Internal Control and Public Sector Revenue Generation in Nigeria: an Empirical Analysis

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A b s t r a c t

This study an empirical analysis of internal control and public sector revenue generation in Nigeria at Federal Inland Revenue Service (FIRS) with a view to establish whether such internal controls have produced any meaningful results in increased collected revenue. The study population was the senior staff during the calendar year 2016. The research was conducted using both qualitative and quantitative approaches. Questionnaires were used on a population of 38 respondents in gathering primary data for the study. Data was analyzed by use of the linear regression. The data collected was then analyzed and findings have revealed that the five components of control environment, risk assessment, control activities, information and communication and monitoring must be available for internal controls to work as they are positively significant. The study therefore concludes that internal controls do function although with hiccups and that there is a significant effect between internal controls and revenue collection in FIRS. The study recommends FIRS to cultivate integrity and ethical values among its employees and management. Effective board of directors, management, and internal audit departments should be established in organizations. Management should design internal controls to ensure efficiency and effectiveness, reliability of financial reporting as well as compliance with laws and regulations. FIRS should adopt internal control and information systems that produce operational, financial and compliance-related information reports to make it possible to run and controls the business. Internal controls need to be adequately monitored in order to assess the quality and the effectiveness of the system's performance over time. Monitoring of tax payers feedback and audits should be conducted periodically by internal auditors. This will improve revenue generation that will ensure sustainable Nigeria economic growth and development.

Keywords: *Control environment, Risk assessment, Control activities, Information, communication, Monitoring and Revenue collection.*

Background of the Study

Internal control is an important issue in accounting and finance. It is fundamental aspect of management stewardship responsibility to provide interested parties with reasonable assurance that their organisation is effectively controlled and that the information they receive are accurate and dependable. Developing a strong system of internal control systems provides this assurance. The heightened interest in internal controls is, in part, as a result of significant losses incurred by several organizations. Muhibat (2016) explained that, an analysis of the problems related to losses indicated that they could probably have been avoided had the organizations maintained effective internal control systems. Such systems would have prevented or enabled earlier detection of problems that led to losses in the banking industry, thereby limiting damage to the organization. This same idea is reflected, that, poor standards of corporate governance had led to insufficient controls being in place to prevent wrong doing in the United States in the 1990s, as demonstrated by the collapse of Enron and WorldCom.

Understanding the concept of internal control is important for developing an understanding of its impact on revenue generation in an organization (Jubb, 2008, Ewa & Uduuayang, 2012 & Sanusi and Mustapha, 2016). The entire internal control system of an organization is strictly interrelated to structures that management use to oversee the activities of the organization; the organization's corporate governance. As a result of effective and efficient internal control systems, on organizations attains good corporate governance which provides proper incentives for the management to pursue and realize the objectives of the organization. Internal controls are essential to corporate success and survival because they provide reasonable assurance on the achievement of objective in a number of categories including: effectiveness and efficiency of operations; reliability in financial reporting; and compliance with applicable laws and regulations (Chambers, 2009 and Muhibat, 2016).

Internal control is one of many mechanisms used in business to address the agency problem. Others include financial reporting, budgeting, audit committees, and external audits. (Karagiorgos, Drogalas, Gotzamanis and Tampakoudis, 2009). Their Studies have shown that internal control reduces agency costs with some even arguing that firms have an economic incentive to report on internal control, even without the requirements of SOX. Their argument assumes that providing this additional information to the principal (shareholder) about the behavior of the agent (management) reduces information asymmetry and lowers investor risk and, therefore, the cost of equity capital. Other research has found that weaknesses in internal controls are associated with increased levels of earnings management Amudo. (2009). Earnings management is the agency problem that motivated SOX legislation in the first place, specifically earnings manipulation by Enron, WorldCom. Internal controls have played a major role in moderating the agency problem in corporations for many years. Accordingly, Samson (2006) document several internal control procedures used by the Baltimore and Ohio Railroad as early as 1831.

According to Ngugi (2011) Internal Control System refers to an organized amalgamation of functions and procedures, within a complete system of controls established by the management and whose purpose is the successful function of the business. Internal Control System is all the methods and procedures followed by the management in order to ensure, to a great extent, as much successful cooperation as possible with the director of the company, the insurance of the capital, the prevention and the detection of fraud, as well as the early preparation of all the useful financial information, Internal Control System resembles the human nervous system which is spread throughout the business carrying orders and reactions to and from the management. It is directly linked to the organizational structure and the general rules of the business.

Whittington (2001) has defined that a system of internal control extends beyond those matters which relate directly to the functions of accounting and the financial statements. In addition, he notes that internal control is a systematic procedure which will lead to evaluate the degree of correlation between those established criteria and the real results of the business. Internal Control, as defined from the APC (Auditing Practices Committee, 1980), is an independent examination and certification from an inspector appointed by the business to control the finances according to the legal framework established each time.

Mawanda (2008) stated that revenue collection is the amount of money that a company receives during a specific period. It is the "top line" or "gross income" figure from which costs are subtracted to determine net income. Revenue collection can be defined as income that a company receives from its normal business activities, usually from the sale of goods and services to customers. Revenue is referred to as turnover. Some companies receive revenue from interest, dividends or royalties paid to them by other companies. Revenue may refer to business income in general, or it may refer to the amount, in a monetary unit, received during a period of time.

This research is intended to assess the effect of internal controls on revenue collection with emphasis in FIRS. The review of available literature therefore attempted to establish whether there is a correlation between Internal Control as an independent variable and revenue collection as a dependent variable. The review particularly focused on; Control environment, Risk Assessment, Control activities, Information and Communication and Monitoring the main components of Internal Control as proposed by Committee of Sponsoring Organizations of the Tread way Commission, COSO. The review examined the common systems of internal controls employed by the organizations.

Statement of the Problem
There have been incessant cases and stories been told about high frequency of fraud, embezzlement, overcharging, manipulation, missing files and ledger cards and other revenue collection linkages in Nigerians states of board of internal revenue and FIRS today, with the management and government not knowing how to handle the adverse situation. Organizations continue to experience low levels of revenue generation most of which are man-made and therefore avoidable. Despite the numerous rules and regulations, the varying levels in revenue generation occur across all entities in the

government and private sectors. No matter how well it is designed and operated, an internal control system can only provide a reasonable, not absolute assurance that the objectives of the company's internal control system are met in terms of revenue generation. There is a gap in the internal control studies that only one or two variable(s) are used. This study incorporates all the five basic internal control variables. In addition, most of the studies are foreign base with only few Nigerians.

Objectives of the Study
The main objectives of this study is to evaluate internal control which have been put in place by FIRS and their impact on revenue collection. Specifically, this was carried out with a focus on six sub-objectives. And also to assess the impact of control environment, control activities, information and communication, monitoring, risk assessment and on revenue collection in Federal Inland Revenue Service of Nigeria.

Research Questions
To what extent does internal control effect revenue generation in Federal Inland Revenue Service?

Hypothesis of the Study
H_{01}:   There is no significant impact of internal control on revenue collection in FIRS.

Significance of the Study
This study would be important to FIRS in formulating policies and procedures for collection and checking on corrupt tax collection official. The study would create awareness as to the level of internal controls which have been put in place and to use the recommendations proposed to add in to the already implemented. To the practice therefore, the study would help managers to understand how internal controls work and how to implement them and to know the areas of revenue leakage.

The findings of this research would also contribute to literature by providing additional evidence to support the existing theories. Researchers will use information in this study as part of literature review while carrying out other research on the impact of internal control on revenue collection.
This research will also be helpful to the FIRS in coming up with the budget and setting out collection target for the revenue collection body.

The study will contribute to organization/firms to cultivate integrity and ethical values among its employees and management. Effective board of directors, management, and audit division should be established in organizations. Qualified and effective internal auditor should be hired in organizations. Internal and external auditor should be encouraged to interact well. A culture should be developed in organizations for good attitude and policies of management in regard to the importance of internal controls in revenue generation. Management should determine the level of risk carefully to be

accepted, and try to maintain such risk within determined levels. Management should design internal controls to ensure efficiency and effectiveness, reliability of financial reporting as well as compliance with laws and regulations.

Scope of the Study

The scope of this study is to evaluate the relationship between internal control and revenue collection in FIRS, Nigeria. The data was collected through questionnaires administered on the staffs of FIRS in relation to revenue collection and internal control. In addition to that the study also incorporates the government efforts put in place inform of internal control of revenue collection from 2000 to date. The period is considered adequate as its captured democratic rule in Nigeria.

Literature Review
The Concept of Internal Control

This research is intended to assess the effect of internal controls on revenue collection with emphasis in FIRS. The review of available literature therefore attempted to establish whether there is a correlation between Internal Control as an independent variable and revenue collection as a dependent variable. The review particularly focused on; Control environment, Control activities, Information and Communication and Monitoring the main components of Internal Control as proposed by Committee of Sponsoring Organizations of the Tread way Commission, COSO. The review examined the common systems of internal controls employed by the organizations.

Internal controls are measures that organizations institute with the aim of ensuring that the objectives, goals, and mission of the organization are met (Rezaee, 2002). They refer to set of organizational policies and procedures that ensure any transaction is processed in the appropriate way to avoid waste, theft and misuse of organization resources. Through internal control systems, organizations achieve performance and organizational goals, prevent loss of resources, enable production of reliable reports and ensure compliance with laws and regulations. Thus internal control is established by the organizational management to ensure that the business of enterprise is carried out in an orderly and efficient manner. This further ensures adherence to management policies safeguard the assets and secure the completeness and accuracy of the records. Organizations are constantly and extensively working to improve their internal control systems so as to increase revenue inflow, survive in the rapidly changing economic and competitive environments, and adapt to the shifting customer demands and priorities (Kantzos and Chondraki, 2006). Internal control consists of five interrelated components which are derived from the way management runs a business, and are integrated with the management process: control environment; risk assessment; control activities; information and communication; and monitoring (Carmichael, 1996). According to Rittenberg (2005), under the current operations of organizations in general, the importance of internal control can be divided into six major categories; detecting error and fraudulence, decreasing illegal conduct, improving the competence of the business entity, improving the quality of data, helping to create the business infrastructure, and decreasing auditors" fee.

The Concept of Revenue

Revenue refers is that monetary event of asset valves increasing in the organization because of the physical event of production or sales of products or services of the organization. Rittenberg and Schwieger (2005) define revenue as the inflows or enhancements of assets of a firm or settlements of its liabilities during a period from delivery or producing goods, rendering service or other activities that constitutes the entity''s ongoing major or central operations. In addition, described revenue as inflows of asset (almost always cash or accounts receivables) received for products or services provided to customers. Organizational performance is in terms of revenue generation portrayed by the levels of assets accumulation, wealth created, and the quality services by customer level of satisfaction and customer complaints. For better revenue generation, organizations should critically look at customers and other stakeholders in business and establish how best they are satisfying their needs. Organizations should continuously improve their revenue and have an internal control system that is intervened with organizations operating activities and it is most effective when controls are built into the organizations infrastructure in terms of continued improvement on performance standards as part of the competitive advantage of the organization.

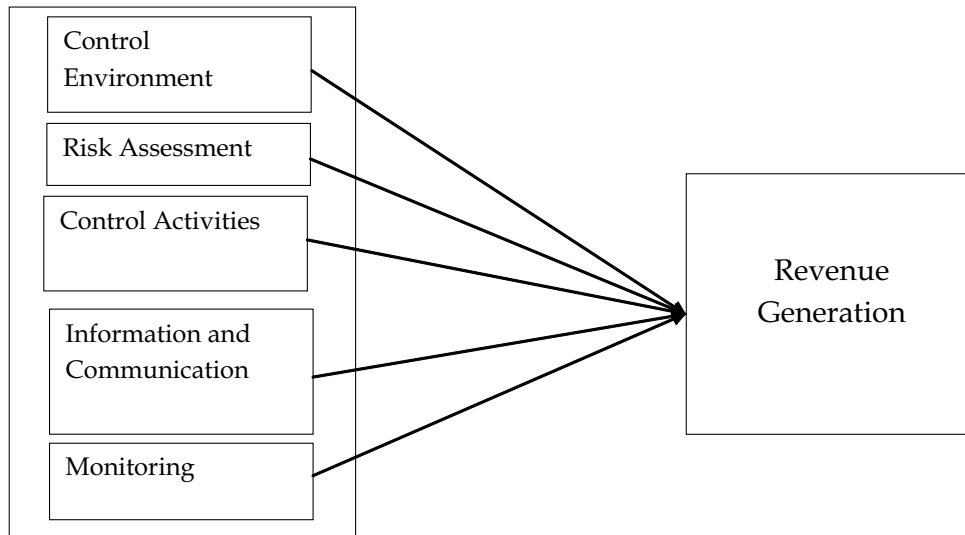**Relationship between Internal Controls and Revenue**

Internal control systems including internal audits are intended primarily to enhance the reliability of financial performance, either directly or indirectly by increasing accountability among information providers in an organization (Jensen, 2003). Internal control therefore has a much broader purpose such that the organization level of control problems associated with lower revenues, which explore links between disclosure of material weakness and fraud, earnings management or restatements (Doyle et al., 2005).

Internal controls provide an independent appraisal of the quality of managerial performance in carrying out assigned responsibilities for better revenue generation. An effective internal control system unequivocally correlates with organizational success in meeting its revenue target level. Effective internal control for revenue generation involves; regular a review of the reliability and integrity of financial and operating information, a review of the controls employed to safeguard assets, an assessment of employees' compliance with management policies, procedures and applicable laws and regulations, an evaluation of the efficiency and effectiveness with which management achieves its organizational objectives.

The model of the study is shown below that connect internal control and revenue collections are as follows:

Internal Control
Independent Variable

Revenue Generation
Dependent Variable

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Control
Environment

Risk Assessment

Control Activities

Information and
Communication

Monitoring
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Revenue
Generation
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Source: Author (2017) Synthesis of Internal Control and Revenue Generation

Control Environment and Revenue Generation
The control environment is the foundation of the five elements in the internal control framework. Its designation and operation Rittenberg (2005), not only affect the enterprise' overall activity, but the other four elements. Therefore control environment directly affects the effect of implementation of internal control framework and the modern enterprises should establish a suitable internal control environment. Muhibat (2016), Sarens and De Beelde (2006) & Ewa and Udoayang (2012) find a positive significant relationship between control environment and revenue generation. They all concluded that control environment is very necessary in revenue generation.

Risk Assessment and Revenue Generation
Risk assessment system Amudo and Inanga (2009), Chambers (2009), Sanusi & Mustapha (2015) is divided into three steps: risk identification, risk analysis and evaluation, risk control and report.
1.   Risk identification. It asks the enterprise to judge and analyze risks, including its nature, types, and reasons of the occurrence, etc.
2.   Risk analysis and evaluation. Risk analysis and evaluation needs quantitative analysis of digital information collected by mathematical method in order to make the risk management based on scientific basis. The result of risk analysis and risk evaluation is the probability of occurrence and size of the risk so as to provide a dependable basis for decision-making.
3.   Risk control and report. As to risk analysis and assessment, management should consider how to control risk. The method of controlling risk usually is to transfer risk, adverse risk and disperse risk.

The studies found a positive significant relationship on revenue generation and concluded that risk assessment is a fundamental factor in revenue generation to be considered.

Control Activities and Revenue Generation
Control activities are to make management instructions designed could be effective implementation of various policies and procedures. Control activities Sarens and De Beelde (2006), Gold Knechel and Wallage (2012), can help enterprises to ensure that it has already took measures to reduce a loss according to realization the goal of the enterprise. It refers to the managers decentralize powers to his subordinates to make them have the right to address the problem and make a choice and share corresponding responsibility. This refers to define the authority and responsibility according to the principle of combining functions of department and it's characteristic. Business process is the procedure of all the business. An operation procedure is how to operate every matter in detail. Control activities was found to have a positive and significant impact on revenue generation (Jubb, 2008, Ewa & Uduuayang, 2012).

Information and Communication and Revenue Generation
Enterprise management activities can be divided Jensen (2003) & Hayes (2005), into the plan, organization, coordination, reports, etc. These studies found that when managers exercise these functions, messages are always the most basic support, namely, all the enterprise business activities are inseparable from information. Therefore, concluded that the information function is the basis of management activities and the level of information processing ability is one of the most important symbols of the level of management. And this information must be delivered timely to those who fulfill its responsibility and other responsible ones in some form. Completing the information transmission is communication and it can translate the abstract goal and plans into language that encourage employees (Amaudo & Inanga, 2009).

Monitoring and Revenue Generation
Monitoring Doyle and McVay (2005), is used to evaluate the quality of enterprise internal control performance by tracking and monitoring the internal control frame and operational status and take the necessary actions to ensure that internal control can operate effectively. Monitoring can be divided into continuous monitoring and individual assessment. Continuous monitoring activities usually are that the management department and each staff at various levels inspect, analyze and evaluate the effectiveness and efficiency of production and operating activities of their respective during execution of the internal control system. It is a kind of self control mode. The higher the level is, the less individual evaluation need. Individual assessment is to evaluate the internal control system regularly and is usually done by the relatively independent internal audit department (Sarens & Beelde, 2006).

Theoretical Framework
There are many theories such as Agency, Attribution, Reliability and Control theories that link the study of internal control and revenue generation. This study reviewed control theory and adapted it to anchor internal control and revenue generation in FIRS. Control

theory has been described as "an interdisplinary branch of engineering and mathematics that deals with the behavior of dynamical systems with inputs. The external input of a system is called the reference. When one or more output variables of a system need to follow a certain reference over time, a controller manipulates the inputs to a system to obtain the desired effect on the output of the system. The objective of a control theory is to calculate solutions for the proper corrective action from the controller that result in system stability, that is, the system will hold the set point and not oscillate around it. Systems (Sarens & Beelde 2006) have inputs and outputs to bring a product after processing and so inputs and outputs of a control system are generally related by differential equations.

Setting objectives, budgets, plans and other expectations establish criteria for control. Control itself exists to keep performance or a state of affairs within what is expected, allowed or accepted. Control built within a process is internal in nature. It takes place with a combination of interrelated components-such as social environment effecting behavior of employees, information necessary in control, and policies and procedures. Internal control structure is a plan determining how internal control consists of these elements (Sanusi & Mustapha, 2015).

Methodology
The study was conducted using descriptive case study research. An explanatory case study is used to explore causation in order to find underlying principles. Case studies are analyses of persons, events, decisions, periods, projects, policies, institutions, or other systems that are studied holistically by one or more methods. Correlation is the determination of whether or not and to what extent and association exists between two or more variables. Correlation therefore was used as a means of trying to examine the effect that internal control brings to revenue collection. The research population is FIRS staff since most employees are directly or indirectly involved in decision making and controls. The study basically targeted top and middle level management members because they are the custodians of internal control as the sample. The researcher therefore used purposive sampling techniques in selecting interviewees with an option of replacing those who don't wish to respond to the researcher's plea.

Data was collected using both primary and secondary data collection techniques. Primary data was gathered basically through structured questionnaires and interviews. Secondary data on the other hand was gathered through review of available relevant materials. The researcher also used a combination of structured questionnaires and interviews. The main instrument of data collection used was the questionnaire. The study used both primary and secondary data. Secondary data was from management and financial reports. The drop and pick method was used to collect primary data. The structured questions were used in an effort to conserve time and money as well as to facilitate in easier analysis as they are in immediate usable form. Primary data was collected using structured questionnaires. The questionnaire consisted of both open and closed ended questions using five Likert Scale.

The data was analyzed using both statistical and narrative methods. Correlation was used as a way of assessing the effect of internal controls and revenue generation. Narrative analysis was also used to explain the qualitative results of the survey. The researcher reviewed the appropriate statistical data analysis tools namely descriptive, inferential and test statistics before analyzing the data. Collected raw data was cleaned and edited for completeness and consistency. It then systematically organized to confirm if it represents the target population and to facilitate objective analysis. The responses were also screened for correctness and accuracy and then they were assigned numerical values which were representing various attributes being measured. Data was analyzed by use of the linear regression model below:

$$ARG = \beta_0 + \beta_1 CET + \beta_2 RMT + \beta_3 ICS + \beta_4 CAS + \beta_5 MNG + \varepsilon \dots\dots\dots\dots\dots\dots(1)$$

Where:
ARG is the annual revenue generation,
β_0-β_5 are coefficients.
CET is control environment. It was measured by the level of integrity, ethical values, and competence of personnel tasked with creating, administering, and monitoring the controls.
RMT is risk management and was measured by level of risk carefully to be accepted and maintained determined levels.
ICS is information and communication systems. This was measured in terms of how information is identified, captured, and communicated in the appropriate form and within stipulated time frame.
CAS is control activities that were measured the number of effective policies, procedures, and mechanisms put in place to ensure directives of the management are properly well.
MNG is monitoring. Monitoring was measured by how frequent the quality and effectiveness of internal controls are assessed. ε is the error term for the model

E-views Software is used to aid in quantitative data analysis in this study. The results were presented in tables. Qualitative data from the open-ended questions was analyzed through content analysis. The output for this study was presented using descriptive statistics like the mean score and standard deviation were used for further representation and regression results.

Result and Discussions
Regression Analysis
As shown in Table 1, the five independent variables that were studied explain 88.3% of the revenue generation as represented by the R^2. This therefore means that other factors not studied in this research contribute 11.7% of the revenue generation at the FIRS. Therefore, further research should be conducted to investigate the other factors (11.7%) that affect revenue generation.

Table 1: ANOVA

MODEL	R	R^2	Adjusted R^2	Std. Error of the Estimate	Sig. F Change (P-value)
1	0.978[a]	0.883	0.590	0.478	0.000

Source: Author Research Data (2017) Eview Result

The P-value of 0.000 (Less than 0.05) implies that the model of internal control system at UNES is significant at the 5 percent significance. As illustrated in the table, the significance value is 0.000 which is less than 0.05 thus the model is statistically significance.

Table 2: Model Summary: Coefficient of Determination

MODEL	Summary	Df	Mean Square	F	Sig
Regression	7.711	5	3.959	2.701	0.012[a]
Residual	20.799	22	1.466		
Total	28.510	27			

Source: Author Research Data (2017) E-view Result

Table 2 shows a summary of the analysis of the model. The F critical at 5% level of significance was 27.711. Since F calculated is greater than the F critical (value = 2.701), this shows that the overall model was significant.

Table 3: Coefficient of Determination

MODEL	Unstandardized Coefficients		Standardized Coefficients	T	Std
	B	Std. Error	Beta		
Constant	2.81	0.57		4.88	0.00
Control Environment	0.26	0.13	0.253	1.98	0.05
Risk Assessment	0.05	0.15	0.042	0.30	0.77
Information and Communication System	0.25	0.14	0.209	1.83	0.07
Control Activities	0.13	0.14	0.105	0.87	0.39
Monitoring	0.01	0.11	0.010	0.10	0.92

Source: Research Data (2017) Eview Result.

Table 3 illustrates results of a linear regression analysis determining the effect of the independent variables (control environment, risk environment, information and communication systems, control activities, and monitoring) on the dependent variable (revenue generation). Using the results, we have the regression equation as

ARG = 2.81+ 0.26CET+ 0.05RMT+ 0.25ICS+ 0.13CAS + 0.01MNG …………………(2)

Where ARG is the dependent variable (revenue generation), CET is control environment, RMT is risk assessment, ICS is information and communication system, CAS is control activities, and MNG is monitoring.

According to the regression equation established, taking all factors into account with constant at zero, revenue generation will be 1.819. The data findings analyzed also show that revenue generation is greatly control environment followed by information and communication system. Taking all other independent variables at zero, a unit increase in control environment to a 0.26 billion naira increases in revenue generated while a unit increase in information and communication system will result in a 0.25 billion naira increases in revenue generated by FIRS. On the other hand, one unit increase in monitoring will result to only 0.01 billion increases in revenue generated.

Summary and Interpretation of Findings
FIRS play a number of roles in supporting the systems by ensuring all documents are authentic, correct and confirm that the relevant officers have signed all documents before processing to prevent misappropriation of revenues. According to Hayes et al. (2005), internal control comprises five components; the control environment, the entity's risk assessment process, the information and communication systems, control activities and the monitoring of controls.

Weaknesses identified within the system are addressed through relevant recommendations made. Systems of internal control were functioning as per the intended plan thus enhancing efficiency and accurate data capturing. Internal controls are essential to corporate success and survival because they provide reasonable assurance on the achievement of objective in a number of categories including: effectiveness and efficiency of operations; reliability in financial reporting; and compliance with applicable laws and regulations (Chambers, 2009). Numerous audits are conducted in line with technological changes to ensure the systems' sustainability. This enhances easy detection of few errors that have occurred. Frequent audits have helped in evaluating and improving the effectiveness of the systems. Checks and balances of the organizational form a basis for the authority functions to minimize the potential losses due to fraud, abuse and mismanagement (Sarens and De Beelde, 2006).

Conclusion
The study revealed that FIRS reviews its ICS when need arises. FIRS play a number of roles in supporting the systems by ensuring all documents are authentic, correct and confirm that the relevant officers have signed all documents before processing to prevent

misappropriation of revenues. Timely bank reconciliation, customer records reconciliation and report accurately on revenue collections are undertaken. There was existence of loopholes through which revenue is lost. The study concluded that systems of internal control were functioning as per the intended plan thus enhancing efficiency and accurate data capturing.

Recommendations

The study recommends FIRS to cultivate integrity and ethical values among its employees and management. Effective board of directors, management, and audit division though established in organization should be enhanced. Qualified and effective internal auditor should be hired in organizations. Internal and external auditors should be encouraged to interact well. A culture should be developed in organizations for good attitude and policies of management in regard to the importance of internal controls in revenue generation. Management should determine the level of risk carefully to be accepted, and try to maintain such risk within determined levels. Management should design internal controls to ensure efficiency and effectiveness, reliability of financial reporting as well as compliance with laws and regulations. This can be achieved by periodic performance review and evaluation of the adequacy and effectiveness of the controls designed by the internal audit department. Further research is recommended in internal control and other areas of capacity of governance that can ensure economic growth and development.

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