

**THE ASSESMENT OF INTERNAL AUDIT PRACTICES IN
COMMERCIAL BANK OF ETHIOPIA: THE CASE OF SELECTED
PRIVATE BANKS.**

**A THESIS SUBMITTED IN PARTIAL FULFILLMENT OF THE
REQUIREMENTS FOR THE DEGREE OF MASTER OF SCIENCE IN
ACCOUNTING AND FINANCE**

PREPARED BY: WAKOYA KENATE



**JIMMA UNIVERSITY
COLLEGE OF BUSINESS AND
ECONOMICS DEPARTMENT OF
ACCOUNTING AND FINANCE**

JUNE 2021

JIMMA, ETHIOPIA

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UNDER GUIDANCE OF

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CERTIFICATION

This is to certify that the thesis entities “Assessment of Internal Audit Practices in Private Commercial Banks of Ethiopia: The Case of Selected Private Banks” submitted to Jimma University for the award of Degree Masters of science in Accounting and Finance is record of valuable Research work carried out by Wakoya Kenate under my Guidance and supervision. Therefore we hereby declare no part of this thesis has been submitted to any other university or institution for the award of any degree or diploma.

Advisors:-Milion Gizaw Date.....Signatures.....

Co-Advisors:-Gelila Eshetu Date.....Signatures.....

DECLARATION

I, Wakoya Kenate hereby declare that the research work entitled; “Assessment of Internal Audit Practices in Private Commercial Banks of Ethiopia: The Case of Selected Private Banks” submitted by me for the partial fulfillment of MSC program in department of Accounting and Finance under the guidance of Milion Gizaw (Assist. Prof.) and Gelila Eshetu. The thesis is original work and it has not been presented for the award of any other Degree or Diploma in any university.

Researcher’s Name.....Signature.....Date.....

APPROVAL SHEET

As members of the Examining Board of the Final Open Defense, we certify that we have read and evaluated the thesis prepared by Wakoya Kenate entitled, “Assessment of Internal Audit Practices in Private Commercial Banks of Ethiopia: The Case of Selected Private Banks” and recommend that it be accepted as fulfilling the thesis requirements for the award of the degree in Master of science in Accounting and Finance.

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Name of External Examiner	Signature	Date

ABSTRACT

The purpose of this research is to assess internal Audit Practices on selected private commercial banks of Ethiopia. Internal auditing plays a critical role in the governance and operation of an organization. When effectively implemented, operated and managed, it is an important element in helping an organization to achieve its objectives. This study therefore sought to investigate the internal audit practice in commercial banks in Ethiopia. Specifically, how the internal audit was functioning in line with the audit work quality, scope of the audit work, the level of independence of the internal audit function and adequacy of competent internal audit staff. This study employed a descriptive research designed. The study used purposive sampling method and covered only focused on four private banks at Jimma head office internal auditors. Data collected from questionnaires was coded and analyzed with the aid of the Statistical Package for Social Sciences (SPSS) version 20 for descriptive statistics. Based on the conclusion and the finding the internal auditing practice of private Banks in Jimma city relatively better and follow the theoretical aspects of internal audit practice.

Key Words: *Auditing Practices, Scope of Audit, Audit Quality, Independence and Adequacy of Internal Audit Staff.*

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ACRONYMS AND ABBREVIATIONS

ACCA _____ the Association of Chartered Certified Accountants

CEO _____ Chief Executive Officer

CIA _____ Certified Internal Auditor

IAF _____ Internal Audit Function

IAS _____ Internal Auditing Standards

IA _____ Internal Auditor

IIA _____ the Institute of Internal Auditors

IPPF _____ International Professional Practices Framework

SPSS _____ Statistical Packages for Social Scientists

CHAPTER ONE

1. INTRODUCTION

1.1. Background of the study

The globalization of economy, technological advancement, and complexity of business and allegations of fraudulent financial reporting have recently sharpened the ever increasing attention to internal control and internal auditing (Karagiorgos et al., 2009). The developing role of the internal auditing is also reflected in its current definition, i.e. internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organizations 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 process (Savcuk, 2007). It can be argued that from this definition of internal auditing the internal auditor is required to be a multi skilled individual. This definition also signifies that internal audit has undergone a paradigm shift from an emphasis on accountability about the past to improving future outcomes to help auditors operate more effectively and efficiently (Nagy and Cenker, 2002; Sterm, 1994; Goodwin, 2004).

Internal auditing plays a critical role in the governance and operation of an organization. When effectively implemented, operated and managed, it is an important element in helping an organization to achieve its objectives. Organizations that effectively use internal auditing were better able to identify business risks, process and system inefficiencies, take appropriate corrective action and ultimately support continuous improvement (Institute of Internal Audit, 2010). According to Gunther and Moore (2002) internal auditing were conducted in diverse legal and cultural environment within organization that varied in purpose, size, complexity and structure; and by persons within or outside the organization. While differences may affect the practice of internal auditing in each environment, conformance with the Institute of Internal Auditors (IIA) international standards for the professional practice of internal auditing is essential in meeting the responsibilities of internal auditors and the audit activity.

Internal audit function has helped keep bad things from happening, assure good things can happen and help management understand where their risks are, whether the risks are under control and whether the risks are worth taking. Internal auditors evaluate the controls that help

Organizations manage risks to ensure controls are in place, working and cost-effective. Well performing internal audit function is one of the strongest means to monitor and promote good governance system in an organization. Internal auditing is an integral part of the corporate governance mosaic in both the public and the private sectors (Cohen et al., 2002).

Corporate governance is described as the framework of rules, relationships, system and processes within and by which authority is exercised and controlled within organizations. It encompasses mechanisms by which companies are held accountable (AUX, 2003).

The need to focus on improving corporate governance has increased in many developed and developing economies during the past few decades, especially in the wake of economic collapse and financial crises (Brown and Caylor, 2006). According to the Organization for Economic Cooperation and Development (OECD, 2004) countries: “Corporate governance is the system by which a business corporation (or a nonprofit organization) is directed and controlled, at its senior level, in order to achieve its objectives, performance and financial management, but also accountability, integrity and openness”. More recently, Roe (2004) defines corporate governance as the relationships at the top of the firm-the board of directors, the senior managers, and the stockholders. In his opinion institutions of corporate governance are those repeated mechanisms that allocate authority among the three and that affect, modulate and control the decisions made at the top of the firm. The above definition of corporate governance indicates idea of objectives correspondence, incentives, monitoring and control.

Good corporate governance should provide proper incentives to the Board of Directors and the company's management to seek to achieve the goals that are in the interest of the company and its shareholders and should facilitate effective control (OECD, 2004).

To achieve the quality of governance, the company must focus on all cornerstones of corporate governance and in particular the internal audit function. It assesses the commitment to the ethics of the organization and its goals, programs and activities. It is also an important source to other cornerstones such as the external audit, the Audit Committee, Board of Directors and senior management.

The banking industry differs fundamentally from other industries in any country. An apparent area of variation is in the products and services it provides. Banks mainly deal with the liquid and largely risky assets of business, cash and cash equivalents. Banks lie at the heart of the world's financial system. They represent the source we often visit to find a loan to purchase a home or automobile, start a new business, or finance a college education etc. (Peter and Sylvia, 2008).

For the fact that the banks have differences in the scale, diversity, complexity and geographical coverage, each bank is adopting different management structures. Of particular significance is the functioning of the internal audit unit in the various banks. Each bank is subject to different degrees and types of risks. The internal audit function is therefore tailored in such a way as to manage the risk exposure of the banks (Mahama, 2009).

One of the financial institutions that contribute a major role in the Ethiopia's economy is the banking sector. Banking, in Ethiopia, is relatively a new concept. The history of banking in Ethiopia can be traced back to the establishment of Bank of Abyssinia in March 1905 and gradually after certain years of lapse the first private domestic bank, Addis Ababa Share Company, was established in October 1964. The intermediary role of financial institutions takes different forms in different economic systems.

Furthermore, the banking industry in Ethiopia is highly regulated and closed from foreign competition. Banks operate extremely in conservative lending policies and require physical collateral for virtually all loans constrain inclusive growth.

Currently, two public banks namely Commercial bank of Ethiopia and Development bank of Ethiopia; and sixteen privately owned banks- Awash, Dashen, Abyssinia, Wegagen, United, NIB, Cooperative Bank of Oromia, LIB, OIB, Zemen, BIB, Berhan, Abay, AdIB, Debub Global and Enat banks have been operating in Ethiopia.

1.3. Statement of the problem

According to Hermanson and Rittenberg (2003), an effective IAF is an important "frontline player" in two fundamental governance activities; monitoring of risks and providing assurance regarding controls. Moreover, IAF plays a key role in compliance work and may also spend considerable time on consulting or operational-oriented work, with the objective of enhancing the organization's effectiveness and efficiency; and all these elements map directly in to organizational governance.

There has been evidence to suggest that internal audit function played a key role in effective corporate governance within Commercial banks. With appropriate support from the board and audit committee the internal audit is in the best position to gather intelligence on inappropriate accounting practices, inadequate internal controls and ineffective corporate governance (Zekele, 2007).

Basel committees (2012), principles for enhancing corporate governance states that bank should have an internal audit function with sufficient authority, stature, independence, resources and access to the board of directors. Independent, competent and qualified internal auditors are vital to sound corporate governance. The committee further summarized the principles into three groups that are principles relating to: the supervisory assessment of the internal audit function; the relationship of the supervisory authority with the internal audit function and finally the supervisory expectation related to the internal audit function.

Despite its significance, empirical studies that are conducted in developing countries particularly in Africa showed the non-independence work of internal auditors (Dawuda et al., 2015) and are embracing the conservative approach which is primarily concerned with compliance and monitoring rather than adopting value added approach to achieve the objective of the organization (Ramachandran 2012).

Empirical investigation indicated that for internal audit to function efficiently and effectively there are different factors. Some of these are the following, first the internal audit quality contribute a lot to increase business performance. This could be achieved through audit planning, reporting, follow up and quality review. Secondly the internal audit scope should be defined. Internal audit must thirdly be independent from all decisions factors involved in corporate governance, in this regard activities being audited must be independent from everyday internal processes, and must be able to exercise its assignment on its own initiative in all departments, establishments and functions of the organization. Finally the internal audit function must be adequately staffed with the right people to deliver on its mission and objectives.

This study reviews different researches, because the role of IAF in promoting effective corporate governance and in increasing business performance is high and an unexplored area in Ethiopia. Exceptions that closed to this study are Mihret (2010) in his research on factors associated with attributes of IA department concluded that in organization that are exposed to high risk management tends to appreciate internal auditors assistance in managing risk and thus strengthens IA. Mihret and Yismaw

(2007) studied IA effectiveness in public sector higher educational institutions in Ethiopia. The results indicated that IA was ineffective in terms of proficiency, planning, recommendations and limitations to the scope of work. Furthermore, the study revealed that audit quality and management support are the two most important factors influencing IA effectiveness respectively.

Moreover, Mihret et al., (2010) revealed that IA effectiveness is influenced by the dynamics prevailing in an IA setting. In addition, Belay (2007) suggested that well performing IAF is one of the strongest means to monitor and promote good governance systems in an organization.

The internal auditor's value lies in how well the department has been able to contribute to the achievement of the overall organizational goals. However, according to researches and surveys conducted by different individuals, much of the work of internal audit department of private commercial banks in Ethiopia has been very restrictive in terms of scope.

A research done by Jayalakshmy (2012) indicated that the internal audit in Commercial Banks within Tanzania is still embracing the conservative approach which is primarily concerned with compliance and monitoring rather than adopting value added approach, the inference of the study whereby funds are being spent on activities which do not add value to the Stakeholders implying that the audit approach employed could be the challenge by itself that can hamper the audit practice effectiveness.

The study done with the objective of identifying the most important factors affecting audit quality in Jordanian Commercial Banks (JCBs) has shown that a positive correlation between audit quality and audit efficiency, the reputation of auditing office, auditing fees, the size of audit firm, and the proficiency of auditor mean to say that these factors as being challenges that affect the audit quality (Abdulhadi, 2013).

A study conducted on commercial banks in Ethiopia in title, factors determining internal audit quality has come to a conclusion, that internal auditors in Ethiopian commercial banks believe the performance, competence and use of information technology by internal auditors as significant factors affecting internal audit quality (Wubishet and Dereje, 2014) and this study tried to assess the internal audit practice of four selected private Bank.

The scope of the IAF in Ethiopia did not go far from the traditional practice Kedir (2014). Arefayne (2019) recommended to the National Bank of Ethiopia to do more on ensuring organizational

independence of internal auditors. Mihret and Yismaw (2007) indicated the low technical staff and high staff turnover in the internal audit office of the organization. However, those studies were conducted in governmental organizations and other financial institutions. This study therefore sought to investigate the internal audit practice in commercial banks of Ethiopia the case of selected private Bank. Specifically, how the internal audit was functioning in related to the quality of the audit work, scope of the audit work, the level of independence of the internal audit function and adequacy of competent internal audit staff in Commercial Bank.

Based on the above ground this study fills the above literature gap in the area by assessing the practice of internal auditing of commercial Banks and identify the most significant problem that affect the internal audit practice in order to give important solution and recommendation.

1.4. Research Questions

The research was conducted to answer the following research questions;

- i .What is the effect of the scope of internal audit work on internal audit effectiveness in Selected Private Bank?
- ii. What is the effect of the audit work quality on internal audit effectiveness in Selected Private Bank?
- iii. What is the effect of independence of internal auditors on internal audit effectiveness in Selected Private Bank?
- iv. What is the effect of competency and adequacy of internal audit staff on effectiveness of internal audit in Selected Private Bank?

1.5. Objectives of the study

1.5.1. General Objectives

The general objective of the study was to assess the internal audit practice in Commercial Bank of Ethiopia.

1.5.2. The specific objectives of the study were

- i. to assess the internal audit scope of internal audit work on internal audit effectiveness in Selected Private Bank.
- ii. To evaluate the internal audit quality in Selected Private Bank.
- iii. To assess the level of independence of the internal audit function of Selected Private Bank.
- iv. To assess the adequacy and competency of internal audit staff on effectiveness of internal audit in Selected Private Bank.

1.6. Significance of the Study

This research could contribute to Internal audit function literature by providing empirical evidence that increase the body of knowledge in understanding the Internal audit practice in private commercial banking sector's Internal Auditing in Ethiopia in general and on four Private Bank in particular.

In addition, this study might be used to improve stakeholders (Board of directors, Board audit committee and external auditors) understanding of the Internal Audit practice in the achievement effective corporate governance in Private Bank.

The study could also add value to the management who are able to appreciate the importance of an effective internal audit function in their organization; the internal auditors who through this study be in a position to appreciate their role in promoting effective corporate governance in the bank.

1.7. Scope of the study

The study was restricted to the assessment of internal audit function in Selected Private Bank in Jimma city. Data were collected only at selected private Bank Jimma city.

The study's specific focus was on the assessment of the internal audit practice with emphasis on internal audit function in line with scope of the audit work, internal audit quality, the level of independence of the internal audit function and adequacy of competent internal audit staff. The study was conducted using primary data.

1.8. Limitation of the study

Like any other study, this study was subject to some limitations. Firstly this studies only Jimma City to explore data about the internal audit practice of the Selected Private bank. The other limitation of this study was that the data collection method was limited to questionnaire. Other data collection methods were not used like interviews. To mitigate this limitation large number of questions were prepared to conduct the study and to reach on conclusion. Some of distributed questionnaires were not fully answered and responded. There were resource constraint, in terms of time and logistics as well as the difficulties in getting other staff from other departments some of concerned parties did not cooperate the researcher. Some information achieved cannot confidential.

1.9. Organization of the research study

Review of the related literature; the theoretical and empirical parts including the research gap

are discussed thoroughly in the second chapter of the report. The third chapter focuses on the research design and methodology. Types and sources of data, the target population, sample size and sampling techniques, method of data collection are described accordingly. In the fourth chapter of the report, an exhaustive analysis of the collected data is discussed and interpreted. In the last chapter, the conclusions and recommendations that drawn based on the research results are forwarded to the respective audites and users for their future proper implementation and view.

CHAPTER TWO

2. REVIEW RELATED LITERATURE

2.1 Theoretical Review

2.2. Introduction

This chapter focuses on the review of relevant literature on internal audit practices and other core aspects of the topic under study. Areas such as definition of related concepts, key features of effective internal audit function, functional role of internal audit, development of internal audit, duties and responsibilities of internal auditors, importance of internal auditing and the like are covered. The review includes literature in the area of internal audit role and its effectiveness on sound corporate governance and finally the summary of the review and screening the gap in the existing literature. The chapter thus presents the conceptual and theoretical basis for the study.

2.3. Definition of Internal Audit

The Institute of Internal Auditors (IIA) defines Internal Auditing as an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. The internal audit activity 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.” According to this definition the major scope of the internal auditors are making assurance to the organization and giving consultant services to the overall managements of the corporate governance. By providing the independent opinion and conclusions regarding the operation, function, system and wellbeing of the organization the IA can provide assurance services; and by giving the advisory service based on the specified requests of an engagement client the internal auditor can give the consulting service to the organization (Hailemariam,2014).

Unegbu and Kida (2011) defined internal audit as “an aspect of the internal control system established by management of an organization in order to ensure proper compliance with the stipulated policies and procedure in order to achieve management objectives”. As cited in Badara and Saidin (2012) ; Jurchescu (2010) defined internal audit” as an independent and objective functional activity which provides security and management advice with the

aim of ensuring effective management of public income and expenditure, ensuring proper activities within public organization, helps the public organization to achieve their objective through systematic and methodical approaches, evaluate and improves the efficiency and effectiveness of internal control system, risk management and management processes”. Internal audit are the mechanism through which information about the effectiveness of the quality system is gathered by auditors selected from within the company but, who are independence of the area, function or procedures being audited. The Internal Audit Function (IAF) is the mechanism through which the operation of the quality management system is formally monitored and in accordance with the documented quality system is assured (MoFED,2004).

2.5. Theories of Internal Audit

Various theories have been formulated on internal audit and financial performance, some of these theories are; Agency theory, contingency theory and Lending credibility theory. The theories are discussed below:

2.5.1. Agency Theory

Agency theory is concerned with resolving problems that can exist in agency relationships; that is, between principals (such as shareholders) and agents of the principals (for example, company executives). The two problems that agency theory addresses are: the problems that arise when the desires or goals of the principal and agent are in conflict, and the principal is unable to verify what the agent is actually doing and the problems that arise when the principal and agent have different attitudes towards risk. Because of different risk tolerances, the principal and agent may each be inclined to take different actions.

Adams (1994) in his article stated that Agency theory can provide for richer and more meaningful research in the internal audit discipline. Agency theory contends that internal auditing, in common with other intervention mechanisms like financial reporting and external audit, helps to maintain cost-efficient contracting between owners and managers. Agency theory may not only help to explain the existence of internal audit in organizations but can also help explain some of the characteristics of the internal audit department, for example, its size, and the scope of its activities, such as financial versus operational auditing. Agency theory can be employed to test empirically whether cross-sectional variations between internal auditing practices reflect the different contracting relationships

emanating from differences in organizational form.

2.5.2. Contingency Theory

The goal of an audit is to test the reliability of a company's information, policies, practices and procedures. Government regulations require that certain financial institutions undergo independent financial audits, but industry standards can mandate audits in other areas such as safety and technology. Regardless of the audit subject, various factors impact a company's final results, and the contingency theory takes these factors into account during the audit process.

The contingency theory of leadership and management states that there is no standard method by which organizations can be led, controlled and managed. Organizations and their functions depend on various external and internal factors. The functions of audits are themselves, types of organizations that are affected by various factors in the environment. The presence of such factors is why auditing can be managed by applying the contingency theory, with recognition that processes and outcomes of audits are dependent on variable and contingent factors.

On a broad level, the audit process is straightforward. Auditors require access to documents, systems, policies and procedures to manage an audit. They must remain compliant with industry standards, government regulations and internal requests. Audit teams may begin the audit process with meetings where they gather risk and control awareness, after which the field work begins. During the audit process, auditors perform substantive procedures and test controls. They then draft reports that they submit to management and regulatory authorities. The audit sub processes, particularly in planning and field work, include contingencies such as business type, employee skill level, applicable laws, available audit workforce, available technology and systems, and deadline.

Daft (2012) in his book writes: Contingency means: one thing depends on other things and Contingency theory means: it depends. Audit functions are task-oriented and can be loosely structured. The functions also can vary considerably, depending on the area of a company under audit and the type of business model, so auditors must carefully manage their inspections and take variables into account to get the job done. The contingency theory also

can be applied to an audit team structure.

Audit teams use a mix of structure and contingency to get the output rolling quickly. The subject of auditing projects can include such diverse areas as evaluation of production processes, inspection of company accounts, and assessment of compliance with industry standards. Selecting auditors with specialized training or those who have a particular skill in the subject area minimizes the learning curve and reduces opportunities for errors. The quality and output of audits remain assured when audit teams use resources according to expertise and experience, and when auditors are flexible and can adapt to process fluctuations. For example, an auditor experienced in evaluating financial instruments can be effective in an audit exercise of a bank or hedge fund, even when the financial instruments the institution offers do not fit the typical mold (Davoren, 1994).

2.5.3. Lending Credibility Theory

Volosin (2007) in his book mentioned that the lending credibility theory is similar to the agency- theory and it states that audited financial statements can enhance stakeholder's faith in management's stewardship. The business world consists of different groups that are affected by, or participate in, the financial reporting requirements of the regulatory agencies. They are shareholders, managers, creditors, employees, government and other groups. The major recipients of the annual reports are the shareholders, including individuals with relatively small shareholding and large institutions such as banks or insurance companies. Their decision is usually based on the financial reporting and the performance of the company's management, who have a responsibility to act in the interests of investors.

The auditor is appointed by the company's shareholders and reports his results to his clients. The aim of the auditor's report is to comment on how accurately the company presents its financial situation and how it is performing. This should reassure the shareholders that their investment is secured and also help to reduce the practice of misleading accounting procedures designed to show the company in a more favorable light. Basically, the audit is represented as a process designed to evaluate the credibility of information of a company's financial statements (Letza, 1996).

2.6. Functional Classification of Auditors: Internal Audit vs. External Audit

The institute of chartered accountants of India classified the auditors in two broad categories on the basis of functional division; auditors can be, namely, external auditors and internal auditors. External auditors are the persons who practice the profession of accountancy having qualified in the professional examination and are external to the organization of which they audit the accounts. The internal auditors, on the other hand, may also be professionally qualified and are internal to the organization in which they are appointed to perform specific work. They are considered internal because their appointment is done by the management and the scope of work is also specified by it. They may be appointed either on a contract basis or as employees to undertake auditing of the books and records as a part of management control and appraisal system.

The external auditors, on the other hand, are appointed by the owners of the organization, say, shareholders of the company and thus they are treated external to the organization in which they have been appointed. When an external auditor is appointed under a particular statute, such auditor may be known as the statutory auditor. Their scope of work is determined by the statute under which they have been appointed. Another significant distinction between the internal and external auditor is that the former is not considered independent to the management of the organization while the latter is independent of the management of the organization which is responsible for the preparation of the books of account. Finally the scope of work of an internal auditor may extend even beyond the financial accounting and may include cost investigation, inquiries relating to losses and wastages, production audit, performance audit, etc. It must be remembered that the basic foundation of any type of auditing, whether internal or external, envisages that the auditor must be independent of the activity for which he/she is going to conduct an audit. Even though the internal auditor is an employee yet he must be independent to the extent practicable.

2.6.1. Functional Role of Internal Audit

The role of internal auditing has increased dramatically in the past two decades primarily because of the increased size and complexity of many corporations. The primary role of internal audit is to provide assurance but, financial and non-financial information and

mechanism for control. Internal auditors are powerful to help management by evaluating controlling system and Point out weaknesses with in internal control. It also review and appraises, soundness adequacy and application of accounting, financial and other operating activities and recommending effective control and ascertaining the extent of compliance with established price, policies and procedures. In order to does it in a professional and independent fashion internal audit unit should be kept distinct from other functional engagement in analyzing and reporting performance? The internal auditors should participate in the design of the data processing system to ensure that the system provides a proper audit trail and includes adequate internal auditor reviews all aspects of system on attest basis, to determine that prescribed internal control are operation as planned. Internal audit is assuring the management that the system of internal control is effective in design and operation. Internal auditing is a profession having in role, upholding basic standard of excellence not adhering to a code of ethics. Certification as a professional internal auditors requires one to have been mastered the common body of knowledge judged as essential for satisfactory over areas enable broad area (Kurt Panyoray, 1997).

The internal auditing function includes verification, evaluation, and competency of the operation. The functions of internal audit includes review and appraise internal control procedure, ascertain effectiveness and efficiency of operations, verify compliance to established policies procedures and plans, ascertain the extent to which company assets are accounted for and safeguarded from losses of any kind, ascertain reliability of data documents, evaluate quality performance in carrying out assigned responsibilities, and recommend improvements in better management controls. The internal auditor can perform the work through either functional approach operational approach, or financial approach (Johannes and Engida, 2009).

Internal auditing is a staff function therefore the auditor ideally is not in disposition of line function. The position and place in the organization is determined by the scope of the function performed and the extent of responsibility entrusted to internal auditor by management. It is desirable that she/he should be placed as high as possible in the organization structure if she/he is truly to be of service to management without intimidation and be in position of several once over all the organization activates (Joh, 2009).

2.6.2. Internal Audit Function and Banks

According to Basel committee on banking supervision (2010), the board should recognize and acknowledge an independent, competent and qualified IA since it is vital to the corporate governance. The board and senior management can enhance the ability of the IAF to identify problems with a bank's risk management and internal control systems by encouraging internal auditors to adhere to national and international professional standards, such as those established by the Institute of Internal Auditors, promoting the independence of the internal auditor, for example by ensuring that internal audit reports and/or has direct access to the board or the board's audit committee, recognizing the importance of the audit and internal control processes and communicating their importance throughout the bank, utilizing in a timely and effective manner, the findings of internal audits and requiring timely correction of identified problems by senior management, and engaging internal auditors to judge the effectiveness of the risk management and compliance function, including the quality of risk reporting to the board and senior management, as well as the effectiveness of other key control functions.

Rossiter (2007) noted that effective IAFs help financial services companies to accomplish key business objectives by bringing a systematic, disciplined approach to evaluating and improving the effectiveness of governance, risk management and control processes. Furthermore, the researcher revealed, IAFs in the banking and financial services industry are responding to new challenges, changes and expectations in today's business environment. They are striving to provide greater value as a key component of their organizations' governance framework. As a result, IA has emerged as an independent, objective assurance and consulting activity designed to add value and improve operations.

2.7. Types of Audits Performed by Internal Auditors

Internal audits are conducted for different reasons and with varying objectives and with each type of risk exposure an organization would need to conduct a particular type of internal audit. Some audits are required by regulation or policy, while others are requested by management to help improve processes or identify internal control weaknesses (Olga, 2017). The following is a summary of the various types of audits which will generally be conducted in an organization.

2.7.1. Operational Audit

Operational audit evaluates performance of a particular function or department to assess its efficiency and effectiveness. Financial data may be used, but the primary sources of evidence are the operational policies and achievements related to organizational objectives. Internal controls and efficiencies may be evaluated during this type of audit. Some areas of operational audits include: organizational structure, processes and procedures, accuracy of data management and security of assets, staffing, and productivity (Arens, Best, Shailer and Fiedler, 2005; Olga, 2017).

2.7.2. Compliance Audit

Compliance Audit evaluates an areas adherence to established laws, standards, regulations, policies, and procedures. Compliance audits are done because of a policy or statutory requirement. While the audit is done for regulatory reasons, the objectives are still to ensure adequate control over an important internal process (Arens et al., 2005; Olga, 2017).

2.7.3. Financial Audit

Financial Audit is a historically oriented, independent evaluation performed for the purpose of attesting to the fairness, accuracy and reliability of financial data. The central objective is to ensure that the financial activity of the department, unit or area is completely and accurately reflected in the appropriate financial reports (Arens et al., 2005; Olga, 2017).

2.7.4. Follow up Audit

Follow up Audit is audits conducted approximately six months after an internal or external audit report has been issued. They are designed to evaluate corrective action that has been taken on the audit issues reported in the original report. The purpose of a follow-up audit is to revisit a past audit's recommendations and management's action plans to determine if corrective actions were taken and are working, or if situations have changed to warrant different actions (Arens et al., 2005; Olga, 2017).

2.7.5. Investigative Audit

Investigative Audit is an audit that takes place as a result of a report of unusual or suspicious activity on the part of an individual or a department. Fraud and financial

irregularity audits are designed to verify the existence and magnitude of suspected fraud and financial irregularities. It is usually focused on specific aspects of the work of a department or individual.

Investigations are conducted to determine the extent of loss, assess weaknesses in controls, and make recommendations for corrective actions conducted at the request of the Audit Committee of the Board of Trustees, the President, or other senior members of organization management as a result of a tip from the organization's hotline; or at the discretion of the Director (Arens et al., 2005; Olga, 2017).

2.7.6. Information Technology Audit

Information technology (IT) Audit is evaluates controls related to the institutions automated information processing systems. The information technology audit function develops audit programs to assess, evaluate and make recommendations to management regarding the adequacy of internal controls and security inherent in organizations information systems, and the effectiveness of the associated risk management. The goal is to ascertain that IT systems are safeguarding assets, maintaining data integrity and efficiently operating to achieve business objectives (Olga, 2017).

2.7.7. Management Audit

Management Audit Also called performance audit, are internal consulting projects. Because an internal audit is an activity independent of management, it is often an excellent resource to provide independent and objective insight on the efficiency of business processes. Management can request internal auditors to review a business process, organization, or strategy and the auditors do not have to worry about backlash from management. A common management audit is a review of organizational structure, such as having internal audit look at how administrative work is divided among divisions and if there are opportunities to be more efficient (Olga,2017).

2.7.8. Grant and Contract Audits

Grant and contract audits are designed to evaluate the contracting process, compliance with the provisions of grants and contracts, and third-party contractual performance. These audits may be performed with respect to any function, activity, department, or unit of the

organization and may include all types of contracts; e.g., federal and private grants and contracts, construction contracts, and professional service contracts (Arens et al.,2005).

2.7.9. Internal Audit Effectiveness

The word “effectiveness” have been defined by different researchers, for instance Arena and Azzone (2009) defined effectiveness “as the capacity to obtain results that are consistent with targets objective,” while, Dittenhofer (2001) view effectiveness as the ability toward the achievement of the objectives and goals. In the same context, a program can be seen as effective if its outcome goes along with its objectives (Ahmad, Othman, and Jusoff, 2009; Mihret et al,2010).

The Institution of Internal Audit (2010) defined internal audit effectiveness “as the degree (including quality) to which established objectives are achieved. While Mizrahi and Ness-

Weisman (2007) give their own definition which is in line with the ability of the internal auditor intervention in prevention and correction of deficiencies and they finally defined internal audit effectiveness as “the number and scope of deficiencies corrected following the auditing process.”

Therefore, going by the above definitions of effectiveness and audit effectiveness, it’s clear that audit effectiveness or internal audit effectiveness is means the same thing because they all have central target which is „the ability of achieving established objective.

2.8. Factors Affecting Internal Audit Effectiveness

Internal audit effectiveness could be affected by different factors. Based on the above definition, this study focused on the assessment of internal audit effectiveness by considering the following factors; the quality of audit work, scope of internal audit work, adequacy and competency of internal auditors, and internal audit independence and objectivity.

2.8.1. Quality of Audit Work

Glazer and Jaenike (1998) argued that performing auditing work according to internal auditing standards contributes significantly to the effectiveness of auditing. Ridley and Dsilva (1997) found in the UK that complying with professional standards is the most

important contributor to internal audit added value. Internal audit quality, which is demonstrated by the offices' capability to provide useful and its findings and recommendations, is one of the most prominent factors on which audit effectiveness is anchored. The performance standards of the IIA (1996) require the auditor to plan and perform the work such that he or she would be able to arrive at useful audit findings and forward recommendations of improvement. The officer's ability to properly plan, perform and communicate the results of audits is proxy for audit quality. Therefore, audit quality is debatably a function of extensive staff expertise.

In general, formal auditing standards recognize that internal auditors also provide services regarding information other than the financial reports. They require auditors to carry out their role objectively and in compliance with accepted criteria for professional practice, such that internal audit activity will evaluate and contribute to the improvement of risk management, control and governance using a systematic and disciplined approach. This is important not only for compliance with legal requirements, but because the scope of an auditor's duties could involve the evaluation of areas in which a high level of judgment is involved, and audit reports may have a direct impact on the decisions or the course of action adopted by management (Bou-road, 2000). It can thus be argued that greater quality of internal audit work understood in terms of compliance with formal standards, as well as a high level of efficiency in the audit planning and execution will improve the audit effectiveness. The internal audit guide line also states that internal auditors are expected to comply with standards for the professional practices of internal auditing published by the institutes of internal auditors (IIA) so as to conduct quality audit work. It also states that the quality assurance and improvement program should cover all aspects of the internal audit activity and continuous monitoring of its effectiveness which includes ongoing internal monitoring and periodic internal and external quality assessments.

2.8.2. Audit Planning

The audit planning is a major part of audit works for both internal and external audits. A good audit planning will help the auditor to minimize its risks, improve audit efficiency, and meet its objective at the minimum effort. Auditors are required to prepare a proper audit plan to ensure that all audit risks are identified and correct audit strategies are

deployed to detect all concerning risk areas. It is essential for the auditor to prepare a good strategic audit plan. If the plan is well prepared, all kind of audit risks is identified and detected. This will help the auditor to minimize the audits risks of issuing the incorrect opinion to financial statements.

Good audit planning should include the following basic elements, Background information: Brief outline of the audited body's activities, objectives and financial circumstances, Significant events: Details of any events or changes which are likely to affect the entity's operations and the audit, Audit/examination areas: Certification requirements describing the scope of the audit for each area, Audit programs: Audit programs are prepared to serve as a guide for the audit, Administrative arrangements and timetable: Any administrative arrangements required to coordinate the work and the proposed timetable for the audit to meet the agreed deadline, Staff allocation and responsibilities: This section enables appropriate allocation of staff to the audit in terms of number, grades and experience. It also shows the officers' responsible for supervision and review.

2.8.3. Objectives of planning

The main objective of audit planning is to ensure appropriate attention is given to all areas of the audit. Proper planning facilitates efficient use of audit resources and effective carrying out of the audit. When planning is correctly done, audit team is likely to identify events, transactions and practices which may have material effects on the financial statements and subsequently the auditor's opinion.

2.9. Internal Audit Reporting Structure

Theoretically, the Chief Audit Executive should report functionally to the board or audit committee and administratively to the chief executive officer of the organization and functional reporting line for the internal audit function is the ultimate source of independence and authority (Rupsys, 2005).

Report functionally means that the governing authority would approve the overall charter of the internal audit function, approve the internal audit risk assessment and related audit plan, receive communication from the C.A.E on the results of the internal audit activities or other matters that the C.A.E determines are necessary, private meeting with the C.A.E

without management present, approve all decisions regarding the appointment or the removal of the C.A.E, approve the annual compensation and salary adjustment of the C.A.E, and make appropriate inquiries of the management and the C.A.E to determine whether there are scopes or budgetary limitation that impede the internal audit function to execute its responsibility. On the other hand, administrative reporting is the reporting relationship within the organization's management structure that facilitates the day to-day operation of the internal audit function it typically includes, budgeting and management accounting, human resource administration including personal evaluations and composition, internal communication and information flow, administration of the organization's internal policies and procedures (Gleim, 2002).

2.10. Scope or Functions of Internal Auditing

Internal audit is a control that is concerned with the examination and appraisal of other controls. The ultimate purpose of internal audit is protection of the properties or assets of the business, not only from fraud but also from other factors like waste, loss, etc.. Internal audit involves five major functions or areas of operation. They are as below:

Reliability and Integrity of Information: The internal auditor should review the reliability and integrity of financial and operating information and examine the effectiveness of the means used to identify, measure, classify, and to report such information.

Compliance with Policies and Procedures: The systems and procedure also have considerable impact on the operation of the business enterprise. The internal auditor should gauge the effectiveness and impact of such systems and report thereon.

Safeguarding the Assets: The internal auditor should review the existing system for safe guarding the assets and if necessary should verify the existence of such assets.

Economical and Efficient Use of Resources: The internal auditor should also appraise the economy and efficiency with which the resources are employed. Further the internal auditor should identify the conditions, which would prevent the economical use of resources. They are as follows: Underutilization of capacity, non-productive work procedures, which are not cost, justified, over staffing or under staffing.

Accomplishment of the Established Objectives and Goals: The internal auditor should make a review of the operations or programs of the enterprise and should ascertain whether the results are not inconsistent with the established goals and objectives of the enterprise. He should also ascertain whether the programs are carried out as per plan.

2.11. Competency of Internal Auditors

According to Mihret and Yismaw (2007) in today's dynamic business environment, it is imperative that internal auditors are qualified as they should be thorough in their knowledge of business, systems, developments and other business topics. They should be able to interpret what works and what doesn't the strengths, weaknesses of standards, code systems and procedures. Appropriate staffing of an internal audit department and good management of that staff are keys to the effective operation of an internal audit. An audit requires a professional staff that collectively has the necessary education, training, experience and professional qualifications to Conduct the full range of audits required by its mandate (Al-Twaijry and Gwillian, 2003). Auditors must comply with minimum continuing education requirements and professional standards published by their relevant professional organizations and the IIA (2008).

According to IIA (2006), the competence of all staff involved in the internal audit function is crucial being classified as a prime component of effective internal audit activity. Internal auditors must be sufficiently qualified and in possession of all the required knowledge and skill to discharge the responsibilities associated with audit duties International Standards for the Professional Practice of Internal Auditing (ISPPIA). Competency can be relate to the ability of an individual to perform a job or task properly base on the educational level, professional experience and the effort of the staffs for continuing professional development. Auditors'' competency determines the effective auditing in the organization. It contributes to the ability of the auditors to perform the systematic and discipline audit approach to improve the effectiveness of internal audit.

The MoFED (2004) identified that adequate staffing is necessary in the institution to its full capability. Weakness in staffing can lead to mismanagement, error and neglect and fraud, which can affect other controls. The size of internal audit staff and the competency of internal audit are the critical characteristics of internal audit quality that can't be separated.

This means at the absence of one dimension the other cannot contribute to the quality of internal auditors. Seol and Sarkis (2005) describe the two types of skills as very relevant. These skills are cognitive and behavioral skills. Cognitive skills is required to demonstrate technical, analytical and appreciative skills, whereas in behavioral skills it is essential that auditor good interpersonal and organizational skills.

The quantity of audit effort and the quality of professional care exercised will determine the overall quality of the internal audit work (Cohen and Sayag, 2010) and additionally stated that internal audit effectiveness increase in particular when the relation between the number of skilled internal auditors and employees grows. This shows that sufficiently large number of skilled professionals enables the internal auditors to do its duties.

2.11.1. Professionalism

In the current scenario, the demands for professionalism, knowledge and integrity has increased manifold. To be effective, auditors must serve as objective assurance providers and advisors to the other participants in the governance process like Board of Directors and the audit committee; provide guidance on improving operational efficiency and control; evaluate risk and advise the management on risk identification, risk tolerance and risk management.

The scope on internal audit has widened and may cover the whole gamut of organization's activities. It is the internal auditor's task to operate within the framework of professionalism to assist the company in achieving the highest-quality results and long-term objectives. This calls for clear and concise guidance that can be readily adopted and followed regardless of the industry, audit specialty, or sector.

2.11.2. Proficiency

Internal auditors must possess the knowledge, skills, and other competencies needed to perform their individual responsibilities. The internal audit activity collectively must possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities.

2.11.3. Due Professional Care

The internal auditor is expected to apply due professional care which is expected from a reasonably prudent and competent internal auditor. The internal auditor should exercise due professional care by considering the extent of work, adequacy of risk management, internal control procedures, probability of errors, misstatements or irregularities, cost incurred in relation to expected benefits.

2.11.4. Continuing Professional Development

Internal auditors should enhance their knowledge, skills, and other competencies through continuing professional development.

2.11.5. Professional Behavior

Internal auditors need to act professionally and maintain the good reputation of the profession. The organization should benefit from the internal audit activity in its risk management and internal control process.

An auditor's responsibility is not limited to satisfy the needs of an individual employer. The standards of the accountancy profession are heavily determined by the public interest, for example internal auditors provide assurance about a sound internal control system which enhances the reliability of the external financial information of the employer. Accountancy and audit bodies like IIA and IFAC have formulated some important principles of behavior.

2.12. Independency and Objectivity of internal Auditors

The International Standard for the Professional Practices of Internal Auditing defines "independence" in terms of freedom from conditions that threaten objectivity and the appearance of objectivity. According to Manasseh (2004) internal auditors are independent when they can carry out their work freely and objectively. Independence permits internal auditors to render the impartial and unbiased judgments essential to the proper conduct of audits. It is achieved through Organizational structure and objectivity. We expect our auditors to maintain independence of mental attitude in the conduct of all assigned work; to be objective, fair, and impartial; and to conduct them so that auditees and third parties will see our office in this way. Each staff member must promptly notify the Director, or higher,

in writing concerning any situation that would impair the staff member's or the office's independence on an audit, or that might lead others to question it. If a staff member has any doubt about whether a situation may be impairment, he or she should resolve the question in favor of disclosure. Internal auditors are independent when they render impartial and unbiased judgment in the conduct of their engagement.

According to Tasklaganos (2005), Objectivity” means internal auditors are expected not to subordinate their judgment on audit matters to that of others, especially management independence, based on the criterion of objectivity, is pivotal to the internal auditing profession and internal auditors. Independence is unavoidable for internal auditors. To maintain objectivity, internal auditors should have no personal or professional involvement with or allegiance to the area being audited; and should maintain an un-biased and impartial mindset in regard to all engagements. Objectivity is a mental attitude which internal auditors should maintain while performing engagements.

The internal auditor should have an impartial, un-biased attitude and avoid conflict of interest situations, as that would prejudice his/her ability to perform the duties objectively. The results of internal audit work should be reviewed before they are released in order to provide a reasonable assurance that the work has been performed objectively. Ideally, internal auditors must be free to report matters they audit as they are and their reporting activities are not subject to any influences (Arena and Azzone, 2009). Independence is a basic to the reliability of auditor’s reports. If the reports of auditors are not believable investors and creditors will not get be satisfied for it, if auditors are not independent in information and appearance. The assurance services provided by auditors derive their value and credibility from the fundamental assumptions of independence of mind and independence in appearance (Stewart and Subramanian, 2010). It is the essence of auditing: an internal auditor must be independent of both the personnel and operational activities of an organization otherwise the integrity of the auditors opinions, conclusions and recommendation would be suspect.

Many auditors to attend their goals and be effective organizational independence are more important. The level of authority where internal audit staff report influence the objectivity of its work and also organizational independence is also an important to the effectiveness of

internal auditors as it protects the auditor from pressure or intimidation, and increases the objectivity of the auditing work (Cohen and Sayag, 2010).

In a study done in United Arab Emirates, the research result revealed that there is significant positive effect of audit committee effectiveness on the objectivity of internal auditors; the results indicate that having an effective audit committee member will enhance the internal auditor's objectivity. Also, the result showed significant positive effect on the objectivity of internal auditors related to having effective audit committee with authority over the employment (appointment/dismissal). Also, the result indicated significant difference between the effectiveness of the audit committee members and the internal auditors' objectivity related to qualifications, and no relationship between the effectiveness of the audit committee members and the internal auditors' objectivity related to the experience. The research revealed that effective audit committees strengthen the position of the internal audit function by increasing the objectivity of internal auditors (Muqattash,2013).

The internal audit function should report functionally to the chairman of the audit committee, recognizing that on a day-to-day basis it should report administratively to the CEO of the organization.

The IIA (2002) also suggests that regardless of the reporting relationship the organization chooses, there are key measures that will ensure that the reporting lines support and enable the effectiveness and independence of the internal audit function. These key measures could be that the head of internal audit should meet privately with the board/audit committee without the presence of management. This will reinforce the independence and direct nature of the reporting relationship. In addition the board/audit committee should have the final authority to review and approve the annual audit plan and all major changes to the plan. Moreover the board/audit committee should review the performance of the head of internal audit and the overall internal audit function at least once a year, as well as approve the compensation levels for the head of internal audit. Finally the charter for the internal audit function should clearly articulate both the functional and administrative reporting lines for the function as well as its principal activities.

2.13. Organizational Independence and Objectivity

The internal audit activity should be independent from the activities it audits. It should also be free from interference in determining the scope of its work, in performing its duties and in communicating the results. To maintain its independence, it should have “solid-line” reporting relationship to the audit committee with a “dotted-line” reporting relationship to a senior executive in the organization for administrative purposes i.e. it should report functionally to those responsible for governance (which can be the audit committee, the board of directors, or another appropriate body) and administratively to an appropriately senior level within the organization.

The audit committee should safeguard internal audit independence by regularly reviewing and approving the internal audit charter and mandate. Administrative matters relate to the organization’s management structure; and the reporting line for them should facilitate the activity’s day-to-day operations. The chief audit executive should have the appropriate seniority in the organization so that the person has sufficient authority. This will reinforce the Organizational status of internal auditing and support its unrestricted access to staff and information.

The activity has to safeguard its independence by getting involved in functional activities like setting the risk appetite for the organization, decision-making, and implementation of responses. It can play the role of facilitator but should not be accountable for implementation of organization’s response to risks or any other operational responsibility.

2.14. Risk Management and Corporate Governance

Risk taking drives corporations to push ahead and make steep gains. When risks pay off, profitability makes shareholders and stakeholders happy. Technology has created greater global interconnectivity, which is an asset for most businesses. Consequently, interconnectivity makes the perspective of risk taking extremely complex. The changing landscape of risk is creating a global conversation about how principles for corporate governance need to evolve to respond more appropriately to the relationship with risk management (insights.diligent.com).

To evaluate how well risks are being managed the internal auditor will assess the quality of risk management processes, systems of internal control and corporate governance processes, across all parts of an organization and report this directly and independently to the most senior level of executive management and to the board's audit committee.

Internal audit activities play an important part in the effective governance and risk and control framework of an organization. Organizations with internal audit activities are better able to identify business risks and system inefficiencies, take appropriate corrective action and ultimately support continuous improvement.

An effective internal audit function provides independent assurance to the board of directors and senior management on the quality and effectiveness of a bank's internal control, risk management and governance systems and processes, thereby helping the board and senior management protect their organization and its reputation (Robert, 2007).

2.15. Review of Empirical Studies

Different researches were conducted on the existing practices of internal auditing in the Ethiopian context. The focus of those papers varies in terms of sectors, industries and institutions. Highlights of some previous research papers on similar subject areas including the research conclusions and recommendations are discussed as part of the assessment of previous empirical evidences and presented as follow:

The review of the literature in general suggested that IAF contributes a key role in effective corporate governance and it is one of the mechanism (or cornerstone) of corporate governance with board of directors (or management), audit committee and external auditors. Sarens (2009)

said; IAF quality has a positive impact on the effectiveness of internal audit. Indicators of effective internal audit such as audit work quality, scope of the audit work, independence of internal audit and adequate and qualified staff of the internal audit are discussed explicitly and their implication on internal audit effectiveness, where appropriate are emphasized.

Mihret and Yismaw (2007) shown that the internal audit office of the organization studied

has low technical staff proficiency and high staff turnover, which would limit its capacity to provide effective service to the management. Furthermore, most of the employees have a short-term employment contract and need to upgrade their competencies to enable them to provide the expected high quality service.

The study by Mulugeta (2008) indicated that the activities of IAF are more of traditional type that emphasize on verification of accounts, compliance, internal control and a little on fraud investigation. Similarly, Kedir et al (2014) studied internal auditing standards and its practice the case of east Arsi zone, Ethiopia concluded that the scope of the internal audit function in the enterprises surveyed did not yet go far from the traditional practices and much time is devoted in performing financial and compliance audits. Mihret and Yismaw, (2007) highlighted that the scope of internal audit services is limited to regular activities. Extending the scope of services by widening the range of systems and activities audited, with appropriate risk analysis, would improve audit effectiveness.

A study conducted on determinants of internal audit effectiveness in Gurage zone local administration by Ayitenew (2018) using primary data through random sampling concluded that the quality of audit work, auditor's independence, auditor's professional proficiency and organizational setting have significant impact on the effectiveness of internal audit. He argued that the scope of the audit work was insignificant for the effectiveness of the internal audit. Yewubnesh (2018) conducted a research on "Determinants of Internal Audit Quality of Economy Budgetary Public Sectors in Ethiopia" using purposive sampling and questionnaires and interview, she concluded that experience of internal auditors, and Independence of internal audit and training were strong and statistically significant effect on the quality of internal audit in budgetary public sectors in Ethiopia.

A research conducted by Arefayne (2019) on the factors affecting internal audit effectiveness in the case of Ethiopian Insurance companies using both primary and secondary questions, argued independence of IA is the sole factor determining effectiveness of internal audit in Ethiopian insurance companies. The researcher mainly recommended; the country's financial regulatory organ (i.e National bank of Ethiopia) should work more on the ways of ensuring the organizational independence of internal auditors and should have to develop transparent and well organized approaches. According

to his study; competence of IA teams, quality of IA were strong but not significantly effect on the effectiveness of internal audit regarding value adding role, enhance department performance, and enhance organizational performance. Ayteneu

(2018) on the other hand argued quality of audit work and auditors professional proficiency were significant factors affecting effectiveness of internal audit.

A research conducted by Tewodros (2016) reveals that insufficient auditor's knowledge on contemporary banking systems, lack of qualified staff and scarcity of facilities were the challenges faced by commercial banks in Ethiopia. He used structured questionnaire to gather data from the respondents of internal auditors while interview has been made with executives. The study used purposive sampling specifically on the selection of chief audit executives.

Tamiru (2018) conducted a study on the current practices of internal audit in Private Commercial Banks of Ethiopia through taking the Mandatory Guidance requirements of IPPF as a benchmark and concluded that the mandatory guidance requirements conformance level within the selected Private Commercial Banks of Ethiopia did not move up to the expectation that satisfies the IAS. The sample of the research focused on five private banks that selected by using purposive sampling technique. Both qualitative and quantitative data types were applied in the study. He used primary and secondary data collection methods to conduct the study.

Mulugeta (2008) conducted a research on "Internal Audit: Reporting Relationship in Ethiopian Public Enterprises" With objectives of analyzing the reporting line of internal audit and investigate its relationship with internal audit scope, independency, good governance and audit committee. He conducted the survey study on selected Ethiopian public enterprises and recommended possible ways to cope up with the problems identified in the research so as to promote the good image of internal audit profession. The results of the survey showed that the functional reporting lines in practice were not always organized according to the theoretical assumptions, particularly in ETC (i.e. at Zonal and regional level) and Zequala steel rolling Factory; internal audit has been seen as outside the management structure (outsider) and board members are ministers who have several other

responsibilities so that they do not have sufficient time to deal with the oversight of the internal audit function; the Ethiopian public enterprises internal audit scope is more limited on the verification of financial transaction (Financial audit), compliance audit, assessments of internal control, and fraud investigation. The researcher finalized his study by recommending corrective actions to address the weaknesses identified. (Mulugeta, 2008)

2.16. The Research Gap

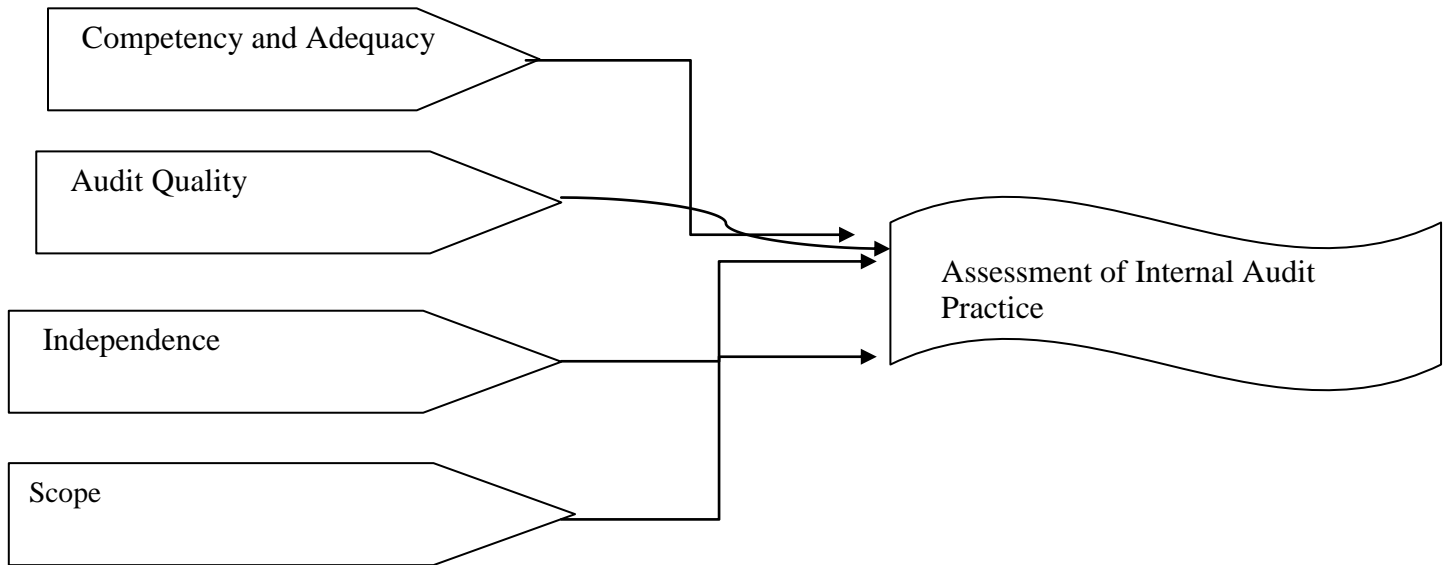
In general, the literature review indicates that internal auditing role is wide. Within the context of improving risk management, control and governance processes, and the type of work undertaken to add value to an organization will vary greatly. Besides internal audit effectiveness is strongly influenced by internal audit quality and management support Mihret and Yismaw (2007) Hence, IA effectiveness does play a role in ensuring effective management in public sector there is needs to enhance the technical proficiency of the internal audit staff and minimize staff turnover so as to foster audit effectiveness. The organizational status and internal organization of the internal audit office are fairly rated, but internal audit's lack of authority on budgets reduces its control of resource acquisition and utilization, improvement in the areas of audit planning, documentation of audit work, audit communications and follow-up of recommendations. In additions, the lack of attention by management may send a wrong signal about the importance of internal audit services to the auditee, which in turn adversely affects the auditee attributes (Mihret and Yismaw,2007).

The review of empirical studies reveals that most of the studies are outside Ethiopia. There are few studies on internal audit practices in Ethiopia but they focused on governmental organizations. Accordingly, the researcher attempted to carry out this study for the reason that it is unexplored area in private commercial Banks in Ethiopia in general and Particularly in Selected Private Bank. Therefore, examining the Internal Audit effectiveness helps in promoting effective corporate governance and performance of the organization and could fill the gap to the literature in general in Ethiopian context.

2.17. Conceptual Framework

The conceptual framework is a diagrammatic representation of the study variables. In other words, the framework outlines how the variables interact. Figure 1 illustrates the

conceptual framework for this study.



Source- Developed from preliminary literature review

The conceptual framework indicates that there are four different variables which include competency and adequacy of internal auditors, scope of the audit work, internal audit quality, and level of independence of auditors to assess the internal audit effectiveness.

CHAPTER THREE

3. RESEARCH DESIGN AND METHODOLOGY

3.1. Introduction

The following different sections were discussed in this chapter. The first section presents the research methodology and design. Types and sources of data, the target population, sample size and sampling techniques were presented in the subsequent sections. In the last section methods of data distribution and collection, and methods of data analysis by preceding methods of data interpretation and presentation, were briefed accordingly.

The research methodology used may vary from research to research. Depending on the

philosophical stance, strategies of inquiry and specific methods, a research approach can be categorized as quantitative research approach, qualitative research approach and mixed research approach. Quantitative research most often uses deductive logic, in which researchers start with hypothesis and then collect data which can be used to determine whether empirical evidence to support that hypothesis.

This refers to the type of research that is based on the methodological principles of positivism and neo positivism, and adheres to the standards of a strict research design developed prior to the actual research. It is applied for quantitative measurement and hence statistical analysis is used. Quantitative research is used in almost every sphere of life, such as in clinical, biological, epidemiological, sociological and business research (Adams et al., 2007). This research study intended to assess the internal audit practice of Commercial Bank of Ethiopia using close ended questions. Therefore, the study was quantitative and describes the internal audit practice of Commercial Banks.

3.2. Research Design

This study used a descriptive design to assess internal audit practice. A quantitative research design was set out to collect data. A descriptive study is one in which information is collected without changing the environment, nothing is manipulated. Descriptive research design is a scientific method which involves observing and describing the behavior of a subject without influencing it in any way (Bickman & Rog, 2007). Descriptive study type of research was used because this method or type of research is commonly conducted to collect detail description of existing phenomena with the intent of employing data to justify current conditions and whenever possible to draw valid general conclusions from the facts discovered (Koul, 2006).

This Study also helps in assessing internal audit practice within selected Ethiopian private banks. Therefore, internal auditors and control department executives have been chosen as the statistical target population. To do so, the study has highly focused on primary and based on the data collected, results are interpreted.

3.4. Target Population

The target population of the study was assessment of internal auditing practice to all private

commercial banks that have been currently operating in Ethiopia.

3.5. Sample Size

The sample for this study focused on 16 commercial Bank of Ethiopia only selected four private Bank: Awash International Bank ,Addis International Bank, Oromia International Bank, Cooperative Bank of Oromia, were selected By using Survey sampling. Survey sampling is the process of choosing, from a much large population, a group about which wish to make generalized statements so that the selected part represent the total group (Leedy, 2000).The study employed only internal auditors who are assigned to Internal Audit (Control) Departments of the selected banks. The researcher sample on 35 employees from each selected four private Bank, the total sample size of this study was 35respondents.

3.6. Sampling Techniques

Accordingly 35 staffs of Awash International Bank, Addis International Bank, Oromia International Bank, Cooperative Bank of Oromia respectively were fully recognized in the sample.

3.7. Sources of Data Collection

Quantitative data used in the study. Furthermore, the sources of data were primary. Developing and distribution of questionnaires to the concerned employees of Commercial Bank was the primary and major source of data gathering instrument. The data was expected to be reliable, because the questionnaire was distributed to the internal auditors of the bank and as a profession the respondents expected to be ethical and their response determine the validity of the study.

3.8. Methods of Data Collection

The study used primary data collection methods. The primary source of data basically focused on questionnaires distribution and collection. The questionnaire is a fast way of obtaining data as compared to other instruments (Mugenda, 2003). Questionnaires give the researcher comprehensive data on a wide range of factors. Questionnaires allow greater uniformity in the way questions are asked, ensuring greater compatibility in the responses. Accordingly, 35 Questionnaires were prepared and distributed to the internal audit staff and control department employees at the Commercial Bank. The collected data was analyzed by using SPSS.

The data was expected to be reliable, because the questionnaire was distributed to the internal auditors of the bank and as a profession the respondents expected to be ethical and their response determine the validity of the study.

3.9. Methods of Data Analysis

After collecting and sorting the relevant data, the responses was sorted, coded, computed, and analyzed using Statistical Package for Social Sciences (SPSS) software-version 20.0 for descriptive statistical methods particularly by measure of central tendency (mean) values, frequency, percentage, measure of central dispersion (standard deviation). Also the results of the study have been presented by using various tables and to assess the reliability and consistency of the instrument, the Cronbach's Alpha (α) analysis was conducted.

3.10. Reliability

It is a way of assessing the quality of the measurement procedure used to collect data in a dissertation. In order for the results from the study to be considered valid, the measurement procedure must first be reliable (learntech.uwe.ac.uk). In this regard the study investigated the internal audit effectiveness of Commercial Bank in related to the scope of the audit work, audit work quality, the level of independence of the internal audit function and adequacy of competent internal audit staff. To carry out the reliability analysis, Cronbach's Alpha (α) is the most common and would have been deployed.

3.11. Validity

Bond, (2003) comments that validity is foremost on the mind of those developing measures and that genuine scientific measurement is foremost in the minds of those who seek valid outcomes from assessment. Validity can be seen as the core of any form of assessment that is trustworthy and accurate (Bond 2003). This study investigated the effectiveness of the internal audit practice in Commercial Bank using primary data. Questionnaire is one of the best methods of collecting valid information. The questionnaires are taken from Mr. Desalegn (2008) and they were strong and Supportive to measure the effectiveness of internal audit practice.

3.12. Ethical Considerations

The research was conducted in commercial Bank and it may help the company in

strengthening its internal audit practice as a result the employees of the bank would give their opinion without any frustration. Generally the study would have benefit to the bank as well as the employees.

CHAPTER FOUR

4. DATA ANALYSIS AND INTERPRETATIONS

4.1. Introduction

The primary concern of this study was to investigate the internal audit practice in Commercial Bank. Specifically, how the internal audit is functioning in related to the audit plan, scope of the audit work, reporting, follow-up and quality review, the level of independence of the internal audit function and adequacy of competent internal audit staff in Selected Private Bank. The aim of this chapter is therefore to analyze and interpret the data obtained in the study.

4.2. Data analysis and interpretation

Data were analyzed using Statistical Package for Social Sciences (SPSS Version 20) program through a descriptive statistics to provide details concerning question and qualitative analysis was used as data analysis technique. Primarily the data was collected through the questionnaires and analyzed by using descriptive statistics for responses to be obtained by using open-ended and close ended questions. The study targeted a sample size of 35 respondents from which 32 filled in and returned the questionnaires making a response rate of $32/35=90\%$. This response rate was satisfactory to make conclusions for the study because a response rate of 70 percent or above is usually taken as adequate (Roberts2004).

To measure the consistency of the questionnaire particularly the Liker type scale, the reliability analysis is essential in reflecting the overall reliability of constructs, which it is measuring. To carry out the reliability analysis, Cranach's Alpha (α) is the most common measure of scale reliability and a value greater than 0.700 is very acceptable (Field, 2009; Cohen and Sayag, 2010).

According to the under listed table, the reliability analysis result of all variables revealed 0.789 and hereby the responses generated for all of the variables'' used in this research were reliable enough for data analysis.

Reliability Statistics

Cronbach's Alpha	N of Items
.789	5

Source: Reliability statistics analysis by SPSS (20).

Questionnaires designed for this particular research were distributed to 35 internal auditors and 3 control department members at head office level. However, three questionnaires from internal auditors were not returned to the researcher. From the total questionnaires distributed, $32/35=90\%$ of the questionnaires were filled by the respondent and returned to the researcher. Hence, 3 control department executives and 32 internal auditors took part in this research.

4.4. Demographic Characteristics of the Respondents

4.5. Gender of Respondents

The researcher wanted to determine the gender of the respondents and therefore requested the respondent to indicate their gender. The study found that majority of the respondents as 56.7% were males whereas, 43.3% of the respondents were females. This is an indication that both genders were involved in study. As the sample considers only the job position held in the bank, fortunately the finding of the study did not suffer from gender bias.

Source: Questionnaire results analysis by SPSS (20).

Table 4.1 Gender Profile

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid F	17	43.3	43.3	43.3
M	18	56.7	56.7	100.0
Total	35	100.0	100.0	

Source: Questionnaire results analysis by SPSS (20).

4.6. Position of Respondents

The researcher requested respondents to indicate their position in the bank and find out that the sample population is largely dominated by internal auditors with 93.3% and the remaining 6.7% were internal audit manager and section head.

Table 4.2 Position Profile

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid IA	30	93.3	93.3	93.3
Other	2	3.3	3.3	96.7
IAM	3	3.3	3.3	100.0

Total	35	100.0	100.0	
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4.7. Academic Qualification

The study also sought from the respondents about their educational status and as depicted in the table below the majority of the sample group holds a degree which accounted 26 (86.7%) and the remaining 4 (13.3%) were masters holders. All of the respondents are educated, it can be concluded that almost all employees are capable of understanding and answering the questions in the questionnaires.

Table 4.3 Academic Qualification Profile

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Degree	26	86.7	86.7	86.7
	Masters	9	13.3	13.3	100.0
	Total	35	100.0	100.0	

Source: Questionnaire results analysis by SPSS(20).

4.8. Related Certification of Respondents

Among the whole only one of the respondent was ACCA holder which accounts 3.3%, the remaining 96.7% do not have related certification, and it indicates the department lacks qualified and certified staffs.

Table 4.4 Related Certification Profile

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	NRC	32	96.7	96.7	96.7
	ACC A	3	3.3	3.3	100.0
	Total	35	100.0	100.0	

Source: Questionnaire results analysis by SPSS (20).

4.9. Experience of Respondents

The researcher requested the respondents to point out the number of years they served in Selected private Bank and the finding of the study reveal that internal auditors have served the Bank from more than a year up to less than 15 years. From the respondents, only 2 of them worked more than ten years. Most of the respondents have served the company between one and five years comprising 63.3% of the study group, and the remaining 30% served the bank between six and ten years.

Table 4.5 Experience Profile

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid =>1 Years Less than 5 Years	30	63.3	63.3	63.3
=>5 Years Less than 10 Years	3	30.0	30.0	93.3
=>10 Years Less than 15 Years	2	6.7	6.7	100.0
Total	35	100.0	100.0	

Source: Questionnaire results analysis by SPSS (20).

4.10. Statements Regarding the Internal Audit Competency and Proficiency

The following eight questions (Q1-Q1H) were distributed and used to analyze the competency and professional due care of internal auditors in the bank. The results are analyzed as follows.

Q1A. The internal audit department is large enough to successfully carry out its duties
 Q1B. Internal audit obtains a sufficient budget to successfully carry out its duties

Q1C. Internal auditors possess sufficient experience to understand the organizations systems
 Q1D. The internal audit staffs possess knowledge and skills in a variety of areas (beyond accounting and finance), as necessary

Q1E. Internal audit has policies for training of internal audit staff

Q1F. Internal auditors undertake continuous professional development activities (such as professional association sponsored programs and correspondence courses)

Q1G. Adequate short-term training is arranged for internal auditors each year
 Q1H. There is a complete internal audit manual to guide internal audit work

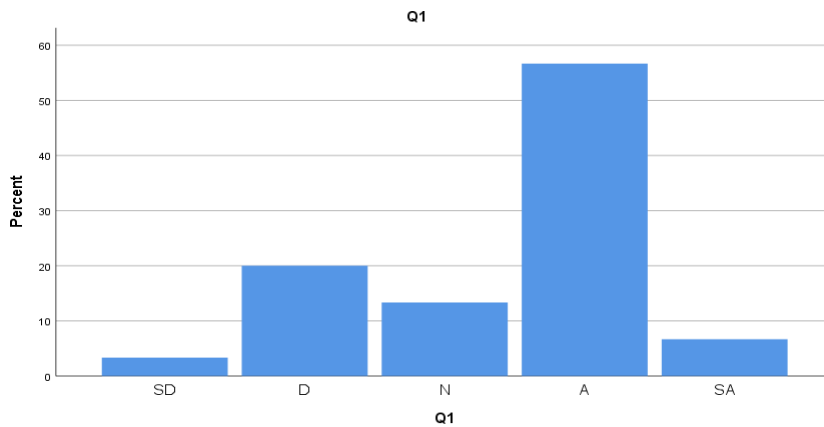
Table 4.6 Descriptive Statistics for Competency and Proficiency

		Q1A	Q1B	Q1C	Q1D	Q1E	Q1F	Q1G	Q1H
N	Valid	35	35	35	35	35	35	35	35
	Missing	0	0	0	0	0	0	0	0
Mean		3.43	3.27	3.40	3.43	2.83	2.30	2.30	4.33
Median		4.00	3.50	4.00	4.00	3.00	2.00	2.00	4.00
Mode		4	4	4	4	2	2	2	4
Std. Deviation		1.006	.944	1.102	1.040	1.117	1.055	1.055	.661

Source: Questionnaire results analysis by SPSS(20).

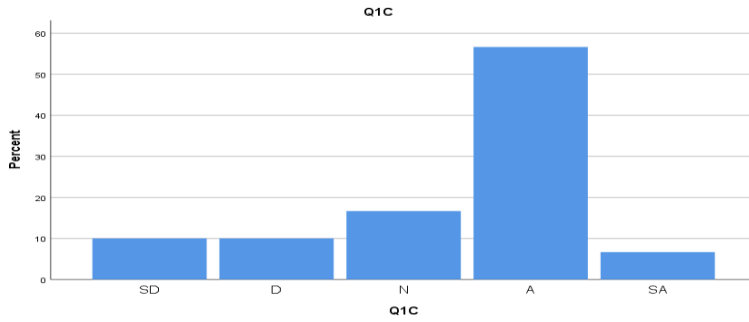
As table 4.6 indicates, most of the respondents agreed with the existence of sufficient man power and budget comprising of 56.7% and 46.7% respectively to carry out the audit activity of the bank. With the exception of total of 23.3% who responded as strongly disagree and disagree on these, most of the respondents believe that the internal audit

department is adequately staffed and adequate budget is allocated to perform the audit work.



Graph 1 The internal audit staff adequacy

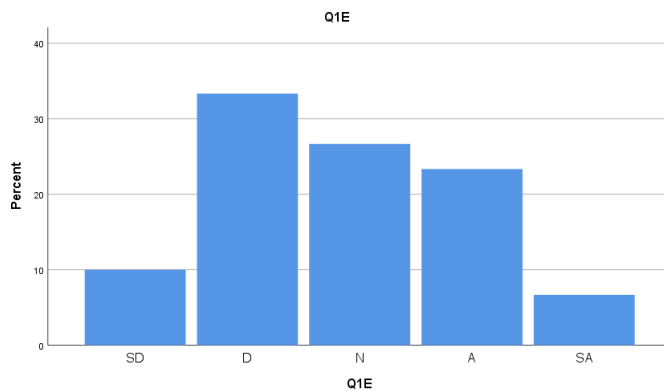
As table 4.6 indicates, 56.7% of the total respondents agree with the existence of experience sharing program set by internal audit department to help auditors flow their ideas, teach and learn and discuss thoroughly about the auditing matters they encounter by raising various cases and come up with a solution. The graph below indicates their trend. 46.7% respondents believe that the internal audit staffs possess adequate knowledge and skills to understand the organizations systems. The mean value 3.4 signifying that most of the respondents agree with the internal auditors adequate knowledge and experience to be familiar with the Bank`s system and other operations as well.



Graph 2 Experience of auditors in understanding the organizations' system

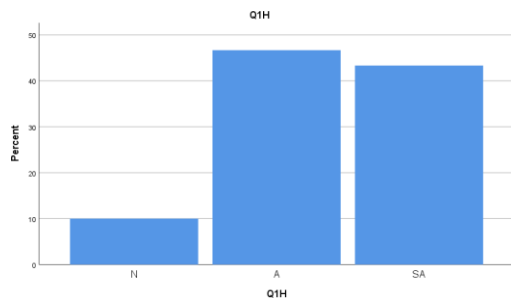
Majority of respondents constituting 33.3% were disagreed with the existence of internal audit department policies for regular training purpose implying that the department lacks competent updated staff that could resolve the challenges they face from within. Moreover the mean value

2.83 indicate that majority of respondents' disagreement towards the training policy the department has for internal auditors. With regards to short term training, 43.3% responded the inadequacy of short term training as being the threatening fact for the department in the course of accomplishing its predetermined duties. The mean value 2.3 also indicates the majorities' disagreement towards this variable. Regarding the continuous professional development activities, 43.3% of the respondents disagreed with the existence of association sponsored programs and correspondence courses.



Graph 3 Responses on Policies for training of internal audit staff

According to the analysis results most of the respondents which comprises 46.7% agreed with the existence of internal audit manual. The department has developed and provided a



complete internal audit manual which helps the internal auditors to perform their duties accordingly.

Graph 4 Existence of complete internal audit manual to guide internal audit work

According to (Albrecht et al. 1999, Ratliff 1996) the greater the professional Qualification of the internal auditors in a given department, defined by the length of their professional training, experience and educational level, the greater the effectiveness of this department. As it is shown in table 4.6, the internal audit department is not giving necessary training and development program that could enhance the auditors' skill and experience to audit all the banks systems by preparing proper plan for risk identification so as to deliver high quality audit services to the bank.

The international standard for the professional practice of internal Auditing (ISPPIA 1210) suggests that internal auditors must possess the knowledge, skills, and other competencies needed to perform their individual responsibilities. The internal audit activity collectively must possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities. The chief audit executive must obtain competent advice and assistance if the internal auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement. Accordingly the department has to provide sufficient training to internal auditors to enhance their skill and knowledge.

4.11. Statements Regarding Audit Work Quality

The following five questions (Q2A-QE) were used to analyze the practice of the internal audit plan of the bank which has effect on the work of audit quality.

Q2A. Annual internal audit plan is prepared

Q2B. Risk assessment is done as part of audit planning

Q2C. Senior management input is considered in setting internal audit priorities

Q2D. During the examination of audit evidence, analytical audit procedures (e.g. ratios, trends, etc.) are used as appropriate

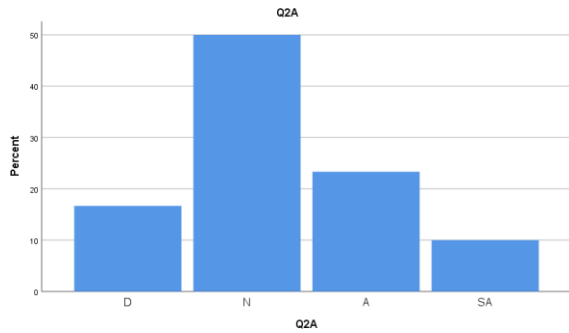
Q2E. Audit work is documented and maintained in a file of audit working

papers

		Q2A	Q2B	Q2C	Q2D	Q2E
N	Valid	35	35	35	35	35
	Missing	0	0	0	0	0
Mean		3.27	3.27	3.33	3.30	3.93
Median		3.00	3.00	3.00	3.00	4.00
Mode		3	3	3	3	4
Std. Deviation		.868	.691	.711	.877	.980

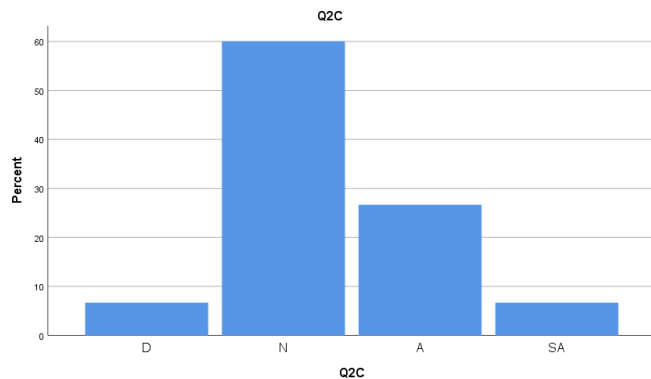
Source: Questionnaire results analysis by SPSS (20).

Majority of the respondents constituting 50%, were neutral regarding the preparation of the audit plan in the bank., 16.7% of respondents disagreed with the preparation of audit plan, 23.3% and 10% of respondents agreed and strongly disagreed with the audit plan preparation. Likewise 56.7% of respondents were neutral on whether the risk assessment is done as part of audit planning or not. The other 30% of respondents believe that risk assessment is done as part of audit planning; the remaining 10% of respondents expressed their disagreement on the issue. The mean 3.27 indicates that most of the respondents lies between neutral and agree which implies the existence of information gap between the internal auditors and control department executives.



Graph 5 the audit plan preparation

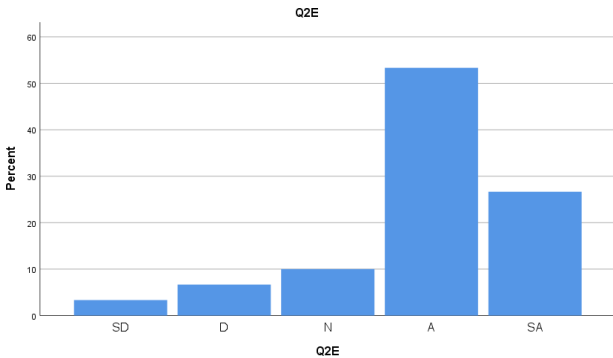
As table 4.7 indicates 60% of respondents which comprises the majority expressed their neutrality whether the senior management input is considered in audit planning or not. The other 6.7%, 26.7%, and 6.7% respondents disagreed, agreed, and strongly agreed respectively on the consideration of senior management as an input in audit planning. Most of the respondents comprising 46.7% were neutral regarding the use of analytical audit procedures such as ratios and trends during audit evidence examination. The other 33.3% of respondents believe with the use of analytical audit procedures during audit evidence examination. Few of the respondents comprising 13.3% do not agree with use of analytical audit procedures.



Graph 6 Consideration of Senior management input in setting internal audit priorities

The aggregate results as shown in table 4.7 revealed that the audit work is documented and maintained in a file of audit papers with the average mean 3.93, and the standard deviation 0.980 was revealed and witnessed that the variance of perception among internal auditors

was low.



Graph 7 Documentation of the audit file

The following questions (Q2F- Q2R) used to analyze the reporting, follow up and quality review trend in the bank. The results of the questionnaire analyzed as follows.

Q2F Were audit observations communicated fairly, clearly, accurately, and in a timely manner during the course of the audit?

Q2G Were your concerns adequately addressed and differences of opinions, if any, resolved before the final audit results were communicated?

Q2H Was the content of the audit report communicated clearly, fairly and accurately and the report issued in a timely manner?

Q2I Audit findings are discussed with auditees before being reported on

Q2J Internal auditors follow up implementation of corrective actions relating to audit findings Q2K The reporting level varies with the importance of internal audit findings

Table 4.8 Descriptive statistics on Audit work quality

		Q2F	Q2G	Q2H	Q2I	Q2J	Q2K
N	Valid	35	35	35	35	35	35
	Missing	0	0	0	0	0	0
Mean		3.93	3.53	3.90	3.23	4.03	3.93
Median		4.00	4.00	4.00	4.00	4.00	4.00
Mode		4	4	4	4	4	4
Std. Deviation		.868	.900	.885	1.455	.615	.740

Source: Questionnaire results analysis by SPSS (20).

Majority of the respondent, comprising 56.7% agreed on the fair, clear accurate and timely communication of audit observation findings during the course of the audit. The other 10% disagreed and 23.3% of respondents strongly agreed on this. The mean 3.93 implies the banks good trend reporting. Out of the total respondents 60% believes their concerns adequately addressed and differences of opinions resolved before the final audit results were communicated. Six of the respondents which account 20% from the total expressed their disagreement on this. The mean 3.53 and the standard deviation 0.900 indicate the internal auditors concern was adequately addressed.

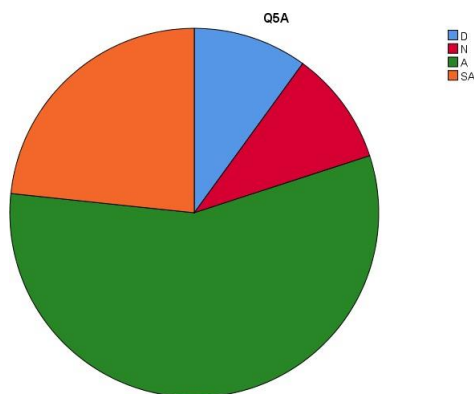


Chart 1 Accurate, fair and clear communication of audit observations

Out of the total respondents 35% of them agreed on the existence of discussion with the

auditees before the finding it was reported to the concerned body. The other 16.7% and 20% of respondents respectively strongly disagreed and disagreed on this. The standard deviation 1.455 indicates there was high variation among the respondents and this implies the existence of weak trend of discussing with the auditee before reporting. Majority of the respondents comprising 73.3% believed internal auditors had follow up implementation of corrective actions relating to audit findings. The other 3.3% and 16.7% disagreed and strongly agreed respectively on the existence of corrective actions. The mean 4.03 and the standard deviation 0.615 witnessed the good trend of corrective actions.

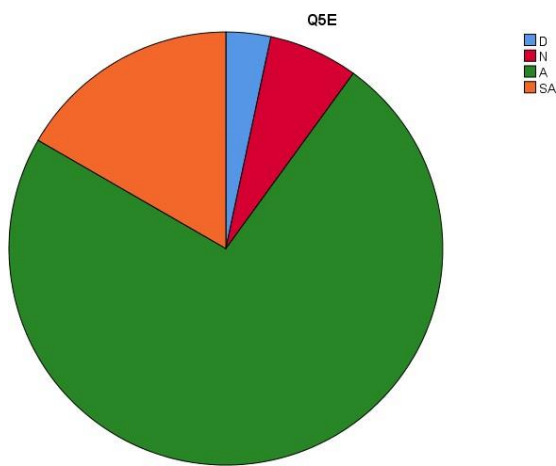


Chart 2 Existence of follow-up implementation of corrective actions

Majority of the respondents constituting 76.7% believes that the reporting level varies with the importance of internal audit findings. The other 10% and 13.3% of respondents disagreed and strongly agreed on existence reporting level. The mean 3.93 and the standard deviation 0.740 witnessed the presence of reporting level on the basis of the audit findings.

Table 4.9 Descriptive statistics on Audit work quality

	Q2L	Q2M	Q2N	Q2O	Q2P	Q2Q
N Valid	35	35	35	35	35	35
Missing	0	0	0	0	0	0
Mean	2.90	3.07	4.20	4.03	4.20	2.90
Median	3.00	3.00	4.00	4.00	4.00	3.00
Mode	3	4	4	4	4	2
Std. Deviation	1.155	1.172	.407	.718	.664	1.155

Source: Questionnaire results analysis by SPSS (20).

Q2L Corrective action plan is agreed with management before the report is issued

Q2M Management takes timely corrective action based on internal audit recommendations

Q2N How often the following included in the internal audit reports? The audit purpose and scope (Always)

Q2O The audit findings and conclusions (Always)

Q2P Audit recommendations (Always)

Q2Q Auditees,, comments regarding audit findings (Always)

Regarding the corrective action plan agreement with the management on the basis of audit recommendations 23.3% of respondents expressed their disagreement, 13.3% strongly disagree, 26.7% agree and 6.7% strongly agree. The mean 2.90 indicates the poor practice of preparation of action plan agreement with the management. The standard deviation 1.155 implies the existence of high variation among the respondents.

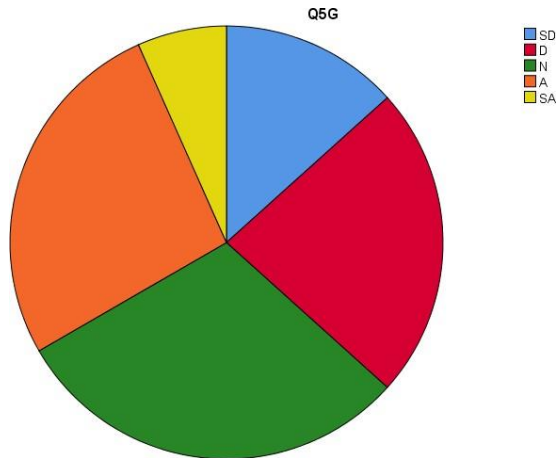


Chart 3 Existence of corrective action plan agreement with the management

Majority the respondents comprising 40% agreed and believes the management takes timely corrective action based on internal audit recommendations. The other 26.7% of respondents disagreed. The mean 3.07 indicates the existence somewhat moderate corrective action. The variance 1.172 implies the existence of high variation among the respondents.

The internal audit report of the bank contains the audit purpose and scope with 80% agreement of the respondents and the remaining 20% of respondents strongly agreed on. The mean 4.2 and the standard deviation 0.407 witnessed the inclusion the audit purpose and scope in the audit report of the bank. Likewise most of the respondents which account 70% agreed on the inclusion of audit findings and conclusions in the report. The mean 4.03 and the standard deviation 0.718 witnessed the good practice of reporting.

Out of the total respondents 63.3% of them agreed on the inclusion of audit recommendations in the audit report. The mean 4.2 witnesses this and the standard deviation 0.664 implies there was little variation among the respondents. Majority of the respondents constituting 40% believe auditees comment regarding the internal audit report were not included. The other 20% and 23.3% of respondents agreed and strongly agreed respectively on this. The mean 2.9 indicates the exclusion of auditees comments in the audit report. The standard deviation 1.155 implies the existence of high variation among the respondents.

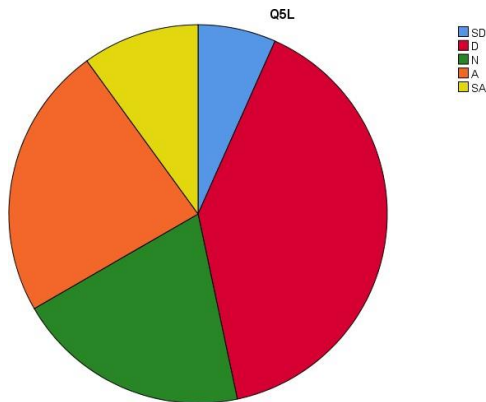


Chart 4 Existence of auditee comments regarding audit findings

4.12. Statements Regarding Internal Audit independence and Objectivity

The following seven questions (Q3A – Q3G) were used to assess the independence and objectivity of the internal audit. The result the data discussed as follows below.

Q3A Internal audit is free from intervention in performing its duties

Q3B Internal auditors feel free to include any audit findings in their audit

reports Q3C Internal audit provides reports to the board of directors (or audit committee)

Q3D The board of directors or audit committee oversees employment decisions in internal

audit Q3E Internal auditors are not assigned to audit areas in the system design of which they participated

Q3F Internal auditors do not participate in audit of activities for the operation of which they were responsible

Q3G Internal audit staff assignments are rotated periodically

Table 4.10 Descriptive statistics on the internal audit independence and objectivity

Statistics

	Q3A	Q3B	Q3C	Q3D	Q3E	Q3F	Q F
N Valid	35	35	35	35	35	35	35
Missing	0	0	0	0	0	0	0
Mean	3.10	3.47	3.40	3.33	2.47	2.53	3.63
Median	3.50	4.00	4.00	3.00	2.00	2.00	4.00
Mode	4	4	4	3	2	2	4
Std. Deviation	1.242	1.074	1.248	.547	.860	.819	1.189

Source: Questionnaire results analysis by SPSS (20).

Regarding the intervention of the management majority of the respondents which comprises 40%, agreed on the absence of intervention of the management on performing their duties as the chart below indicates. The mean 3.10 indicates most of the auditors feel free to perform their job without interference from the management. Most of the respondents which comprises 50% agreed upon including any findings on their report without fear of the management. The mean 3.47 witnessed the internal auditors feel free to include any finding and they have free access to all necessary information and records.

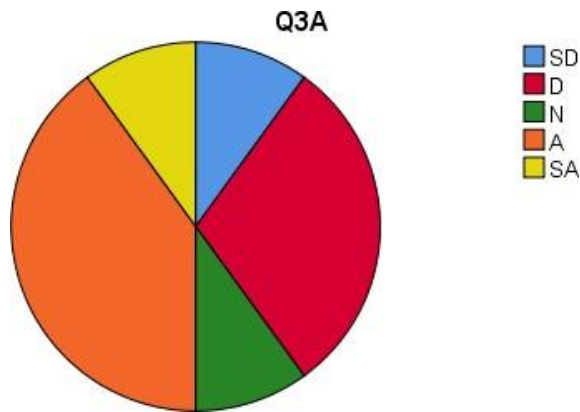
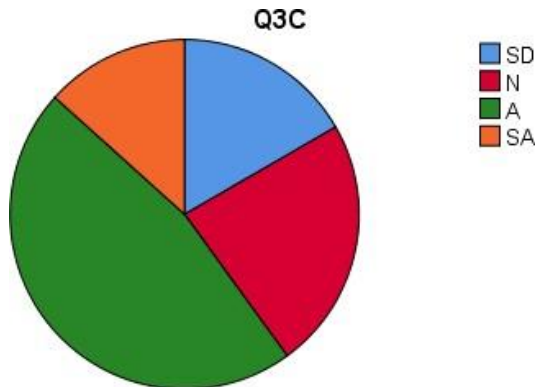


Chart 5 Responses on the freedom of the IA from intervention of the management

Based on the data collected 46.7% of the respondents believed with the delivery of the audit report to the board of directors through the audit committee. The other 16.75% of the respondents strongly disagreed on the delivery of the report to the board and 23.3% of respondents were neutral as the chart below shows. Majority of the respondents comprises 60% were neutral regarding whether the board of directors or audit committee oversees



employment decisions in internal audit, while 36.7% of the respondents agreed, and the remaining 3.3% of respondents disagreed on the oversee of the audit committee or the board of directors on employment decisions.

Chart 6 Delivery of the audit report to the board of directors

Majority of the respondents constituting 56.7% disagreed and believed on internal auditors do not assigned to audit areas in the system design of which they participated. 16.7% of the respondents agreed with this idea and the other 20% of the respondents are neutral. As the above table indicates most of the respondents comprises 56.7% disagreed on the internal auditors do not assigned on the operation in which they are responsible to audit. The other 16.7% respondents agreed with issue. The mean 2.53 indicates most of the respondents believe the internal auditors assigned to perform operations in which they are responsible to audit. It is shown below in the chart.

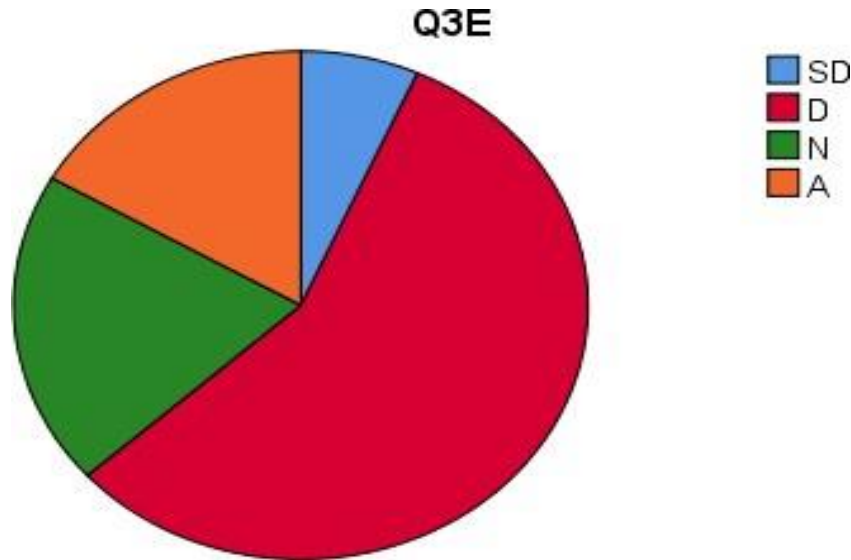


Chart 7 Internal auditors do not assign on the operation they are responsible to audit

Regarding the periodical rotation of internal auditors 50% of the respondents agreed and believe the existence of periodic rotation of employees from internal auditors. The other 10% of respondents strongly disagree with the periodic rotation, 6.7% of respondents disagreed, 13.3% disagreed and the remaining 20% of respondents strongly agreed. The mean 3.63 implies the existence of periodic rotation of employees from one Bank to the other.

International standards for the professional practice of internal Auditing (ISPPA 1100) suggest that the internal audit activity must be independent, and internal auditors must be objective in performing their work. Organizational independence of internal auditors can be obtained by means of reporting to levels within the organization that allow the internal audit department to perform its responsibilities free from interference; avoiding conflict of interest; having direct contact with the board and senior management; having unrestricted access to records, employees and department; the appointment and removal off the head of internal audit not being under the direct control of executive management. Regarding the independence of the auditors the survey result indicates that they are free from intervention of the management and they are free to include any findings in the audit report.

4.13. Statements Regarding the Scope of Internal Audit Work

The following questions (Q4A- Q4O) used to analyze scope of the internal audit work in the bank. The results of the questionnaire analyzed as follows.

Q4A Did Internal audit solicit feedback from you and your staff during the entrance conference to ensure your concerns were adequately addressed during the audit?

Q4B Did you receive written/verbal notification of the overall audit scope and objectives during the initial phase of the audit?

Q4C Do you feel that the scope of the audit (i.e., the processes, activities, period of coverage, etc.) is sufficient and key risk areas were covered?

Q4D Checking adequacy of the auditees,, record keeping when

appropriate Q4E Verifying accuracy of amounts in financial records

Q4F Reviewing information contained in reports of operating departments

Q4G Checking efficiency of operating results (e.g. whether cost saving alternatives

areused) Q4H Ascertaining compliance with organizational policies and procedures

Table 4.11 Descriptive statistics on the scope of the internal audit work

	Q4A	Q4B	Q4C	Q4D	Q4E	Q4F	Q4G	Q4H
N Valid	35	35	35	35	35	35	35	35
Missing	0	0	0	0	0	0	0	0
Mean	3.07	3.80	3.57	3.77	3.97	3.50	2.83	4.10
Median	3.00	4.00	4.00	4.00	4.00	4.00	3.00	4.00
Mode	4	4	4	4	4	4	3	4
Std. Deviation	1.172	.887	1.006	.728	.765	.900	.986	.885

Source: Questionnaire results analysis by SPSS (20).

36.7% and 2.7% of agree and strongly agree with the existence of request of feedback from internal auditors to ensure whether their concerns are addressed or not. The mean 3.07 indicates majority of them lies between agree and neutral. The standard deviation 1.172 implies the existence moderate variation among the respondents.

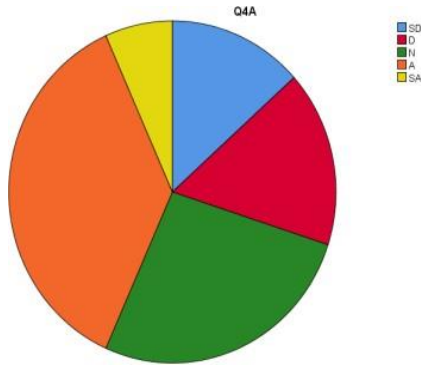


Chart 8 Feedback request from internal auditors

A total of 66.6% of respondents believe on the existence verbal or written notification the overall audit scope and objectives during their entrance in the department. Only 3 respondents with 3.3% and 6.7% strongly disagree and disagree on this. The standard deviation .877 implies that their little variation among the respondents on the case. As the chart below indicates 56.7% of respondents believe with the sufficiency of the internal audit scope. Total of 4 respondents with 6.7% each strongly disagree and disagree on the sufficiency of the internal audit scope. Therefore, from the result it can be concluded that internal scope i.e., the processes, activities, period of coverage, etc. is sufficient.

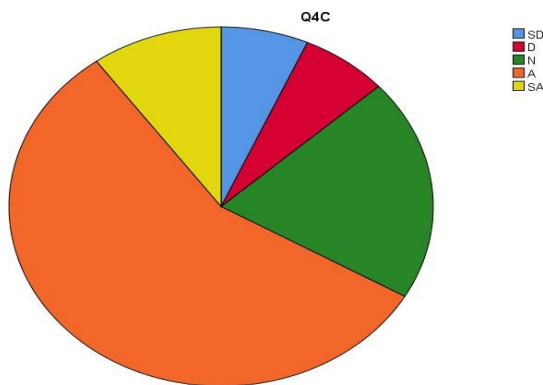


Chart 9 The sufficiency of the internal audit scope

From the total 80% of the respondents believed and agreed that the internal auditors check the adequacy of the auditees record keeping. The mean 3.77 witnessed this. The standard deviation 0.728 implies there was little variation among the respondents on the case.

Majority of the respondents comprising 70% believes that the internal auditors verify accuracy of amounts in financial reports of the operational department. The mean 3.97 and the standard deviation 0.765 witnessed the existence of verifying amounts in the financial statements. Only one of the respondents strongly disagreed with the case. Besides to amounts 63.3% respondents believe the internal auditors also review information contained in reports of operating department. The following chart implies the agreement of the majorities on this.

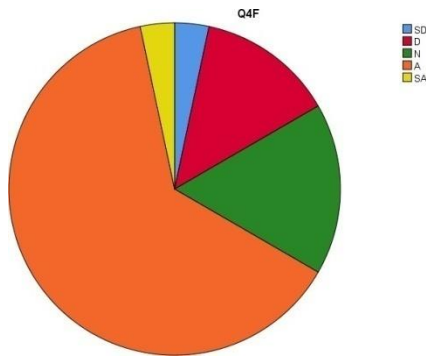


Chart 10 Reviewing information of operating departments

30% of the respondents agreed on the role of the internal auditor in checking efficiency of operating results (e.g. whether cost saving alternatives are used). The other 26.7% of respondents disagreed on the case and the mean 2.83 indicates there was little attention in checking efficiency of operating results. From the total respondents 60% of them agreed and believes the internal auditors ascertain compliance with organizational policies and procedures. The mean 4.10 witnessed the existence of checking the operation against the established operational manual. The standard deviation 0.885 implies there was little variation among the respondents and it can be concluded that the auditors cross check whether the operational activity was conducted in line with the established operational manual or not.

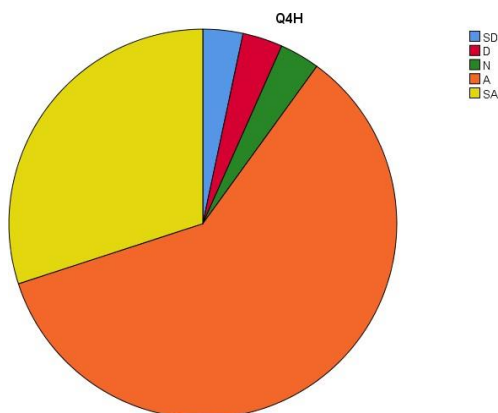


Chart 11 Ascertaining Compliance with organizational policies and procedures
 Q4I Checking compliance with contracts when applicable
 Q4J Checking compliance with external laws and regulations when applicable
 Q4K Ascertaining that operating objectives are consistent with organizational goals
 Q4L Ascertaining that operating procedures are consistent with the operational goals
 Q4M Reviewing operations to ascertain they were implemented as intended
 Q4N Assisting the management by identifying risk exposures of the organization
 Q4O Providing consulting services to management where internal audit has the expertise

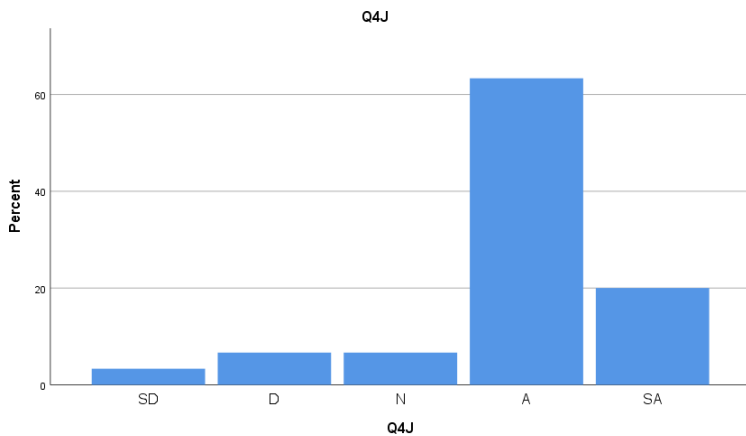
Table 4.12 Descriptive statistics on the scope of the internal audit work

	Q4I	Q4J	Q4K	Q4L	Q4M	Q4N	Q4O
N Valid	35	35	35	35	35	35	35
Missing	0	0	0	0	0	0	0
Mean	3.90	3.90	3.53	3.70	3.77	3.63	3.43
Median	4.00	4.00	4.00	4.00	4.00	4.00	3.50
Mode	4	4	4	4	4	4	4
Std. Deviation	.995	.923	1.008	.837	.679	.615	.626

Source: Questionnaire results analysis by SPSS (20).

Majority of respondents constituting 66.7% agreed on checking compliance with contracts when applicable the mean 3.90 and standard deviation 0.995 witnessed its existence. The other 6.7% and 3.3% respondents expressed their strong disagreement and disagreement on this respectively.

The commercial banks of Ethiopia are performing their operation on the basis of the rules and regulations established by the National bank of Ethiopia. If the banks failed to perform in line with this they would be fined. The internal auditors were responsible to check the agreement of the bank activity with those rules and regulations. Regarding this 63.3% of respondents believe that the internal audit checks compliance with regulations issued by concerned government organ. The mean 3.90 and the standard deviation 0.923 witnessed the practice.

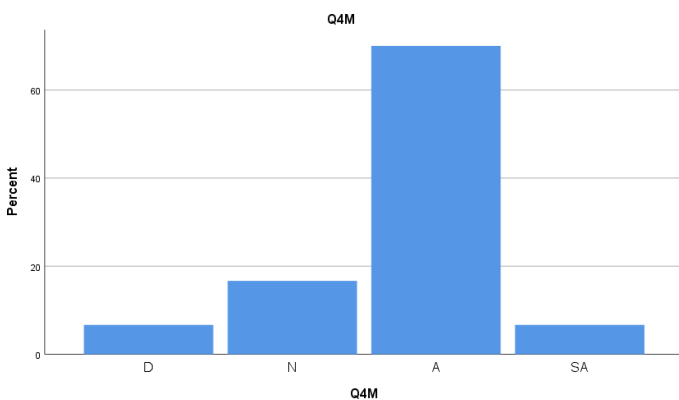


Graph 8 Compliance checking with external laws and regulations

When organizations establish operational procedures they should consider their goals and objectives. Operational or procedures guidelines are vital for the success of the organizations performance. From the total 56.7% of respondents agreed and believed on ascertaining operating objectives are consistent with organizational goals. The other 16.7% and 3.3% of respondents

Disagreed and strongly disagreed on this. The mean 3.53 indicates most of the respondents agreed and indicates the existence of the practice.

In the business world most of the organizations have their own goals and objectives and to achieve their goals and objectives they established procedures to perform their operation in line with that procedure. Besides to establishing the implementation is necessary. Majority of the respondents comprising 70% agreed that internal auditors Reviews operations to ascertain they were implemented as intended. Some of the respondents comprising 6.7%



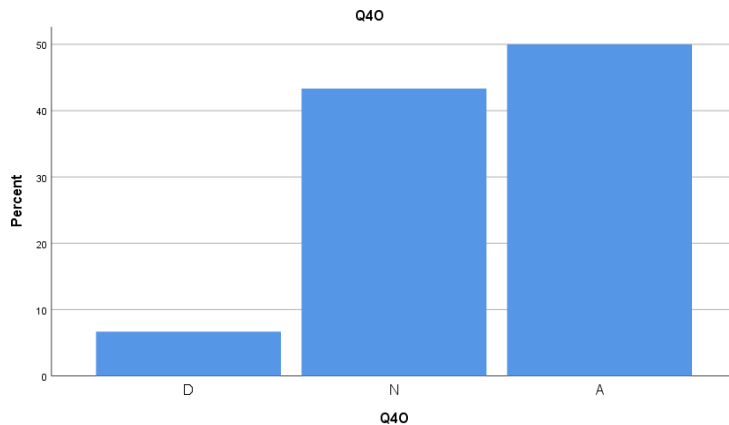
disagreed on the ascertaining of the implementation by internal auditors. The standard

deviation 0.679 witnessed the little variation among respondents.

Graph 9 Checking operations were implemented as intended

The possibility of an event occurring that would have an impact on the achievement of objectives is not certain, therefore identifying risk exposure areas and being proactive enables to reduce the occurrence of risks. Out of the total respondents 60% of them were agreed on providing consulting service to the management by identifying risk exposure areas. Only one respondent with 3.3% disagreed on this. The standard deviation 0.615 implies the little variance among the respondents.

Majority of the respondents constituting 50% agreed and they were providing consulting services to management where internal audit has the expertise. The other 6.7% of respondents disagreed and were not forwarding consultant services to the management. The mean 3.43 implies the existence of consulting service in the organization by internal auditors.



Graph 10 Giving consulting service to management

CHAPTER FIVE

5. Summary of Finding, CONCLUSIONS AND RECOMMENDATIONS

5.1. Introduction

5.1. Finding

Based on the findings this chapter provides the summary of findings, conclusions reached on the assessment of the internal audit practice in commercial banks in Ethiopia the case of selected private Bank and finally state some recommendations for further studies.

The findings from the questionnaires on the internal audit practice of commercial banks in related to the audit work quality, scope of the audit work, the level of independence of the internal audit function and competency and adequacy of internal audit staff, are discussed as follows.

Almost all internal audit employees of the internal audit department are degree holders and capable to compute and effectively operating due professional. However, the internal audit process is not giving necessary training and development program that could enhance the auditor's skill and experience to audit all the banks systems by preparing proper plan for risk identification. The internal auditors in the internal audit process in general do not have additional required certification that may help the internal auditors to conduct effective audit. The internal auditors are currently enjoying organizational independence in their day to day activities of audit work.

The internal audit process has guide line related to their process which is prepared to help the internal auditors to do their job accordingly. But the guide line lacks periodic revision and detailed steps needed to be followed by the auditors which may have an adverse effect on their audit activities. The preparation of internal audit plan is performed at head office in department level but some of the respondents are neutral whether the audit plan is prepared or not.

The internal audit department performs different activities in commercial banks like checking compliance with contracts, checking compliance with external laws and

regulations, review implementation of operational guidelines, but most of the internal auditors are neutral and not providing consultant service to the management. The internal audit report includes the purpose and scope of the audit, findings and conclusions, and recommendation of internal auditors however, the report do not include auditees comments regarding the audit findings.

The study reveals the existence of poor practice of management's commitment in providing greater attention to internal audit recommendations and there is no corrective action agreement with the management regarding the audit findings. The absence of management support may cause less effort of internal auditors in their engagements which in turn could affect the effectiveness of internal audit practice.

There are a number of recommendations forwarded from some of the respondents. These are enhancing management commitment to internal auditing, developing modern auditing software, updating audit procedural manuals, and promoting online auditing for prompt disparity identification. The recommendation will benefit the internal audit department and commercial banks at large if effected appropriately.

5.2. Conclusions

As internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organizations operations, issues as how effectively it performs this role have emerge with greater prominence than before. The recent global financial crisis has led to questioning of how successful internal audit is, both in its more conventional role of monitoring compliance with internal control and financial probity and its more recent, and to extent, self-proclaimed role as an integral part of the risk management culture within the organizations. It is obvious that effective internal audit helps organizations specifically banks to accomplish their objectives by bringing systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Against this background, it is of utmost importance to assess internal audit effectiveness in order to make the audit services more effective to the auditors in particular and the banking industry in general.

This study was aimed at assessing the internal audit practice in commercial banks in Ethiopia the case of Selected Private Bank by taking sample from internal auditors and control department executives.

The study reveals that the internal audit department has no training policy. It is better to develop training policy and to give adequate training to the internal auditors. The survey data also revealed that most of the internal auditors do not have the additional required certification in internal audit which can enhance their skill and expertise such as Certified Audit (CIA), Certified Information System Audit (CISA), Certified Fraud Examiner (CFE) and the Association of Chartered Certified Accountants (ACCA).

The study also revealed that there is weakness in related to corrective action plan which is useful in rectifying the audit findings. The study also indicates the audit report do not include auditees recommendation about the findings.

5.3. Recommendations

From the data analysis and findings the researchers arrived at the following recommendation. Multiple approaches are needed to produce effective audit report in organization and particularly in the internal audit process. No single approach is likely to fully and cost-effectively address the effectiveness of audit activity in the study area since it has multiple causes which could highly affect it. Generally, understanding better these different variables and their interrelationships that impact the effectiveness of audit activity can help to develop targeted strategies for effective audit practice which in turn contributes for effective corporate governance.

High quality audit work is arguably the function of effective guide and extensive staff expertise; periodic reviews of the internal audit activities by CIAs or other competent audit professionals; the internal audit process have to try its utmost effort to revise the existing guide line in a manner to assist the auditors by incorporating the necessary detailed step and make use of the above mentioned facts for conducting effective audit of high quality for the auditees.

The internal Audit process should have appropriate program for training developing the internal auditors, giving an opportunity for continuing education and certification in CIA, CISA, CFE and ACCA so as to produce effective audit. The internal audit process should consider the correction of the audit findings. The audit findings should be corrected and corrective action agreements should be made with the management to conduct effective audit work in the bank.

The banks have to modify their internal audit report format and it is better to include auditees recommendations on the findings identified by internal auditors to get attention of the management to rectify the discrepancies identified.

In modern auditing besides checking accuracy of amounts in financial reports and other activities of the operating department, consulting service plays a vital role in enhancing effective corporate governance. Therefore besides giving compliance conformance with operations guiding the internal auditors to give consulting service will benefit commercial banks.

5.4. Recommendation for Further Studies

This research focused on assessing the internal audit practices in commercial banks in Ethiopia the case of Selected Private Bank. The researcher recommends a similar study in commercial banks considering different private banks and in-depth study to be done taking other financial institutions both private and government owned in to consideration than leaning on one company so as to get comprehensive as well as further inputs on the topic.

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**APPENDIX
JIMMA UNIVERSITY**

DEPARTMENT OF ACCOUNTING AND FINANCE

COLLEGE OF BUSINESS AND ECONOMICS

QUESTIONNAIRES FOR INTERNAL AUDIT STAFF

Dear Sir, The aim of this questionnaire is to explore information regarding Internal Audit practice of Commercial Bank. The information you provide in response to the items in the questionnaire will be used as part of the data needed for the study. I would like to assure you that the information you provide will be accessible only to the investigator. Your involvement is regarded as a great input to the quality of the research result. Hence, I believe that you will enlarge your assistance by participating in the study. Your honest and thoughtful response is precious and supportive for the quality of the research result.

Thank you

Part 1: General Information

Please put a tick [] where applicable to indicate your answer

Gender: Male Female

Position of respondent in the Bank

Internal audit manager Internal Auditor Other (specify) _____

Number of years of experience in the bank

<1 year 1-5 years: 6-10 years: 11-15 years: Over 15 years

Academic Qualification

Diploma BA Degree MSC/MA Other(specify) _____

Professional certifications:

CPA ACCA CIA Norelated certification

Part 2: List of statements pertaining to internal audit in your organization.

Please indicate whether you agree or disagree with each statement by ticking () on the spaces that specify your choice from the options that range from “**Strongly Agree,**” which is represented by “**5**” to “**Strongly Disagree,**” represented by “**1**”.

Note:- Strongly Agree = “5”, Agree = “4”, Neutral = ”3”, Disagree = “2”, and

Strongly Disagree =”1”.

	A. Competency and Adequacy of Internal Audit	5	4	3	2	1
1	The internal audit department is large enough to successfully carry out its duties					
2	Internal audit obtains a sufficient budget to successfully carry out its duties					
3	Internal auditors possess sufficient experience to understand the organizations systems					
4	The internal audit staffs possess knowledge and skills in a variety of areas (beyond accounting and finance), as necessary					
5	Internal audit has policies for training of internal audit staff					
6	Internal auditors undertake continuous professional development activities (such as professional association sponsored programs and correspondence courses)					
7	Adequate short-term training is arranged for internal auditors each year					
8	There is a complete internal audit manual to guide internal audit work					
	B. Audit Work Quality					
1	Annual internal audit plan is prepared					
2	Risk assessment is done as part of audit planning					
3	Senior management input is considered in setting internal audit priorities					
4	During the examination of audit evidence, analytical audit procedures (e.g. ratios, trends, etc.) are used as appropriate					
5	Audit work is documented and maintained in a file of audit working papers					

6	Were audit observations communicated fairly, clearly, accurately, and in a timely manner during the course of the audit?					
7	Were your concerns adequately addressed and differences of opinions, if any, resolved before the final audit results were communicated?					
8	Was the content of the audit report communicated clearly, fairly and accurately and the report issued in a timely manner?					
9	Audit findings are discussed with auditees before being reported on					
10	Internal auditors follow up implementation of corrective actions relating to audit findings					
11	The reporting level varies with the importance of internal audit findings					
12	Corrective action plan is agreed with management before the report is issued					
13	Management takes timely corrective action based on internal audit recommendations					
14	How often are the following included in the internal audit reports?					
	<ul style="list-style-type: none"> the audit purpose and scope(Always) 					
	<ul style="list-style-type: none"> the audit findings and conclusions(Always) 					
	<ul style="list-style-type: none"> audit recommendations(Always) 					
	<ul style="list-style-type: none"> auditees,, comments regarding audit findings (Always) 					
	C. IA independence and Objectivity					
1	Internal audit is free from intervention in performing its					

	duties					
2	Internal auditors feel free to include any audit findings in their audit reports					
3	Internal audit provides reports to the board of directors (or audit committee)					
4	The board of directors (or audit committee) oversees employment decisions in internal audit					
5	Internal auditors are not assigned to audit areas in the system design of which they participated					
6	Internal auditors do not participate in audit of activities for the operation of which they were responsible					
7	Internal audit staff assignments are rotated periodically					
	D. Scope of Internal Audit work					
1	Did Internal Audit solicit feedback from you and your staff during the entrance conference to ensure your concerns were adequately addressed during the audit?					
2	Did you receive written/verbal notification of the overall audit scope and objectives during the initial phase of the audit?					
3	Do you feel that the scope of the audit (i.e., the processes, activities, period of coverage, etc.) is sufficient and key risk areas were covered?					
4	Checking adequacy of the auditees,, record keeping when appropriate					
5	Verifying accuracy of amounts in financial records					
6	Reviewing information contained in reports of operating departments					
7	Checking efficiency of operating results (e.g. whether cost					

	saving alternatives are used)					
8	Ascertaining compliance with organizational policies and Procedures					
9	Checking compliance with contracts when applicable					
10	Checking compliance with external laws and regulations when applicable					
11	Ascertaining that operating objectives are consistent with organizational goals					
12	Ascertaining that operating procedures are consistent with the operational goals					
13	Reviewing operations to ascertain they were implemented as intended					
14	Assisting the management by identifying risk exposures of the organization					
15	Providing consulting services to management where internal audit has the expertise					
	E. Effectiveness of Internal Audit					
1	Internal audit ensures that it adds value to the business.					
2	Internal audit improves organizational performance.					

If you have any additional comment regarding the topic, please specify -----

