CHAPTER VII : INTERNAL CONTROL ARRANGEMENTS

FINANCE DEPARTMENT

7.1 Internal Control Mechanism in Finance Department

7.1.1 Introduction

Internal control is a management tool used to provide reasonable assurance that management's objectives, *viz.*, reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations, *etc.*, are being achieved. A good system of internal control should comprise *inter alia* (i) proper allocation of functional responsibilities within organisation, (ii) proper operating and accounting procedures to ensure the accuracy and reliability of accounting data and (iii) the review of the work of one individual by another whereby the possibility of fraud or error is minimised.

Internal audit is an appraisal activity established within an entity as a service to the entity. Its functions, *inter alia,* include examining, evaluating and monitoring the adequacy and effectiveness of the accounting and the internal control system. Internal audit works as the 'eyes and ears' of the management. It also helps the management to bring out changes in the system necessary to rectify and prevent defects, loopholes and shortcomings that are detected and pointed out.

7.1.2 Organisational set up

For effective financial management and internal control, the Finance Department has seven branches, *viz.*, Establishment, Control, Economic Affairs, Budget, Audit and Fund (A&F), Pay Revision and Pension. The Chief Secretary is the overall in-charge of the department and is assisted by the Commissioner and Secretary, Additional Secretary, Joint Secretary, besides Deputy Secretary, Under Secretary and Superintendent of the respective branches. The department is also assisted by the Director of Accounts and Treasuries (DAT) and the Examiner of Local Accounts (ELA). While the training in Government finance, accounts and audit as well as rendering advice to the Government on financial and accounts matters is the responsibility of the DAT, the ELA is responsible for conducting internal audit.

The duties, powers and functional jurisdiction of the ELA as prescribed under the notification of October 1990 are (i) to examine and carry out the audit of accounts of local bodies and accounts of various departments of the Government, aided educational institutions, other organisations as specified in the Local Audit Manual and such other accounts of organisations/offices, *etc.* as may be entrusted by the Government from time to time in this regard and to pass and issue Audit/Inspection Report thereon and, (ii) to supervise and inspect the audit of the aided institutions/organisations and offices throughout the State.

7.1.3 Manpower

For comprehensive and effective internal audit, skilled manpower is necessary. The men-in-position for internal audit *vis-à-vis* sanctioned strength as of March 2004 was as follows:

Table 7.1

Posts	Sanctioned strength	Men-in-position
Audit Officer	27	9
Auditor	35	35
Assistant Auditor	72	54

Source: Information furnished by the ELA.

Out of existing manpower, the services of two Audit Officers and 13 Assistant Auditors are placed at the disposal of nine Directorates and two Audit Officers and three Auditors are attached to the Directorate of Local Accounts for scrutinising Inspection Reports received from the field audit staff and calculation of Death-cum-Retirement Gratuity, *etc.* The remaining five Audit Officers, 32 Auditors and 41 Assistant Auditors are with the ELA and their services are utilised for conducting audit of various accounts and fixation of pay in the revised scale of deficit schools.

The position of manpower for internal control management as of March 2004 was as under:

Table 7.2

Post	Men-in-position	Deployment
Examiner of Local Accounts Director	 1 1	In the individual Directorate of (i) Examiner of Local Accounts (ii) Accounts and Treasuries
Officer on Special Duty	1	Finance Department
Financial Adviser/Finance	19	Deployed in different

and Accounts Officer		departments/directorates
Finance & Accounts Officer	14	One in Directorate of Housing & Social Welfare and 13 in Treasuries as TO/STO

Source: Information furnished by the Finance (Establishment) Department.

7.1.4 Auditing standards

To ensure the quality of the audit and to avoid sub-standard work, auditing organisations frame either their own auditing standards or adopt some prevailing and accepted auditing standards. The work done by the auditors should continuously be compared to the adopted standards to ensure quality. The ELA had not yet framed any auditing standards. Internal Audit Manual of their own had not been brought out by the Directorate/Government and the auditors had been following the Assam Local Funds (Accounts and Audit) Act, 1930 as adopted by the Government of Meghalaya. According to the department, besides the Act of 1930 other rules framed by the Government as standard for auditing were also followed by the Local Audit Department. Details of such rules had not been furnished.

7.1.5 Audit planning

For efficient and optimum utilisation of the limited manpower and financial resources, audit planning is required to be done every year. This ensures coverage of all required units over a period of time, prioritisation of auditee organisations in audit according to need, finalisation of time schedule for audit, *etc.* No such planning was ever done by the ELA, with the exception of grants-in-aids institutions where audit is taken up as per plans and programmes drawn up by the ELA. Consequently, most of the auditee units remained uncovered, as discussed in paragraph 7.1.6 below.

7.1.6 Reporting, issuance and monitoring of Inspection Report

The ELA had not fixed any time limit for issuance of Inspection Reports (IR) to guard against any delay.

Auditors from the field after conducting audit send the IRs to the ELA for record and pursuance. Copies of IRs are also sent to the administrative heads for their information. According to the department, the Audit Reports are monitored through individual files of auditee institutions and the time limit fixed for issuance of Audit Report was soon after completion of audit. Reasons for not fixing specific period for issue of IRs had not been furnished.

The target for coverage of auditee units during 2001-2004 against 1,226 units under the jurisdiction of the ELA and the achievement thereagainst were as under:

Table 7.3

Year	Units targeted (Percentage with reference to total units)	Unit covered by audit (Percentage)	Percentage of shortfall with reference to		Number of Inspection Report (IR) issued	Number of IR settled	Number of IR outstanding (Percentage)
			total units	target			
2001-02	702 (57)	104 (15)	92	85	88	50	38 (43)
2002-03	765 (62)	130 (17)	89	83	124	60	64 (52)
2003-04	730 (60)	120 (16)	90	84	78	70	8 (10)

Source: Information furnished by the DAT.

The table above shows that though the target for coverage was only 57 to 62 *per cent* of the total units, the ELA failed to cover 83 to 85 *per cent* of the said target. Consequently, most of the auditee units (89 to 92 *per cent*) remained uncovered, reasons for which were not on record.

7.1.7 Independence of internal audit

For an effective internal audit, it is necessary that functional independence of the group is ensured so that it is able to function in an objective manner.

According to the existing system, audit of the Government departments/offices is taken up only when a request comes from the respective heads of the departments/offices. This indicates that internal audit has no free access to Government departments/offices.

7.1.8 Training

Staff training is one of the important aspects of manpower development. Training of the internal audit staff plays a vital role in equipping them with latest development/changes in the system of maintenance of accounts or new technology. The audit staff of the ELA has to pass the prescribed course of training as per the provisions of the Service Rules. No other training for improvement of the quality of audit is imparted.

7.1.9 Failure of the internal control system

The system of internal control in the Finance Department was not really effective as exemplified in the following cases:

(i) Computerisation of Treasuries and Accounts

To improve management control of both the State and the district level administration and for speedy and accurate generation of accounts for the purpose of better planning and monitoring, the Tenth Finance Commission had recommended computerisation of treasuries and earmarked Rs.50 lakh for the purpose.

The National Informatics Centre (NIC), Meghalaya State Unit was assigned (1997-98) the job for computerisation of treasuries in the State. As of July 2004, installation of computer network in three out of eight treasuries and the Directorate of Accounts and Treasuries was completed at a cost of Rs.26.93 lakh[a]. In four treasuries, the work of computerisation was still in progress and the expenditure so far was Rs.21.09 lakh[a]. In the remaining one treasury and five sub-treasuries, installation of computer network was yet to be completed after incurring an expenditure of Rs.10.06 lakh out of Rs.1 crore recommended by the Eleventh Finance Commission (EFC) for computerisation of treasuries and sub-treasuries. Further amount of Rs.80.96 lakh out of the EFC's award was also drawn on Abstract Contingent (AC) Bill by the DAT and kept in 'Deposit-at-call' with the State Bank of India, Shillong in April 2004.

Thus, failure to complete installation of the computer network in the treasuries/sub-treasuries even after six years and despite availability of required funds indicated lack of internal control in timely utilisation of funds to achieve the desired objectives.

(ii) Lack of control over sanctioned funds

According to the Meghalaya Treasury Rules, 1985, the Controlling Officers are to submit Detailed Countersigned Contingent (DCC) Bills to the Accountant General against the drawal of AC Bills within a month from the date of drawal.

From the details furnished (July 2004) by the Finance (A&F) Department, it was noticed that drawal of Rs.12.61 crore on AC Bills by different departments was approved by the Finance (A&F) Department between April 2003 and March 2004 with instruction to regularise the amount within one month of drawal. But the Finance Department had not yet received any

[a] Provisional figure as the final expenditure figure had not been furnished by the DAT.

intimation from the concerned departments regarding utilisation of the said funds. Absence of this information with the Finance Department, even after four months to over one year of according approval for drawal of funds, indicated a serious deficiency in control over expenditure by Finance.

(iii) Inaccuracy in preparation of revised estimates

According to the Assam Budget Manual (adopted by Government of Meghalaya), the actuals of previous years and the revised estimates ordinarily form the best guide in framing the budget estimate. The revised estimate should not merely be a repetition of the budget figures of the year, but a genuine re-estimation of requirements.

Significant cases of variations between the revised estimate and the actuals during 2002-03 under both receipt and expenditure heads of accounts are given in Appendix XLI. Wide variations (24 to 56 *per cent* under receipts and 26 to 99 *per cent* under expenditure) indicated absence of proper care in estimating the revised provisions by the concerned controlling officers as envisaged in the Budget Manual and failure of the Finance (Budget) Department in exercising adequate check over the rough preliminary revised estimates.

(iv) Unnecessary demand for supplementary grant

According to the Budget Manual, no supplementary demand will be accepted by the Finance Department unless it is accompanied by a specific statement to the effect that the existing provision under the appropriate Grant has been examined and it has been found that there will be no saving available therefrom to meet the present need.

It was noticed that savings under various Grants for the year 2003-04 were surrendered by the concerned controlling officers during the year despite obtaining supplementary provisions. Details of some of the such cases are given in Appendix XLII. Evidently, the Finance (Budget) Department accepted the supplementary demands without the prescribed statement or the statement was defective and thus, the department failed to exercise its control over the supplementary demands and point out the defects.

7.1.10 The matter was reported to Government in September 2004 and followed up with a reminder in November 2004; reply had not been received (November 2004).

7.1.11 Recommendations

On the basis of the shortcomings and deficiencies pointed out in the foregoing paragraphs, the following recommendations are made:

- Internal control system in the Finance Department needs to be streamlined for realistic presentation of budgetary documents.

- Efforts need to be made to cover more units by internal audit so as to ensure transparency in fiscal management.

- Independence of the internal audit system needs to be ensured.

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