



The Extent of Employee's Compliance to the Internal Control System on the Reliability and Creditability of Financial Statements

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Authors' contributions

This work was carried out in collaboration between all authors. Author ZAZ designed the study, wrote the protocol and wrote the first draft of the manuscript. Author OSS managed the literature searches, statistical analysis of the study performed. Author MEH audited the language, managed the distribution and collection of questionnaires. All authors read and approved the final manuscript.

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ABSTRACT

A sound system of internal control depends on an effective management, and the awareness of its employees of the policies and procedures adopted. It is a combined responsibility to maintain it properly and make sure it's effective and reliable. Its management responsibility to make sure that, the internal control procedures adopted and applied is still valid and suitable to achieve. A questionnaire has been designed for this purpose and it was distributed randomly to the working employees and to different management levels. The number of questionnaires analyzed were (100) questionnaires. Resolution data were analyzed using the statistical program SPSS, in addition to other statistical methods. The study concluded that, the effectiveness of the internal control systems in the Jordanian commercial banks is not attributed to demographic variables (sex, age, profession, etc) but mostly, attributed to tight internal control systems adopted, and demonstrated by management. The study recommended that, management should keep tight recruiting policies in order to implement its internal control systems effectively, and finally internal control systems adopted should be applicable and easy to understand.

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1. INTRODUCTION

Over the past decades, organizations have invested heavily in improving the quality of their internal control systems. They have made the investment in order to ensure that operating, financial and compliance objectives are met, and to develop specific support for their certifications and assertions. The reliability and creditability of financial statements depends on the efficiency of internal control mechanism, and the extent of employee's compliance to the internal control system adopted by management [1]. Mere compliance with applicable laws, rules, and regulations will not guarantee effective internal control system, since those measures cannot change the culture within an organization. Effective internal control procedures can only be achieved when all employees add value to the company's sustainable long-term performance, effectively carry out their duty and professional responsibilities, when also employees are held accountable and personally responsible for their performance, and when they develop a practice of not only complying with applicable regulations, but also committing to doing the right thing, observing ethical principles of professional conduct in avoiding potential conflicts of interest, and acting in the best interests of the company and the achieving of its objectives.

Establishing a sound system of internal control always rests on the shoulders of management, it is their responsibility to maintain it properly and make sure its effective, and reliable [2,4]. A sound system of internal control works as a controller over recruitment strategy set by the human resources department. Its management responsibility to examine and evaluate the internal control system periodically, so it can make sure that, the methods and procedures adopted and applied is still valid and suitable to achieve the objectives of the system effectively. A sound system of internal control should reflect the control environment, as it is considered the basic structure on any control system [3]. The other components of the system include the elements of control activities, elements of information and communication, elements of risk assessment, and elements of monitoring [4]. An effective control system should have an effective control procedure, tight policies, but at the same time it should be simple and easy to understand and apply [5]. In order to check the effectiveness of a sound internal control system, it requires a continuous process of evaluation. Reviewing and evaluation the internal control system adopted is necessary to detect weaknesses points, and to ensure healthy and reliable outcomes.

Many of the audit failure from the 1980s up to now are due to either improper ethical values or to weak internal control systems. Monitoring and auditing are considered a key aspect procedure to check whether the quality system is operating as intended. As the reliability and creditability of financial statements depends on the efficiency of internal control mechanism, and the extent of employee's compliance to the internal control system adopted by management, the idea of this research was developed trying to measure the extent of Jordanian commercial banks employee's compliance to the internal control systems adopted and its effect on the reliability and creditability of financial statements disclosed to end users. Many professional accounting associations have participated in developing accounting standards to ensure reliability, credibility and quality of the financial statements to end users. One of these professional accounting associations is The Committee of Sponsoring Organizations of the Tread way Commission (COSO) and The Institute of Chartered Accountants CA. Both of these organizations have participated in providing guidance to companies, which can be used as a measure of effectiveness. Both guidance will be used in

the current study; the questionnaire is designed to fulfill the objectives of study using the guidance of both COSO and CA.

2. STUDY PROBLEM

Many of the audit failure from the 1980s up to now are due to either improper ethical values, or to weak internal control systems. Mere employees' compliance with applicable laws, rules, and regulations will not guarantee effective internal control system. The current study will try to answer whether the employees are complying to internal control systems and the degree of their reaction towards the internal control system components and procedures.

3. STUDY IMPORTANCE

Importance of the current study can be derived through management obligations and functions. One of these functions is making decisions in a timely manner, processing information and recruitment of employees. Based on the above, the integrity and credibility of accounting information presented in the final financial statements, depends on a healthy internal control system. It's important that every company should have an effective control system that can minimize risk, and ensure reliable financial statements. Quality assurance of company's financial statements can be derived not only through monitoring and auditing procedures adopted by the organization, but also by understanding and following the internal control system completely by the employees.

4. STUDY OBJECTIVES

The current study aims to examine the extent of employees' compliance to internal control systems in the Jordanian commercial banks. Efficient internal control system is reflected on the quality of the financial statements disclosed. Generally, effectiveness is attributed to adoption of a sound control system, then, applying the system in the right way. So, we can say that, the effectiveness depends on two factors, the material of the system in the first place, and the employees who are applying the system. The reliability of the financial statements disclosed depends upon the efficiency of the company's internal control system. COSO and CA institutions have participated in providing guidance to companies, which can be used as a measure of effectiveness. Both guidance will be used in the current study.

5. STUDY HYPOTHESIS

- H01: There is No statistical significant relationship between employee commitment of internal control systems and the reliability and creditability of financial statements.
- H1: There is a statistical significant relationship between employee commitment of internal control systems and the reliability and creditability of financial statements.
- H02: There is no statistical significant relationship between employees' credentials and knowledge of internal control systems and the reliability and credibility of financial statements.
- H2: There is a statistical significant relationship between employees' credentials and knowledge of internal control systems and the reliability and credibility of financial statements.

6. LITERATURE REVIEW

Internal control systems are control procedures put in place by the management of an organization to ensure efficient and effective operation of her activities, so as to meet the organization's objectives [6]. COSO defines internal control as a process, affected by an entity's board of directors, management and other personnel. This process is designed to provide reasonable assurance regarding the achievement of objectives in effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations [7]. The auditor's objective in an audit of internal control over financial reporting depends on the integrated framework developed by the Committee of Sponsoring organization of the Treadway Commission. The framework consist five interrelated components, which four of it relates to the design and operation of the system of internal control such as control environment, risk assessment, control activities, and information and communication. The fifth component is monitoring, which is designed to ensure that internal control continues to operate effectively [8].

In other words, internal controls are techniques employed by managers to ensure that specific control objectives are continuously met. Controls can be implemented to protect anything of value to a company's economic performance or continued sustainability. The objective of internal control system is to ensure a proper assets protection, but the execution should be done by the internal auditors not by management, this is because that auditors are the most eligible to undertake this responsibility [9]. Risk associated to business can be reduced throughout internal control as it composed of the set of policies and procedures necessary to realize the objectives of the enterprise [10]. Internal control effectiveness creates reliability of financial reporting, and also the relationships between antecedent variables such as risk management efficiency, quality of compliance, potential of intra communication, and continuous monitoring adequacy and internal control effectiveness [11]. Common objectives of internal control systems include the propriety of transactions, reliability of information, compliance with regulations, security and efficiency.

6.1 Evaluating the Effectiveness of Controls

Effectiveness must be evaluated in order to be able to assess control risk at below the maximum level. To evaluate effectiveness, the auditor should obtain evidence about the design and operation of effectiveness [12]

6.1.1 Test of controls for design effectiveness

Test of control to evaluate design effectiveness are concerned with whether the control is suitably designed to prevent or detect material misstatement in specific financial statement assertions. To evaluate design, an auditor generally needs evidence about what action the control requires, when it is to be done, and who is to do it.

6.1.2 Test of controls for operating effectiveness

A well-designed control is not, by itself, sufficient to reduce control risk; it also must operate effectively. Therefore, to assess control risk at below the maximum level, the auditor must evaluate the operating effectiveness of controls. To evaluate operating effectiveness, the auditor needs evidence about how the control is usually applied, how consistently it is applied, and who applies it.

6.2 Procedures Used as Test Controls

Many audit procedures can be used as tests of controls to evaluate either design effectiveness or operating effectiveness. These procedures include making inquiries of appropriate entity personnel, inspecting documents and records pertaining to the design or application of the control, and observing the application of the control. Another procedure used as a test of controls for operating effectiveness is re-performance of the application of the control by the auditor.

6.2.1 Inquiries

Evidence can be obtained about either design or operating effectiveness by making inquiries of appropriate entity personnel. For example, an auditor may ask about the organization structure or the accounting system for purchases to obtain evidence about their design. An auditor also may ask who performs the bank reconciliation to obtain evidence about how the segregation of duties affects the operating effectiveness of the control.

6.2.2 Inspecting documents and records

Documents and records may provide evidence about design effectiveness by describing how a control is intended to work. For example, the entity's accounting manuals may discuss in some detail the design of its accounting system, or its personnel manual may describe its personnel policies and practices. Inspecting documents and records also can provide evidence that a credit approval is operating control is operating such as stamps or initials, or the auditor may inspect computer generated exception reports pertaining to the processing of inventory transactions as evidence that the computer control is operating.

6.2.3 Observing entity activities

Observation is often used as a test of controls for design effectiveness. For example, an auditor may observe the processing of cash receipts to obtain evidence about how effectively the accounting system for cash receipts is designed. Observing the application of a control also provides evidence about its operating effectiveness. For example, the auditor may observe who prepares the bank reconciliation to evaluate the effectiveness of segregation of duties or may observe client personnel taking a physical inventory to evaluate whether they are actually following prescribed controls.

6.2.4 Re-performance

Re-performance occurs when the auditor redoes a control to obtain evidence about whether it operated effectively. For example, if a control activity requires a clerk to check the calculations on sales invoices, the auditor may re-compute those calculations to determine if the clerk effectively performed the control.

7. METHOD

The primary data needed for the study objectives were collected through a survey conducted among the main Jordanian Commercial bank. A questionnaire has been designed for this purpose and it was distributed randomly to the working employees taking part in actions and activities on carrying out business in their banks in January 2013 and to different

management levels. The number of questionnaires analyzed were (100) questionnaires. Resolution data were analyzed using the statistical program SPSS, in addition to other statistical methods.

Quantitative data were collected using a self-administered questionnaire, in which the employees were asked to state the likelihood (on a 5-point scale: [5] strongly agree; [4] agree; [3] neutral; [2] disagree; [1] strongly disagree), 100 copies of the questionnaire were delivered by hand on the respondents, 85 copies were returned (percentage of 85%); these 85 copies were accepted and used in the pilot analysis (percentage of 85%) of the original distributed copies), Table 1 shows 5-point scale intervals.

Table 1. 5-Point likert median scales

Low	Moderate	High
1-2.49	2.5-3.49	Above 3.5

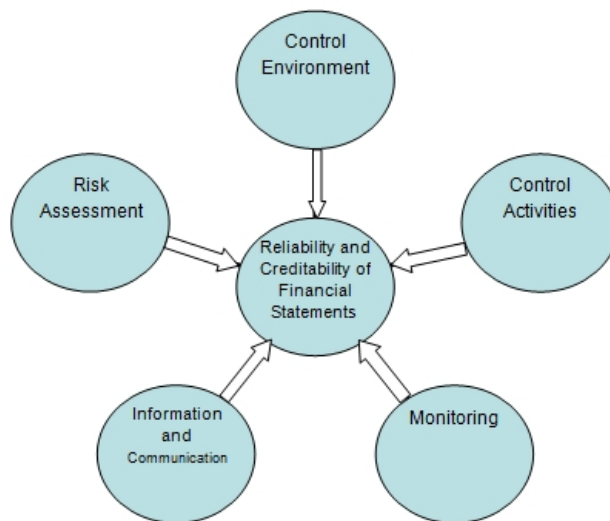
Other Data is collected from secondary sources. Secondary data is collected from articles published by the well-known periodicals, books and dissertations.

7.1 Statistical Analysis

The Statistical Package for Social Sciences (SPSS) was applied in analyzing the data received; Statistical Analysis tools include the followings:

1. Descriptive Statistics, mainly frequencies and percentages, were used to analyze sample characteristics according to job, educational level, professional certificates, and experience.
2. Means and Standard Deviation were used to analyze and describe Study variables from a statistical point.
3. Reliability Test using Cronbach’s Alpha was used to test the reliability of the scale.

7.2 Research Design



Research design is formed out of five elements which constitute the internal control system. Employee's compliance to these elements affects the reliability and creditability of the financial statements.

7.3 Data Analysis and Findings

7.3.1 Reliability test

Cronbach's alpha was used to test the internal reliability of the measurement instrument. In this study 0.60 or higher is considered acceptance [13]. As shown in Table 2 the Cronbach's Alphas (α) ranged from 0.869 to .97, thus establishing the reliability of the survey questionnaire. It is obvious that all values of alpha are high. This indicates that for each measurement of a variable, the items are highly correlated and hence highly consistent. The Table 2 shows the Cronbach's alpha for each scale:

Table 2. Cronbach's Alpha

Field Of Study	No. Of Questions	α Coefficient
Control Environment	7	0.917
Risk Assessment	3	0.953
Control Activities	7	0.970
Information and Communications	7	0.932
Monitoring	6	0.869
Total	30	0.973

7.3.2 Sample characteristics

The respondents were 81.2% male and 18.8% female; most of them were young people, 80% were less than or equal 45 year old. Most respondents had average experience in their bank; for example, 81.2% had more than 6 years' experience. The respondents were from middle and first-line management levels 88.2% :Accountants 50.6% , Accounting officers 25.8% , CEO 11.8% , most of respondents had no professional certificates (73%) just like JCPA or CPA , Demographic data is shown in Table 3.

7.4 Variables Analysis

7.4.1 Descriptive analysis

Means and Standard Deviations were used to describe attitudes towards many questions as follows:

First: Do Jordanian Commercial Banks establish a basis of its internal control environment (Control Environment Components). In an internal control environment what are the techniques or approaches currently being used by the Commercial Banks in Jordan?

Table 4 shows that there are positive attitudes towards all the seven questions since their means are above 3 with question No.5 having the highest positive mean (3.765)with (0.766) standard deviation, followed by question No. 3 with mean (3.577) and with (0.943) standard deviation, there is no a negative attitude towards any question of these attitudes. This gives

an indicator that Control Environment components in commercial banks in Jordan are applied and employees are complying with its rules and procedures.

Table 3. Demographics Data for the Pivot Study

Variable	Group	Frequencies	%
Sex	Male	69	81.2
	Female	16	18.8
Total		85	100%
Age	Less than 25 years	13	15.3
	From 26 years—35 years	29	34.1
	More than 36 years—45 years	26	30.6
	More than 46 years	17	20
Total		85	100%
Professional Certificate	JCPA	16	18.8
	CPA	7	8.2
	Accounting Degree	62	73
Total		85	100%
Job Title	Accountant	43	50.6
	Accounting officer	22	25.8
	CEO	10	11.8
	Member of the Board of Directors	10	11.8
	Total		85
Experiences	Less than 5 years	16	18.8
	From 6 years – 10 years	36	42.4
	More than 11 years – 15 years	19	22.3
	More than 16 years	14	16.5
Total		85	100%

Second Question: Do Jordanian Commercial Banks establish a basis of its internal control risk protection (Risk Assessment Components). In an internal control system, what are the techniques or approaches currently being used by the Commercial Banks in Jordan to protect the firm from risk?

Table 5 shows that there are also positive attitude towards the three questions since their means are above 3 with question No.8 having the highest positive mean (3.682) with (0.941) standard deviation, followed by question No.10 with mean (3.682) and with (0.889) standard deviation, there is no a negative attitude towards any question of these attitudes . This gives an indicator that Risk Assessment components in commercial banks in Jordan are applied and employees are complying with its rules and procedures.

Third Question: Do Jordanian Commercial Banks are conducting control activities (Control Activity Components). In an internal control system, what are the techniques or approaches currently being used by the Commercial Banks in Jordan to perform its control activities efficiently?

Table 6 shows that there are also positive attitude towards all questions, except questions nos. (16), (17) are moderate in their means, the others, since their means are above 3 with question No.15 having the highest positive mean (3.765) with (0.766) standard deviation, followed by question No.13 with mean (3.577) and with (0.943) standard deviation, there is

no a negative attitude towards any question of these attitudes . This gives an indicator that Control Activities components in commercial banks in Jordan are applied and employees are complying with its rules and procedures.

Table 4. Means and Standard Deviations for Control Environment Components

No.	Elements of Control Environment	A. Means	S. Deviation	Rank	Median Likert Scale
1	Top management had clearly clarified job ethical values, and clearly identified employee's integrity	3.565	0.905	3	High
2	The board of directors demonstrates independence of management and exercises oversight for the development and performance of internal control	3.565	0.931	3	High
3	Management establishes, with the board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives.	3.577	0.943	2	High
4	The organization holds individuals accountable for their internal control responsibilities in the pursuit of objectives.	3.506	0.881	4	High
5	The organization chart specifies clearly the responsibilities of each department and each position	3.765	0.766	1	High
6	There is a strong management commitment to financial reporting competencies	3.424	0.836	5	Moderate
7	Human resources department keeps continuous, conferences, development, and training courses in order to achieve the objectives of the organization	3.329	0.730	6	Moderate
	Total	4.015	0.854		High

Fourth Question: Do Jordanian Commercial Banks establish a basis of its information and communication policies (Information and Communication). In an internal control system, what are the techniques or approaches currently being used by the Commercial Banks in Jordan to perform its information and communication activities efficiently?

Table 7 shows that there are also positive attitude towards the last two questions since their means are above 3 with question No.24 having the highest positive mean (3.659) with (0.664) standard deviation, followed by question No.23 with mean (3.553) and with (0.587) standard deviation, the other questions having moderate arithmetic means, no negative attitude towards any question of these observed. This gives an indicator that Information and Communication components in commercial banks in Jordan are applied and employees are complying with its rules and procedures.

Fifth Question: Do Jordanian Commercial Banks establish a basis of its monitoring function (monitoring). In an internal control system, what are the techniques or approaches currently being used by the Commercial Banks in Jordan to perform its monitoring function efficiently?

Table 5. Risk assessment

No.	Elements of Risk Assessment	A. Means	S. Deviation	Rank	Median Likert Scale
8	Management specifies objectives with sufficient clarity to enable the identification and assessment of risk relating to objectives.	3.682	0.941	1	High
9	There is clear and careful consideration of factors that may cause exposure and increase risk	3.659	0.838	3	High
10	Management has clear strategy of how to assess risk and determining the acceptable level, and how to manage the risk to a desired risk level	3.682	0.889	2	High
Total		3.675	0.851		High

Table 6. Control activities

No.	Elements of Control Activities	A. Means	S. Deviation	Rank	Median Likert Scale
11	There is certain policies and procedures that are conducted in order to identify and prevent the occurrence of risk	3.565	0.905	3	High
12	Authorization is adopted by management as one of the control activities	3.565	0.931	3	High
13	Segregation of duties is adopted by management as one of the control activities	3.577	0.943	2	High
14	Independent reconciliation is adopted by management as one of the control activities	3.506	0.881	4	High
15	Proper documentation is adopted by management as one of the control activities	3.765	0.766	1	High
16	Advance protection methods is adopted by management as one of the control activities	3.424	0.836	5	Moderate
17	There is continuous development of control activities	3.329	0.730	6	Moderate
Total		3.533	0.791		High

Table 7. Information and Communications

No.	Elements of Information and Communications	A. Means	S. Deviation	Rank	Median Likert Scale
18	Management has a sound information and communication practices process	3.424	0.585	5	Moderate
19	Management provides information about the external events, activities and conditions.	3.447	0.698	4	Moderate
20	Management communicates information to all levels of enterprise.	3.424	0.564	5	Moderate
21	Management uses information technology	3.482	0.547	3	Moderate
22	Management has clear vision of its need of information	3.368	0.574	6	Moderate
23	Management practice tight control over the information	3.553	0.587	2	High
24	The enterprise has its own board of control over communication	3.659	0.664	1	High
	Total	3.479	0.510		Moderate

Table 8 shows that there are moderate attitude towards all questions, except question no. (30), that has the highest rank, this item refers to the Internal auditing which supported by top management, whether audit committee, or the board of directors, the others has moderate ranks, This gives an indicator that monitoring components in commercial banks in Jordan are relatively applied and employees are complying with its rules and procedures as it has been shown in Table 8.

It's obvious from the Tables 4, 5, 6, 7 and 8 that, the arithmetic means for all categories are mostly high, which indicates that, the study's hypothesis will be rejected in its null form, since the computed mean >3, (the hypothetical).

Finally, the second hypothesis was tested to find whether there is a relationship between employees credentials and knowledge of internal control systems and the reliability and credibility of financial statements. Unvaried analysis has been performed to test if there is significant relationship between credentials and knowledge, and reliability and creditability of financial statements. We found out that the significance level equals 0.454 which is higher than 0.05, (Sig>0.05), therefore there is no relationship between credentials and knowledge of internal control systems and the reliability and credibility of financial statements. Table 9 illustrates this result.

Table 8. Monitoring

No.	Elements of monitoring	A. Means	S. Deviation	Rank	Median Likert Scale
25	Management select, develops and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.	3.306	0.463	3	Moderate
26	Management conducts periodic evaluation of the internal control system.	3.306	0.463	3	Moderate
27	There is a feedback report that reports the deficiencies occurred during the year.	3.235	0.610	5	Moderate
28	The board of directors and the audit committee has clear roles towards the internal control process and evaluation.	3.338	0.490	2	Moderate
29	Internal auditing is properly organized, management and the audit committee can monitor the reliability and integrity of financial and operating information	3.271	0.605	4	Moderate
30	Internal auditing has the complete support of top management, the audit committee, and the board of directors	3.577	0.661	1	High
Total		3.353	0.426		Moderate

Table 9. Tests of between-subjects effects dependent variable: xyz

Source	Type III Sum of Squares	Df	Mean Square	F	Sig.
Corrected Model	28.107a	29	.969	19.579	.000
Intercept	386.037	1	386.037	7798.294	.000
x	18.887	18	1.049	21.196	.000
certification	.079	2	.040	.800	.454
x * certification	.216	9	.024	.485	.879
Error	2.723	55	.050		
Total	1139.160	85			
Corrected Total	30.830	84			

a. R Squared = .912 (Adjusted R Squared = .865)

8. CONCLUSIONS AND RECOMMENDATIONS

8.1 Conclusions

According to Data Analysis, and Hypothesis testing the study had concluded the following:

- 1 Control Environment components in commercial banks in Jordan are applied.
- 2 Risk Assessment components in commercial banks in Jordan are applied.

- 3 Control Activities components in commercial banks in Jordan are applied.
- 4 Information and Communication components in commercial banks in Jordan are applied.
- 5 Monitoring components in commercial banks in Jordan are relatively applied
- 6 The effectiveness of the internal control systems in the Jordanian commercial banks is not attributed to demographic variables (sex, age, profession, etc) but mostly, attributed to tight internal control systems adopted, and demonstrated by management.
- 7 Effectiveness can be attributed also to other factors such as, the training courses demonstrated by the bank's management and the selection of a highly qualified employees.
- 8 Effectiveness does not mean that every internal control should be effective rather it means that, for the purpose of the guidance, internal controls considered by management should include all types of controls including those of operational and compliance nature, as well as internal financial controls.

8.2 Recommendations

According to the study conclusions the researchers recommend the following:

- 1 Management should keep tight recruiting policies in order to implement its internal control systems effectively.
- 2 Internal control systems adopted should be applicable and easy to understand.
- 3 Incentives should be offered and made, to employees who are in compliance with the internal control structure, procedures, and policies.
- 4 More research to be carried on the same field of effectiveness of internal control systems, but on other work areas such as factories, universities, and merchandising companies.

COMPETING INTERESTS

Authors have declared that no competing interests exist.

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