Theoretical approach in an Internal Control System: A conceptual framework and usability of internal audit in hotel business.

George Drogalas, PhD Candidate
Department of Business Administration
University of Macedonia
N. Egnatia Str. 156, 54006, Thessaloniki, Greece
Tel:0030 2310 891590, Fax: 0030 2310 891678, E-mail: georgedrogalas@yahoo.gr

Theofanis Karagiorgos, Assistant Professor,
Department of Business Administration
University of Macedonia
N. Egnatia Str. 156, 54006, Thessaloniki, Greece,
Tel:0030 2310 891596, Fax: 0030 2310 891678, E-mail: karagth@uom.gr

Petros Christodoulou, Assistant Professor,
Department of Business Administration
University of Macedonia
N. Egnatia Str. 156, 54006, Thessaloniki, Greece,
Tel:0030 2310 891592, Fax: 0030 2310 891678, E-mail: christod@uom.gr

Artemis Euaggelidou, PhD Candidate
Department of Business Administration
University of Macedonia
N. Egnatia Str. 156, 54006, Thessaloniki, Greece
Tel:0030 2310 891590, Fax: 0030 2310 891678, E-mail: artemis@uom.gr

Abstract: All auditing information is established as an essential mean for the exact management of any business economic resources. Within the framework of modern business world, the role of an internal control system is catalytic since it is regarded as a source from which core abilities are given or drawn and are subsequently transformed into competitive advantages.

The vital role of internal audit, especially in hotel business has only just commenced. However, the necessity which issues from the administration, for distinguished management of the available resources, incalculable expenses, limitation and evasion of misconduct, imposes internal audit as a priceless support in the hotel business management effort.

The purpose of the present paper is to examine in a theoretical level the meaning of internal audit and demarcate its provinces in the contemporary sector of hotel enterprises.

The results of this extended literature review indicate that, internal audit is a knowledge field, which approaches the shortcomings and recommends realistic solutions in the extremely fluid business environment.
1. Introduction

As a concept, Internal Control is distinguished by its scope and its high level of the services offered. Through an extended literature review, there will be an attempt to approach theoretically its catalytic contribution to the extremely fluid business environment. The purpose of this paper is to highlight the resulting bunch of benefits that occur as a result of the role that Internal Control (Internal Audit) plays both from the viewpoint of the prevention of shortcomings as well as the limitations posed by the negative influences in business.

Within the framework of this vital role of internal audit, this paper is structured in three sections. In the first section, we make reference to the conceptual framework of internal control through a grid of its definitions. In the second section, internal control is mentioned as a catalytic element that offers additional value to the modern hotel business. Finally, we analyze the importance and the crucial role of internal control in each field of operation.

2. Theoretical approach of the term “Internal Control” and “Internal Control System”

In the modern business world, the term “Internal Control” is being used to refer to two basic concepts: the Internal Control System and the Internal Control itself.

2.1. Internal Control System

The Internal Control System refers to an organized amalgamation of functions and procedures, within a complete system of controls established by the management and whose purpose is the successful function of the business (Cheung, 1997). The Internal Control System is all the methods and procedures followed by the management in order to ensure, to a great extent, as much successful cooperation as possible with the director of the company, the insurance of the capital, the prevention and the detection of fraud, as well as the early preparation of all the useful financial information (Meigs, 1984; Papadatou, 2005). According to Cook and Wincle (1976), the Internal Control System resembles the human nervous system which is spread throughout the business carrying orders and reactions to and from the management. It is directly linked to the organizational structure and the general rules of the business (Cai, 1997).

2.2. Internal Control

The term was adopted by the Anglo-Saxons (“Internal Auditing”) and refers to the unit of Internal Control which aims at the evaluation of the sufficient functioning of the Internal Control System, that is the secondary functions (Controls) and suggests that there is room for improvements in cases where weaknesses are being discovered (Financial Postman magazine, 2004).

What is indicative of the importance of Internal Control is the sum of the definitions that have been given for this term.

According to the AICPA, (1963) a system of internal control extends beyond those matters which relate directly to the functions of accounting and the financial statements. In addition, based on the ASOBAC (Committee on Basic Auditing Concepts, 1973), internal control is a systematic procedure which will lead to evaluate the degree of correlation between those established criteria and the real results of the business.

Internal Control, as defined from the APC (Auditing Practices Committee, 1980), is an independent examination and certification from an inspector appointed by the business to control the finances according to the legal framework established each time.

Furthermore, according to Miller and Bailley (1989), internal control is a systematic review and a subjective investigation of one element and encompasses the verification of the specific information as these are determined from the general practice.

The internal control helps the company to achieve its goals using a systematic approach of assessing the effectiveness of handling dangers (IIA, 1999).
Internal control, as defined from the Hellenic Institute of Internal Auditors (H.I.I.A., 2004) is an independent, objective, adequately designed and organized procedure, which through the technical and the scientific approaches, assess how adequately the system of internal control functions. From the above definitions, it is clear that the internal control is not just an one-sided tool for controlling the order and rightness of certain situations, but it is a method of detecting the value added up to a company, achieving the index of effectiveness and profitability of the company (Nagy and Cenker, 2002) (Goodwin, 2004). Besides, the purpose of this control is the intentional, the programmed and focused effect of the company on the current situation, so as this situation to be reformed in the future and become the one that ought to exist (Mcnamme and Mcnamme, 1995). The deviation between the already achieved and the programmed situation can also become possible through controlling the parameter of correct handling of danger situations.

Bounton and KellerWalter (1996) claimed that the objective purpose of Internal Control is, on the one hand, the allowance of specific and high level of services offered towards the management, and on the other hand, the allowance of assistance towards the members of the organization for the most effective practicing of their duties. The Internal Control Systems are being implemented in businesses as tools that add up value to the company. In this way, we can achieve a systematic approach towards the most effective operation of the organization, as a unity (Schleifer and Greenwalt, 1996).

Finally, as mentioned by the COSO report (Committee of Sponsoring Organizations of the Treadway Commission, 1992), Internal control is defined as a procedure which offers fundamental security to the business concerning the credibility of financial affairs. The report defines internal control and describes a framework for internal control. But the difference of this report is that it also provides criteria for the management to utilize so as to evaluate controls. (Aldridge and Colbert, 1994)

3. The field of hotel businesses in Greece

The year of 2004 has been a landmark in the field of the country, as looking forward to the Olympic Games, important investment plans were completed. These plans not only upgraded the existing hotel infrastructure, but also created new hotel units of the highest standards.

Based on the evidence of the Hotel Chamber, the hotel units that have operated in the whole country in the year of 2004 have come up to 8,999 compared to 6,423 in the year of 1990 (2,476 new hotel units in a time period of 15 years). Table 1

As far as the potentiality for allocation of all these hotel units of the country is concerned, most of them are 3rd category’s hotels, whose number has risen to 4,473 in the year of 2004 (50.3% share of the total). 4th and 5th category’s hotels follow next with 1,731 units (19.5% share) and the 2nd category’s hotel with 1,660 units (18.7% share). 1st category’s hotels were far fewer in 2004 (896 units), while even less fewer were the Premium Quality hotels (139 units). Table 1

Concerning the geographic allocation of the total of hotel beds in the country, according to the evidence obtained in 2004 from the total of 668,271 beds available, in the prefecture of Crete there were 140,502 units in operation (21% share) Table 2.

In order to obtain a more thorough understanding of the field of hotel businesses tables 1 to 3 are presented in the appendix where the most important characteristics that shape today’s hotel businesses in the Greek region are shown.

4. Internal Control in the hotel business

The service of internal control is considered to be the security belt of the business for avoiding either the involuntary or the intentional release of
information concerning any form of useful first hand stock as well as the avoidance of loss of income from misuse or from any errors in operation (Papastathis, 2003).

Within this framework, a complete Internal Control System involves (Mara, 1991):

1. the verification of incomings and expenditure ‘per field of operation’
2. the monitoring of expendable material from the market and their entrance in the hotel until the point of their final consumption
3. the control of monitoring the warehouse where expendable materials and non-expendable goods are stocked
4. the monitoring of the financial operation
5. other controls, according to the bureaucratic structure of the hotel business.

**Control of the main fields of operation**

By the term ‘fields of operation’ of a hotel we mean those sections of the hotel in which the production procedure of the tourist goods and services as well as their availability takes place with the purpose of achieving profit.

The main fields of utilization within a modern hotel unit are:

- the bedrooms
- the bar
- the buffet
- the restaurant

**Controlling the field of bedrooms**

The field of bedrooms is considered the most important field as it ensures the greatest percentage of profit for the hotel business. As a consequence, the control of the field of bedrooms has paramount importance for achieving the goal of successful internal control.

The control of the income is achieved through the research of the following:

- the number of rented rooms
- the number of people staying overnight
- the application and the correct completion and monitoring of the invoices
- the confirmation of invoices for the avoidance of mis-numbering and of errors in the lodging of debts and credits

The basic representative evidence (Mara, 1991) for the correct application of the control of income from the bed units is the following:

- the book of arrivals and departures (door book)
- the book used for keeping the customers’ accounts (MAIN-COURANTE)

The control of the MAIN-COURANTE (Karaxontzitis, 1989) is the basic auditing procedure of the incomes derived from the bedroom units and is implemented through the following:

- the transfer of the customer’s evidence from the day before
- the control of correct entry of the customers that have arrived
- the control of correct entry of the customers that have departed
- the comparison of the electronic file which monitors the bedrooms with the book keeping and the costumers’ crediting.

Comparison of the evidence that has been entered in the MAIN-COURANTE system with those that have been entered in the personal accounts of the customers is the main goal of this control.

**Control of the field of the restaurant**

The restaurant is a field that demands specialized staff and the right equipment and the one which significantly influences the satisfaction of the customer’s needs (Sotiriadis, 1999). Within this framework, the field of the restaurant is connected to:
the field of the bar where drinks are available
the field of the buffet, where the confectionary is offered as well as
the other fields of operation which are of secondary importance

As soon as the customer makes an order, the waiter gives out an ordering bill in three copies out of which one remains in the management, the second is handed in the section of the food preparation and the third is handed into the sales supervisor.

The control of the incomes of the restaurant includes:
- the control of the ordering bills of the waiters
- the control of the entries of the availabilities to the restaurant’s bills
- the control of whether those sales with credit have been entered to the corresponding customers’ cards and whether those sales which have been made in cash have been entered to the daily cards of the customers
- the control of the entries of the restaurant’s credit bills which correspond to the papers and the debit bill shares of the MAIN-COURANTE customers
- the control of the hospitality book and of the cash received by the members of the staff according to the organization of the hotel unit
- comparison of the sum of the restaurant’s income with the total charge to the customer’s list

Control of the field of the buffet

The charges for breakfast are distinguished into three cases:
- When the breakfast that customers have is obligatory the charge for the customer’s portion of food is made irregardless of whether the customer had breakfast or not
- When the breakfast that customers have has been agreed but it is not obligatory. Likewise, in this second case, the charge in the customer’s portion of food is made irregardless of whether he/she has had breakfast or not, but once the customer has been properly informed about it.
- When the breakfast that customers have is free of charge. In this third case, the control is succeeded through the receipt.

The control of the entries of the buffet does not present some special difficulty.

The control of the income of the buffet includes:
- Comparison of what is written on the order list and what is written on the bill
- Control of the entry of the right amount of money to the bill and to the list of the restaurant’s incomes
- Control that the charge was entered correctly to the MAIN-COURANTE

Control of the field of the bar

The bar constitutes an integral part of the hotel unit. The bar is considered a special field of operation, in which the specialized product offered to customers includes (Laloumis, 1998):
- The material itself, the alcoholic drinks, the soft drinks, the ice cream, the snacks
- The era of where the bar is located, the decoration, the arrangement, the music
- The human relationships

As far as control is concerned, the bar is considered one of the most difficult auditing procedures. A bar within a restaurant operates in one of the three following ways:
- The owner is also a bartender at the same time so as not to have any other people working at the bar.
The bartender operates the bar for his account but there is also another employer who keeps the owner informed. The bartender operates the bar for the account of the hotel business. Each and every one of these ways of operation demands a different system of Internal Control System (Mara, 1991).

The management of the bar’s income money is similar to this of the procedure followed in the restaurant. Along with the order placed, there is also a bill of the goods purchased which is issued and which accompanies the goods offered. When the customer wishes to leave, the bills are added up and he/she pays in cash the sum of money. At the end of the day, the bills are entered and added up in a list of daily incomes and expenditures. The money is handed to the cash point and the debit bills to the book where a list with all the customers’ bills is kept (MAIN-COURANTE).

The control of the income money of the bar includes:

- The control of whether those sales with credit have been entered to the corresponding customers’ cards and whether the sales that have been made in cash have been entered to the daily customers’ cards
- The control of the entries of the credit bills of the bar to the corresponding lists and to the customers’ debit portions
- Comparison of the sums of the accounts with the entries on the complete list
- Comparison of the sum of cash of the complete list with the sum of money received at the central cashier’s desk
- Comparison of the sum of the restaurant’s income money to the total charge presented at the customers’ list.

Control of the warehouse’s consumable and non-consumable material

Control of the warehouse’s consumable material

The goods that are intended to be expended to the different departments of the hotel business are controlled. Within this framework the following actions are taken (Lekarakou, 1994):

- Control of the import invoices and comparison with the actual quantities of items that exist in the warehouse
- Control of the export invoices and comparison with the actual quantities of the items that exist in the warehouse
- Control of the actual quantities that exist in the warehouse with the evidence on the cards with the goods that exist in the warehouse
- Control of keeping the “safety limit in the quantity of the items that exist in the store” for avoiding having stock.

Its purpose is to monitor the distribution of the goods, in relation to their quantities and their prices.

The control of the quantities has to do also with the cases in which there is variation or in the cases in which there is some shortage, whereby the possibility of destruction and damages of goods is controlled and whereby the limit of supplies of such goods is being re-programmed. The control of the prices is achieved through an investigation on the basis of the prices stated on the bill, the competition in process of the supplies.

Control of the warehouse’s non-consumable material

The control of the non-consumable material in the warehouse does not present any special handling and procedures and is achieved on the bases of the cards of the products and the inventory of the control mechanism.
Control of consumable material

Counting of material and using financial indexes

The goods that are intended to be consumed are controlled. In this way, their usage is quantified. To be more specific, the control procedure includes the following stages:

- The control division counts the exports of the warehouse towards the different fields of utilization,
- The total of the primary material that each division uses is being controlled,
- The correspondence of these products with the sales that have been actually made is being controlled,
- There is an accounting census of the shares
- There is a comparison of the materials that have been used with those that should have been used.

Control of the “value” of the consumable material

The procedure mentioned above is time-consuming and therefore the control of the value of the expendable material is suggested, whereby the value of the material which have been received from every division is compared with the returns that have been achieved during that time period.

Control per operation and stage

The main aim of the control is the monitoring of the expendable material throughout the duration of:

- The supply of the material, whereby the competitive prices, the quality of the goods in relation to the price and the different costs, are controlled.
- The receipt of the material, whereby the quality and the quantity of the material that are received from the supply division are being controlled
- The storage of the material, whereby the damages, the alterations and the correct renewal of the supplies are controlled
- The export of the material, whereby the correct entry of the goods that are exported from the store and generally the keeping of the procedures that relate to the exports are controlled.

Control of the financial operation

The control includes those actions taken that relate to the funding of the hotel unit, that is, with the capital which is necessary for its smooth running. The danger of the lost capitals and the credit danger appear to be the determining factors from its viability.

Within the framework of limiting the danger of correct constitution of financial affairs, the following actions are in effect:

- Controls of the procedures, whereby a check is held to ensure whether the investments are always in accordance with the approved investment policy.
- Controls of the evaluations, whereby the cost of the investments with the running values is mainly compared as well as a check of the “cash point”, the “deposits” and the “loans”.
- Controls of the availabilities, the bank deposits and loans, during which their frequent update and the confirmation of other ones is necessary.

Furthermore, Internal Control enables the hotel management to examine whether the right strategic of financial management is followed.

As far as the accounting department is concerned,

- The person responsible for the accounts office on the one hand controls the expense allocation to different centers of cost and production while on the other hand ascertains the right calculation of short-term results.
• The person responsible for the entries fulfills the demands of the accounting picture of the fact, whereas the internal inspector assesses its effectiveness.

Other controls and special controls

Control of the computerization
The development and maintenance of the most suitable computerization systems, is obligatory to be conducted on the basis of a specific plan. Within this framework the hotel unit conducts the following control measures:

• Control of the computerization systems, whereby it is discovered whether there is the right know-how in terms of the procedure of the finance computerization
• Control of data processing, whereby it is discovered whether there is a correct input and output of the data
• Control of the security systems of the computerization, whereby it is discovered whether the security copies are kept safely and whether there is a regulation for an emergency.

Completion and retrospective on the issue of Control
The classification of the conclusive evidence is performed with clarity, completion and logical sequence. In this way the following are made easier:

• Locating the most neuralgic points of the control procedures
• Calculating the time and the cost that was necessary for the completion of each control
• Locating of the people responsible for carrying out each important stage of the control

5. Conclusions
The harmonic operation of the modern hotel unit demands the adoption of Internal control as a means of assistance for the effective completion of the goals set by the modern businesses. The Internal Control moves within a greater scope of management philosophy and of practical application, and adds up value, offering at the same time a systematic scientific approach on the assessment and the improvement of the effectiveness of the hotel businesses.

The Internal Control, within the framework of its application in the hotel businesses, consists of a sum of procedures that cover the whole range of its actions, and is catalytic to the location of the weaknesses in management, to the prevention and the suppression of unexpected events. By adapting the grid through which we can approach the essential functional areas of the business the functional weaknesses are pointed out.
### Table 1: Greek Hotels

<table>
<thead>
<tr>
<th>YEAR</th>
<th>AA</th>
<th>A</th>
<th>B</th>
<th>G</th>
<th>D &amp; E</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>45</td>
<td>470</td>
<td>1571</td>
<td>2722</td>
<td>1615</td>
<td>6423</td>
</tr>
<tr>
<td>1991</td>
<td>46</td>
<td>515</td>
<td>1674</td>
<td>2840</td>
<td>1572</td>
<td>6647</td>
</tr>
<tr>
<td>1992</td>
<td>46</td>
<td>560</td>
<td>1773</td>
<td>2910</td>
<td>1567</td>
<td>6856</td>
</tr>
<tr>
<td>1993</td>
<td>51</td>
<td>629</td>
<td>1896</td>
<td>2923</td>
<td>1636</td>
<td>7135</td>
</tr>
<tr>
<td>1994</td>
<td>52</td>
<td>595</td>
<td>1294</td>
<td>3592</td>
<td>1637</td>
<td>7170</td>
</tr>
<tr>
<td>1995</td>
<td>60</td>
<td>621</td>
<td>1328</td>
<td>3719</td>
<td>1659</td>
<td>7387</td>
</tr>
<tr>
<td>1996</td>
<td>62</td>
<td>656</td>
<td>1362</td>
<td>3750</td>
<td>1647</td>
<td>7477</td>
</tr>
<tr>
<td>1997</td>
<td>65</td>
<td>681</td>
<td>1405</td>
<td>3615</td>
<td>1628</td>
<td>7394</td>
</tr>
<tr>
<td>1998</td>
<td>72</td>
<td>728</td>
<td>1449</td>
<td>3870</td>
<td>1666</td>
<td>7785</td>
</tr>
<tr>
<td>1999</td>
<td>77</td>
<td>745</td>
<td>1456</td>
<td>3907</td>
<td>1671</td>
<td>7856</td>
</tr>
<tr>
<td>2000</td>
<td>79</td>
<td>766</td>
<td>1474</td>
<td>3967</td>
<td>1650</td>
<td>7936</td>
</tr>
<tr>
<td>2001</td>
<td>90</td>
<td>816</td>
<td>1543</td>
<td>4189</td>
<td>1646</td>
<td>8284</td>
</tr>
<tr>
<td>2002</td>
<td>97</td>
<td>847</td>
<td>1579</td>
<td>4329</td>
<td>1658</td>
<td>8510</td>
</tr>
<tr>
<td>2003</td>
<td>104</td>
<td>870</td>
<td>1613</td>
<td>4403</td>
<td>1699</td>
<td>8689</td>
</tr>
<tr>
<td>2004</td>
<td>139</td>
<td>896</td>
<td>1660</td>
<td>4473</td>
<td>1731</td>
<td>8899</td>
</tr>
</tbody>
</table>

Source: Hellenic Chamber of Hotels

### Table 2: Geographical Distribution of the Greek Hotels (2004)

<table>
<thead>
<tr>
<th>Prefecture</th>
<th>Hotels</th>
<th>Rooms</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sterea</td>
<td>1260</td>
<td>93654</td>
</tr>
<tr>
<td>Peloponnesus</td>
<td>688</td>
<td>44871</td>
</tr>
<tr>
<td>Ionian</td>
<td>853</td>
<td>80157</td>
</tr>
<tr>
<td>Epirus</td>
<td>244</td>
<td>10797</td>
</tr>
<tr>
<td>Aegean</td>
<td>404</td>
<td>21858</td>
</tr>
<tr>
<td>Crete</td>
<td>1492</td>
<td>140502</td>
</tr>
<tr>
<td>Dodecanese</td>
<td>988</td>
<td>112990</td>
</tr>
<tr>
<td>Cyclades</td>
<td>888</td>
<td>39458</td>
</tr>
<tr>
<td>Thessaly</td>
<td>553</td>
<td>26706</td>
</tr>
<tr>
<td>Macedonia</td>
<td>1439</td>
<td>91797</td>
</tr>
<tr>
<td>Thrace</td>
<td>90</td>
<td>5481</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>8899</strong></td>
<td><strong>668271</strong></td>
</tr>
</tbody>
</table>

Source: Hellenic Chamber of Hotels

### Table 3: Overnight Stay and Complement of Greek Hotels

<table>
<thead>
<tr>
<th>Year</th>
<th>Overnight Stay</th>
<th>Complement %</th>
</tr>
</thead>
<tbody>
<tr>
<td>1994</td>
<td>52891918</td>
<td>60,6</td>
</tr>
<tr>
<td>1995</td>
<td>51294196</td>
<td>56,3</td>
</tr>
<tr>
<td>1996</td>
<td>47294196</td>
<td>54,4</td>
</tr>
<tr>
<td>1997</td>
<td>53364507</td>
<td>58,4</td>
</tr>
<tr>
<td>1998</td>
<td>56549442</td>
<td>61,1</td>
</tr>
<tr>
<td>1999</td>
<td>60256902</td>
<td>63,5</td>
</tr>
<tr>
<td>2000</td>
<td>61302903</td>
<td>65,0</td>
</tr>
<tr>
<td>2001</td>
<td>58832656</td>
<td>62,7</td>
</tr>
<tr>
<td>2002</td>
<td>55840611</td>
<td>61,7</td>
</tr>
<tr>
<td>2003</td>
<td>54502104</td>
<td>51,7</td>
</tr>
</tbody>
</table>

Source: National Statistical Service of Greece