

# The importance of internal control for agricultural organizations and ways to improve it

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**Abstract.** The article reveals the important role and importance of internal control for agricultural organizations, its purpose and objectives are given. It is noted that the internal control system is a set of methods and techniques that ensure compliance with regulatory legal acts, the safety of assets, the timely reflection of business transactions in the accounting, prevention of abuse by staff, and the formation of reliable financial statements. The higher the level of organization of internal control, the lower the risk of material distortion of the data in the financial statements of agricultural organizations. At this stage of development, internal control is not only a verification of the accuracy of accounting, but also is a control function of management. In the process of its implementation, the risks of the organization and their consequences are assessed. The article focuses on the risks that distort the financial statements of the organization, and also provides ways to minimize them.

## 1 Introduction

The stability of an organization depends not only on positive financial indicators, but also on the construction of an internal control system. Agriculture is one of the main industries in the Russian economy. Improving the internal control system remains an urgent task for agricultural organizations in connection with the implementation of mandatory requirements in the legislation. The necessity of application of internal control in the organization is presented in the law No. 402-FZ "Accounting Act", namely, from 01.01.2013, internal control is mandatory for all economic entities. The consolidation of this norm in the Federal Law is an important step towards organizing a qualitative approach to the introduction of internal control. The organization accounting policy must establish the procedure for organizing and conducting internal control.

Among the urgent most significant problems of internal control are following:

- Spot organization of internal control. As a rule, in organizations, internal control is aimed at accounting objects that are more risky and, as a result, other accounting objects remain uncontrolled.

- Organizations try to control all possible risks associated with their activities, but do not always pay sufficient attention to the risks associated with accounting. Incomplete

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reflection of the facts of business life in accounting and other risks may remain out of control and lead to distortion of financial statements, which will also negatively affect the activities of the organization.

## **2 Materials and Methods**

The legislative and regulatory framework for the organization and setting of internal control in agricultural organizations, scientific works of Russian researchers on the problems and directions of improving internal control in agriculture in market conditions have been studied. The main methods used in this work are the analysis and assessment of factors affecting the effectiveness of the internal control system of the agricultural business in the context of each of its five elements.

## **3 Results and Discussion**

The main purpose of control is to ensure compliance with applicable laws. Many agricultural organizations have an internal control system, since the process of financial and economic activities involves constant control and evaluation of actual achievements, identification of deviations and their elimination, as well as effective use of reserves identified in the course of control. However, not all agricultural organizations pay due attention to the management of the internal control system, as there are no clear regulatory standards for the implementation of these processes [3,4].

Internal control as a mechanism to protect the interests of owners is quite justified, more than that, it also protects the interests of employees, creditors, and business partners.

Setting up a system of internal control in an organization, one should pay attention to the last principle specified in the information of the Ministry of Finance. The costs of implementing internal control should not exceed its effectiveness. Internal control must be organized as an integral ordered system, covering all objects of control at all hierarchical levels [5].

The following methods may be used to establish internal control in an organization:

- the creation of a structural unit with subordination to its management or the appointment of an auditor, who will also report to the head of the organization;
- the creation of a permanent commission.

The choice of the method for organizing internal control largely depends on the structure of the organization, its scale and financial capabilities. It is not always possible to organize a structural unit or introduce an additional position due to financial constraints.

According to the recommendations of the Ministry of Finance, the internal control process in action should ensure the reliability and timeliness of financial statements, and International Standard on Auditing (ISA) 315 speaks about the reliability of reporting. Reliability assumes that users of the financial statements can confidently use the information provided and that it does not contain any material misstatements, i.e. it is reliable. For agribusiness companies this is especially important because of the special nature of production, the orientation of agro-industrial companies to innovation in organizational, technical and technological aspects to maintain competitiveness and relationship with society [6, 7].

The internal control system has different goals, but the main goal is to minimize the risks of the organization. In order to minimize risks, it is necessary not only to competently organize and apply the internal control system, but also to improve it in accordance with the strategic goals of the organization.

In order to minimize the risks of material misstatement, the internal control service should establish their classification (table 1).

**Table 1.** Classification of risks of material misstatement of an entity's financial statements

<b>Types of risk</b>	<b>Risk characterization</b>
Risk of incompleteness	It is characterized by incomplete information specified in the financial statements, which may arise due to insufficient knowledge of accounting rules and legislation.
Periodization error risk	This risk is associated with incorrect distribution of transactions by periods, for example, early closing of transactions on accounts may lead to understatement of the report data, and later overestimate them.
Risk of estimation error	It arises when assets or liabilities in the reporting are estimated incorrectly.
Risk of unreasonableness of accounting records	This type of risk assumes that the reflection of the fact of economic life has no basis. Errors in unreasonableness of accounting records lead to overestimating the financial statements.
Risk of incorrect or inaccurate reflection	The risk manifests itself in case of incorrect transfer of account balance to reporting forms or in case of transfer of these branches, separate subdivisions, which have separate balance.

The risk of incomplete reflection can be eliminated by internal control forces as a result of the planned inventory and the appointment of a responsible person.

The risk of periodization error is usually classified into two groups: early and late closing of accounts. Errors of this kind arise due to late receipt of primary documents. Therefore, it is very important to establish internal control over the document flow in the organization.

It is possible to prevent the risk of unreasonableness of accounting records during regular inventories.

The risk of incorrect or inaccurate reflection distorts the accounting statements of the organization and incorrectly reflects its financial condition.

Consequently, the main role in organizing the system of internal control of agricultural operations is assigned to the management bodies and accounting departments.

ISA 315 presents five elements of internal control. The first in the list of elements is the control environment, it is considered the most important component of internal control, since it is it that touches the general tone of staff's attitude to the internal control system. According to the recommendations of the Ministry of Finance, this element is regulated by the management of the organization. If the management is not interested in the transparency of business processes, then the effectiveness of the internal control system will be low. Management should motivate employees to apply internal controls and to operate effectively.

The next component is the organizational structure. It is very important to take into account the fact that several people can monitor one process, but in the end, proper control is not carried out. In another case, on the contrary, one person may not have time to follow several processes.

An equally important component of the control environment is the personnel policy on the part of the management. The selection of personnel should be based on experience, professionalism, and the ability of additional education on the part of the employee.

The process of risk assessment is a search, assessment of risks, as well as the development of measures to minimize them. In large agro-industrial companies, this

process involves the preparation of a risk matrix, development of risk reduction programs. Changes in legislation, the emergence of new requirements in the field of accounting, the recruitment of new employees, the emergence of new markets for products, company expansion and other processes pose a risk for many agribusiness companies.

The information system as one of the elements of the internal control system is the most time-consuming; it is characterized by large volumes of documentation and records. The effectiveness of the information system depends on many factors, such as the automation of business operations, the competence of the employees of the financial department, consistency in the assessment of the same type of operations, timely registration of transactions, etc.

The following measures are used to ensure compliance with internal control procedures:

- analysis of performance results (comparison of the plan with the fact, management and financial analysis, etc.);
- control over information processing (control over changes in software, arithmetic calculations, correctness of correspondence of accounts, numbering of documents, etc.);
- physical control over assets and processes (video surveillance, inventory of assets and debts, setting passwords for files, computers and corporate networks).

Monitoring of controls is the control of the internal control system itself, assesses its effectiveness and eliminates vulnerabilities.

Testing of the control environment reveals whether an agricultural company has or does not have an internal code of ethics, as well as the internal control department and the person responsible for internal control, and if so, the level of the control environment can be assessed as high.

The entire aggregate efficiency of all elements of internal control, including the formation of reliable financial statements, depends on the effective functioning of monitoring of controls. In addition, the internal control system should act as a mechanism for the economic security of the agricultural business [8].

## 4 Conclusion

The main proposed measures to improve internal control in an agricultural organization are:

1. Improving the efficiency of the risk assessment process by building a Risk Matrix, which is a table or diagram showing the significance of the risk and the likelihood of its occurrence.

2. Creation of a system for storing the knowledge of employees, in order to transfer and use them by new employees.

The procedure for hiring new employees is accompanied by certain difficulties. When changing an employee, a serious problem of adaptation of a new employee arises, associated with the search for information from the previous period. The collection of information must be carried out by employees in easily accessible archives, which will contain job descriptions and rules in the context of each specialist. Disclosure of specific operations, contracts and suppliers will be helpful to facilitate the onboarding of new employees. The transfer of knowledge should be carried out not only electronically, but also train new employees with periodic certification.

3. Permanent monitoring of changes in legislation and the emergence of new methods of accounting. In order to minimize these risks and negative consequences, it is necessary to subscribe to a source with regulatory documents and specialized journals. These measures will allow to respond to changes in legislation in a timely and prompt manner, thus minimizing the risks of distortion of information concerning the law.

4. Development of the Regulation on internal control. This document is approved by order of the head of the organization. It defines the organization of control procedures. When approving this document, it is necessary to specify the rights and responsibilities of inspectors and heads of department, who will exercise control. This procedure will allow the organization to improve its performance by carrying out constant checks, identifying violations and distortions.

The measures proposed to improve the internal control system will help improve the financial and economic activities of agricultural organizations and avoid the risks of material misreporting.

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