EFFECTIVENESS OF INTERNAL CONTROL SYSTEMS ON CASH RECEIPTS AND DISBURSEMENTS: THE CASE OF KEKO MWANGA MEDICAL STORES DEPARTMENT DAR ES SALAAM

By
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A research report submitted in partial fulfilment of the requirements for the award of the degree of Master of Science in Accounting and Finance (MSc-A&F) of Mzumbe University, Dar es Salaam Campus College

2014
CERTIFICATION

We the undersigned, certify that we have read the dissertation and found it to be in a form acceptable for the final Submission for the award of a Master Degree in Accounting and Finance, a dissertation entitled **Effectiveness of Internal Control Systems on Cash Receipts and Disbursements: The Case of Keko Mwanga Medical Stores Department Dar Es Salaam** in partial fulfillment of the degree of science in accounting and finance of the Mzumbe University.

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Internal Examiner

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This work is a product of countless individuals whose thoughts, ideas, perspectives and works have given me the exposure to the knowledge I have placed in this study. While it is not possible to mention all of them by name I would like to thank the following few individuals.

I wish to particularly mention my supervisor, Mr. Freddy Feruzi at Mzumbe University for providing support and guidance for the preparation and completion of this work. I also thank all individuals and members of staff of MSD Keko Mwanga, who spared their precious time to respond to my questionnaire and participated in the interview. There are also many more important persons not listed here to whom I owe them a lot of thanks. To these all I say “Ahsante Sana”!

Nevertheless the opinions expressed in the report and the implications thereof are my sole responsibility, and by no way do they bear implication to the people mentioned in this acknowledgement.
DEDICATION

To the esteemed love of my beloved mother, Ntuli Susan Mwakyambiki, who took me to school and taught me the value of education, and also to my brother, Heri and my uncles, for their love and full support in moral and financial terms during my entire study time at Mzumbe University.
<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tr>
<td>AICPA</td>
<td>American Institute of Certified Public Accountant</td>
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<td>CG</td>
<td>Corporate Governance</td>
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<td>GAAP</td>
<td>General Accepted Accounting Principles</td>
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<td>ICS</td>
<td>Internal Control Systems</td>
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<td>MSD</td>
<td>Medical Stores Department</td>
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<td>SIMEX</td>
<td>Singapore International Monetary Exchange</td>
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<td>SOX</td>
<td>Sarbanes Oxley Act</td>
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<td>USD</td>
<td>United States Dollars</td>
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<tr>
<td>PPRA</td>
<td>Public Procurement Regulatory Authority</td>
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<td>TFDA</td>
<td>Tanzania Food &amp; Drugs Authority</td>
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<tr>
<td>TBS</td>
<td>Tanzania Bureau of Standards</td>
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<tr>
<td>PHLB</td>
<td>Private Health Laboratory Board</td>
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<td>TGCLA</td>
<td>Tanzania Government Chemist Laboratory Agency</td>
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<tr>
<td>TAEC</td>
<td>Tanzania Atomic Energy Commission</td>
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<td>TFNC</td>
<td>Tanzania Food and Nutrition Centre</td>
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<tr>
<td>NEMC</td>
<td>National Environmental Management Council</td>
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<td>MTSP</td>
<td>Medium Term Strategic Plan</td>
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ABSTRACT

This study on the effectiveness of internal controls on the flow of funds was conducted at MSD KEKO MWANGA Dar es Salaam Branch. The study was a survey that used questionnaires, interview guide personal observation and documentary reviews as its means of data collection.

The study found out that the MSD is only currently, after the concern of the CAG, is constructing its internal controls to be able to assess risks and detect financial frauds that have at times led it to scandalous reporting by the media.

Because of absence of effective controls, regardless of the presence of an internal audit department, there have been reports of thefts at the organization, failure to procure essential drugs even though there had been sufficient money to procure; and even procurement without compliance with PPRA law and regulations.

MSD are advised to train their staff on forecasting, risk assessment and financial fraud detection skills in order to protect the organization’s resources and save unnecessary losses and scandals.
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CHAPTER ONE

INTRODUCTION AND BACKGROUND

1.1 Introduction
This chapter explains the process which attributes to the initiation of this study. It discusses the background of the study, problem definition, research questions, research objectives and relevance of the study.

1.2 Background to the study
In 1968 the Government of Tanzania experienced few challenges in managing and controlling public funds in banks and public institutions because their revenues matched expenditures. By that time, even financial reports were prepared and submitted to appropriate authorities timely because there was less volume of work. At that time, cases of misappropriation of public funds through over-expenditure, frauds and embezzlement were quite rare.

In 1972 came economic reforms and big gaps between revenue and expenditure began to be noticed and reported. Cases like thefts and embezzlements by dishonest employees began to be heard of. Want for accountability and transparency on the part of officers, also began to arise, leading to inaccurate and unrealistic financial reporting. With regard to internal financial controls, this meant that this was the beginning of weak and ineffective internal control over flow of funds.

Following these real risks in funds management, there arose need for establishment of effective and efficient internal financial controls that would enable the government, banks and other financial institutions to protect their resources and funds against waste, frauds and thefts; controls that would make officers comply with corporate policies intended to safeguard assets and achieve corporate goals and objectives.

1.3 Statement of the problem
Before proper financial management systems were introduced in government institutions like the Medical Stores Department (MSD), these institutions
experienced significant problems related to the management and control of funds. According to Ngumbulu P. (1996), the financial management scenario of the time encountered such snags like very weak budgeting capacity, inadequate control of expenditure, poor security of funds, faltering accountability, elements of misappropriation and even thefts. All these culminated into corporate failure to honour debts, poor processing of financial transactions, poor asset management, and frequent purposeful, untimely and inaccurate financial reporting. Outcomes of a weak financial control system would definitely include uncertainty over adequacy of receipts and payments, return of dishonoured cheques, loss of customer and client confidence, unsatisfactory organizational performance, failure of demand management and donor and creditor complaints over untimely, incorrect and inaccurate financial reports.

In the light of the outcomes of weak internal controls, this study aimed to determine how competent internal control systems protect an organization from the risks of unbalanced cash flows. It aimed to ascertain whether truly in reality, strong or effective internal controls strengthen organizational funds flow management, and thus protect organizations from experiencing waste, embezzlement, thefts and frauds over their assets, and particularly their funds.

1.4 Research Objectives

1.4.1 General / Main Objective
The main objective of this study was to evaluate the effectiveness of internal control systems operational at the Keko Mwanga Medical Stores Department (MSD) and the part it plays in the organization’s funds flow management

1.4.2 Specific Objective
i. To show that internal control systems play a significant part in the orderly and efficient running of an organization; and

ii. To prove that internal control systems have a fundamental role in stabilizing an organization’s funds flow
1.5 Research Questions

This research was guided by the following questions:

1. To what extent do internal control systems affect the orderly and efficient running of an organization?
2. To what extent does the MSD use its internal control systems to manage its funds flow, i.e. cash receipts and disbursements?
3. What challenges do organizations face while implementing internal controls, specifically accounting controls?

1.6 Significance of the study

This study is important because:

1. It will help public institutions to assess their internal control measures and make amends where necessary
2. It forms a basis for further research on methods of handling 21st century challenges that arise in the process of implementing their internal controls.

1.7 Scope of the study

The motive of the study was to evaluate the effective use of internal controls on funds flow in public institutions, using the MSD as a case study. For this reason, therefore, this study was confined to the evaluation of internal controls of the Keko Mwanga branch of the MSD, in Dar es Salaam. Dar es Salaam was convenient location because it is home for many public organizations, but more importantly, it is the researcher’s home. Proximity of research location to home helped the researcher to keep research costs to their minimum.

1.8 Limitation of the study

The researcher acknowledges that a comparative study on the effectiveness of any measure would be better than a case study of a single entity. However, financial cost and time deadlines limited the study to a single facility. Moreover, the dangers of having a single facility for a study risked one other limitation, that of empirical literature.
CHAPTER TWO
LITERATURE REVIEW

2.1 Introduction
This chapter presents the review of concepts, theories and empirical studies related to proper control of funds flow in an organisation.

2.2 Theoretical Literature Review
In every business organisation, management is charged with the primary responsibility of safeguarding the assets of the entity so as to prevent occurrence of errors and frauds, or to facilitate their early detection. To discharge this responsibility, it requires the management to lay down regulations, policies and procedures that will provide operational efficiency, secure reliability of records and safeguard the assets. Reliable records and accounts show a true and fair view of financial statements, which represent a good summary of the results of operations. The policies, procedures and regulations that management set up with the aim of attaining efficiency and security are referred to as internal controls.

According to the Auditing Practices Committee (APC 1980) (of Nigeria), internal control systems can be defined as the whole system of control, financial or otherwise, established by management in order to carry on the business of the enterprise in an orderly and efficient manner, ensure adherence to management’s policies, safeguard the assets and secure as far as possible, the completeness and accuracy of the records.

An Internal control system is a means by which organization’s resources are directed, monitored and measured. It plays an important role in preventing and detecting fraud and protecting the organization’s resources. At the organizational level, internal control system relates to the reliability of financial reporting, timely feedback on the achievements of goals, compliance with laws and regulations and the prevention of detection of fraud. At the specific transaction level, internal control refers to the actions taken to achieve a specific objective such as the procedure for payment of money for services rendered.
According to the Treadway Commission of the US (1994), internal control is broadly defined as a process, effected by an entity’s board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- Effectiveness and efficiency of operations.
- Reliability of financial reporting.
- Compliance with applicable laws and regulations.

According to the Commission, (op cit.), the first category of internal controls addresses an entity’s basic business objectives, including performance and profitability goals and safeguarding of resources. The second relates to the preparation of reliable published financial statements, including interim and condensed financial statements and selected financial data derived from such statements, such as earnings releases, reported publicly. The third deals with complying with those laws and regulations to which the entity is subject. These distinct but overlapping categories address different needs and allow a directed focus to meet the separate needs.

Internal control systems operate at different levels of effectiveness. Internal control can be judged effective in each of the three categories, respectively, if the board of directors and management have reasonable assurance that:

- They understand the extent to which the entity’s operations objectives are being achieved.
- Published financial statements are being prepared reliably.
- Applicable laws and regulations are being complied with.

A discussion on the internal control process undertaken by the same Commission (Treadway, ibid.), considers that while internal control is a process, its effectiveness is a state or condition of the process at one or more points in time. The Commission sees that internal control consists of five interrelated components, and these are derived from the way management runs a business, and are integrated with the
management process. The components apply to all entities but small and mid-size companies may implement them differently than large ones. A small sized company’s control may be less formal and less structured, yet it can still have effective internal control. The components are:

- **Control Environment** — the control environment sets the tone of an organization, influencing the control consciousness of its people. It is the foundation for all other components of internal control, providing discipline and structure. Control environment factors include the integrity, ethical values and competence of the entity’s people; management’s philosophy and operating style; the way management assigns authority and responsibility, and organizes and develops its people; and the attention and direction provided by the board of directors.

- **Risk Assessment** — Every entity faces a variety of risks from external and internal sources that must be assessed. A precondition to risk assessment is establishment of objectives, linked at different levels and internally consistent. Risk assessment is the identification and analysis of relevant risks to achievement of the objectives, forming a basis for determining how the risks should be managed. Because economic, industry, regulatory and operating conditions will continue to change, mechanisms are needed to identify and deal with the special risks associated with change.

- **Control Activities** — Control activities are the policies and procedures that help ensure management directives are carried out. They help ensure that necessary actions are taken to address risks to achievement of the entity’s objectives. Control activities occur throughout the organization, at all levels and in all functions. They include a range of activities as diverse as approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets and segregation of duties.

- **Information and Communication** — Pertinent information must be identified, captured and communicated in a form and timeframe that enable people to carry out
their responsibilities. Information systems produce reports, containing operational, financial and compliance-related information, that make it possible to run and control the business. They deal not only with internally generated data, but also information about 5 external events, activities and conditions necessary to informed business decision-making and external reporting. Effective communication also must occur in a broader sense, flowing down, across and up the organization.

- All personnel must receive a clear message from top management that control responsibilities must be taken seriously. They must understand their own role in the internal control system, as well as how individual activities relate to the work of others. They must have a means of communicating significant information upstream. There also needs to be effective communication with external parties, such as customers, suppliers, regulators and shareholders.

- Monitoring — Internal control systems need to be monitored—a process that assesses the quality of the system’s performance over time. This is accomplished through ongoing monitoring activities, separate evaluations or a combination of the two. Ongoing monitoring occurs in the course of operations. It includes regular management and supervisory activities, and other actions personnel take in performing their duties. The scope and frequency of separate evaluations will depend primarily on an assessment of risks and the effectiveness of ongoing monitoring procedures. Internal control deficiencies should be reported upstream, with serious matters reported to top management and the board.

2.3 Theoretical Literature Review

Various Theorists have given their view concerning this research topic. In any business organization the management is charged with the primary responsibility of safeguarding the assets of the entity so as to prevent errors and frauds or facilitate their early detection.
To discharge this responsibility it needs the management to lay down the regulations, policies and procedures so as to give efficiency in operation and in order to secure reliability of records and safeguard the assets. From the reliable records maintained the management will be able to render annual reports to include annual accounts to show true and fair view of financial statements and results of operation.

2.4 What Internal Control Can Do
Internal control can help an entity achieve its performance and profitability targets, and prevent loss of resources. It can help ensure reliable financial reporting. And it can help ensure that the enterprise complies with laws and regulations, avoiding damage to its reputation and other consequences. In sum, it can help an entity get to where it wants to go, and avoid pitfalls and surprises along the way.

2.5 What Internal Controls Cannot Do
Unfortunately, some people have greater, and unrealistic, expectations. They look for absolutes, believing that:
- Internal control can ensure an entity’s success — that is, it will ensure achievement of basic business objectives or will, at the least, ensure survival. Even effective internal control can only help an entity achieve these objectives. It can provide management information about the entity’s progress, or lack of it, toward their achievement. But internal control cannot change an inherently poor manager into a good one. And, shifts in government policy or programs, competitors’ actions or economic conditions can be beyond management’s control. Internal control cannot ensure success, or even survival.

- Internal control can ensure the reliability of financial reporting and compliance with laws and regulations. This belief is also unwarranted. An internal control system, no matter how well conceived and operated, can provide only reasonable — not absolute — assurance to management and the board regarding achievement of an entity’s objectives. The likelihood of achievement is affected by limitations inherent in all internal control systems. These include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because
of simple error or mistake. Additionally, controls can be circumvented by the collusion of two or more people, and management has the ability to override the system. Another limiting factor is that the design of an internal control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Thus, while internal control can help an entity achieve its objectives, it is not a panacea.

2.6 Roles and Responsibilities

Everyone in an organization has responsibility for internal control.

- **Management** — The chief executive officer is ultimately responsible and should assume “ownership” of the system. More than any other individual, the chief executive sets the “tone at the top” that affects integrity and ethics and other factors of a positive control environment. In a large company, the chief executive fulfills this duty by providing leadership and direction to senior managers and reviewing the way they’re controlling the business. Senior managers, in turn, assign responsibility for establishment of more specific internal control policies and procedures to personnel responsible for the unit’s functions.

In a smaller entity, the influence of the chief executive, often an owner-manager, is usually more direct. In any event, in a cascading responsibility, a manager is effectively a chief executive of his or her sphere of responsibility. Of particular significance are financial officers and their staffs, whose control activities cut across, as well as up and down, the operating and other units of an enterprise.

- **Board of Directors** — Management is accountable to the board of directors, which provides governance, guidance and oversight. Effective board members are objective, capable and inquisitive. They also have a knowledge of the entity’s activities and environment, and commit the time necessary to fulfill their board responsibilities. Management may be in a position to override controls and ignore or stifle communications from subordinates, enabling a dishonest management which intentionally misrepresents results to cover its tracks. A strong, active board, particularly when coupled with effective upward communications channels and
capable financial, legal and internal audit functions, is often best able to identify and correct such a problem.

- **Internal Auditors** — Internal auditors play an important role in evaluating the effectiveness of control systems, and contribute to ongoing effectiveness. Because of organizational position and authority in an entity, an internal audit function often plays a significant monitoring role.

- **Other Personnel** — Internal control is, to some degree, the responsibility of everyone in an organization and therefore should be an explicit or implicit part of everyone’s job description. Virtually all employees produce information used in the internal control system or take other actions needed to effect control. Also, all personnel should be responsible for communicating upward problems in operations, noncompliance with the code of conduct, or other policy violations or illegal actions.

A number of external parties often contribute to achievement of an entity’s objectives. External auditors, bringing an independent and objective view, contribute directly through the financial statement audit and indirectly by providing information useful to management and the board in carrying out their responsibilities. Others providing information to the entity useful in effecting internal control are legislators and regulators, customers and others transacting business with the enterprise, financial analysts, bond raters and the news media. External parties, however, are not responsible for, nor are they a part of, the entity’s internal control system.

### 2.7 What to Do

The study made by the Treadway Commission (ibid.) states that making internal control work is the business of many individuals and groups, within and outside the organization. Those involved in making internal controls work include:

- **Senior Management** — All senior executives of organizations have a duty and are basically supposed to be “in control” of their organizations. However, there can be areas of their companies — a division, a department or a control component that cuts across activities — where controls are in early stages of development or otherwise
need to be strengthened. In such cases, the chief executive should initiate a self-assessment of the control system. Using this framework, the CEO, together with key operating and financial executives, can focus attention where needed. Under one approach, the chief executive could proceed by bringing together business unit heads and key functional staff to discuss an initial assessment of a control. Directives would be provided for those individuals to discuss this report’s concepts with their lead personnel, provide oversight of the initial assessment process in their areas of responsibility and report back findings.

Another approach might involve an initial review of corporate and business unit policies and internal audit programs. Whatever its form, an initial self-assessment should determine whether there is a need for, and how to proceed with, a broader, more in-depth evaluation. It should also ensure that ongoing monitoring processes are in place. Time spent in evaluating internal control represents an investment, but one with a high return.

- **Board Members** — Members of the board of directors should discuss with senior management the state of the entity's internal control system and provide oversight as needed. They should seek input from the internal and external auditors.

- **Other Personnel** — Managers and other personnel should consider how their control responsibilities are being conducted in light of this framework, and discuss with more senior personnel ideas for strengthening control. Internal auditors should consider the breadth of their focus on the internal control system, and may wish to compare their evaluation materials to the evaluation tools.

- **Legislators and Regulators** — Government officials who write or enforce laws recognize that there can be misconceptions and different expectations about virtually any issue. Expectations for internal control vary widely in two respects. First, they differ regarding what control systems can accomplish. As noted, some observers believe internal control systems will, or should, prevent economic loss, or at least prevent companies from going out of business. Second, even when there is agreement about what internal control systems can and can’t do, and about the
validity of the “reasonable assurance” concept, there can be disparate views of what that concept means and how it will be applied. Corporate executives have expressed concern regarding how regulators might construe public reports asserting “reasonable assurance” in hindsight after an alleged control failure has occurred. Before legislation or regulation dealing with management reporting on internal control is acted upon, there should be agreement on a common internal control framework, including limitations of internal control. This framework should be helpful in reaching such agreement.

- **Professional Organizations** — Rule-making and other professional organizations providing guidance on financial management, auditing and related topics should consider their standards and guidance in light of this framework. To the extent diversity in concept and terminology is eliminated, all parties will benefit.

- **Educators** — This framework should be the subject of academic research and analysis, to see where future enhancements can be made. With the presumption that this report becomes accepted as a common ground for understanding, its concepts and terms should find their way into university curricula. We believe this report offers a number of benefits. With this foundation for mutual understanding, all parties will be able to speak a common language and communicate more effectively.

Business executives will be positioned to assess control systems against a standard, and strengthen the systems and move their enterprises toward established goals. Future research can be leveraged off an established base. Legislators and regulators will be able to gain an increased understanding of internal control, its benefits and limitations. With all parties utilizing a common internal control framework, these benefits will be realized.

General Internal Control overview comprised of the whole system of control financial or otherwise established by the management in order to carry out business entity in an orderly and efficient manner, to ensure adherence and management
policies, safeguarding the assets and secure as far as possible for completeness and accuracy of the records, (Woof E, “Auditing Today” 8th edition, 1987)

As discussed in the journal of (AICPA) American Institute of Certified Public Accountant, pg 48. Internal Control comprised the plans of an organization and all coordinate methods and means adopted within the business to safeguard the assets, check the accuracy and the reliability of its accounting data, promote operation efficiency and encouraging adherence to prescribes managerial policies.

2.8 Competence Of Staff As The Means Of Strengthening Internal Controls

For any organization or company to have an impact of internal control system, it is vital important to have the staff who are competent enough in their field of work. Everybody of persons, whether corporate or incorporate, engage in Tanzania in any trade business a profession which has,

- Assets in Tanzania, the value of which exceeds one hundred million shillings or
- An annual gross income in Tanzania exceeding fifty million shillings shall employ at least one certified public accountant in public practice or one certified public accountant (i.e. CPA Holder)

Without prejudice to the prevision of the above explanation the organizations or company shall be obliged to keep proper books of accounts (National Board of Accountant and Auditors).

All the above recommendations is for the aim of ensuring that, if the accounting staff are qualified enough, the accounting work will be performed to the best practice. It is obviously that no system can be better than the people who operate it. The accountant who lacks adequate training and ability would be unlikely to develop a good set of the accounting records or produce useful and reliable accounting statement.

Prospective employees should be careful screened to assure that only qualified people are employed and talents should be utilized to the maximum by advancing employees to more responsible positions as quick as their performance merits such
advancement. Training programs are an effective means of accelerating employee’s development and of increasing the number of persons who are available to assume greater responsibility (Howard F. Stettler 1974:63)

2.9 Definition of Terms and Concept Used in The Research

2.9.1 System Of Internal Control Over Flow Of Funds:
This is the system of controls established by the management in order to safeguard its inflow and outflow of funds and secure as far as possible the accuracy and reliability of funds flow transactions records.

The details of the procedures of internal control of the flow of funds vary from one entity to another depending upon its size, nature of business and quality, however the principles of internal control of the flow of funds valid to all types of organization (Walgenback 5edtion).

According to Mrema A (1996) an adequate system of internal control of the flow of funds has the following components;

- All receipt and disbursements must be recorded in cash receipt and disbursement journal.
- Bank account to be maintained and reconciled periodically.
- In addition, Walgenback (1980) recommends that,
  - Cash should be handled separately from the recording of cash transaction.
  - The work and responsibilities of cash handling and recording are divided in such a way that error are readily disclosed and the possibility of irregularities is reduced.
  - All cash receipt is deposited in bank each day.
  - All major disbursement are made by cheque and an imprest fund is used for petty cash disbursement.

The nature of an organization in the same way determines which controls are to be used. The non-profit making organization differ from profit making organization
mainly in the extent to which beneficiaries or customers work as internal control. In this context customer of profit oriented organization are good internal controls, as they always demand receipts or services they acquire. On the other hand, beneficiaries of non-profit making organization rarely demand the correctness of receipts or disbursements procedures as long as they get their share. Due to this reason there is a need to have special additions of controls for non-profit organizations. (Emerson O.H 1992).

2.9.2 Internal audit as the means of strengthening internal control

One of the effective ways in strengthening other controls principles is to establish an internal audit department.

In all large organization an important element of internal control is the auditing staff. Internal auditors are professional level employees with responsibility of investigating throughout the company, the efficient of operation in every department or other organization units. The are continuously studying both administrative and accounting controls and reporting to the top management on compliance with company standards and problems which require strengthening of internal control.

2.9.3 Objectives of internal audit department

- Ensure that the company’s assets are safeguarded against misuse or theft by dishonest employees.
- To ascertain that the company policies, plans and procedures are compiled with.
- To ascertain the compliance and reliability of accounting data.
- To facilitate the achievement of company policies such as budget, targets etc.
- Enhances the presence of strong internal control system which enables the company to run its business activities in an orderly manner.
2.9.4 Accounting system
Is the method procedure and advice used by an entity to keep track of its financial activities and summarize these activities in a manner useful to decision makers (Lorson D.K and Pyle W.W 1988).

2.9.5 Cheque
Is an instrument or document used to meet obligation or receiving money from bank.

2.9.6 Cash receipt
It covers all resources immediately available to management for business purposes or is accepted by bankers for deposit at face value. Cash will include all deposit with bank that is available upon demand and money items on hand that can be used as a medium of exchange. (P.H.Mahushi 1985:85).

- Mechanical devices such as safes, strong rooms, cash register should be fully utilized.
- Collection and depositing should be centralized.
- All transactions of cash between banks specifically approved and recorded in the ledger.
- Monthly bank reconciliation is prepared by a person not taking part in handling cash or signing cheques.
- All invoicing cheque and currency are immediately recorded and deposited on a daily basis.
- Post dated cheques and or returned cheque are recorded and held by a responsible official till they are dealt with accordingly.
- Surprise checks are regularly made on cash collection reports and other records to verify that all collection is properly accounted for.
- Canceled receipts are retained for audit inspection and verification.
- Open cheques to be respectively closed and made payable to the Company’s account only.
- All remittance is listed on numbered remittance sheet.
It is point to note that the main objective of internal control is to safeguard the assets of the company, to run the business smoothly and to have accuracy and reliability of all the records. For this, the control might spread over to books of account, production or even quality where the internal control is good, chances of fraud in accounts or in documents would be reduced to the minimum. On the other hand if such system is adequate, the chances of errors and fraud may be enhanced (V.H Kishwadalla, and M.V Sheet 1992).

2.9.7 Effectiveness
Means the attainment of predetermined goals (A.S.Horn 1984).

2.9.8 Funds flow
Means movement of money or fund or cash in and out of the organization.

2.9.9 Financial statement
Are any statements prepared in respect of each accounting period for purpose of providing information on the operating results of an enterprise during that accounting periods (W.B.Meighs and R.F Meighs, 1990)

2.9.10 Back ground for medical stores department as a case study
Medical Stores Department was established by an Act of Parliament No.13 of 1993. Its core functions are to procure, store and distribute medicines and medical supplies to approved public health facilities throughout Tanzania. The Medical Stores Department has a near monopoly on the national medical supply chain for Tanzania’s public facilities, which account for 60% of all health facilities nationwide. The medicines and supplies used in those public facilities are purchased with government funding that is deposited directly into MSD accounts, which then procures drugs through the Public Procurement Act of 2004.

This act, though introducing an additional layer of regulation and sometimes long lead times, enables MSD to procure quality drugs at favorable prices compared to market prices. In addition, MSD provides supplies to private facilities and large
international donor programs. There are approximately 5,000 health centers and facilities in Tanzania divided into nine MSD zones which are DSM Zone, Dodoma Zone, Iringa Zone, Mbeya Zone, Moshi Zone, Mtwara Zone, Mwanza Zone, Tabora Zone and Tanga Zone and approximately 131 districts. The purchasing power and national reach of MSD make it a desired partner for non-government entities.

Funding given to MSD for the purchase of medicines from the government and donors has increased significantly over the past ten years, both for essential medicines used in primary health care and also vertical medicines to treat specific diseases, such as HIV/AIDS. Many projects support MSD and the medical supply chain system, including a $14 million warehouse project by The Global Fund and an additional $9.5 million from USAID to increase the capacity and quality of MSD storage areas.

Unfortunately, data on the actual procurement and delivery of medicines and medical supplies down the supply chain in Tanzania are unreliable and difficult to collect. In addition, Tanzania must comply with multiple reporting requirements by donors. The result has been frequent public disputes in Tanzania and among members of the international donor community about whether donated funds and medical supplies reach the intended communities. In June 2010, the Global Fund released a report saying that MSD lacked transparency and accountability. In addition, in July 2011, the MSD was publicly attacked by the local newspapers and the general assembly for corruption.

Although private facilities and vertical programs that focus on single diseases, such as TB and HIV/AIDS can often purchase supplies from other sources, shortages at MSD cause nationwide stock outs in government primary health facilities and in the public medical supply chain. The average national fill rate for orders from primary health facilities is only 60-65%, meaning that 35-40% of orders are not filled, leading to stock outs. Reasons for the stock outs are numerous and involve organizations and actors outside of MSD, including the following:

- Inadequate budget allocations to health facilities
Delays in distribution of allocated funds
- Delay in delivery to facilities
- Inaccurate forecasting at the facility and national level
- Theft of medications at all levels
- Stock-outs at the national warehouse run by MSD
- Malfunctioning back order system for unfilled items

Twenty to thirty percent stock out rates at government facilities mean that patients either go without needed medical supplies, or must purchase them at a much higher cost from private pharmacies. This creates barriers to delivery of health services. For those supply chain issues within MSD's control (e.g. not problems with government budgeting or allocation of funds), lack of management capacity is repeatedly cited as a root cause. Although several changes have been made to address these problems, stock outs at health facilities and at MSD continue to pose a serious obstacle to improving health services in Tanzania.

Table 2.1: Board of Trustees

<table>
<thead>
<tr>
<th>SN</th>
<th>NAME</th>
<th>STATUS</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Prof. Idris Mtulia</td>
<td>Chairperson</td>
</tr>
<tr>
<td>2</td>
<td>Mr. Gabriel Paschal Malata</td>
<td>Member</td>
</tr>
<tr>
<td>3</td>
<td>Mr. Celestine M. Mgoba</td>
<td>Member</td>
</tr>
<tr>
<td>4</td>
<td>Hon. Dr. Faustine Ndugulile</td>
<td>Member</td>
</tr>
<tr>
<td>5</td>
<td>Dr. Margareth Mhando</td>
<td>Member</td>
</tr>
<tr>
<td>6</td>
<td>Hon. Ms. Martha Mlata</td>
<td>Member</td>
</tr>
<tr>
<td>7</td>
<td>Hon. George M. Lubeleje</td>
<td>Member</td>
</tr>
<tr>
<td>8</td>
<td>Dr. Ahmed Hingora</td>
<td>Member</td>
</tr>
<tr>
<td>9</td>
<td>Hon. Albert O. Ntabaliba</td>
<td>Member</td>
</tr>
<tr>
<td>10</td>
<td>Mrs. Monica Mwamunyange</td>
<td>Member</td>
</tr>
</tbody>
</table>

Source: Researcher field Data, 2014.
2.9.11 Director General’s Office
The Directorate General is responsible for providing day to day leadership for the organization as well as managing strategic relations with stakeholders. Under the Directorate General there are four oversight units and one Public Relation Office.

2.9.12 Internal audit
The Internal audit is an independent, objective assurance and consulting activity designed to add value and improve MSD operations. It evaluates and improve the effectiveness of risk management, controls and governance processes. The head of the Internal Audit reports administratively to the Director General and functionally to the Audit and Risk Management Committee of the Board. The unit monitors the implementation of its recommendations and Board Directive on the same.
In order to enhance business operations and ensure that MSD achieves its set goals and objectives, Management, has set in place a risk management processes at all MSD business units.

2.9.13 Legal matters
The legal unit is the secretariat to the MSD and Board of Trustee and is responsible for all contracts, litigation and custody of all MSD legal and statutory documents. The unit also has the responsibility of participating in the drafting of bills, legislations and other legal documents which have impact on the department, ensure safe-keeping of board of trustees records and other legal documents, liaise with the ministry and attorney general’s chambers in legal matters and ensure department’s compliance with legal and regulatory bodies.

2.9.14 Quality assurance
MSD believes in continuous improvement and quality of medicines and medical supplies helps to ensure that the end use gets the best for their money. The quality assurance unit provides comfort that MSD goods, Works, Service and systems are of high quality and in line with the accepted international standards. The unit works in close cooperation with the Tanzania Food and Drugs Authority, Tanzania Bureau of
Standards, Tanzania Private Health Laboratories Board to ensure the quality of medicines and medical supplies are upheld.

2.9.15 Monitoring and evaluation
The unit assists the Department with better means for learning from past experience, improving service delivery, planning and allocating resources, and demonstrating results as part of accountability to stakeholders. To ensure the department's accountability the unit discharge the following functions; set performance standards and indicators for the directorates and department, administer institutional self assessment exercises, ensure coordination of guidelines, annual plans and medium-term strategic plans, coordinate periodic performance reports and compilation of monitoring and evaluation reports, ensure availability of inputs for plans, programs and budgetary activities in the department, undertake researches on the impact of projects and programs undertaken by MSD, ensure that service delivery surveys are conducted and coordinate preparation of mid-year and annual performance reviews.

2.9.16 Public relations office
Public Relations Office is under the Director Generals' office. The Head of this office reports to the Director General. Public Relations office represents Medical Stores Department image that the public and media see.

Public Relations office is the head of Communication (Internal and External).
PR Office is responsible for:
- Planning, developing and implementing PR strategies
- Liaising with key spokespeople for several MSD issues raised
- Researching, writing and distributing press releases to the targeted media and MSD reports.
- Collating and analyzing media coverage on MSD and the Ministry of Health
- Writing and editing in-house magazines, articles, reports and all other MSD publications
- Organizing all MSD events, press conferences, exhibitions, visits, open days and press tour
- Maintaining and updating MSD website.
• Respond to requests for information from the media or designate another appropriate spokesperson or information source.
• Managing crisis situation
• Establish and maintain good relationship with MSD stakeholders
• Purchase advertising spaces and air time as required for public announcements or awareness programs, campaigns, and special programs.
• Building relationships with the media
• Advice management on good external and internal communications
• Preparing MSD promotional materials
• Maintaining internal communication
• Implementing Corporate Social Responsibility Support

2.9.17 Organization structure
The Medical Stores Department (MSD), serving the nation's healthcare needs was created by an act of Parliament in 1993 with the express objective of furnishing to the nation good quality drugs and medical equipment at accessible prices, made available through approved government and non-government agencies throughout Tanzania.

MSD is an autonomous department of the Ministry Of Health and operates on a commercial basis, being responsible for its own self sustaining financially. MSD management reports to a board of trustees (BoT) composed of eminent public servants, medical professionals and business persons, who provide guidance and oversight to MSD operations. MSD’s commercial operations provide funds sufficient for the maintenance and growth of the department without drawing upon outside resources. Thus, management works on the strictest of principles regarding cost analysis, cost effective operations and transparency. Integrity is of the highest importance and MSD relies on Internal auditing as well as external audit procedure to validate all financial operations.
Key among the objectives of management was to restructure MSD with a view for broader management focus on key core functions such as Customer Sales and Service, Information Technology, Logistics and Distribution. With strong support from the Director of Finance, more emphasis was placed on Administration and Human Resources.

Restructuring also provided the means for greater participation by personnel in programmes designed to build capacity, train and reinforce critical task management, creating a sense of urgency and also ownership that demands the full participation of everyone. MSD believes strongly that promotion from within is an essential task coupled with succession planning to assure management for the future. Human Resources section under Directorate of Corporate Affairs is responsible to manage the challenge of meeting the needs of over 300 employees. Medical Stores Department is organized in various directorates that execute different roles in the Department.

- Director General’s Office
- Directorate of Human Resources and Administration
- Directorate of Finance
- Directorate of Information and Communication Technology
- Directorate of Logistics
- Directorate of Procurement
- Directorate of Zonal Operations and Customer Service
Figure 2.1: Organization Structure for MSD

Source: MSD website: www.msd.or.tz

2.9.18 Directorate of Finance

The nature of MSD business is essentially the management of a drug supply chain that entails the process of procurement, storage and distribution functions. The three functions form part of the drug management cycle. However, for the three functions to hold together in a sustainable manner, management support systems are required. That is, there should be a functional organizational structure, adequate and sustainable financing arrangements, reliable management information systems and motivate staff. The functions of the Directorate of Finance and Administration is therefore to ensure that MSD has adequate management support systems and
resources, and that it manages those resources in a sustainable manner. The following are the functions of this directorate;

- To ensure that the accounting systems, procedures and records are maintained in a form that conforms to the best commercial accounting standards and generally accepted practices, and safeguards resources against wasteful activities.
- To ensure that sound management information systems and business processes are developed, maintained and continuously improved to support the process of management. For instance, in analysis, planning, decision making and control.
- To ensure that sound financial management systems and procedures based on sound commercial principles and practices are installed to ensure judicious use of resources (physical assets, inventories, investments, cash and people) and best return on investments.
- To ensure that there is a functional organizational structure and a supportive organizational culture for attainment of organizational goals and objectives.
- To ensure that the right number and caliber of staff are recruited, developed, maintained and motivated to attain excellence in performance.

2.10 Empirical Studies Related to Internal Control over Flow of Funds

In 1972 the American Institute of Accountants (now AICPA) clarify that controls especially Accounting Controls provide reasonable assurance that transactions are executed as authorized, transactions recorded to permit GAAP statements and maintain accountability for assets, access to assets only as authorized, regularly compare recorded assets with actual assets.

Foreign Corrupt Practices Act: Took the language of the 1972 AICPA pronouncement and made it law.

Since 1977, all publicly owned corporations legally required to: Keep books which accurately and fairly reflect transactions and dispositions of assets and, devise and maintain a system of Internal accounting controls sufficient to provide reasonable assurances that transactions are authorized by management, transactions are recorded so GAAP statements can be prepared and maintain accountability for
assets, access to assets is authorized by management, and periodic inventory is required to compare recorded assets with existing assets.

1Administrative control includes but is not limited to, the plan of organization and the procedures and records that are concerned with the decision processes leading to management's authorization of transactions. Such authorization is a management function directly associated with the responsibility for achieving the objectives of the organization and is the starting point for establishing accounting control of transactions.

Accounting control comprises the plan of organization and the procedures and records that are concerned with the safeguarding of assets and reliability of financial records and consequently are designed to provide reasonable assurance that; Transactions are executed in accordance with management's general or specific authorization, transactions are recorded as necessary to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements and to maintain accountability for assets, access to assets is permitted only in accordance with management's authorization, the recorded accountability for assets is compared with the existing asset at reasonable intervals and appropriate action is taken with respect to any differences.

2Internal control should not be viewed as something that must be superimposed on an organization's normal operating structure. To do so only means costs that can inhibit the organization's ability to compete. Internal control should be built into the infrastructure of an enterprise. When controls are integrated with operational

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1 Statement on Auditing Standards No.48, effective for periods beginning after August 31st, 1984

activities, and a focus on controls has been instilled in all personnel, the result is better control with minimum incremental cost. Such integration avoids a superstructure of control procedures on top of existing activities. Whenever management considers changes to their company's operations or activities, the concept that it's better to 'build-in' rather than 'build-on' controls, and to do it right the first time, should be fundamental guiding premises.

Management policies and rules regarding employee behavior provide reasonable assurance that control objectives are achieved by; Proper Authorization which includes empower employees to perform tasks and make decisions that impact assets which usually involves signature and authorization and general and specific authorization of transactions, Segregation of Duties which also includes ensuring that no single individual is given too much responsibility no employee should be in a position to both perpetrate and conceal irregularities and three general categories of functions that must be separated in authorization function and recording function of preparing source documents, maintaining journals, preparing reconciliations, or preparing performance reports and custody of asset either in directly or indirectly way for example receiving checks in mail also there is another control which can be practiced without segregation of duties like

If responsible for both custody and recording accounts receivable, could divert some cash receipts and falsify accounts to conceal diversion, If can authorize account write-offs and has custody of cash receipts, could authorize false write-off and divert subsequent collection on account and authorizing issuance of purchase orders to specific vendors and responsible for recording inventory receipts, could issue purchase order to fictitious vendor and prepare fictitious inventory receipt record, resulting in disbursement of funds for something never received another way of achieving control objectives is through Adequate Documentation and Records, and Independent Checks on Performance.
In March 1992, a senior executive in Singapore wrote a letter to the head of the equity department in London stating that “My concern is that once again we are in danger of setting up a structure which will subsequently prove disastrous and with which we will succeed in losing either a lot of money or client goodwill or probably both. In my view, it is critical that we should keep clear reporting lines and if this office is involved in SIMEX “then Mr. Lesson (an employee who caused the loss of $1 billion) should report to the Singapore office operations department not the London derivatives department.

An internal audit in the summer of 1994 cited lax internal controls and made a specific recommendation that the trading and settlement duties be separated. Mr. Lesson was monitoring himself by doing both duties. Mr. Lesson used an error account to hide trades he did not want his superiors to know and managers were reluctant to impose tight controls which might reduce profits and bonuses.

On February 23, 1995 a 232 year old British bank, Baring Bros. and Co., was bankrupt by a loss of $1 billion in futures trading caused by employee called Nick Lesson as stated in the above case then a statement by the Singapore International Monetary Exchange (SIMEX) attributed the loss to a failure of internal controls. Senior Executives conceded that controls should have been much tighter and the organization ignored several warning signs of internal control weaknesses over several years.

A study from Italy for May 2009 stated that: (CG) Corporate Governance theme has recently been the subject of significant measures to try to restore confidence among investors by encouraging information and communication transparency. The

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4 Associated Press March 5, 1995

5 Journal of Management & Governance Volume 13,Issue 1-2,pp75-100 (cover date:2009/05/01)
Italian Parliament approved Law 262 in 2005; and in 2006 the CG Committee of the Italian Stock Exchange approved the new Self-Regulatory Code for listed companies. This paper deals with control matters and moves on to causes and cases of their failures in relation to a sample of Italian companies. More precisely, it investigates, through an empirical survey, the main limits and areas for improvement in the working of company Internal Control (IC) system(s) and in the objectives of the role of the three main professional bodies currently in charge of it in Italy (i.e. Internal Auditing, Statutory Auditors and External Auditors).

The results obtained show that the Italian situation is very unusual, due to a long tradition: the possibility to choose between different administration and control systems, often with coexisting and overlapping roles, creates problems in terms of responsibility and control. The first answers to the critical issues highlighted are given by the aforementioned laws, intended as the main catalysts for a review of the roles of all IC bodies. However, much work has still to be done. The final aim was to come up with suggestions about the possibility of finding areas for improvement within those companies’ IC systems.

2.11 Research Gap
This gap reviews theories which have been commented by others for what has been written in the literature and the empirical studies. This is going to happen due to application of weak internal controls in the management over flow of funds or assets this problem will be caused by Abuse of responsibility, management override of controls, frauds, changes in environment making controls inadequate, human cleverness and the requirements of the professional standards. This might produce materially misstated financial statement.

2.12 Review of Theories
According to Ainokea 003, (May 2010), Internal controls are to be an integral part of a company’s financial and business policies and their procedures. An internal control consists of measures taken by a company for the purpose of ensuring accuracy and reliability in accounting and operating data.
Systems of the internal controls will operate at different levels of effectiveness by deciding if a particular Control system is effective, it is a judgment based on results of an assessment which will include five components, which are; Control Environment, Risk Assessment, Control Activities, information and Communication and Monitoring which are also present and functioning.

The Sarbanes-Oxley Act (SOX) of 2002, also known as the Public Company Accounting Reform and Investor Protection Act is a U.S. Federal Law enacted as of July 30, 2002. Stated, “Aspects of SOX in Section 404, which requires management to report on the adequacy of a company’s internal control over financial reporting.” It is known to be the most costly aspect of the legislation for companies to document and test important financial manual and automated controls requires efforts.

If the company will announce the deficiencies in its internal controls would probably experience downfalls in their stock prices because other companies might see their product as a weakness. Material weakness in the internal control system affects an auditor’s report, a company’s financial statements and the capital markets’ reaction to the existence of such weakness.

2.13 Conceptual Frame Work

The Table below represents the relationship between the three components of the variables.
Table 2.2: Conceptual Frame Work

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Intervening Variables</th>
<th>Dependent Variables</th>
</tr>
</thead>
<tbody>
<tr>
<td>- MSD Receipts and Payments through Debtors Collections and Creditors Payments Or Disbursements.</td>
<td>- Internal Audit skills.</td>
<td>- Proper control of funds</td>
</tr>
<tr>
<td>- Sales and Expenditure Budgets which should not exceed Estimated Budgets.</td>
<td>- Monitoring and evaluating.</td>
<td></td>
</tr>
<tr>
<td>- Use of resources (physical assets, inventories, investments, cash and people).</td>
<td>- Transparency and Accountability.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Good management skills.</td>
<td></td>
</tr>
</tbody>
</table>

Source: Researcher Field Data, 2014
CHAPTER THREE
RESEARCH METHODOLOGY

3.1 Introduction
This chapter describes the methods that the researcher employed to answer the research questions. It describes the research design, the sample and sampling methods the researcher used, data collection methods and instruments, as well as data analysis techniques that were used to extract information from the data.

3.2 Research Design
This study was a case study. A case study (like this one done at MSD Keko Mwanga Branch), involves in-depth, contextual analysis of situations which could occur in other organization, where the nature and definition of the problems happen to be the same as experienced in the current situation. It is useful particularly when one intends to gain a rich understanding of context of the study, as is typified by Robson (2002).

Saunders (2004), defines a case study as a strategy for doing research which involves an empirical investigation of a particular contemporary phenomenon within its real life context using multiple sources of evidence and sometimes strategies which will involve the use of questionnaire, interviews, observations, and documentary review as possible.

3.3 Study Area
The field research for this study was to investigate the effectiveness of internal controls over flow of funds. The study was conducted at MSD KEKO MWANGA BRANCH in Dar Es Salaam. The reason for the choice of this study area arose from the fact that, the researcher is an Accountant and is having more interactions with many individual works with MSD, hence expected easier access to information. Also, MSD is one government institutions in the country that provides various medical services to customers within and outside of the country, and therefore, their financial services need sanguine and proper internal controls.
3.4 Sample Size and Sampling Techniques

3.4.1 Sampling Techniques and Sample Size

The researcher used non-probability, judgmental sampling technique where she chose only those elements which had required data. Setting and ensuring the effectiveness of internal controls is the work of professional and managerial levels in the organization. Required data on effectiveness of the systems can, therefore, best be expected to reside with senior and middle managers, and those ordinary employees with foremen duties. A non-probability sampling technique was, therefore, an appropriate method for sample selection at the MSD.

The sample selection involved a total of 30 MSD officers. Of these, the researcher picked the top five (5) senior officers – i.e. Director General, Director of Finance, Chief Accountant, the Treasurer, and the Receipts and Expenditure Accountants. The remaining 25 were ordinary subordinates and employees.

Table 3.1: Sample Respondents: Sample Size

<table>
<thead>
<tr>
<th>Category</th>
<th>Number of Respondent</th>
<th>% to the total sample size</th>
</tr>
</thead>
<tbody>
<tr>
<td>Top MSD Officials</td>
<td>5</td>
<td>16.67</td>
</tr>
<tr>
<td>Normal MSD Employees</td>
<td>25</td>
<td>83.33</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>30</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

**Source:** The researcher data, 2014

3.5 Data Collection Methods

Data refers to all the information a researcher gathers for his or her study (Mugenda and Mugenda, 1999). For this study, both qualitative and quantitative data collection techniques were used in order to counterbalance shortcomings of each technique (Saunders et al, 2005). The decision to use multiple instruments in collecting data was to ensure validity of data as one instrument complemented the other (Ledgerwood, 2000; Saunders et al, 2005).
The study was essentially a survey by which various methods of data collection including interviews; participant observation techniques, questionnaires and documentary reviews were used. The researcher recorded all verbal answers from the respondents who answered to the interviews. Similarly, the researcher observed and noted each respondent’s behavior and attitude while answering the interview questions. On the whole, the aim of administering such a triangulation strategy was to generate sufficient data that would lead the researcher to develop insights on the effectiveness of internal controls over flow of funds.

3.6 Research Data
Two types of research data namely primary data and secondary data were collected. The data collected were geared at answering the three research questions namely:

i. To what extent do internal control systems affect the orderly and efficient running of an organization?

ii. To what extent does the MSD use its internal control systems to manage its funds flow, i.e. cash receipts and disbursements?

iii. What challenges do organizations face while implementing internal controls, specifically accounting controls?

3.6.1 Primary Data
Kothari (2004) defines primary data simply as first-hand information collected from the field. Primary data is collected specifically for the research project being undertaken. Primary data in this study were collected by means of interviews, questionnaire and participant observation techniques, at Keko Mwanga Branch of the MSD.

3.6.2 Secondary Data
Secondary data, as defined by Kothari (2001), is second-hand information collected for some other purpose. Secondary data allows comparison of information with primary data enabling a more generalized triangulation of the findings. Kervin (1999), argues that the criteria for accessing secondary data are comparison of the costs of acquiring them with the benefit they bring. Cost, includes both, time and
financial resources that you need to devote to obtain the data. Stewart and Kumins (1993), urge that if you are using secondary data you are at an advantage compared with research using primary data, as primary data has additional cost of both time and finance.

This researcher collected secondary data through review of existing MSD records, which included records on control over debtors and creditors, control over cash receipts and petty cash, banking transactional control, cash inflows and outflows and work and staff performance on fund management and control.

3.7 Data Collection Instruments

3.7.1 Observation

Observation involves the systematic observation, recording, description, analysis and interpretation of people’s behaviour. In this type of strategy participatory observation was applied. According to (Gill and Johnson, 1997:113) in participatory observation the researcher gets fully involved in the lives and activities of the subject and thus becomes a member of the institution in all departments concerned with what he/she is researching, as in the case of the MSD, fund management and control. According to Delbridge and Kirkpatrick (1994) data collected through observation is categorized as primary and secondary.

The researcher got involved in various activities including sorting cheques received during the day, giving out balances to customers, and recording receipts in the books.

3.7.2 Interview

An interview is a purposeful discussion between two or more people (Kahn and Cannell, 1957) Interview may be highly formalized and structured, using standardized questions for each respondent or they may be informal and unstructured conversations. Interviews may be categorized as structured interviews, semi structured interviews and unstructured interviews. (Saunders, Lewis and Thornhill 2007:264).
With regard to this research, personnel interviews were conducted with MSD top officials and regular officers according to the sample. The interview guides contained questions that ranged from general questions to quite specific ones. A sample of such questions included:

- Is there proper control of unused receipt copies?
- Are all payments done through authenticated vouchers?
- What are the existing opportunities for improving the system?
- Are all staff competent enough to carry out the work allocated to them?

Other questions were on proper control of debtors and creditors, cash receipts and petty cash, banking control and cash flow.

### 3.7.3 Documentary review

Documentary view may be employed to secure secondary data. The documents for review can include notices, correspondences, minutes of meetings, reports to shareholders as well as diaries. Other written documents also include books, journal and magazine articles and newspapers (Saunders, Lewis and Thornhill 2007: 208)

For this study, the researcher went through different official records kept for reference, particularly audit reports, files, journals, magazine, and financial regulations. The study of the organization’s accounting manuals was done to be able to relate/compare the details and information that was collected mainly from interviews.

### 3.7.4 Questionnaire administration

Questionnaire is a data collection instrument that includes all techniques in which each person is asked to respond to the same set of questions in a predetermined order (Saunders, Lewis and Thornhill, 2007: 300-301). The choice of questionnaire data collection instrument is always influenced by the fact that questionnaires are flexible, easy to apply and less expensive. In this study the questionnaires were designed in English Language.
3.7.5 Response rate

All questionnaires that were distributed were 30. Total questionnaires returned were 25, were equal to 83.3 per cent (See below table)

Table 3.2 Respondents and Response Rate

<table>
<thead>
<tr>
<th>Response Category</th>
<th>Number of Questionnaire Distributed</th>
<th>Sample Required</th>
<th>Returned Questionnaires</th>
<th>% of Questionnaires returned</th>
<th>% of Responses over the required sample</th>
</tr>
</thead>
<tbody>
<tr>
<td>MSD Top Officials</td>
<td>5</td>
<td>5</td>
<td>5</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>MSD ordinary Employees</td>
<td>25</td>
<td>25</td>
<td>20</td>
<td>66.67</td>
<td>80.00</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>30</td>
<td>25</td>
<td>83.33</td>
<td>83.33</td>
</tr>
</tbody>
</table>

Source: Research Report work 2014

3.8 Data Management and Analysis

3.8.1 Data management

While designing both questionnaires and interview guide, the researcher kept in mind the need to collect correct, complete and accurate data. These are characteristics of reliable and valid data. Data validity is the correctness and reasonableness of data. Questionnaire and interview guides therefore, need to contain only valid questions, and to do so, the instruments (questionnaires and interview guides) ought to be pre-tested before being put to final use in the field (Saunders, 2003).

In this study, to ensure validity, the questions were verified for correctness and reasonability. The questionnaires and interview guides were pre-tested using two focus discussion group (FDG) of three individuals each, who comprised of two accountants and an auditor. Each questionnaire obtained was checked for validity and all inadequate, invalid and erroneous questions were corrected, completed or
weeded out before they could be sent into the field. In the field, for unclear interview responses, respondent were asked to specify what actually they intended say.

Data reliability refers to collected data that is independent from the collector. The purpose is that if the same questionnaire were administered by another person should yield the same results. To increase reliability in this study, each respondent was given a pre-amble describing the objectivity of the study and its implications. Employees and the top officials were asked to be free and were assured that anonymity was highly observed.

3.8.2 Data analysis

Data was analysed using both quantitative and qualitative techniques. Quantitative data was classified and tabulated using Microsoft Excel-Spreadsheet software. Qualitative analysis was based on description and interpretation of findings using tables where necessary.
CHAPTER FOUR
RESEARCH FINDINGS ANALYSIS AND DISCUSSION

4.1 Introduction
This chapter presents the research results in the light of the predetermined research questions and objectives. The chapter analyses the findings obtained from primary and secondary data collected through questionnaires, in-depth interviews, and observation. Secondary data were collected through review of existing records (reports and manuals) as well as from MSD website.

4.2 Characteristics of Respondents
As stated in the introduction of this chapter, data for this study were collected through questionnaires, interviews and observation. A total of 30 respondents were provided with questionnaires and interviewed. Out of the 30 questionnaires, only 10 (33%) were not returned. It was interesting in this case that all the respondents were university graduates, and also, only 5 were women.

Table 4.1: Characteristics of the Respondents (for MSD officials)

<table>
<thead>
<tr>
<th>Respondent’s Category</th>
<th>Category</th>
<th>Number of respondents</th>
<th>% of the total sample</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gender</td>
<td>Male</td>
<td>15</td>
<td>75</td>
</tr>
<tr>
<td></td>
<td>Female</td>
<td>5</td>
<td>25</td>
</tr>
<tr>
<td></td>
<td>No formal Education</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td></td>
<td>Primary</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Education attainment</td>
<td>&quot;O&quot; Level Sec.</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td></td>
<td>&quot;A&quot; Level Sec.</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td></td>
<td>University Education</td>
<td>20</td>
<td>100</td>
</tr>
<tr>
<td>Skills Possession for the</td>
<td>Basic</td>
<td>3</td>
<td>15</td>
</tr>
<tr>
<td>Internal Control Software</td>
<td>Intermediate</td>
<td>9</td>
<td>45</td>
</tr>
<tr>
<td></td>
<td>Expert</td>
<td>8</td>
<td>40</td>
</tr>
<tr>
<td></td>
<td>Questionnaires filled</td>
<td>20</td>
<td>67</td>
</tr>
<tr>
<td>Account Information</td>
<td>Not filled</td>
<td>10</td>
<td>33</td>
</tr>
</tbody>
</table>

Source: Research field data, 2014.
4.3 Responses to Research Questions

The main research question of this study was – to what extent do internal control systems affect the orderly and efficient running of the MSD, particularly management of its funds flow?

The first and most fundamental question before answering any other question is whether the MSD has any internal controls and how it uses them.

It would be absurd for an organization, as important as the MSD, not to have any internal controls, for these are the reason for having boards of directors. Internal controls, even without mentioning the MSD, are essential to the effective operation of any organization, be it for profit or not for profit. Simply put, internal controls are activities or procedures designed to provide reasonable assurance that operations are “going according to plan.” Without adequate internal controls, management has little assurance that its goals and objectives will be achieved. Properly designed and functioning controls reduce the likelihood that significant errors or fraud will occur and remain undetected. Internal controls also help ensure that departments (other than the main finance office) are performing as expected.

It was also the agreed opinion of top management of MSD (top 5 directors) that internal controls are tools that should ensure corporate goal achievement, normalize employee conduct and behaviour, and at the same time assist management in controlling operations and securing resources against unauthorised use or removal. With regard to accounting controls, the management stressed that they assure that all transactions are authorised, and recorded, and access to assets is allowed only for authorised purposes. With reference to the management of cash inflows and outflows, management emphasised that good controls should ensure timely collection of debts and payment to claims. This ensures continuity of operations and grasp of business opportunities when they arise.

A documentary review of the Controller and Auditor General’s (CAG’s) Performance and Forensic Audit Reports for the period ending March 2011, has explained that the mission of the MSD is to make available at all times, essential
medical supplies of acceptable quality at cost effective prices to the population through government and approved non-governmental health facilities. Responsibility of risk assessment and handling of suspicions of fraud is vested in the MSD Management. The management is, therefore, expected to continuously and periodically conduct risk assessment and handle suspicious fraud evaluation.

From the CAG’s emphatic description of the duties of the MSD management, it is clear that in no way can MSD avoid having designed and operationalized internal controls (in form of policy, procedures and regulations) for the said purposes of detecting assessing and handling risk and suspicious fraud. Anything different from having internal controls would disqualify the existence of a board of directors at the MSD.

It was to the surprise of the CAG when he found, during this forensic audit that “the MSD does not conduct any risk assessment with a view to prevent fraud or other types of irregularities in its own operations. In his own words the CAG states in the report that:
There are no specific documented procedures for detecting, investigating and handling indications of fraud. The risk assessment policy and strategy document does not provide guidelines for investigative assignment. (CAG, 2012, ibid).

To answer the question – to what extent had internal controls at the MSD helped the organization achieve its objectives on funds flow management, the management assured that for the past five years, MSD had not been served with a dirty audit certificate by the Controller and Auditor General (CAG). This was sufficient proof that MSD’s funds were well controlled. In other words, cash received and cash paid out followed or complied with accounting principles, in terms of balancing of amounts, recording and safe custody. It also implies that procurement followed set principles and regulations as set by PPRA, debtors were duly followed up and creditors were duly paid.
More than not having been served with a dirty audit certificate by the CAG, MSD does also have an internal audit department in its organisation structure. The Internal audit section, has among its duties, to evaluate and improve the effectiveness of risk management, controls and governance processes. The head of the Internal Audit reports administratively to the Director General and functionally to the Audit and Risk Management Committee of the Board. The unit monitors the implementation by the department, of its recommendations and Board directives on the same (MSD website).

However, a documentary review of the CAG’s 2012 report on the Audit of Public Authorities and Other Bodies for the financial year 2010/2011 indicated that the MSD was by then owed by the Government Sh. 40 billion (uncollected fund); had monies in its accounts while health centres lacked essential drugs and facilities; and that it had procured some drugs and medical supplies and equipment contrary to procurement law (2004) and its regulations of 2005. All these indicate gross noncompliance with internal controls and external regulations. In the words of the CAG:

As at 30th June, 2011 MSD had a net amount of around Shs.16 billion in health facilities accounts, whereas at the same time most facilities lacked drugs and medical supplies needed on a daily basis such as ALU and absorbent surgical gauzes. The health facilities therefore use their scarce resource from other sources to buy such items from other suppliers whilst their allocations are lying idle at MSD because of unavailability of good facilities including drugs and medical supplies. Further, special audit revealed contracts of Shs.3.95 billion, USD.9.4 million and EURO 1.5 million which were not approved by the MSD Tender Board and therefore contravened Section 30(c) of the PPA 2004 and Regulation 41 of GN.97

The next research question wanted to find out the extent to which the MSD uses its internal control systems to manage its funds flow, i.e. cash receipts and disbursements?
Successful cash flow management depends on the timing and amounts of money flowing into and out of a business. Income and expenditure rarely occur together, with income usually lagging behind. Good cash flow management will help an organization (like the MSD) to prepare for shortfalls and to make the most of cash surpluses (ASB, 2014). Cash flow management is therefore the management of the differences between what the organization earns and what it pays out.

The cash flow management process involves, on the side of cash receipts, – managing (timing and enforcing) receipts from customers for goods and services sold to them; receipt of a bank loan; interest or returns on savings and investments; shareholder investments; and rental income on investment properties. With regard to cash disbursements, it involves the execution and enforcement of purchases of or payments for inventories, raw materials or tools; payment of wages, rent, and daily operating expenses; purchases of fixed assets; loan repayments; dividend payments; drawings from the business; payments for income tax, corporation tax, and other taxes.

According to MSD documentation, MSD sources of funds include, Shareholders investments, i.e. investments from the Government of Tanzania; WHO; DANIDA; USAID; SCMS; and The Global Fund. Their other sources are revenue from sale of drugs and other medical facilities and supplies (MSD website).

Government policy is that government health facilities have their funds allocation at the MSD and therefore, their purchases of medical supplies and equipment are on deductible balance schemes. For non-governmental health facilities, procurement is by cash (cheque).

There has not been any report made public with regard to MSD failing to collect any monies from their customers. However, there have been reports from the CAG that the Government has, from time to time, failed to provide part of the money budgeted for MSD. In his Annual General Report of 2010/2011, the CAG lamented that he had noted that not all funds allocated for purchasing drugs and medical supplies were actually disbursed to MSD. Out of the budgeted amount of Shs.148.3 billion for the
two periods (2009/2010 and 2010/2011), only Shs.132.2 billion was disbursed to MSD for purchase of drugs. This does not show any failure on the part of MSD compliance with their internal controls, rather a challenge in managing their cash flows.

However, a report by ……..lists a few weaknesses of the MSD internal control systems, some of which, for instance are: delays in distribution of allocated funds to health facilities (hospitals, laboratories, dispensaries, etc.); delay in delivery to facilities; inaccurate forecasting at the facility and national level; theft of medications at all levels; stock-outs at the national warehouse run by MSD and Malfunctioning back order system for unfilled items. These weaknesses explain failure of management to detect anomalies and risks beforehand, making it difficult to plan for cash inflows and outflows.

One essential question that arose during documentary review on the effectiveness of internal controls at the MSD was – if the organization did not conduct any risk assessments or fraud detections, what possibly were the reasons?

Answers for the question above came essentially from the CAG again. In his forensic report (ibid, pg. 8) the CAG states clearly that he found no specific documented procedures for detecting, investigating and handling indications of fraud. The risk assessment policy and strategy document does not provide guidelines for investigative assignment.

In the absence of any written guidelines, it is difficult to say that internal controls of an organization are effective or not effective since they are not there and no one could try nothing.

The third research question asked about challenges that MSD faces in the process of its internal controls, particularly cash flow controls.
Respondents to question five in the questionnaire raised a number of challenges that they face when trying to implement internal controls. Among these questions included:

- Sometimes the MSD was required to buy emergency medicines while they were not in procurement plan.
- Sometimes MSD is forced to sell medicines on credit while the policy is sale on cash.
- Instructions from outside of MSD requiring the organization to contribute money to some public events while events not budgeted.
- Required reports not prepared timely which in turn affect forecasting and procurement of drugs and other medical supplies.

Documentary review also came up with additional challenges facing MSD:

- The MSD does not use staff with relevant education and experience when performing investigations.

4.4 MSD Audit Preparation

4.4.1 Introduction

The typical audit is intended to determine whether or not the area under review is following prudent business and administrative practices consistent with the mission of the organization, official policies and bylaws of the organization, and the laws or requirements of external authorities, as may be applicable. When we are able to verify that these issues are taken seriously by both management and support personnel, and that these practices are actively carried out in their daily work routines, we will invariably conclude that a strong internal control environment (also known as a system of checks and balances) is in place. The existence of an effective internal control environment in all of the organization administrative and support functions is an integral part of maintaining a sound financial position and providing quality services in support of academic excellence. The existence of these features, along with providing quality controls, will contribute towards achieving organization goals.
4.4.2 The typical audit at MSD

The MSD director or department head of the area to be audited was contacted by the Director of Internal Audit to inform him/her of our intentions to perform an audit of the area's operations and to arrange an entrance meeting. A formal Engagement Letter is then be delivered to the client, along with a Pre-Entrance Meeting Questionnaire, an Audit Policy statement, and a Customer Satisfaction Survey. The questionnaire, which provided the auditors with basic background information about the operations to be audited, was completed by the client prior to the entrance meeting. The survey, which offers the client the opportunity to evaluate our audit process, was completed by the client subsequent to audit completion.

An entrance meeting serves to allow the Audit Department to describe to the client the goals and objectives for performing the audit. Any questions or concerns the client may have regarding the audit brought forth at this meeting. The entrance meeting also utilized to determine the appropriate contact personnel, set-up any necessary appointments, and determine the desired and most efficient methods of communication during the course of the audit.

One of the primary objectives of the auditor is to gain an understanding of the client's operations. The auditor asked to examine any existing written policies and/or procedures which your area may have produced. Additionally, the auditor asked to interview key personnel in order to develop (or update) our understanding of the operations being audited. Upon completion of this stage of the audit, the auditor prepared a control document (flowchart, narrative, or questionnaire). This document was utilized to help assess the operation's control strengths and weaknesses and to determine the nature and extent of audit testing to be performed.

Audit tests serve to determine whether or not the stated controls are working effectively. The client may be asked to provide documentation or other appropriate evidence pertinent to their operation that assisted in audit testing. The auditor may require assistance in obtaining documentation and in answering questions that may arise during the course of the audit. Based on the review of the control environment
and audit test work conducted, the auditor attempted to identify any actual or potential control weaknesses and/or findings. These areas of audit concerned informally communicated to the client during the course of the audit and summarized into a draft report once the audit review has been completed.

The draft report forwarded to the client for review and arrangements are made to have an exit meeting to discuss the draft report. The client carefully reviews the draft report for accuracy of content prior to the exit meeting. This meeting allowed for the discussion of the audit concerns detailed in the report and the audit process in general. Additionally, this provides a forum for both the auditor and client to reach agreement or discuss alternatives to any audit recommendations in the report. The meeting also provides the auditor an opportunity to make any necessary edits prior to issuing the formal audit report.

The formal audit report or memorandum is issued to the client subsequent to the exit meeting. The client having 2 weeks (or other mutually agreeable time frame) in which to prepare a formal response to the audit report forwards the response to the auditor and serves as the client's corrective action plan. The audit report and client response was packaged with a cover letter from the Director of Internal Audit addressed to the client's immediate supervisor, with additional copies to other appropriate organizational personnel. Any audit issues not be satisfactorily resolved via the client's corrective action plan, the auditor followed these issues through with the client until a satisfactory resolution been established.

**4.4.3 What auditors need during MSD auditing period**

- Cooperation on the part of the client and auditor are essential to a successful audit. In conducting routine audits, our purpose is to identify potential opportunities for improvement which are in the best interests of both the organization and the area being audited.

- Acceptance of responsibility for creating and maintaining a good system of internal control over the activities (financial and non-financial) occurring within your
organization. Establishment of a good system of internal control (and accountability for the lack thereof) is the responsibility of department and executive management, not the auditors. MSD assist in identifying potential exposure areas and provide suggestions and recommendations as to how you might rectify these situations if and when they exist.

• A current organization chart of your area of responsibility. This and other information will assist the auditor in gaining an understanding of your administrative structure, nature of your operations and familiarity with your employees. Policy/Procedure manual (if available) we encourage all departments to maintain a current policy/procedure manual. In addition to assisting the auditor in understanding your operation more thoroughly, a well-documented policy/procedure manual will guide new as well as veteran employees regarding the established and approved methods of doing business.

• Temporary work space for the auditor(s) within reasonable proximity to the office staff and records. Since many of the original documents and records auditors need to examine are located at the local department level, the auditor(s) needed a temporary work area with adequate space and lighting. The amount of time needed for the auditors to be physically present at your location varied from audit to audit. We attempted to perform as much of the audit as possible from our office so as to minimize any disruption of your operations.

• Access to all employees and pertinent records. As stated in the Audit and Investigation Authority Policy, the Audit Department is authorized to have access to organization employees and records which may reasonably be necessary in the course of conducting our audits. The auditor's analysis of your operation may require that several of your employees at various levels be asked to explain in detail how they perform their jobs. In addition to examining hard copy records, it may be necessary for the auditor to make photocopies, and/or obtain samples, of key
documents for our files. Regarding computerized records, our access authority is "Read Only." The confidentiality of records reviewed during the course of the audit (i.e.: payroll, etc.) are maintained by the auditor(s).

- An honest and candid appraisal of the audit process at the conclusion of the audit. As stated earlier, the department head of the area being audited are provided with a Customer Satisfaction Survey. Each member of the audit staff has been professionally trained in the practice of internal auditing. They are expected to abide by the professional standards and ethics established by the Institute of Internal Auditors as well as our own departmental standards. Your objective answers and constructive comments on the survey form will assist us in evaluating and improving the effectiveness of our program.

### 4.4.4 Fraud investigations

We do occasionally have the unfortunate task of conducting investigations of alleged fraudulent activity. However, largely due to the honesty of individual, hard-working employees, combined with sound internal control processes, the occasions for such investigations have been relatively few. In these cases, all of the resources of the Office of Audit and Management Advisory Services, executive management, selected offices as legal offices, public relations offices are used, as necessary, to bring the matter to its appropriate conclusion.

### 4.4.5 Audit objectives

Our performance audit of the Cash Receipts Operations and Department had the following audit objectives:

1. To assess the effectiveness and efficiency of the Department's cash receipts operations.
2. To assess the effectiveness and efficiency of the Department's revenue recording function.
4.4.6 Audit scope
MSD audit scope was to examine the cash receipts operations processes and related records of the Departments. MSD audit was conducted in accordance with Government Auditing Standards issued accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

4.4.7 Audit methodology
MSD audit procedures were performed between June - September. To accomplish our objectives, MSD examined the Department's records and activities covering the period October through. We reviewed management plans and Department policies and procedures. We obtained an understanding of the internal control structure for the Department's cash receipts operations and recording of revenue.

4.5 Control of Cash Payments At MSD
4.5.1 Salaries payment
Before the end of the month, the payroll unit will send to the expenditures cashier the payroll sheets and the individual employees pay in slips for the Dar Es Salaam employee who are paid in cash and others through bank. Are lump sum cheque for the total amount of cash salaries, then the expenditure accountant will post the concern to each employees account. As each employees come to collect his/her amount, pay accountant will check the employees identity card and obtain the employees signature (even though now day’s bank use the ATM cards).

4.5.2 Staff medical and transport allowance
Previously all employees were paid medical and transport allowance as a means of secure their working conditions but due to the organization transition period, all employees should take care of him/herself on medical and transport expenses (top management offered this services)
4.5.3 Meal allowance
All employees are offered meal allowances which attract the employees to do work/job where by the meal is being supplied to the employees during lunch hours.

4.5.4 Cash flow
The purpose of maintaining the cash flow on a monthly basis is to enable the management to receive the performance of the business and to take any corrective action as soon as it becomes necessary. The following below verify the above explanation:-

Table 4.5 for Cash Flow from MSD financial statement

<table>
<thead>
<tr>
<th>DESCRIPTIONS</th>
<th>2013</th>
<th>2012</th>
<th>2011</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Tshs 000</td>
<td>Tshs 000</td>
<td>Tshs 000</td>
<td>Tshs 000</td>
</tr>
<tr>
<td>Net cash flow from operating</td>
<td>(1,528,959.00)</td>
<td>141,421,356.00</td>
<td>(12,166,162.00)</td>
<td>10,185,206.00</td>
</tr>
<tr>
<td>Activities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net cash flow from investing</td>
<td>(1,280,571.00)</td>
<td>(16,642,724.00)</td>
<td>(451,867.00)</td>
<td>(236,525.00)</td>
</tr>
<tr>
<td>Activities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net cash flow from financing</td>
<td>-</td>
<td>(4,530,757.00)</td>
<td>11,220,660.00</td>
<td>11,743,349.00</td>
</tr>
<tr>
<td>Activities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net increase in cash and bank</td>
<td>(1,809,530.00)</td>
<td>(11,752,125.00)</td>
<td>(1,397,369.00)</td>
<td>11,792,030.00</td>
</tr>
<tr>
<td>Balance</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Opening cash and balance</td>
<td>121,397,803.00</td>
<td>121,354,322.00</td>
<td>1,751,691.00</td>
<td>12,500,333.00</td>
</tr>
<tr>
<td>Closing cash and balance</td>
<td>180,207,334.00</td>
<td>101,397,803.00</td>
<td>(9,354,322.00)</td>
<td>13,792,363.00</td>
</tr>
</tbody>
</table>

Source: Researcher field data, 2014.
4.5.5 Findings from the Interview at MSD

4.5.6 Organizational strategic assessment (from MSD strategic plan or budget for 2006 i.e. from 2007-2013)

The first Medical Stores Department Strategic Medium Term Strategic Plan (MTSP) was prepared in 2006 to cover the period of six years (2007-2013). Over the past six years, MSD achieved a number of outcomes as a result of implementing the MTSP. These include; reduced stock outs, improved efficiency and performance through introduction of framework contracts, strengthening of ILS, reduced lead times, improved ICT systems with achievements such as implementation of modern ERP and improved communication with stakeholders. The image of MSD as well as the client relationship has been improved by implementing recommendations of customer service surveys.

The end of first MTSP, called for preparation of the new plan to give direction for the new time horizon. The development of a new MSD MTSP (2014 – 2020) has been built upon the success and challenges of implementing the previous strategic plan. This part looks at MSD ability and capacity expressed in terms of Financial Management; Operational Performance; Procurement; Storage and Distribution; Zonal operations; Information and Communication Technology; Customer Service; Human resources and Organization.

The financial position and sales growth figures of MSD are generally good and encouraging. MSD has been able to self-sustain its operations as required by MSD Act of 1993. The sales volume has substantially increased mainly due to the growth of vertical programs (VPs) accounted for 55%, other sales 2% and special procurement (SP) sales which accounted for 7% of total sales in 2011/12. Normal sales accounted for only 36% of the total sales. The growth of VP sales is due to increased donor funding for HIV/AIDS, Malaria TB and Leprosy programs.

However, the gross margin has decreased from 20.3% in 2006 to 12.46% in 2012 due to increase in operations such DD and low margin for VP. However, the debt growth is leading to the challenges of working capital to finance the MSD revolving funds.
for procurement of medicines and medical supplies. Due to expansion of MSD operational base, the debt may lead to challenges in maintaining sufficient working capital to finance the sales growth, and in financing the direct delivery (DD) of medicines and medical supplies to health facilities in terms of; fleet replacement, fuel, repair and human resource.

Working capital has been well managed in relation to growth in sales, stock levels have been on average of four months requirements. However, the government debt resulting from accumulated clearing charges and handling of VPs and quarterly disbursements have increased to Tzs.42.6 Billion as of June, 2012. Table below gives key financial parameters for MSD financial position.

**Figure 4.3: Sales growth**  **Figure 4.4: Working capital and government debt**

![Sales Growth](image)

![Working Capital and Government Debt](image)

**Source:** MSD Website: [www.msd.or.tz](http://www.msd.or.tz)
Capital expenditure has continued to be financed by MSD, Development partners in particular, Global Fund and United States Agency for International Development (USAID).

Financial performance of MSD has improved over the period; however, the long term financial sustainability of MSD has not improved. During the period, the working capital has declined from TZS. 81 billion in 2007 to TZS. 24.5 billion in 2013. The decline in working capital is due to the current pricing structure which results in lower margins and net surplus which does not improve financial sustainability. The use of predetermined prices which are fixed on an annual basis, delay and erratic disbursement of funds from the government puts enormous financial strain on MSD.
The following is the table for key financial performance parameter at MSD

**Table 4.6: Key financial performance parameters**

<table>
<thead>
<tr>
<th>Description</th>
<th>YTD ($zs. Millions)</th>
<th>2012-Jun Budget</th>
<th>2013 - Jun Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>Normal Sales</td>
<td>40,055</td>
<td>42,974</td>
<td>55,276</td>
</tr>
<tr>
<td>NS Growth</td>
<td>-23%</td>
<td>7%</td>
<td>29%</td>
</tr>
<tr>
<td>Vertical Programs</td>
<td>58,636</td>
<td>74,224</td>
<td>58,078</td>
</tr>
<tr>
<td>VP Growth</td>
<td>22%</td>
<td>27%</td>
<td>-22%</td>
</tr>
<tr>
<td>Special Procurement</td>
<td>6,515</td>
<td>8,247</td>
<td>6,453</td>
</tr>
<tr>
<td>SP Growth</td>
<td>27%</td>
<td>22%</td>
<td>14%</td>
</tr>
<tr>
<td>Total Sales</td>
<td>105,206</td>
<td>125,445</td>
<td>119,806</td>
</tr>
<tr>
<td>Total Sales Growth</td>
<td>-0.20%</td>
<td>19.20%</td>
<td>-4.50%</td>
</tr>
</tbody>
</table>

**Margin**

<table>
<thead>
<tr>
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</tr>
</thead>
<tbody>
<tr>
<td>Gross Margin</td>
<td>10,077</td>
<td>13,209</td>
<td>15,051</td>
<td>17,846</td>
<td>20,466</td>
<td>31,769</td>
</tr>
<tr>
<td>Gross Margin Percentage</td>
<td>9.60%</td>
<td>10.50%</td>
<td>12.50%</td>
<td>9.60%</td>
<td>12.40%</td>
<td>55%</td>
</tr>
<tr>
<td>Other Income</td>
<td>1,882</td>
<td>7,040</td>
<td>7,203</td>
<td>8,618</td>
<td>5,215</td>
<td>9,409</td>
</tr>
<tr>
<td>Growth /previous year</td>
<td>-32%</td>
<td>274%</td>
<td>2%</td>
<td>19.64%</td>
<td>-30.48%</td>
<td>60%</td>
</tr>
<tr>
<td>Other Income as a percentage of total income</td>
<td>2%</td>
<td>0%</td>
<td>6%</td>
<td>4.60%</td>
<td>-0.40%</td>
<td>5%</td>
</tr>
<tr>
<td>Net Results</td>
<td>2,326</td>
<td>7,904</td>
<td>4,474</td>
<td>6,576</td>
<td>6,348</td>
<td>2,387</td>
</tr>
<tr>
<td>Net Results as a percentage of sales</td>
<td>0.20%</td>
<td>6.30%</td>
<td>3.7%</td>
<td>3.50%</td>
<td>3.60%</td>
<td>1%</td>
</tr>
<tr>
<td>Working Capital</td>
<td>81,073</td>
<td>77,004</td>
<td>80,744</td>
<td>83,130</td>
<td>69,142</td>
<td>24,510</td>
</tr>
<tr>
<td>Working Capital/Sales in %</td>
<td>77%</td>
<td>61%</td>
<td>67%</td>
<td>44%</td>
<td>42%</td>
<td>12%</td>
</tr>
</tbody>
</table>

**Stock levels (Normal business)**

<table>
<thead>
<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Medical Stocks</td>
<td>30,028</td>
<td>39,004</td>
<td>28,639</td>
<td>27,765</td>
<td>37,256</td>
<td>60,875</td>
</tr>
<tr>
<td>Stock/ Sales in months</td>
<td>3.70%</td>
<td>4.18%</td>
<td>3.28%</td>
<td>16.50%</td>
<td>22.70%</td>
<td>30%</td>
</tr>
<tr>
<td>Government Debt</td>
<td>14,187</td>
<td>26,111</td>
<td>37,904</td>
<td>40,969</td>
<td>42,800</td>
<td>69,400</td>
</tr>
<tr>
<td>Government Debt growth%</td>
<td>80%</td>
<td>50%</td>
<td>10%</td>
<td>4%</td>
<td>63%</td>
<td></td>
</tr>
</tbody>
</table>

**Source:** Researcher field data, 2014.

MSD financial performance during the past six years has been improving steadily, due to improved financial planning, budgeting and reporting. However, the overall financial viability of MSD is healthy but not sustainable due to growing government debt with erratic disbursement of funds from MoHSW. Disbursements delay and falling of normal sales are the major challenges for the survival of the MSD business.
operations in the near future. MSD pricing policy is not commercially determined as it uses pre- determined prices which are fixed on annual basis and remained unchanged despite market fluctuations. The current margin on sales is 18.4% for normal sales, 14.6% for VP and 15% for Special procurements. The upward revision of margin to 20% for Normal, VP and SP sales will increase the surplus been generated which has been declining in the last six years.
CHAPTER FIVE
SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction
This chapter presents summary, conclusions and recommendations on the findings in Chapter Four.

5.2 Summary
This study examined the effectiveness of internal controls on cash flows at the MSD, Keko Mwanga branch in Dar es Salaam. The study was conducted using interview guide, questionnaire, personal observation and a review of organizational documents.

The study found out that MSD obtain their funds mainly from their partners – the government and donor community, and from sale of medical supplies and equipment to government and non-governmental health facilities and operators. The study also found out that MSD do not have power to force the government to allocate it all the funds they need as they budget, and also that they cannot make it provide them with all the funds allocated to them by parliament. In this way their cash inflows are highly affected by government allocation.

This study also learnt that MSD themselves don’t have documented mechanisms of detecting fraud in the organization, nor mechanisms for assessing possibility of risk. This was reported by the CAG in his reports from 2009 to 2012, although they have an Internal Audit department and a Strategic Plan. These remarks of the CAG discredit MSD from having working internal controls, not only for financial security alone but for entire performance effectiveness.
5.3 Conclusion.
This research aimed at finding out whether internal controls at the MSD are working, i.e. effective enough or not. In the actual sense, the MSD are at present working hard to put in place good, working internal controls, but only after strong recommendations of the Controller and Auditor General in his 2009/10 and 2010/11 Special Audit Reports. The CAG’s reports paint a picture that the MSD is sailing in very dangerous waters given the facts that for long they never had much useful controls nor that their staff had adequate knowledge and skills on financial risk analysis and fraud detection, taking into account their sensitive role on national health safety and security.

It is the duty of the board of directors at MSD to ensure that the controls that MSD is working hard to put in place at present will be complied with because having them without complying with them will not hive out the MSD from its cash flow straps and the consequences will be injurious to all their clients, i.e. health facilities and finally, the health condition of the entire nation.

5.4 Recommendations
- The Board of Directors has a duty to establish internal controls not only for accounting functions but for administrative purposes as well. Good controls are evidence of good governance which comprises of transparency, accountability and fairness. And this is the principal function of Boards of Directors. To ensure that their organizations are governed by rule of law.

- The Board of Directors must ensure that management of the MSD complies with both, internal controls that will be established and others like those of the PPRA on effective and efficient procurement. Compliance, particularly to PPRA and its regulations (PPA) of 2004 will help the MSD to procure according their procurement plan, as well as avoid single sourcing, which always raises the CAG’s eye browses. Good internal controls will, among other things, alert management of the dangers of contributions to events or other institutions outside their budgets or rules, which at times lead them to unnecessary cash straps. Internal controls will also strengthen
them to collect their receivables without discrimination or fear of who is the debtor, and in this way guard their cash inflows as required.

- MSD staff must be exposed/trained on risk assessment and financial fraud detection skills in order to save losses which would happen. It is inappropriate for an organization of its importance to national health to have staff who are least exposed to risk identification and handling. Staff with required skills in risk assessment will know the potential loopholes through which assets may pilfer or impending thefts and frauds, and in this way they will alert security management to handle the matters.
REFERENCES

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National Audit Office A General; (March, 2011); Report of the Controller And Auditor General on The Performance And Forensic Audit Reports for the period ending 31st march, 2011


Journal of Management & Governance, Volume 13, Issue 1-2, pp. 75-100 (Cover date 2009-05-01)

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NBAA, Tanzania Statement of Standard and Accounting Practice.


www.msd.or.tz.
APPENDIX

Introduction
This research project carried out on effectiveness of internal control system over flow of funds as for the case of MSD. The researcher is a student of Mzumbe University Dar Es Salaam Business School, who did a research as the partial fulfillment of the requirements for the award of Master’s in Accounting and Finance (Msc.A&F) of Mzumbe University. Please answer the questions freely in the space provided.
You cannot be identified by the information you provide as your name is not required. All the information you provide was treated in the strict confidence and used sorely for academic purpose only.

1. What skills do you possess in the Fund Control System that is being operated in this organization?
   (i) Basic ( )
   (ii) Intermediate ( )
   (iii) Expert ( )

2. Do you receive any regular training and seminars on the Internal Control System that is currently being used?
   (i) Yes ( )
   (ii) No ( )

3. Is the Control System used in Fund Management efficient in processing banking and accounting activities and data to the organization? Give short description.
   ………………………………………………………………………………………………………………………………..
   ………………………………………………………………………………………………………………………………..

4. Does the use of Internal Control software facilitate the preparations of financial statements?
   (i) I agree ( )
5. What are the major leading factors affecting the currently internal control system of funds in your organization?

**Positive factors**

(i) ........................................................................................................................
(ii) ........................................................................................................................
(iii) ........................................................................................................................
(iv) ........................................................................................................................

**Negative factors**

(i) ........................................................................................................................
(ii) ........................................................................................................................
(iii) ........................................................................................................................
(iv) ........................................................................................................................

6. Is the control system accurate and reliable in fund management?

(i) Yes ( )
(ii) No ( )
(iii) None ( )

7. What measures are taken by the organization in making sure that proper control system is taken:

(i) Over inflow and Outflow of funds?
..............................................................................................................................
..............................................................................................................................
..............................................................................................................................

(ii) In compliance with the policies and procedures to meet organization objectives through fund management?
..............................................................................................................................
..............................................................................................................................
..............................................................................................................................
..............................................................................................................................