOSAI, 2005).

INTOSAI, 2005 also states that, a supervisor's delegation of work should not diminish the supervisor's accountability for these responsibilities and duties. Supervisors also provide their employees with the necessary guidance and training to help ensure the errors, waste and wrongful acts minimized and that management directives are understood and achieved.

2.3.4 Information and Communication

Information is necessary for the entity to carry out internal control responsibilities in support of achievement of its objectives. Communication occurs both internally and externally and provides the organisation with the information needed to carry out day-to-day internal control activities.

There are three principles relating to Information and Communication

1. The organisation obtains or generates and uses relevant, quality information to support the functioning of other components of internal control.
2. The organisation internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of other components of internal control.
3. The organisation communicates with external parties regarding matters affecting the functioning of other components of internal control.

According to INTOSAI (2005), a precondition of reliable and relevant information is the prompt recording and proper classification of transactions and events. Pertinent information should be identified, captured and communicated in form and timeframe that enables staff to carry out their Internal Control and other responsibilities. All Internal Control systems pertaining transactions and significant events should be fully captured.

Information systems produce reports that contain operational, financial and non-financial and compliance related information and that make it possible to run and control the operation. These systems do not only deal with internally generated data but also information about external events, activities and conditions necessary to enable decision making and reporting. Management's ability to make appropriate decisions is affected by the quality of information

which implies that the information should be appropriate, timely, current, accurate and accessible (INTOSAI, 2005).

INTOSAI 2005 further elaborates that, information is a basis for communication which must meet the expectations of groups and individuals, enabling them to carry out their responsibilities effectively. Effective communication should flow down, across and up the organization throughout all components and the entire structure. All personnel should receive a clear message from top management and control responsibilities should be taken seriously. The most important aspect of communication channels is the relationship between staff and management. Management must be kept up to date on performance, developments, risks and the functioning of Internal Control and other relevant event issues. Communication should raise awareness about the importance and relevance of effective Internal Control, communicate the entity's risk appetite and risk tolerances and make personnel aware of their roles and responsibilities in effecting and supporting the components of Internal Control.

2.3.5 Monitoring Activities

Ongoing evaluations, separate evaluations, or some combination of the two are used to ascertain whether each of the five components of internal control, including controls effect the principles within each component, are present and functioning.

There are two principles relating to Monitoring Activities:

- The organisation selects, develops and performs ongoing and separate evaluations to ascertain whether the components of internal control are present and functioning.
- The organisation evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the board of directors, as appropriate.

Monitoring should ensure that audit findings and recommendations are adequately and promptly resolved. Monitoring Internal Control is aimed at ensuring that controls are operating as intended and that they are modified appropriately for changes in conditions. Monitoring should also assess whether in pursuit of the entity's mission, the general

objectives set out in the identification of Internal Control are being achieved. This can only be accomplished through ongoing monitoring activities, separate evaluations or a combination of both in order to help ensure that internal control continues to be applied at all levels and across the entity and the Internal Control achieves the desired results.

2.4 Roles and Responsibilities in Internal Controls

The International Standards of Supreme Audit Institutions (INTOSAI) provide the following roles and responsibilities in internal controls.

Everyone in an organisation has some responsibility for internal control:

Managers

Managers are directly responsible for all activities of an organisation, including designing, implementing supervising proper functioning of, maintaining and documenting the internal control system. Their responsibilities vary depending on their function in the organisation and the organisation's characteristics. Managers may include in a case of a government department Directors, Chief Directors and Deputy Director Generals who normally make strategic decisions within the department.

Internal Auditors

Internal auditors examine and contribute to the ongoing effectiveness of the internal control system through their evaluations and recommendations and therefore play a significant role in effective internal control. However they do not have management's primary responsibility for designing, implementing, maintaining and documenting internal control. As discussed above it is a duty of the accounting officer of a department to ensure that the system of internal audit does exist within the department is functioning properly.

Staff Members

Staff members contribute to internal control as well. Internal control is an explicit or implicit part of everyone's duties. All staff members play a role in reporting problems of operations, non-compliance with the code of conduct, or violations of policy. Staff members are often those frontline individuals who apply controls, review controls, correct for misapplied controls and identify problems that may best be addressed through controls in conducting their daily assignments.

External parties such as the AG do play a role in the internal control such as providing advice and recommendations on how to improve or enhance the system of internal control although they are not directly involved in the planning and implementation of the organisation's objectives.

King III Report on Governance for South Africa, rule 2.1.3 states that the board should report on the effectiveness of the company's system of internal controls. It further states that internal controls should be established not only over financial matters, but also operational, compliance and sustainability issues in order to manage the risk facing the company

2.5 Characteristics of internal controls

Timeliness: An internal control system should detect potential or actual deviations early enough ensuring management can take corrective action timeously and limit unnecessary cost.

Economy: Although an internal control system should provide assurance that the objectives of an institution are achieved, this should also ensure minimum cost and the least undesirable side effects as possible.

Accountability: An internal control should ensure that staff is held accountable for their assigned responsibilities and tasks. This is achieved by applying prescribed procedures.

Flexibility: Changing work environments are inevitable, particularly as politics dominates the approach to service delivery in the public sector. Internal controls are preferably designed to accommodate changes without themselves requiring change.

Placement: Internal controls should be installed in areas where they have the most impact, such as before an expensive project phase, where one operation ends and the next starts, where corrective action is easier to implement, or when there is enough time left for this.

Appropriateness: Internal controls should be designed to meet the needs of management in achieving objectives. Internal controls should fit into the personnel and organisational structure of the institution.

Management override: Management tend sometimes to ignore the internal control system and follow their own discretion, thereby destroying the built-in controls. (Visser & Erasmus, 2002:293-294)

In order for the Department to attain its objectives, there should be systems in place that seek to safeguard the department's assets. These systems can assist the department in minimizing risks in government due to factors like incapacity.

2.6 Limitations on Internal Control Effectiveness

An effective internal control system, no matter how well conceived and operated, can provide only reasonable – not absolute – assurance to management about the achievement of an entity's objectives or its survival. It can give management information about the entity's progress, or lack of it, toward achievement of the objectives. But internal control cannot change an inherently poor manager into a good one. Moreover, shifts in government policy or programs, demographic or economic conditions are typically beyond management's control and may require managers to re-design controls or adjust the level of acceptable risk.

An effective system of internal control reduces the probability of not achieving the objectives. However, there will always be the risk that internal control will be poorly designed or fail to operate as intended. Because internal control depends on the human factor, it is subject to flaws in design, errors of judgment or interpretation, misunderstanding, carelessness, fatigue, distraction, collusion, abuse or override.

Another limiting factor is that the design of an internal control system faces resource constraints. The benefits of controls must consequently be considered in relation to their costs. Maintaining an internal control system that eliminates the risk of loss is not realistic and would probably cost more than is warranted by the benefit derived. In determining whether a particular control should be established, the likelihood of the risk occurring and the potential effect on the entity are considered along with the related costs of establishing a new control.

Organisational changes and management attitude can have a profound impact on the effectiveness of internal control and the personnel operating the system. Thus, management needs to continually review and update controls, communicate changes to personnel, and set an example by adhering to those controls. (INTOSAI, 2004:12)

According to the research conducted by WJJ Botha.2003, Internal control is not a failsafe mechanism that will lead to the achievement of all management objectives. Things don't always work as they are supposed to work. Internal control systems can and often do fail, with potential material consequences, especially when such failures are related to instances of fraud, corruption and business failure. Even small and apparently insignificant breaches of an organisation's internal control system can eventually add up to represent a major internal control breakdown.

Any system of internal control is constantly exposed because of certain inherent factors, i.e. factors inherent within the concept of internal control as generally defined and applied. This applies to all systems of internal control, irrespective of design, size and environment. The degree to which these inherent limitations are present or are under control or can however differ, because individual internal control systems are implemented, operated and managed differently, including the influence of subjective characteristics such as attitudes, integrity, ethical values, etcetera. (Botha, 2003: 53)

The inherent internal control limitations referred to above vary from department to department, common amongst others are the following:

- Lack of understanding of organisational objectives: Employees might not be aware of what it is expected from them as a result they do not perform their duties with due diligence.
- Lack of skill and education: Employees might not be educated enough or have the required skill needed to perform their duties as a result they make unnecessary mistakes over and over again thus compromising the internal control system.
- Lack of supervision: Employees might work without supervision for longer periods as a result they will not know if whether they are doing the right thing or not.
- Political influence: Politicians might instruct junior employees to perform tasks that are not in line with the internal control processes, because of the position that the politician hold in the department and employee might perform the task as instructed without questioning the validity of the transaction.
- Fraudulent employees: Some employees might take an advantage of the loophole that is created by non-supervision of the employees and start to make fraudulent transactions.
- Technology: Hackers might access the financial systems of the department and make fraudulent transactions, an example of that was when the South African Post Office was robbed millions of rands in 2011 by hackers who went in to their system and transferred funds to their accounts.
- Communication: Lack of communication by employees might damage the internal control system if employees do not communicate about the processes to be followed when performing their activities.

2.7 Internal Control and the Management Process

In the Government sector there are no board of directors however there are members of executive council and ministers. The decisions made by these politicians are not part of internal controls, e.g. a decision to approve a plan of action or a policy does not form part of internal control however the process of executing that plan might be part of an internal control.

According to the Institute of Internal Auditors (2000), management is actually required to provide more than one assessment of internal controls in its filing with the SEC. the SEC defined disclosure controls as controls and procedures that are designed to ensure that information

required to be disclosed by entity in its Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. Disclosure controls and procedures include without limitation controls and procedures designed to ensure that information required to be disclosed by the entity's management and its officials for timely assessment and disclosure pursuant to the SEC's rules and regulations.

The process of evaluating, improving and reporting on the internal control system could include distinct six steps (Visser & Erasmus, 2002:293-294) (Mckinnney (1995:85-7).

Step 1: organise

Responsibilities should first be determined and assigned ensuring efficient evaluation, improvement and reporting on internal control. Next, consideration should be given to assigning responsibilities for internal reporting, documentation personnel supervision, and scheduling of the evaluation process, which includes vulnerability assessments and internal control reviews.

Step 2: divide the institution into various areas for assessment

The institution should first be divided components, programmes, and administrative functions to facilitate evaluation of internal controls and execution of a vulnerability assessment. Next the following factors should be considered to identify assessable units:

- Existing organisational structure, operating, number, special, and sub-programmes
- Administrative functions;
- Uniqueness of the operating systems;
- Extent of centralization or decentralization;
- Budget allocations, and
- Number of personnel.

Step 3: conduct vulnerability assessments

Criteria and guidelines must be developed determining programmes susceptible to waste, loss, and unauthorised use or misappropriation. The potential existence of the following must be assessed:

- Lack of compliance of costs and obligations with applicable policies
- Lack of adequate safeguard of funds, property, and assets.
- Lack of properly recorded and accounted for revenues and expenditure generating unreliable financial reports and accountability for assets.
- **Step 4: develop plans for subsequent action**

Summarise the results of the vulnerability assessment to determine necessary actions. The aim is to strengthen the system whereby a more cost effective result can be achieved. Classify identified programmes and functions according to vulnerability exposure, thereby ensuring timely achievement of improved outcomes and enhancement of the system. Corrective action can be taken by:

- Scheduling and implementing internal control reviews;
- Recommending that an audit be initiated;
- Setting improved monitoring procedures in motion;
- Carrying out staff training programmes;
- Issuing clearly stated instructions, and
- Modifying existing procedures and documents.

Step 5: conduct internal control reviews

Defining the event cycle forms the basis of internal control review. A cycle consists of a series of actions to be taken to carry out a specific activity, of function. An example is the administrative function, which can involve payroll issues, supplies, and handling of correspondence.

Step: 6 prepare reports on internal controls

Two types of reports are prepared, the first in which corrective actions are suggested is submitted to programme managers, the second goes to heads of departments (Director-Generals) and includes:

- A detailed description of system weakness, and ways to rectify these, and
- Recommendations in terms of economy and efficiency.

Other aspects of internal control to be dealt with in these reports are:

- The overall extent to which the system is efficient in providing the framework necessary for effective control functioning.
- The areas where internal control are nonexistent, and those where they are planned.
- The areas in which internal controls, and policy or procedural requirements are excessive and creating inefficiencies.

If government departments would follow suit the auditors would have more clean audits that they have at the current moment. The Department of Education in Eastern Cape should pay much more attention to what the guidelines and Integrated Framework say in order for the Department to have effective and efficient Internal Controls.

2.8 Summary

This chapter has given an overview of related literature on Internal Controls and also a theoretical description on internal control appliance. It covered the contextual overview of the Internal Controls in the public sector. This chapter has given the reader an overview of what has already been researched in the field of study and the opinions and findings from other researchers in the field and also the internal control functions of the Eastern Cape Department of Basic Education. The chapter discussed the purpose of the Integrated Framework for Internal Control and other relevant legislations.

Chapter 3 deals with the research methodology.

CHAPTER 3

RESEARCH METHODOLOGY

3.1 Introduction

This chapter provides an overview of the methodology used in obtaining the data from the officials across the financial spectrum focusing mainly on salary administration which takes the biggest chunk in the departmental spending, payments section which deals with payment of service providers in the department and also supply chain management which deals with the procurement within the department. These will include, Directors, Deputy Directors, Assistant Directors and other staff members at the head office. The chapter also gives a description of the population, the sampling technique and procedure to be used in selection of respondents. It closes with an outline of the demographic characteristics of the study areas and the ethics considered in the study.

3.2 Research Methodology for this study

The study adopted the qualitative research method. According to Schostak, (2002:230) there are different forms of qualitative research such as ethnography, case study, action research and evaluation which often combine and overlap. There are also many perspectives or schools of thought who interpret qualitative research in different ways. (For instance Marxism view the qualitative approach así , empiricism and others). Qualitative research typically focuses on compiling a selection of micro level case studies which are investigated using informal interviews. Qualitative researchers are interested in giving answers to the questionable processes which do not simply accept the quantitative answers (Schostak, 2006:231).

The research method that will be used in this study is the quantitative method because it provides a broader scope, allows one to look at the broader scale of the society. The method also allows for the use of descriptive and explanatory data. According to Campbell and Stanley (1963), qualitative research is explanatory and the purpose is to understand the environment within which behaviour is determined or processes taking place in order to present case studies of particular communities, individuals or groups. In this case the qualitative method was used to determine the effectiveness and functionality of the existing financial internal controls in the Eastern Cape Department of Basic Education.

The use of a qualitative approach will allow for the researcher to gather first-hand information from the officials who either had been given the necessary task of dealing with financial internal controls and how informative they are when it comes to the expectations.

A qualitative research method will also enable the researcher to clarify on the questions which the respondents would have failed to understand or would have given an insufficient answer to, thus achieving the goal of gathering sufficient information relevant for the this study. It will also allow the researcher to interrogate the management and behaviours and the consequences that they faced as a result of the lack of understanding from their subordinates when it comes to internal controls.

3.3 Research Design

The research will use personal administered questionnaires, where the researcher will provide explanations regarding the questions on the questionnaire and made further enquiries on areas that needed explaining from the respondents. Questionnaires are chosen because they will offer confidentiality to respondents; are generally easier to analyze and turn into qualitative results. The questionnaire will comprise of both closed-ended and open-ended questions. Closed ended questions will be used to gather such facts that need no explanation and those variable measurements that have nominal and ordinal scales.

These include the age, educational levels, and sources of income of officials. As noted by (Hofstee 2006), closed-ended questions make answers easier to quantify and compare but sometimes they fail to extract the respondents' underlying attitudes and opinions. The open-ended questions, allows for more in-depth responses when required. Open-ended questions will be used to gather information that could differ from respondent to respondent, such as the challenges faced the officials when it comes to Internal Controls, their understanding of the guidelines and from where they accessed information. The use of follow up questions from the researcher in the field will also allow greater clarification to employee's responses.

3.4 Units of analysis

The target population is the population group that the study will use from which conclusions will be drawn, (Barbie, 2004:110).The research will be conducted basing on 15 employees of the Department of Education, focusing on Directors, Deputy Directors and officials across the financial spectrum. This study will focus mostly on Supply chain, payments of service providers and salary administration. These units will furnish the study with the information on how assessment is done when it comes to effectiveness and efficient operations, how accurate they are when it comes to financial reporting, for a better understanding of what their challenges are, concerning the knowledge they have when it comes to the implementation of Internal Controls.

3.5 Data Collection

The study will be conducted in the Eastern Cape Department of Education. This will be done so as to capture the differences that may exist amongst the employees of different areas, for example the knowledge on the Integrated Framework and the level of understanding on how guidelines work. According to Ashley and Maxwell (2001) this ensures a balance in the information obtained. Besides, different sources of policy implementation and coping strategies by employees present a wide base for the purposes of comparison, especially with individuals.

The study will use questionnaires that will be distributed through the use of hand delivery and via email. As follow up to the questionnaire, the researcher will ask questions directly to the applicants and employees seeking clarification on the written questions, allowing for more clarity. A set of questions with fixed wording sequence of presentation as well as precise indications of how to answer each question, will be established. Moreover, questions designed will be carefully phrased to avoid ambiguity, sensitive and provocative questions. Interviews will be held with relevant stakeholders. Interviews will be conducted both in English even though the local language is Xhosa but since the researcher will be interviewing professionals and English is the medium language.

The researcher will also review other financial records available in the department such as the annual reports which include the audited annual financial statements,

3.6 Sampling process and sampling procedure

Sampling is a statistical practice concerned with the selection of a subset of individuals from within a population to yield some knowledge about the whole population for the purposes of making predictions based on statistical inference, Strauss and Corbin (2000:5). The sampling for this research will not cover the whole population as it is not possible to survey the entire population. Adèr, Mellenbergh, & Hand, (2008) suggest that there are two reasons that population cannot be whole studied which are: the cost of conducting a research might be too high, and the population might be dynamic in that the individuals making up the population may change over time.

3.7 Variables

According to Hanneman, Kposowa & Riddle, (2013) A variable is a characteristic or attribute that can take on different values or vary across cases.

3.7.1 Dependant variables

The effectiveness of internal control system is the dependant variable that the researcher wishes to explain or predict.

3.7.2 Independent variables

Components of internal control together with the departmental functions are the independent variables that will explain or predict the variation in the dependent variable. These independent variables are grouped into two as follows.

- **Components of Internal control.**
 - a) Control environment: The integrity and ethical values of employees.
 - b) Risk assessment: Proper financial reporting and mitigation of fraud and corruption.
 - c) Control activities: Following procedures correctly and selecting the correct policies to be followed.
 - d) Information and communication: Reliable and relevant information used in financial reporting.
 - e) Monitoring: Continuous assessment and supervision of staff.

- **Departmental activities**

- a) Authorisation procedure: process of validating the transactions.
- b) Segregation of duties: assigning jobs to different people for different functions within the unit.
- c) Personnel: trustworthy and reliable employees performing their functions with high level of morality and ethical behaviour.
- d) Documentation: proper documentation and safeguarding of documents and departmental assets.

3.8 Method of Data Analysis

The Internal control óintegrated framework by COSO, suggest that the effectiveness of internal control is assessed in relation to control environment, risk assessment, control activities, information and communication, and monitoring. These five components of internal control should be present and should be operating together.

The questionnaire that was distributed to the respondents had structured questions that covered all dimensions of the variables.

Data collected was given to a statistician for analysis and verification.

3.9 Delimitation of the study

Although the study will be carefully prepared there will be limitations to it. First because the study will be conducted mainly from the head office because the districts are responsible mainly for education management. Second, since the questionnaire will be designed to measure the official's responsibility in applying the internal controls they might be reluctant in giving the correct information or might be discouraged to provide a feedback. Third, since the researcher will mainly focus on three units within the department and will not go to other units such as budget, accounting services, internal audit and other financial related units the population might be small.

Managers in the public service have a key role to play in creating an environment for their staff to become effective in the way they interact with their work. This requires the motivation of employees to have the necessary tools to do their work. Public officials are less interested in acquiring knowledge of what Internal Controls entail.

3.10 Ethical considerations

All employees will be informed of the objectives of the study, while it will be made clear that contribution in the study was voluntary. The purpose of the study will also be explained to respondents before they fill in the questionnaire and care will be given to respect their right not to participate. No names will be mentioned to incriminate any individuals. Participants will not be misled about matters related to the investigation in any way and they will be made aware that the data collected is going to be used purely for academic purposes without defaming any character.

The researcher will do well in put up with the ethical principles of the University of Fort Hare which states that a researcher should carry out the study; ensuring that the universal values of justice, integrity, discipline, love, kindness, non-injury and concern for the wellbeing of others shall serve as a source of thought, speech and action (University of Fort Hare, 2010). All information will be gathered as such and will be treated with confidentiality.

3.11 Demographic characteristics of the study sample

This section is based on the information that will be obtained about the employees of the Eastern Cape Department of Education through the questionnaire. This covers the demographic information of the employees in the study sample. The purpose of this section is to describe the employees in terms of, age, educational background, and income. These factors might have an impact on how employees manage their responsibilities in the work place.

3.12 Summary

The chapter presented the steps and techniques that will be adopted and implemented in conducting of this research. It discussed the sample and the sampling techniques that are used when conducting a research. It also outlines the research procedure and the tools that will be used in data collection, which are the questionnaire and follow up questions by the researcher in the field. The chapter further described the different demographic characteristics of the sample, focusing on age, educational qualifications and salary income. The research used a qualitative research method.

Chapter 4 deals with the research findings and results of the study.

CHAPTER FOUR

RESEARCH FINDINGS AND RESULTS

4.1 Introduction

The previous chapter discussed the methodology used in obtaining the data to carry out the research. This chapter discusses the research findings obtained from the department in order to answer the research questions of whether or not the Eastern Cape Department of Basic Education does have an effective internal control system. In order to answer the research question, the researcher categorised the responses into the following headings.

- The existence of the internal control system within the Eastern Cape Provincial Department of Basic Education.
- Conceptualising the effectiveness of internal control with the Eastern Cape Provincial Department of Basic Education.
- Understanding of the internal control system by the employees.
- The implementation of the internal control system.

4.2 The existence of the internal control system within the Eastern Cape Provincial Department of Basic Education

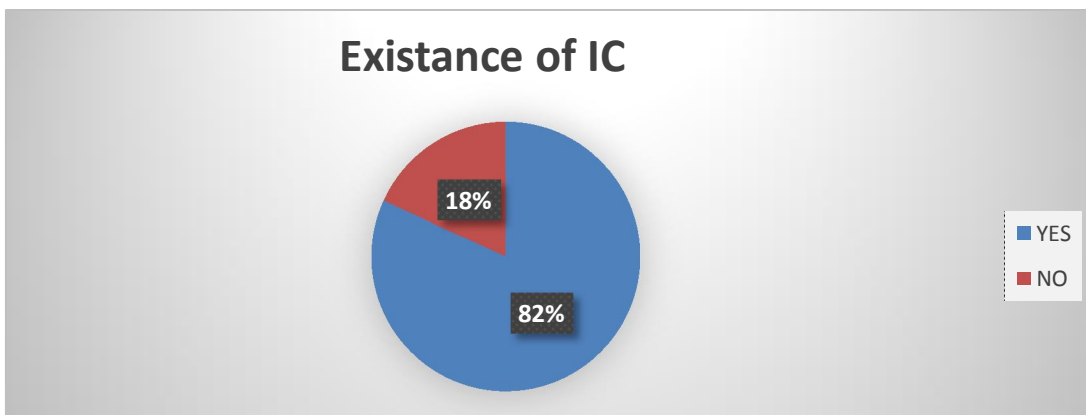


Figure 4.1(a)

The researcher looked at the existence of internal control system within the department and their execution.

82 percent of the respondents have confirmed that internal control does exist whilst 18 percent did not know about the existence of internal controls within the department.

Upon interviewing the chief director for internal control unit it was established that the department had recently created an internal control unit that will oversee all the internal control systems; there was no internal control policy that was approved by the department during the research however a draft document on the internal control policy was available. The internal control policy has been communicated to the executive management of the department and is awaiting approval by the head of department, however the policy has not yet been agreed on by the departmental audit committee which in terms of the Treasury Regulations paragraph 3.1.10 is required amongst others, review the following ó

- a) The effectiveness of internal control systems;
- b) The effectiveness of internal audit function

Paragraph 3.1.13 of the treasury regulations further states that: the audit committee must, in the annual report of the institution, comment on the effectiveness of internal control.

The department has and maintains the system of internal control in its operations although there was no formal departmental internal control policy document that has been approved.

4.3 Conceptualising the effectiveness of internal control with the Eastern Cape Provincial Department of Basic Education

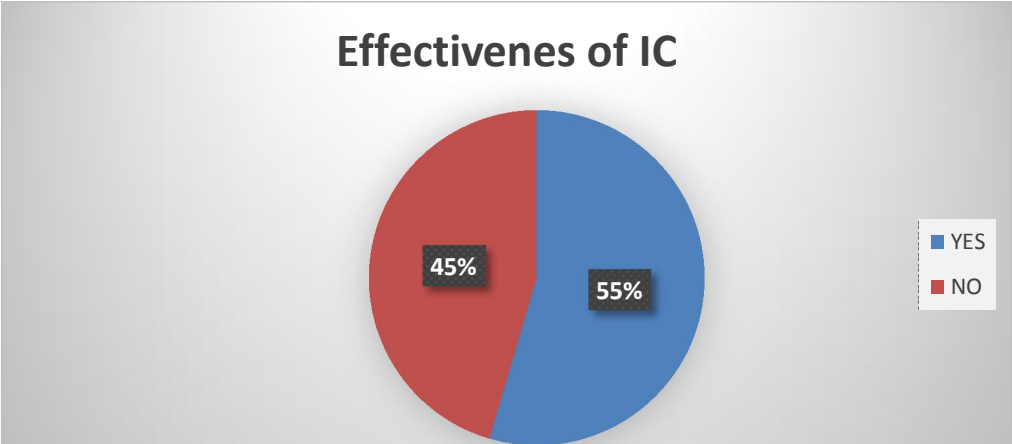


Figure 4.1(b)

Conceptualising the effectiveness of internal control within the Eastern Cape Department of Basic Education in this research refers to the researcher being able to evaluate the effectiveness

of the system of internal control within the department and how the departmental officials execute their duties to achieve the desired results by the system of internal control. The researcher interviewed departmental officials in three different financial units within the department namely Supply Chain Management, Payments Management unit and Salary Administration and also had to interview the head of the internal control unit.

As explained in figure 4.1(b) above 55 percent of the respondents believe that the internal controls within the department are effective whilst 45 percent say they are not effective.

The respondents explained the procedures in relation to their work, respondents from supply chain management highlighted that there was no procurement policy in place and they had to work using relevant legislations available in the government websites such as the supply chain management framework, PFMA and treasury regulations and no regular supervision was done by their superiors. The respondents from supply chain management also said that supplier performances were not being evaluated periodically.

Respondents from the payments section said that there is a procedure manual for all payment processes however they do have a system of comparing the invoice, purchase order and the goods received prior making the payment, this might result in a risk of making a payment for goods that were not received or services that were not rendered. They also explained that they a system of preventing duplicate payment does exist as they put on a paid stamp on the document to prevent reuse. They also explained that they depend on the financial system to ensure that they do not exceed the budgeted funds for the items they have to pay for, this means that there is a risk of the department overspending on their commitments thus having a debt at the end of the financial year.

The respondents from salary administration explained that the procedure manuals they use are the guidelines and frameworks issued by the National Treasury and that there is no departmental procedure manual to guide them on their day to day functions. They also explained that there is no system to prevent payment to retired or deceased employees as they depend on Human Resources department to terminate the employee on the financial system. They also highlighted that the payroll is not adequately signed by employees before or after receiving their monthly salaries.

4.4 Understanding of the internal control system by the employees.

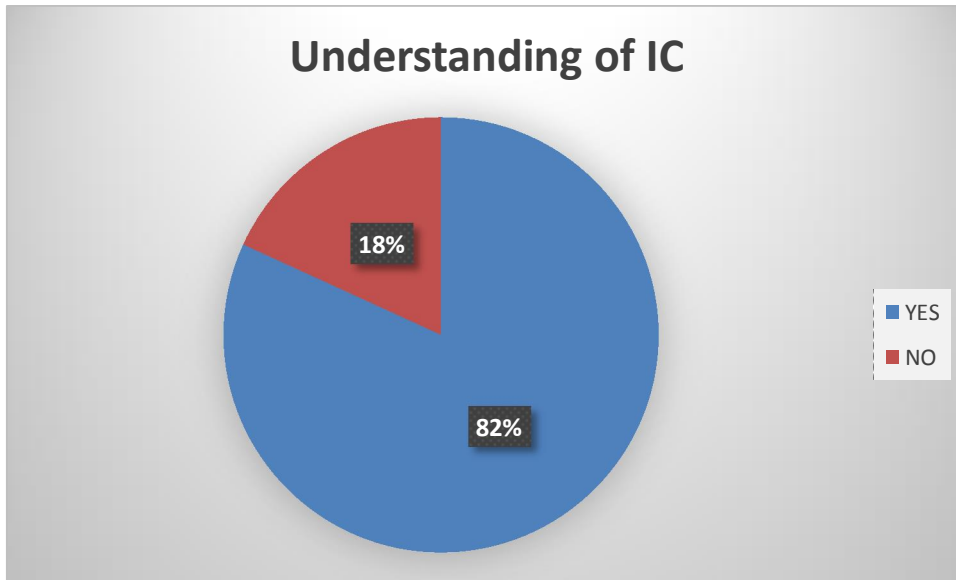


Figure 4.1(c)

With regards to the understanding the internal control system, 82 percent of the respondents said the understood the process on internal control system whilst 18 percent did not understand it.

The researcher had to determine whether the departmental officials are aware of the internal control system in order to be efficient and effective in executing their functions, the researcher also had to determine if the system of internal control has been communicated and understood by all employees.

Treasury regulations paragraph 3.2.1 states that: the accounting officer must ensure that a risk assessment is conducted regularly to identify emerging risks of the institution. A risk management strategy, which must include a fraud prevention plan, must be used to direct internal audit effort and priority, and to determine the skills required of managers and staff to improve controls and manage these risks. The strategy must be clearly communicated to all officials to ensure that the risk management strategy is incorporated into the language and culture of the institution.

The officials are not well informed of how the system works; there are no procedure manuals that talk to the processes of internal control. The latter is confirmed by the fact that the department

only has a draft document of internal control system and the executive management has no yet approved the draft document that is in place. The employees have indicated that are using PFMA, Treasury Regulations and published financial management frameworks such as, supply chain management framework which are very generic and not being specific as per the departmental needs.

4.5 The implementation of Internal Controls

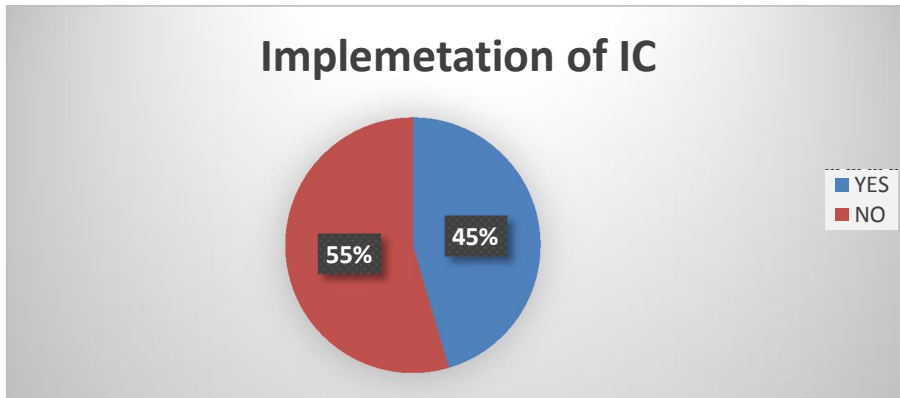


Figure 4.1(d)

As per the Guidelines for Internal Control Standards for the Public Sector, everyone in an organisation have some responsibility for Internal Control from managers to staff members

Managers are responsible for the following:

- All activities of an organisation including, designing, implementing, supervising of proper functioning, maintaining and documenting of the Internal Control system.
- Communication and understanding of Internal Control.

Their responsibilities would of course vary depending on their function in the organisation and the organisation characteristics.

Internal Auditors are responsible for the following:

- Examine and contribute to the ongoing effectiveness of the Internal Control system through the evaluations and recommendations and therefore play a significant role in the effectiveness of Internal Control, however they do not have management's primary

responsibility for designing, implementing maintaining and documenting but play a pivotal role in review and whether the system better suits the departmental needs or not.

- Determine the significance and sensitivity of risks

Staff members are responsible for the following:

- The staff members are the ones that put into effect Internal Controls.
- They report problems of operations, non-compliance with code of conduct or violations of policy.

Other parties are responsible for the following:

- Interacting with the organisation.
- Understanding departmental policies.

In the figure above 55 percent of the respondents say there is no implementation of the internal control procedures whilst 45 percent believe that there is a proper implementation. As per the finding the officials of the department are not familiar with their responsibilities and proper implementation as outlined by the Guidelines for Internal Control Standards for the Public Sector, however they do the work based on PFMA and other norms and standards issued by the national treasury as guidelines and frameworks.

SUMMARY

The chapter has outlined the process of the Internal Control and the role that each employee plays from guidance which is the responsibility of the Head of the department to formulation of the policy which is the responsibility of management and understanding and implementation of the internal control system which is the responsibility of other employees. The chapter has displayed the ineffectiveness of the department when it comes to the knowledge of Internal Controls and implementation.

Chapter 5 deals with recommendations and conclusions.

CHAPTER FIVE

RECOMMENDATIONS AND CONCLUSION

5.1 INTRODUCTION

This chapter gives conclusions and recommendations of the study. The conclusions and recommendations in this chapter were established in line with the problem statement and the objectives of the study that were discussed in chapter one and the research findings in chapter four.

5.2 Discussion of findings.

5.2.1 Internal control systems in the Eastern Cape Department of Basic Education

Results revealed that the internal control system in the department does exist however there is a weakness in implementing the internal controls, the components of internal control system do exist and are functioning as it was revealed that payments are authorised using supporting documentations, procurement of goods and services is performed in line with the National Treasury's procurement policies, payment of salaries of staff is verified by human resource personnel.

5.2.2 Assessing Control environment component

Findings revealed that measures are taken to ensure that staff members perform their duties with high level of ethical standard and integrity however due to lack of supervision by senior management mistakes and errors committed by the staff are not adequately corrected on time thus resulting in the duplication of errors without proper intervention and correction. The management need to attend to this as a matter of urgency and resolve audit queries on time.

Both the staff and the management have the responsibility to ensure that organisational policies and procedures are being implemented on time and the audit advisory report should be attend to in time and all the queries addressed accordingly.

5.2.3 Assessing Risk assessment component

Findings have revealed that there is a risk of fraudulent transaction taking place because of lack of supervision and regular assessment of the work performed by staff. Misrepresentation of financial information arising from fraudulent transactions and lack of supporting documentation might take place due to the fact the internal control policy is not yet available. The management should ensure that the risk management unit is involved in the process of reviewing financial reporting to ensure the reliability of the information submitted for reporting.

5.2.4 Assessing Control activities component

Findings have revealed that the internal control unit has just been established in the department and the control activities have not yet been understood clearly by all staff members. Staff members use policies and procedures that are generic and have been developed by National Treasury such as the PFMA and Treasury regulations, there are no policies available that have been tailored for the process flow of the departmental activities. Procedure manuals should be developed for each and every unit and be evaluated on regular intervals.

5.2.5 Assessing Information and communication component

Findings have revealed that staff members do not know about the existence of the internal control policy and its contents. They are not familiar with what is expected from them hence they continue doing their job without knowing whether they are doing the correct thing or not as there

is no measuring tool or a guiding document that assists them in ensuring whether they are achieving the departmental objectives or not.

5.2.6 Assessing Monitoring component

Findings have revealed that there is no monitoring and supervision of staff by senior management, errors are being committed frequently without any proper intervention, procedures on the payment of invoices and on the requisition of orders are not being reviewed as the respondents have confirmed that they have been using the generic manuals in performing their duties.

5.3 Recommendations

Internal control is not a once off activity, but a series of events that occur in a department on a daily basis and has an impact on the stewardship of the management. Everybody in an organisation has a responsibility to ensure that the internal control system is implemented correctly to achieve departmental objectives.

The control environment is the most critical component of internal control as it is influenced by the history of the entity and its values. This component should be understood by all the role players in the internal control environment as it displays the mission and the vision of the system of internal control, it gives guidance on policies and procedures.

The department should design its internal control system in line with the components of internal control. The department should ensure that the employees are doing what is correct and right and not just complying with the prescribed standards for the sake compliance.

The department should ensure that the risk assessment is done thoroughly as this will assist the department in selecting the appropriate control activities that it will undertake in its daily operations. The risk assessment should look at areas such as fraud prevention when developing these controls, also what strategies will be used to manage the risk. Other areas that should be

looked at are to be able to detect an improper conduct that might emanate and ways to curb poor performances.

Other component that the department should look at is the control activities, these are the activities that will be carried out to achieve the desired achievements. These activities should be authorised by the executive management and endorsed by the audit committee to ensure that they are properly performed, these activities should be performed by officials who have been authorised to do so to ensure that the transactions are initiated by the officials authorised to do so within the departmental protocol. Segregation of duties should be emphasised in order to reduce the risk of unwarranted fruitless and wasteful expenditure, irregular expenditure and unauthorised expenditure.

Information and communication should play a major role in the implementation of the internal controls as this will assist the department with information needed to implement the activities that have been designed.

The department has to effectively communicate the information regarding the internal control system to all employees in order for other units within the department to be able to support the functioning of each other. Outsiders such as suppliers should also be informed about the controls that they are expected to adhere to when dealing with the department an example would be the procedure and documentation required from suppliers when they submit their invoices or making claims for their payments, this will make it easy for the departmental officials to be effective in performing their task as they would not be required to send back suppliers whose documentation are not complete or inappropriate. Management should ensure that the information given to employees is relevant and up-to-date and should be reviewed on regular intervals.

The last component that the department should look at is the monitoring and evaluation of the designed internal control, monitoring and evaluation is a talked about concept in the public sector and it assists in determining whether the department is achieving its pre-determined objectives. Monitoring and evaluating internal control environment will assist the department with understanding whether are the controls effective and efficient in achieving departmental goals and will help in the review of controls that will hamper the delivery of services to the community.

The researcher concludes that although the department does not have an approved internal control policy it has managed to perform internal control functions however a lot needs to be done by the department in professionalizing the system of internal control.

Employees need to be part of the planning process before the internal control policy can be implemented so that they are aware of the new developments within the department thus it will make it easy for the management to get a buy in from the staff members.

5.4 Conclusion

As per the PFMA Section 38(1) (a), the accounting officer is required to ensure that the department has and maintains effective, efficient and transparent systems of financial risk management and Internal Control.

The policy gap that remains in internal control should be narrowed so that all employees within the department have knowledge and understanding of the internal control policy. The executive management should make it a point that all members of senior management including district directors are aware of the draft policy and is communicated to them regularly until the final stages of implementation. Weaknesses and deficiencies that are prolific in undermining the control environment should be attended to on a monthly basis and should be monitored by the monitoring and evaluation unit within the department. There must be a procedure manual for each directorate that deals with financial management in line with the operational plans of all employees in order to minimise the risk of internal control procedures being marginalised due to the lack of supervision from the management

The department should have an effective records management system which is very critical in an organisation of its size in ensuring the all payments made are supported by verifiable and authentic source documentation. The department must apply the best practices on financial management on its daily and monthly control activities in line with norms and standards as prescribed by the National Treasury. Supervision and monitoring of staff should be a priority and performed on daily basis and disciplinary steps should be taken against employees who contravenes the applicable legislations as prescribed in the PFMA.

The internal control unit together with risk management unit should be in the forefront in ensuring that the internal control systems in place are adhered to and proper monitoring and evaluation should be done on the systems to ensure their effectiveness, internal audit should have a plan in place in ensuring that the compliance issues are being monitored and reviewed on regular basis

5.4 REFERENCES

- Adams, J et al. 2007. *Research Methods for Graduate Business and Social Science Students*. London
- Ader.H.J., Mellenbergh, G.J. & Hand, D.J. 2008. *Advising on Research Methods: A consultants Companion*.
- Basopu, M. 2010. *Assessing challenges of corruption in the Eastern Cape Department of Education*. Alice: University of fort Hare
- Brynard, P.A., & Hanekom, SX. 2006. *Introduction to research in management related fields*. Pretoria: Van Schaik Publishers.
- Carlson, K.A and Winqvist, J.R. 2014. *An introduction to Statistics*. Sage publication, USA
- Committee of Sponsoring Organisations of the Treadway Commission. 2011, *Internal control-Integrated Framework*
- Coombs. H. M and Jenkins D. E. 2002. *Public Sector Financial Management*, Singapore
- Eramus. P.W and Visser. C.B. 2002. *The Management of Public Finance*. Oxford University Press Southern Africa.
- Hightower, R. 2008. *Internal Controls Policies and Procedures*. Hoboken, NJ, USA
- Introduction to Research and Research Methods: University of Bradford, School of Management. July 2007
- King III Report on Governance for South Africa. 2009
- Leedy. P.D and Ormond. L.J. 2005. *Practical research : planning and design*, Pearson Education,
- Mikesell. J L. 2011, *Fiscal Administration, Analysis and applications for the Public Sector*, Boston USA.
- Sarbanes- Oxley Internal Controls: Effective Auditing with AS5, CobiT, and ITIL.

Schostak, J.F 2000. Understanding, Designing and Conducting Qualitative Research in Education. Framing the Project. Open University Press

Shah, A. 2007. *Local Public Financial Management*. World Bank. Washington DC.

South Africa (Republic). 2011 Eastern Cape Province. 2010/2011, Annual Report, Department of Education.

South Africa (Republic). 2012. Eastern Cape Province. 2011/2012, Annual Report, Department of Education,

South Africa (Republic). 2013. Eastern Cape Province. 2012/2013, Annual Report, Department of Education

South Africa (Republic). 2014. Eastern Cape Province. 2013/2014, Annual Report, Department of Education

South Africa: Eastern Cape Provincial Budget Speech. 2010

South Africa (Republic) 2008. National Treasury, Technical Competency Dictionary on Internal Controls, Pretoria

South Africa (Republic) 20015. Eastern Cape Province, 2015/16, Operational Plan, Department of Education

South Africa (Republic), 1999. Public Finance Management Act 1 of 1999, updated July 2011. Juta.

South Africa: The Eastern Cape socio-economic review outlook. 2013 ;

Struwing, F.W. & Stead, G.B. (2001). *Planning, designing and reporting research*. 3rd ed. Cape Town: Maskew Miller Longman.