



Evaluation of internal audit practice in afar region: Evidence from some selected public sector offices

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Abstract

This paper examined whether internal auditors perform their activities in such a way that provide an independent, objective and consulting activity designed to add value and improve an organization's operations. In order to investigate the findings; the researchers used a sample of 10 Afar regional public sector offices in which total of 50 questionnaires were distributed. The researchers also used purposive sampling technique and collected primary data through questionnaire and interview. The responses gotten were encoded in to the SPSS 16.0 and analyzed using descriptive approach. The main findings of the study were that the scope of internal audit was restricted only to financial activities, there is no suitable environment for independency of internal auditors, policy for hiring and training, experience, professional certification of internal auditors and management support to internal audit is not good except compliance of audit work and fairness of budget allocation, there is no clear and understandable internal audit charter,. In short internal auditors are not providing as they are expected to increases the operational efficiency of regional sector offices. The management needs to consider the value of internal audit function in the achievement of organizational objectives and better to consider internal audit findings and made commitment to strengthen the department.

Keywords: internal audit, internal audit function, value adding, consulting, independent

1. Introduction

Internal auditors' roles include monitoring, assessing, and analyzing organizational risk and controls; and reviewing and confirming information and compliance with policies, procedures, and laws (IIA, 2010).

To achieve organizational objectives, internal audit plays a great role by providing value-adding services (Mihret and Woldeyohannis, 2007; Mihret and Yismaw 2008) ^[17, 15]. Effective IAFs help an organization to accomplish its key objectives by bringing a systematic, disciplined approach to evaluating and improving the effectiveness of governance, risk management and control processes (Rossiter, 2007).

Internal auditors deal with issues that are fundamentally important to the survival and prosperity of any organization. Unlike external auditors, they look beyond financial risks and statements to consider wider issues such as the organization's reputation, growth, and its impact on the environment and the way it treats its employees (Pilcher, 2011).

It is clear that inadequate internal control can expose the organization to various identifiable risks, such as waste of organization's available resource, fraud by employees, lack of control over asset and further if it is in governmental offices it results loss of public trust. Internal auditors usually assist management in ensuring that there is proper internal control system in place and the operations of the enterprises is running in effective and efficient manner (Fadzil F.H., Haron H. and Jantan M. (2005) ^[7].

Even though the above mentioned points are really expected from internal auditors in helping the management and the organization towards achieving its short and long term objective, in the context of Ethiopia in general and specifically in Afar region internal auditors seems to be not contributing that much.

As per the knowledge of the researchers as indicated reviewed on the literature part there is a lot of studies conducted relater to internal audit, more specifically how internal audit add value, independency of internal auditors,

perception of managements toward internal auditors. In Afar public sector offices, there are no comprehensive studies that examine the practice of internal audit. Therefore, accordingly, the general objective of this study is to evaluate the practice of internal audit in the in Afar region in some selected public sector offices to provide suggestions for improvements on problems available.

The specific objectives of the study are:

1. To identify the availability of clear and understandable internal audit charter.
2. To examine and scope and extent of internal audit being practiced in the regional bureaus.
3. To asses independency of internal auditors in the regional bureaus.
4. To find out the factors that has an influence on internal audit practice, and to forward solutions.

2. Literature Review

2.1 Definition of Internal Audit

Traditionally internal auditing was considered to be restricted to the examination of books of accounts of the organization with the view of ascertaining whether they correctly record the transaction. In fact, a good internal control system should have an integral part. The modern concept of internal auditing shows that internal auditing has moved significantly ahead by shouldering greater responsibilities to become one of the important management control devices (Basu, 2007).

The Institute of Internal Auditors of UK and Ireland defines Internal Audit as:

"Internal Auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes" (IIA, 1999).

2.2 Scope of Internal Audit

The scope and objective of internal audit vary widely and are dependent up on the size and structure of the entity and the requirements of its management (Basu, 2007). In contrast to external audit which mainly focuses on assessing historic financial data, internal audit function encompasses the adequacy and effectiveness of governance, risk management and internal control processes in identifying and responding to all the risks facing the organization (ECIIA, 2005) [6].

2.3 Auditors Independence

Independence can be generally defined as freedom from dependence on, or influence or control by, another person, organization, or state. Internal auditors work for, and primarily report to, the audited entity. For internal auditors, independence is the freedom from conditions that threaten the ability of the internal audit activity or the chief audit executive (CAE) to carry out internal audit responsibilities in an unbiased manner. Independence permits internal auditors to render the impartial and unbiased judgments essential to the proper conduct of engagements (INTOSAI, 2004).

Auditor independence can be assessed in two ways, that is, independence in mind and independence in appearance (IFAC, 2004).

2.3.1 Independence in Mind

Independence in mind is the state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism (IFAC, 2004). Mihret and Yismaw (2007) [15] point out that independence of paramount value in providing effective internal audit service to the management, for it affords an atmosphere of objective and uninhibited appraisal and reporting of findings without influence from the units being audited; and independence of individual auditors is essential to the effectiveness of the IAF.

Appah (2011) also noted that, Independence in mind requires the auditor to be free from bias, personal interest, prior commitment to an interest or susceptible to undue influence. This means that an average auditor possessing the requisite state of mind will act in the correct way that will not affect the professional duty of due care and skill.

2.3.2 Independence in Appearance

According to Nur, Abdul and Hafiz (2005), independence in appearance refers to the public's or other's perceptions of the auditor's independence. Philmore *et al.*, (2006) also stated that, Independence in appearance refers to the subjective state of that relationship as perceived by clients and third parties. Similarly, Eilifsen (2009) mentioned that Independence in appearance relates to a third part's perception regarding the auditor's independence. If the third party doesn't think that the auditor appears to be independent, even though the auditor is independent in his mind, the third party don't trust the auditor due to certain circumstances or relationships which are incompatible with independence and the promise of the assurance that the auditor is supposed to provide is lost.

3. Research methodology

3.1 Research design

This research used mixed approach, quantitative research methods particularly survey method and qualitative methods

particularly interview and documentary analysis to assess the practice of internal audit in Afar region public offices.

3.2 Sources of Data

Under this study, there were two sources of data collection: primary and secondary sources. The primary source of data is the collection of firsthand information using interview and questionnaires that appropriately suit the study based on the researchers assumed perceptions. Just by its name, secondary data is information which have been processed and stored.

This information came from official documented data, journals articles, newspapers, text books and from appropriate websites. The primary sources used as the main empirical data for the analysis, while the secondary source used to describe theories and in the literature review.

The following section highlights the collection technique used to gather data. Questionnaire Interview and document, in which questionnaire is the main sources of evidence to conduct the study.

Questionnaires: As mentioned above in this study a self-made questioner has been used and distributed among internal auditors in some selected public sector offices in Afar region to examine their audit practice. The questionnaire was distributed among 50 internal auditors 'the respondents are all internal auditors, audit division head, human resource director and finance director from 10 regional bureaus. In addition, general managers of the sample organization were interviewed for validating conclusion of the data gathered using questionnaires and document review.

Documentary Sources: A review of internal audit reports, directives from the regional government and procedural manuals serves as documentary sources.

3.3 Sampling Techniques

The researchers purposively decided that it is possible to collect data from 10 bureaus from total of 36 bureaus because those have higher budget balance and organized audit division relatively from others. For under taking the study 50 questionnaires were distributed, the respondents are all internal auditors, audit division head, human resource director and finance director in the selected bureaus as a sample. In addition, general manager of the organization were interviewed for validating conclusion of the data gathered using questionnaires and document review. Further the researchers believe that the selected unit can be considered as representative of the population due to the existence of commonalities in policies, procedures, organizational context of most public sector entities and similar internal audit manual is used by public bodies in the region.

3.4 Method of data presentation and analysis

To present the raw data gathered from the target participants through questionnaires, the researchers used SPSS. Therefore, the quantitative data from the questionnaires was described by using table, percentage and chart. Further, data collected from interview were transcribe in to word document and analyzed through triangulating with data collected through questionnaire and documentary sources resulted from extracting internal audit manual of the region and internal audit report of regional offices.

4. Result and Discussion

4.1 Availability of audit charter and Scope of Internal Audit

4.1.1 Availability of internal audit charter

Table 1: Availability of internal audit charter

No	Particulars	N	Mean	S. deviation
1.	There is internal audit charter showing duties and responsibilities of auditors.	50	2.01	1.211
2	The audit charter is clarity and understandable	50	2.21	1.011
3	Valid N (listwise)	50		

Source: Survey data, 2017

The attribute standard No. 1000 as per the IIA states that the purpose, authority, and responsibility of the internal audit activity should be formally defined in a charter, consistent with the standards, and approved by the board. Despite the fact that, as indicated on the table 1, the mean response of two questions regarding to the availability of internal audit charter were more than 2 and the standard deviation were also more than 1.00 Therefore, internal auditors in Afar region public sector offices disagreed with existence of audit charter in addition On the other hand, respondents were asked during the interview whether The management is ready for the charter preparation they responded that still there is no. The study showed that there is no clear and understandable internal audit charter.

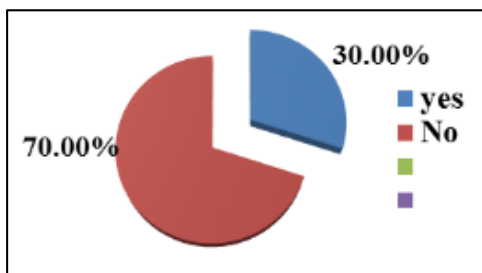
4.2 Scope of internal audit work

Table 2: Responsibilities other than financial audit

	Frequency	Percent
Valid Yes	33	66
No	17	34
Total	50	100

Source: Survey data, 2017

As shown on the table 4.6 majorities of the respondents (66%) assured that they have non additional obligation other than financial activities and (34%) of respondents indicated as their responsibility goes beyond the financial finical audit mentioning their additional responsibilities as compliance and operational audit. Majority of the respondents indicated that they are focused only on financial audit this signifies that as their internal audit functions are more of traditional type that emphasize on verification of accounts, compliance and internal control. The interviews results also imply that IA continuously checks not overall activities of the offices. These results suggest that internal auditors do not help the organization through assessing the operational and compliance audit.



Source: Survey data, 2017

Fig 1: Auditors position to access any transaction

Internal audit division properly accomplishes its objectives and internal auditors performs their job (or to achieve effective audit work) when they have unrestricted access to records and information they need in conducting audits (Mihret & Yismaw, 2007) [15].

To provide their services in such a way that add value to the organization success, internal auditors should have to own unrestricted access to whatever they might need to make an objective assessment. That includes unrestricted access to plans, forecasts, people, data, products, facilities, and records necessary to perform their independent evaluations (Mihret and Woldeyohannis, 2008) [17]. But from the above responses on their access on transaction or any other activities of the organization, most of them (70%) agreed that they are not free to any transaction or area of interest for audit and 30% of the respondent agreed they are on a position to get unlimited access to any activities of the organization. From this we can understand that internal auditors are facing difficulties to properly accomplish their objectives.

Table 3: Co-operation from auditees

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Yes	26	52	52	52
	No	24	48	48	48
	Total	50	100.0	100.0	100.00

Source: Survey data, 2017

The level of auditee’s co-operation influences the extent to which IA properly accomplishes its objectives (Mihret & Yismaw, 2007) [15]. Getting a full co-operation from the auditee’s is one of the basic tools to achieve the very purpose for which internal audit division is established but as shown on table 3 near to half (48%) of the respondents replied that they have no full co-operation from the auditees and in contrast the remaining 52% of respondents agreed that they have a full cooperation from the auditees.

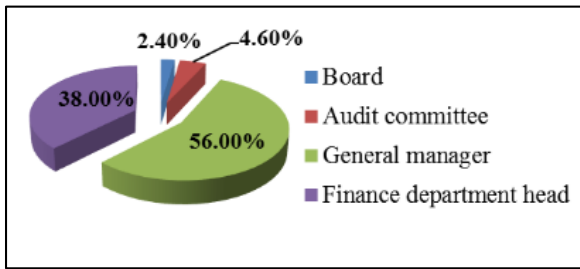
Even though more than half percent’s of the respondents agreed that they have full co-operation from the auditee it needs further improvements, hence, when internal auditors have full access to records and receive co-operation from auditees, they can contributes unique role to the success and growth of an organization (Sirens, 2009). Regarding the attitude towards the internal audit and level of co-operation with auditors, the interview result shows that, accountants or other employees consider the internal audit function as a problem finder rather than a value-adding service provider.

4.3 Internal Auditors Independency

It has long been the recommendation of many researches audit division should report directly or functionally to the audit committee, board of directors, or other appropriate governing authority, and administratively to the chief executive officer (CEO) of the organization. In this context, direct or functional reporting means that the governing authority would set the direction and approve the policies of the internal auditing activities and administrative reporting includes the administrative units facilitates the day-to-day operation of the internal audit activity.

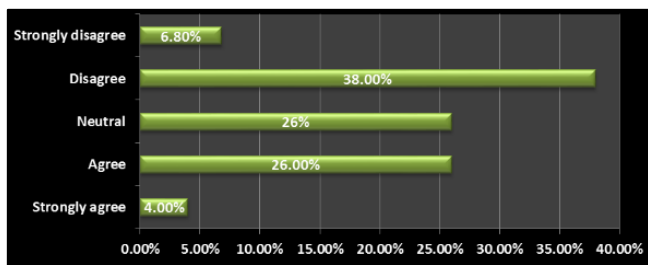
For the question designed to asses to whom internal auditors report as shown on figure 2 most of the respondents (56%) indicated that they report to the general manager and 38.% of the respondents assured that they report to the finance department head. The remaining 4.6% and 2.4% respondents indicated that they report to Audit committee and Board

respectively. Further, according to interview with general manager of regional offices and as it is observed from their organizational manual internal auditors reporting responsibility is functionally to general manager and to the finance head administratively.



Source: Survey data, 2017

Fig 2: Reporting responsibilities of internal auditors



Source: Survey data, 2017

Fig 3: The environment of independency

Yismaw (2007) [15] point out that independence of paramount value in providing effective internal audit service to the management, for it affords an atmosphere of objective and uninhibited appraisal and reporting of findings without influence from the units being audited; and independence of individual auditors is essential to the effectiveness of the IAF. In this regard figure 3, depicts that 26% of the respondents accept as true, that the current internal audit structure promotes independency and 26% are neutral whether there is conducive environment regarding internal auditor’s independency or not. Other respondents, 38% and 6.8% expressed their feeling as disagree and strongly disagree respectively. The last 4%, of respondents replied that the current organizational reporting relationship promotes the internal auditors’ independency very strongly. Most of the respondents those who replied that disagree and strongly disagree explained their reason as there is management interference on internal audit work.

Table 4: Internal auditor’s freedom to include their findings in the audit report

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	31	62	62	62
Yes	19	38	38	100
No	50	100	100	
Total				

Source: Survey data, 2017

Internal auditors are expected to feel free and should be independent to include any audit findings in their audit report to support the organization and to provide effective and efficient audit service. As indicated on the table 4.5 among the respondents, 62% of them replied that they feel free to include any audit findings on their report but the remaining

38% agreed that they do not feel free to do so. This show that auditors have somewhat good freedom to include any of their findings in their audit report but still it needs further improvement to maximize the service they provide.

4.4 Factors affecting internal auditor’s performance

According to (Mihret and Yismaw, 2007) [15] the effectiveness of internal audit function is influenced by organizational setting, management support, internal audit quality, auditee’s attributes and the interplay among them. Thus, the favorability of the four factors positively influences the effectiveness of the internal audit function. Correspondingly, Arena and Azzone, (2009) [4] noted that effectiveness of internal audit function is influenced by resources and competencies of an IA team, activities and processes performed and organizational role. Generally, the effectiveness of internal audit function is influenced by human and capital resources available, the scope of internal audit function and the level of interaction with higher management.

Table 5: Factors affecting internal audit

No.	Particulars	N	Mean	S. Deviation
1	There is high level of management support	50	2.33	1.221
2	There is good Attitude of the management towards internal audit	50	2.30	1.012
3	Status of internal auditors is high in the organizational structure.	50	1.68	.798
4	Valid N (listwise)	50		

Source: Survey data, 2017

The two of the three questions were a mean response of more than 2.00 and standard deviation of more than 1 which states internal audit staffs have low level of support & bad attitude towards internal auditors.

The remaining last question which talks about internal auditors states respondents were disagree and had mean response of 1.48 and standard deviation of 0.933. Also result revealed all responses have standard deviation of more than 1.00 which indicates that the respondents perception were far from one other.

However, even if the interview results shows as the management support was immense, based on some respondents view stated in the place for additional comments that the management support to internal auditors is too low.

Conclusion

- There no clear and understandable internal audit charter that shows auditors responsibility, time of audit, reporting responsibility and outline of independence.
- Independence is a cornerstone issue for auditors particularly for internal auditors in which they are employee of the organization and demanded to be independent. In view of this the study finds out that there is no suitable environment for independency of internal auditors which will overshadow the effectiveness of internal audit function.
- Internal audit scope is more limited on the verification of financial transaction or financial audit. In other words, the regional offices internal auditors’ are primary concerned on accounting and financial issues rather than on managerial matters.

Recommendation

- An internal audit charter which shows the nature of internal auditing, the audit objectives, the scope of audit works, audit's authority and outline of independence should be prepared
- The Internal Audit is responsible for an independent, objective assurance and consulting activity designed to add value and improve the public body's operations. So to bring these activities in to practice internal auditors independency is indisputable, consequently the environment of internal auditor's independency should to be given attention.
- The scope and extent of internal audit work should be improved unless it will difficult to get the required service from the audit division.

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