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Article

The Role of Internal and External Audit in Financial Control

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Abstract: This paper aims at examining the central roles of internal and external audits in enhancing financial control mechanisms. While internal audits are assessments that occur inside the organization with the primary business of assessing internal controls, risk management, and compliance, external audits are independent ones that examine organizational financial statements for accuracy and honesty. Although these audits are defined for separate functions, there is considerable synergy for improvement in the governance and accountability when performed jointly. In light of the existing scarcity of published material on the subject, this study employs a qualitative approach with Research Design that involves a review of both academic and industry literatures, policies and guidelines, as well as case studies. From the results, internal audits improve the internal control, whilst external audits improve accountability and better adherence to rules on financial reporting. Yet there are difficulties, for example, the problem of the scarce financial and human resources, skepticism regarding the conclusions, and questions concerning auditor independence remain rather acute. It is suggested that the specific measures-simple though important, should be followed to expose audit to more people and to enhance utilization of both traditional and technology-enabling audit types. They demonstrate why audit practices must be refined by organizations and regulators, reducing excessive focus while increasing transparency. Awareness might be created for future research to undertake the analyses of integrated audit systems over time, and innovations such as artificial intelligence and blockchain in the audit practices. The outcomes of this study make a significant contribution to filling gaps in accumulated knowledge and improving the auditing approach to meet international financial regulation norms.

Keywords: audit, financial control, prevent fraud, internal audit, external audit

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1. Introduction

It is impossible to overestimate the role of financial control systems in efficient utilizing the organization's resources as well as their legal and ethical usage. As a necessary element of financial control, audit decisions define the quality and validity of financial statements. The audit process is divided into two types: internal and external audits. Both have as their objectives increasing the responsibilities of directors for financial management and raising the level of financial reporting.

However, the former has a broader mission compared to the latter, and employs different strategies.

In this article, the functions of internal and external audits are discussed, and their interaction with the financial control system of organizations, TOP, their contribution to the formation of improved governance, the identification of financial misconduct and fraud are considered.

Theoretical Framework: Financial Control and Audit

Financial control operates in handling of financial resources, their allocation as well as their usage pursuant to the stipulated legislation and organizational policies. The results of audit are used in financial control to verify the numbers as accurate, reliable and conforming to standard.

The internal and external audits are elements of the general financial control that have their own roles and tasks in the framework of the company's governance.

The main purposes of internal audit are to detect possibilities of ineffective or/and inefficient functioning of the internal control system, risks of fraud, and valuable suggestions on their minimization. Internal auditors have direct communication with management in order to explain that corrective action has been made, thus facilitating decision making for the management of the organization and contributing to its objectives. An internal audit may include both financial and operational audits hence giving a detailed assessment of the organization's undertakings.

Literature Review

Internal and external audits play complementary roles in enhancing transparency and accountability, helping organizations not only identify and address existing problems but also prevent their occurrence in the future. Establishing such audit mechanisms is an investment in sustainable development, trust-building, and improved management efficiency, which ultimately contributes to the organization's long-term success (Wallage. P., 2014).

Reducing Financial Risks and Preventing Fraud. Internal and external audits are key in reducing financial risks and preventing fraud. Internal audits focus on assessing the effectiveness of an organization's internal control mechanisms to ensure their capability to detect and prevent fraud, misuse of funds, and errors in financial reporting (Louw. L., 2021).

By examining processes such as cash handling, procurement, and payroll, internal auditors can identify weaknesses in the control system and recommend measures to mitigate the risk of fraud. They also help ensure compliance with regulatory and legislative requirements, including anti-money laundering laws (Spencer, M., & Wright, M., 2018).

External audits, by providing an independent evaluation of financial statements, offer additional protection against fraud and financial irregularities. External auditors' examination of financial data increases the likelihood of detecting material misstatements or fraudulent activities, safeguarding stakeholders' interests and maintaining the organization's integrity (Schilder, A., 2014).

Audit in this context aims to provide reasonable assurance that financial statements are free from material misstatements caused by errors or fraud. The role of audit extends beyond verifying financial data to include identifying weaknesses in internal control systems, improving operational efficiency, and preventing financial risks (Louw, L., 2021)

In the public sector, internal audit plays a key role in ensuring that public funds are used effectively and in compliance with laws and policies. For instance, the U.S. Government Accountability Office (GAO) conducts audits of federal agencies to evaluate how taxpayer money is spent. Regular audits by the GAO have identified inefficiencies and proposed reforms that improved financial control and management practices (GAO, 2020).

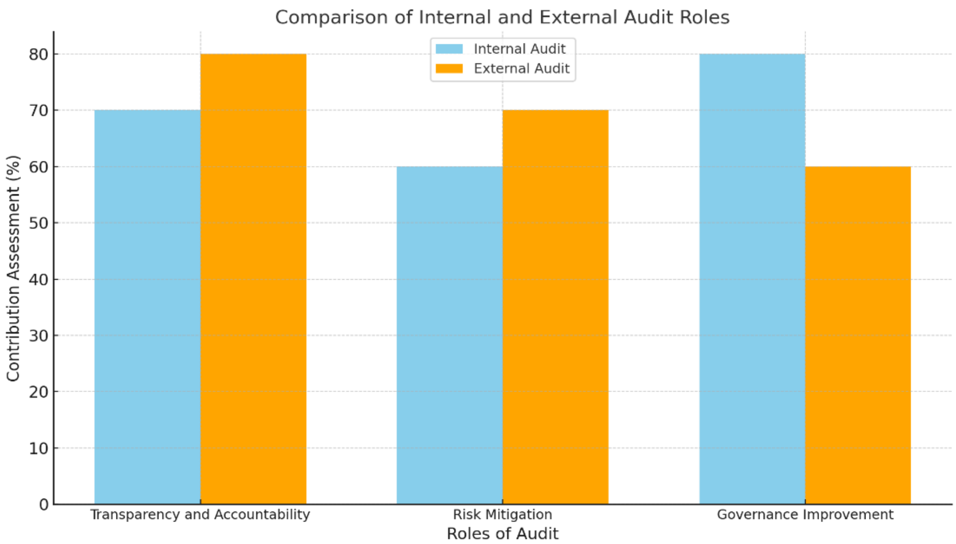
Internal audits are conducted by employees or departments within the organization to evaluate the effectiveness of internal controls, risk management, and policy compliance, whereas external audits are carried out by independent third-party auditors who provide an external assessment of financial statements, offering an impartial opinion on their accuracy and integrity (Spencer, M., & Wright, M., 2018).

2. Materials and Methods

Thus, this article employs a qualitative research approach, using a literature review of past research, analysis of the relevant legislation, and the examination of case data to investigate the functions of internal and external audits in financial control. Both primary and secondary data sources were employed; academic journals, industry reports and International Standards on Auditing, the nature and dynamics of auditing processes were used to develop a theoretical framework. Moreover, practical observations are made with regard to the existing evidential material concerning audit practices within organizations, aimed at demonstrating the applicability and efficiency of audits. The study focuses on the relations between internal and external auditing, while it is underlining how they both can improve the governance and accountability. To guarantee that all the contributions of audit practices to financial control are well understood, the qualitative research methodology called thematic analysis is used for pattern and correlation analysis. This approach of mapping the sources of information used in developing the best practice framework creates a clear linkage and common ground between theory and application to propose practical solutions that can be implemented by organizations interested in improving their audit function.

3. Results

External audit involves a third party, the auditor visiting an organization to verify the authenticity, accuracy and conformity to GAAP or IFRS of the financial statements of the organization that has requested for the external audit. External auditors are usually engaged by the shareholders and or the board of directors and their main role is to give an unbiased report on the summarized financial reports of the organization (Hayes. R., 2014).



Graphic 1. Roles of Internal and External Audit

The chart illustrates the roles of internal and external audit (in percentages):

- Transparency and Accountability: Internal audit contribution - 70%, external - 80%.
- Risk Mitigation: Internal audit - 60%, external - 70%.
- Governance Improvement: Internal audit - 80%, external - 60%.

While external audit largely deals with ascertaining the values of the financial statements. The external auditor then offers an opinion on the certification of the financial statements especially on whether they give a true and fair view of the organizations financial health to enable the external users such as investors, regulatory bodies and creditors to make the right decisions. This paper argues that external audit plays a significant role in increasing the reliability of an organization's financial statements and developing stakeholders' confidence.

Audit in the Framework of Financial Control. It will be important to stress that audit plays the crucial role in the system of financial control as it is a kind of primary guarantee of the financial information reliability. This is critically important in the present set up where many organizations are located dealing with a multitude of challenges that are volatile and fragile call for enhanced check and balance and factual adherence to recognized standards.

Auditing procedures enable one to review the financial data of a company and probably highlight some risks or mistakes that affect the position of the company. Audit assists organizations in improving organizational forms, strengthening internal control and completing obligatory legislation demands.

In addition, the audit process remains relevant in to the process of establishing a sustainable framework of financial systems. This is done by critically assessing the financial transactions and performance of an organization and presenting improvements to enhance operating efficiency and- reliability to the management of the organization in question. They help establish a reliable management system and ensure that long-term goals of the identified company are met.

A second strategic role of audit importance is the improvement of corporate governance standards. Auditors basically focus on pointing out some of the mayor vulnerabilities that are within an organization and as well coming up with ways on how these can be corrected, thus assisting in boosting up the decision systems that are important in the strategic growth and/ajaxibility of a firm.

Other two objectives which will be achieved include; Increasing Transparency and accountability. Another important characteristic of the audit activities is to establish credible financial management system and enhance the confidence on the organizations' financial statements. It includes internal controls and outside audits to keep current in legal requirements and manage resources, reduce risks and exercise proper control.

One of the main objectives of an audit is to find concealed shortcomings or defects of the management and financial reporting that may have a negative effect on the transparency of financial activities. In this regard, internal auditors examine matters of resource input and output, expenditure and revenue, and enhancing strategies and plans. It is an organizational control tool that enables leaders to have better analytical views of internal operations, and gain control of efficiency. For instance, auditors may identify unnecessary or improper costs, recommend economies, or identify threats arising from inadequate use of technology in commercial operations.

4. Discussion

The final area of activity, which is also a function of internal audit as an activity, is its capacity to improve the quality of decisions. And also, internal auditors can provide reality-based decisions by giving management relevant and objective information to minimize skepticism towards effectiveness of managerial decisions. This is especially so if the environment being operated in is competitive or economically unpredictable with accuracy and immediacy of decisions being key success factors. Audit also reduces possibility of conflict of interest in the company hence leveling the playing field for all the stakeholders.

On the other hand, external audit has a significant responsibility of improving the confidence of external users on financial reports through; External reconciliation of financial statements also reduces bias or compromise of the data by the organisation and presents actual financial position of the company. It is especially significant for those businesses operating in the public domain where reporting results depend on public confidence, which in turn controls the company's market capitalization.

In governmental bodies, in particular, external audit also plays a critically important role in the proper use of budgetary funds. For instance, auditors look at the efficiency of dispensing public funds on social services, infrastructure developments or other important activities. This not only allows to determine the inefficiency of resource distribution but also offers suggestions for the forthcoming budgeting. Therefore external auditor acts as a controller and an efficiency maker for any government structures.

What needs to be highlighted, however, is the fact that application of audit as a means to enhance transparency does not only concern economical, but also ethical and, to certain extent, social aspects of management. They encourage organizations and everybody in it to be open about any violations or areas of compliance that were lacking and not an area to be covered up. This goes a long way in building up trust from the employees, customers, investors, and all society in general.

Table 1.

Comparison of internal and external audit

Criteria	**Internal audit**	**External audit**
Target	Assess and improve internal controls and operational efficiency	Independent assessment of financial statements
Focus	Processes, risks, policy compliance	Accuracy and compliance of financial statements
Conducts	Organization employees	Independent third parties
Objectivity	Dependent on the organization	Independent from the organization
Periodicity	Regularly, usually annually	Depends on requirements, usually annually

Internal and External Audit Play Complementary Roles

- Corporation Governance Improvement. Independent audit is an effective component of corporate governance since it helps to maintain high levels of governance within any organization. Internal auditors play a role of helping the management in enhancing corporate governance by pointing out the areas of strength, weaknesses, opportunities and threats of the risk management practices as well as internal controls. These recommendations are useful in enhancing governance systems in relation to the organisation's financial operations and in making certain that those operations are strategic and compliant along with the law.
- The same way external auditor helps in proper corporate management by giving their account of the financial reporting without any bias to the company. These opinions assist in maintaining propriety of the organization and to meet legal and regulatory requirements as well as be Accountable and responsible. The report of the external auditor is very vital and assists greatly to increase confidence of investors, the government and the public.
- Despite the critical role that internal and external audits play in financial control, several challenges exist that affect the effectiveness of auditing processes:
- Limited Resources: Lack of resources is one of the biggest problems which organizations encounter as they attempt to conduct audits. Auditing also necessitates personnel with sound professional qualification, expertise in analyzing complicated financial information and fabrication of strategic solutions with a view to managing or

minimizing risks at the organizational financial control system. That, however, is often not the case: a lack of skilled personnel is a major challenge for many – and especially small – businesses. Having a limited number of qualified staff may cause too little effort being spent on collecting data, and a low quality of audit results.

- • Further, auditing requires the application of current computer technologies and programs that help to streamline work, analyze huge amounts of data, and detect irregularities.. Such tools that may include risk management systems, analytical platforms or analytical data tools are always expensive. Especially for small and medium sized organizations, the acquisition and implementation of these technologies requires substantial financial resources and, thus, organisations risk using less effective instruments or, at least, and are therefore experiencing a decreased audit accuracy and timeliness.
- Resistance to Audit Recommendations:Non-acceptance of audit recommendations is another major problem, which may drastically impair the efficiency of audit and decrease the benefits it produces to the company. Not approving the findings of auditors may be due numerous reasons based on the management. Major change on the other hand raises questions that may include posing a threat to the status quo, disturbances that may be foreseen as per future rhythmic changes, or even incurring of extra cost.
- For instance, changes to existing control systems, modification of corporate policies or changes in working practices across the organization will take time as well as resources, management will usually resist.
- Independence of External Auditors: Its independence is crucial since the external auditors are expected to be impartial, accurate and ethical in the process they undertake. That is, the presence of independence is crucial in order to guarantee the objective rendering of the audit report and guarantee its validity as a trustworthy tool for the evaluation of the efficiency of financial control.
- Nevertheless, different conditions in practice can cause auditors’ independency and therefore their credibility be in danger. Of all the dangerous phenomena, people report conflicts of interest to be one of the most severe. These conflicts can take several different guises, from the purely financial, for example where the auditing firm has a direct financial stake in the organisation it is auditing, to the more subtle but still significant where for instance there are long standing staff professional or socially based relationships between key members of the company’s management personnel and the auditor.For instance, if an auditing firm provides additional services, such as consulting or tax planning, to the organization it audits, this may create a situation where the auditor loses objectivity, striving to maintain the client relationship (Louw. L., 2021).

Table 2.

Main problems and solutions in audit practice

Problem	Solution
Limited Resources	Focus on high-risk areas, attracting external resources
Resistance to recommendations	Involvement of management in the audit process, staff rotation
Conflicts of interest	Rotation of auditors, use of several compa

Solutions to these problems for financial control

• Prioritizing Audit Procedures: However, with limited resources audits can be done selectively on the high risk areas which include fraud, big transactions and areas of wastage. They also hold that this approach cuts costs while improving audit quality.

• Utilizing External Resources: Lack of internal personnel may be another reason that makes organizations turned to external consultants or audit firms for audit services on a temporary basis. This also helps the company minimize the amount of work it gives to internal staff, while still getting quality work done.

• Staff Rotation and Training: Here, there is evidence of how it is possible to train internal audit teams, and there is also evidence of how staff rotation enhances performance. These include the programs such as mentorship and strengths enhancement of the internal auditors to help counter the problem of resource deficient.

• Collaboration with Other Organizations: Lack of adequate funds can be a reason why some organizations engage the services of other organizations in audit exercising. Auditors have found that this approach minimizes cost and increases the efficiency of the exercise.

• Active Management Involvement: This way management understands the audit process starting from planning stage (for instance – the audit plan preparation) and their involvement enhances the perceived relevance of the exercise. The involvement of Management in risk assessment and decision making enhances appreciation of required changes and promoting change.

• Limiting Auditor Contract Terms: It suggest that an independent audited organization is most advisable for an organization to implement a policy regulating the tenure that an auditor serves the company. For instance, it could be laid down that an audit firm cannot serve a particular organization for more than three to four years in a row. This helps to avoid influence of any form of relationship on the subject matter of a research.

• Engaging Multiple Audit Firms: It is sometimes advisable to have one audit firm for an audit and another for a different audit. This way offers a number of perspectives, while overlapping of interests is limited, since both firms act as reviewers of the work of the other.

5. Conclusion

This work examines the synergistic effect of internal and external auditors to enhance financial control, while stressing the contribution of the two activities to the achievement of those goals that relate to governance, risk and operations. Internal audits improve an organization's ability to adapt to change by pointing out areas that require improvement and checking that operations are conducted in accordance with the organization's standards External audits increase stakeholder confidence due to the confirmation that statements made by the organization are independent of its management. The co-integration of these audit types appears to be a promising research direction for obtaining a holistic assessment of organizational processes; however, their practical utilisation and empirical demonstration has not been fully investigated. These implications therefore suggest that both the organisational leaders and the regulatory authorities should consider as a top priority issue, ways and means of the integration and optimal use of audit practices in an effort to improve the levels of organisational transparency and accountability. More research should be directed towards the issues highlighted in the study, especially through employing longer term, and examining the available technologies in auditing. Thus, sustaining the enhancement of identified findings, further research shall advance the development of the auditing practices required to remain responsive and productive within the complex context of international financial regulation.

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