# CHAPTER II
# LITERATURE REVIEW

## 2.1 Internal Control

Control is a concept that is relevant to all systems inherent in a company's accounting information system. The control process is broadly one of the basic functions of management (Minztberg, 1975). Management is obliged to build and implement internal control in the entire set of organizational systems and information systems to ensure that the activities of the organization run as planned.

The effect of internal control in an organization will assure management in achieving organizational goals. Internal control is also a measure of the level of control and internal security of the organization, so it is also called the internal control structure or internal control structure. Structure means that the internal control function is inherent in each company organizational structure. If the internal control structure runs well and effectively then all activities, organizational resources, and data can be monitored and controlled.

Internal control is a process that can effectively works when its supported by organizational leadership, management, and all personnel in the organization (Tuty, 2012). Internal controls designed by organizational management have the objective of achieving effectiveness and efficiency of the organization's operational activities, financial statement trust and compliance with organizational policies and regulations.

According to Romney and Steinbart (2015), the definition of internal control is a process that is implemented to provide a reasonable guarantee that the control objectives can be achieved. Hall (2016) states that internal control is a policy, practice, and procedure used by an organization to achieve several objectives such as protecting company assets, ensuring the accuracy and reliability of accounting information, increasing entity efficiency, and measuring compliance with management policies. Messier (2016), also states that internal control is a mechanism/system designed by the management of an entity to provide reasonable guarantees to achieve the objectives of the entity. 5 components underlie internal control based on the COSO control framework (Warren, Reeve, & Duchac, 2015). These components include:

1. Control Environment

   According to Romney and Steinbart (2015), the control environment gives color to the organization. Environmental control forms the foundation for an organization's internal control. There are several principles in the control environment, including:

   a. Integrity and ethical values, integrity and ethical values need to be owned by the company such by company leaders and company employees to be able to perform internal controls within a company.
   b. Board of Directors and Audit Committee, action and awareness of board of directors and audit committee for achieving good internal control.
   c. Management's Philosophy and Operating Style, a company's operating style and management philosophy will influence policies, procedures, communication, and decisions.

d. Organizational Structure, the organizational structure provides a framework for planning, implementing, controlling and monitoring company activities.

e. Human Resource Policies and Procedures, personnel policies in treating employees need to be considered in creating a good control environment.

2. Risk Assessment

A risk assessment by company management is needed to be able to know the right actions that need to be taken in dealing with possible risks and changes that might affect the company's internal control. Risk assessment can pay attention to the characteristics of the risk itself so that it can know the overall risk.

3. Control Activities

Activity control is a policy, procedure, and regulation that provides reasonable guarantees where control objectives can be obtained and responses to risks can be obtained. There are several control activities including:

a. Provision of appropriate authorization for company activities

b. Separation of responsibilities

c. Changes in management control

d. Securing assets, recording, and data

e. Procedure for proof and security.

4. Information and Communication

Communication needs to be done to obtain information and convey information about the company. This information is also needed in the company's internal control. There are 3 principles of information and communication including:

a. Obtain accurate and relevant information in support of internal control.

b. Deliver internally about company information which can support internal control.

c. Deliver matters regarding relevant internal controls to third parties.

5. Monitoring

Internal controls must be monitored periodically, evaluated, and modified if necessary. Monitoring of internal controls is carried out to see the effectiveness of the internal control process and possible fraud. Monitoring can be seen from the system used and the behavior of employees at work.

## 2.2 Good Worker Performance

According to Prawirosentono (2008), explained that performance is the result of work that completed by a person or group of people in an organization, following their duties and responsibilities to achieve organizational goals legally, not violating legal provisions and by morals and ethics.

According to Miner (2007), stated four aspects of performance, namely as follows:

1. The quality produced, explains the number of errors, time, and accuracy in performing tasks.
2. The quantity produced, concerning how many products or services can be produced.

3. Working time, explain how many absences, delays, and the duration of work that has been undertaken individual employee.
4. Cooperation, explain how individuals help or inhibit the efforts of their coworkers.

## 2.3 Job Training

Job training is the whole activity to give, obtain, improve, and develop work competency, productivity, discipline, attitude, and work ethic at a certain level of skill and expertise by the level and qualifications of the position or job. Job training is one way to improve quality and develop a career in the workforce.

Job training is very important to develop the skills of employees, especially from the performance of employees that to be more improved than the standards from the company. According to Simamora (1999), through training carried out all efforts to improve the performance of employees in the occupation they currently occupy. Training is usually to help employees correct weaknesses in performance.

## 2.4 Job Description

“Job Description is the result of analysis of work as a series of activities or processes to gather and process information about work" (Rivai, 2009). "Job description mentions the duties and responsibilities of a job. Mentioned what was done, why it was done, and where it was done, and briefly how to do it" (Jackson, 2001).

Almost the same definition is proposed by Gary Dessler (2004) stated that "A job description is a written statement about what must be done by the worker, how the person does it, and how the conditions work". Job description indicators according to Malayu S.P Hasibuan (1995), mention indicators of job descriptions, in general, that is:

a. What to do

   Employees understand the duties, authority, and responsibilities carried out by an employee to carry out company organization activities

b. Responsible

   Employees can carry out the tasks given to him and the ability to pay to carry out the responsibilities given by the company.

c. Skills or education needed

   Employees understand that each available position requires what skills and education are needed to occupy the position.

d. Condition

   An employee who sits in a position must be able to see the situation, and understand what must be done in the internal organization and in the external organization

e. The type and quality of people needed for the position

   Employees who will hold office must meet the criteria determined by the company.

## 2.5 Inventory

Inventories are goods that are owned by companies, both in the form of retail or wholesale businesses, and these goods have been purchased to be owned in good condition and ready to sell. While for manufacturing companies, inventories are divided into 3 categories, namely raw materials, work in process and finished good (Skousen & Stice, 2004). Inventories are assets that are intended to be sold in the normal course of business and are crucial in the operation of a company. Inventory is a current asset with a big quantity in a trading and manufacturing company (Sartono, 2001).

Based on the opinion of experts, it can be concluded that inventory is a company's assets that occupy an important position in a trading company or manufacturing company. Also, we know that service companies do not have any inventory. Trading companies only have merchandise inventory but the manufacture companies have 3 types of inventory, namely raw material inventory, work-in-process inventory, and finished goods inventory that are ready for sale.

## 2.6 Inventory Control

Inventory control aims to keep the company from running out of inventory which will disrupt production activities of the company. Besides, inventory control also helps companies to not over in storing the inventory. Inventory control can also avoid small-scale purchases because this will result in ordering costs being too large (Assauri, 2004). It can be concluded that the purpose of inventory control is to obtain the right quality and quantity of materials or goods that are available at the time required with minimum costs for company profits or interests. There are 3 methods of inventory control:

1. Economic Order Quantity (EOQ)

   This method is based on the calculation of the optimal number of orders, for the efficiency of the total cost of ordering, warehousing costs, and costs due to lack of inventory. Ordering fees include all costs associated with processing purchase transactions. Warehousing costs are costs associated with storing inventory activities. Costs due to lack of inventory are costs arising from lack of inventory, such as lost sales opportunities or production delays.

2. Material Requirements Planning (MRP)

   MRP aims to reduce the level of inventory needed by scheduling production, not estimating needs. By using this schedule and manufacturing specifications for each product, the company can determine the number of raw materials, spare parts, and other production equipment, as well as the time point of purchase of the items needed. So using the MRP system can reduce uncertainty about the right time to buy raw materials.

3. Just In Time (JIT)

   JIT seeks to minimize warehousing costs as well as costs due to lack of inventory. The JIT system is characterized by direct delivery of raw materials, equipment, and other goods to locations that require the shipment of these goods, rather than sending large quantities that are occasionally made to reception centers and storage facilities such as warehouses. so a company that uses the JIT system will have several reception points, each of which is assigned to take delivery of goods needed by a nearby work center.