UNIVERSITY OF CAPE COAST

INTERNAL AUDIT AND GOOD GOVERNANCE IN THE PUBLIC SECTOR IN KUMASI

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Dissertation submitted to the Department of Business Studies of the College of Distance Education, University of Cape Coast, in partial fulfilment of the requirements for the award of Master of Business Administration degree in Accounting

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DECLARATION

Candidate's Declaration

I hereby declare that this thesis is the result of my own original research and that no part of it has been presented for another degree in this university or elsewhere.

Candidate's Signature:…………………………… Date:……………………

Name: Monica Boateng

Supervisor's Declaration

I hereby declare that the preparation and presentation of the thesis were supervised in accordance with the guidelines on supervision of thesis laid down by the University of Cape Coast.

Supervisor's Signature:………………………… Date:……………………

Name: Mr. Gilbert Amoako

ABSTRACT

Well performing internal audit function has been argued as one of the strongest means of internal control to monitor and promote good governance system in an organization. While internal audit can be used in order to assist management in order to instill a strong ethical tone in the entire organization, a poor attitude by the management can make it hard for the internal auditor to uphold ethical behaviour. As a result, many countries have increased attention on internal audit as an important component of government financial management and as a tool for improving the performance of the government sector. The objective of this study was to establish the effectiveness of internal audit in promoting good governance in the public sector in Ghana with special focus on the Ministries, Department and Agencies (MDAs) and Metropolitan, Municipal and District Assemblies (MMDAs). The research was both quantitative and qualitative in nature with both descriptive cross-sectional design method and regression analysis preferred for the study. The study also uses logistic estimation technique on the primary data collected to find out the association between corporate governance and internal systems of risk management, compliance and consultancy and internal controls.

The research established that internal audit significantly affects internal controls, risk management and compliance and consultancy. However, internal control and compliance and consultancy are less likely to ensure good corporate governance. The study therefore recommend that the government should recognize the contribution of internal auditing and embrace it as an effective tool so as to realize their objectives set.

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DEDICATION

To my family

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LIST OF ACRONYMS

MDAs	Ministries, Departments and Agencies
MMDAs	Metropolitan, Municipal and District Assemblies
IAA	The Internal Audit Agency
PUFMARP	Public Financial Management Reform Programme
ICAG	Insitute of Chartered Accountants Ghana
UNDP	United Nations Development Programme
USAID	United States Agency for Internaltion Development
LGSC	Local Government Service Council
LGS	Local Government Service

CHAPTER ONE

INTRODUCTION

Background to the Study

A system of effective internal controls is a critical component of company management and a foundation for the safe and sound operation of organisations. As such, ineffective internal controls result in ineffective programmes and losses (Financial Management Manual, 2005). According to Baltaci and Yilmaz (2006), the effort to reform a fiscal system should include internal control and audit due to the crucial role they play in enhancing accountability and effectiveness. Internal audit provides both governments and related parties with a powerful tool for understanding the extent to which the public institution in question has delivered on budget and effective services.

Well performing internal audit function is one of the strongest means of internal control to monitor and promote good governance system in an organisation. Internal auditing is an integral part of the corporate governance framework in both the public and the private sectors (Cohen & Hanno, 2002). As a result, in many countries it has received an increasing attention as an important component of government financial management and as a tool for improving the performance of the government sector. The definition of internal audit contains two fundamental roles:

- Assurance Services to the administration, audit committee, and management, guidance on assessing the effectiveness of corporate management, risk management, and control processes established by management, and

- Consulting Services to the management on risk management and controls (The Institute of Chartered Accountants in England and Wales, 2011).

Analyzing this definition, it seems that the internal audit has evolved from a function of independent evaluation to a function of risk management, so that today it is the primary need of any organisation (Munro & Stewart, 2011). This is because it provides the creation of the added value of organisations through independent, objective assurance and consulting activities (Pickett, 1997).

By assessing the management process, the internal audit provides appropriate recommendations to improve it by fulfilling the following objectives (from the framework of professional activity, Croatian Institute of Internal Auditors, 2011):

- promoting appropriate ethical principles and values within the organisation,
- ensuring effective management of performance and establishing responsibilities in the company,
- effective communication of information on risks and control to the relevant parts of the company,
- effective coordination of activities and communication of information to board members, external and internal auditors, and management.

Good governance is considered as a tool that is used in order to achieve the strategies of an organisation (Belay, 2007). Thus, a number of issues including allegation of financial improprieties and lack of corporate governance structure joined with allegations of financial statement fraud of many government departments has helped to grind the ever increasing attention on corporate governance in wide-ranging and the audit committee in particular. As a result, the function of the committee had changed over years (Rezaee & Olibe, 2003).

Cohen and Hanno (2000) using the Public Oversight Board's perspective, defined corporate governance as "those oversight activities undertaken by the board of directors and audit committee to ensure the integrity of the financial reporting process" However, the best way to define the concept is to adopt the definition shared by the Organisation for Economic Cooperation and Development (OECD, 2004) countries: "Corporate governance is the system by which a business corporation (or a nonprofit organisation) is directed and controlled, at its senior level, in order to achieve its objectives, performance and financial management, and also accountability, integrity and openness".

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.

Corporate governance has been reflected upon since the beginnings of the modern corporation (Kim & Nofsinger, 2007), it certainly has received increased attention and scrutiny over the last two decades. In this period, corporate governance issues have become important not only in the academic literature, but also in public policy debates. Corporate governance ranges throughout countries and firms. A higher quality of corporate governance allows firms to gain access to capital markets more easily, which is greatly significant for firms, which mean to boost their funds.

This view of governance focuses on the control environment and control activities. Corporate governance issues are in general receiving greater attention as a result of the increasing recognition that a firm's corporate governance affects both its economic performance and its ability to access long-term, low investment capital (Mordelet, 2009). Other recent research shows the assurance, compliance and consultant roles of internal auditing are now being recognized at board level in many organisations as valuable contributors to good governance practices.

The Profile of Internal Audit Agency of Ghana

The Internal Audit Agency (IAA) was established by the Internal Audit Agency Act 2003 (Act 658) with a mandate to co-ordinate, facilitate and provide quality assurance for Internal Audit Units in Ministries, Departments and Agencies (MDAs) and Metropolitan, Municipal and District Assemblies (MMDAs). The key requirements of the Act are the provision of internal auditing assurance and consulting services that will ultimately lead to the enhancement of efficiency, accountability and transparency in the management of resources in the public sector.

The creation of the Internal Audit Agency was predicated on the need for the Government to put in place a structure that could support the eventual transfer of budgetary authority and expenditure control to the MDAs and MMDAs. These initiatives are part of the government's efforts under the Public Financial Management Reform Programme (PUFMARP).The Act received Presidential assent on 31 December 2003, Administrative transition was allowed up to 31 August 2004 and effective implementation started in 2005.

The governing body of the Agency is the Board which was sworn in on August 4, 2004. It comprises a membership of nine drawn from the public sector, the private sector and the Institute of Chartered Accountants Ghana (ICAG). The Board formulates policies and establishes appropriate structures for the effective and efficient execution of the Agency"s mandate. It ensures that the Agency operates within the overall framework of Act 658 and also facilitates collaboration with other agencies for the achievement of improved management of national resources. The Secretariat of the Agency is headed by a Director-General, supported by two (2) Deputy Director-Generals and four (4) Directors.

Role of the Internal Audit Agency (IAA)

The Internal Audit Agency (IAA) Act, Act 658 specifically directs the Agency to ensure that:

- financial, managerial and operating information reported internally and externally is accurate, reliable and timely,
- the financial activities of the MDAs and MMDAs are in compliance with laws, policies, plans, standards and procedures,
- national resources are adequately safeguarded,
- national resources are used economically, effectively and efficiently,

- plans, goals and objectives of MDAs and MMDAs are achieved, and
- risks are adequately managed in the MDAs and MMDAs.

Below is the organogram of the institutional arrangement.

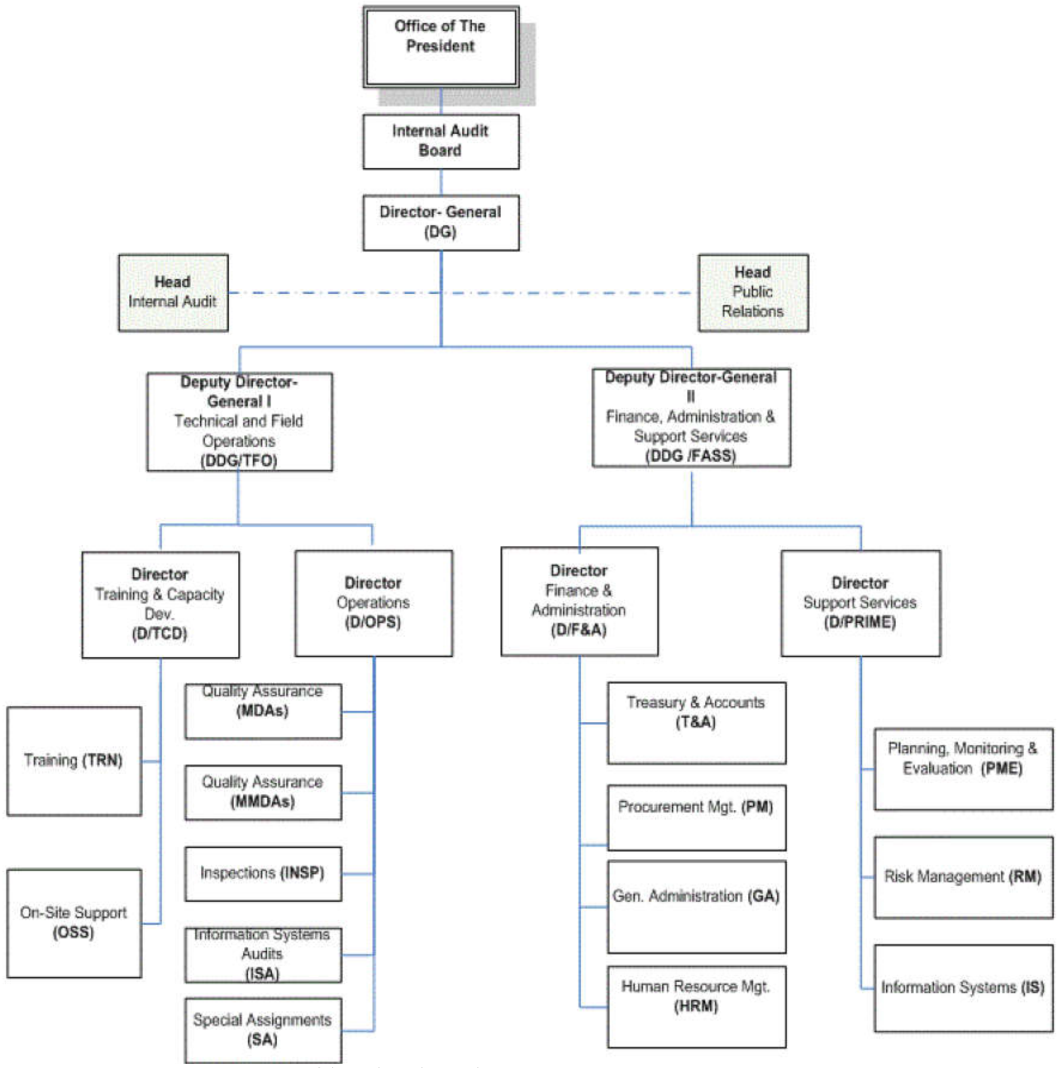

Figure 1. Organogram of institutional arrangement

Source: Austin (2011)

Problem Statement

Internal Auditing in the public financial management system is essential in ensuring proper budgetary control. It reduces misappropriation of funds, improves financial risk management, ensures effective and efficient use of limited resources, reduce corruption and ensures value for money. In this regard, the role of the IAA cannot be underestimated. A study carried out by the World Bank in 2006 on the Public Financial Management in Ghana revealed that insufficient understanding of the role of internal audit in ensuring appropriate control in an environment where the Accounting Officer is formally held accountable for his/her expenditure, combined with weak capacities amongst Internal Audit Unit staff in the MDAs and MMDAs, undermine the effectiveness of the internal audit function in carrying out its roles (World Bank, 2006).

The Auditor General (AG) in his letter dated October 15, 2015, and addressed to the Speaker of Parliament, over his report on the accounts of the district assemblies for the financial year ended December 31, 2014. The Auditor General said there was weakness in the financial management of the assemblies. According to the Auditor-General, significant among the irregularities uncovered during the 2014 under review were misappropriation of funds, unearned salary payments, procurement irregularities, and statutory tax infractions (The AG's report, 2015). For instance, eight assemblies recorded embezzlement of funds totaling GH$ 549,245.59 by diverting cash inflow for their private use and insertions on cheques after endorsement. Due to lack of effective supervision and failure on the part of the management to sanction staff for not accounting for resources of the assemblies, officials of 43 assemblies either failed to pay in total revenue collected, retire impress granted for official assignment, or provide evidence to support receipt and utilization of goods and services, totaling GH¢1,012,953.41 (The AG's report,2015)

Conflicts in different internal auditing roles in enhancing corporate governance have not gone away with contradicting opinions on how internal audit affect the corporate governance with some citing a positive effect (Herdman, 2002; Richards, 2002) and some saying it has very minimal effect if any (Davidson, Goodwin & Kent, 2005). One cannot avoid the question, has internal audit ensured good governance? The researcher has added to literature by focusing on how internal audit influences good governance with special focus on MDAs and MMDAs. The research has gone further to find out the effectiveness of the internal controls, by model estimation for possible predictions.

Research Objectives

The general objective of the study is to investigate the influence of internal audit on good corporate governance in Ghana.

The specific objectives are to;

- examine the relationship between internal audit and good corporate governance;
- investigate the effect of internal audit on good corporate governance.

Research Hypotheses

H_0: Internal audit does not affect good corporate governance.

H_1: Internal audit does affect good corporate governance

Research Question

To investigate the effect of internal audit on good corporate governance the study seeks to address the question;

- Is there a relationship between internal audit and good corporate governance in the MMDAs and MDAs?
- Does internal audit have an effect on good corporate governance in the MMDAs and MDAs?

Significance of the Study

This study will guide the government and policy makers to understand the effect of internal audit in improving governance at the MDAs and MMDAs and subsequently enacting policies that would be in the direction of ensuring good governance. The study may also help management to appreciate the role played by internal auditing function in their organisations and understand the challenges they face in carrying out their roles and help solve them. To the academia, the study contributes significantly to the internal auditing debate through enriching the existing literature regarding the effect of internal audit to corporate governance.

Scope and Limitations of the Study

The study was limited to the Management and Staff of the Internal Audit Departments and Finance, Accounts, budget offices in MDAs in Kumasi, Ashanti Region. The time frame allocated for the study was not adequate. With a time frame of only four months allocated for this study, in-depth study and analysis of objectives could be compromised. The researcher faced the challenge of non-co-operating staff and loss of questionnaires.

Organisation of the Study

The study consists of five chapters. Chapter one deals with the background of the study, the statement of the problem, the objective of the study and research questions. Other aspects of the chapter are significance, scope of the study, research questions, research hypothesis and organization of research work. Chapter two focuses on the review of related literature. In this chapter, books, journals, articles published and unpublished research works relating to the study have been reviewed. The methodology of the study is the subject of chapter three. It describes the research design, the population, sample and sampling procedures of the study. Also covered in the chapter are the variables of the study and methods of data analysis. In chapter four, results and discussion of the findings are presented. Finally the summary of findings, conclusions and recommendations constitute chapter five.

CHAPTER TWO

LITERATURE REVIEW

Introduction

This chapter describes the theoretical foundation of the study and provides a review of literature on the effectiveness of internal audit in ensuring good governance. Various theories on the concept of internal controls and good governance will be reviewed to aid the understanding of the relationship between internal audit and good governance.

The chapter opens with an introduction to the concept of governance followed by the overview of Governance in Ghana. The chapter then looks at the theories underpinning the study where the Agency theory will be reviewed and adapted. The institutional theory, stakeholder's theory and Expectant value theory will also be looked at in this chapter. The chapter also explores the factors influencing good governance with emphasis on internal audit. The chapter ends with empirical studies of good governance and internal audit.

The Concept of Governance

In most dictionaries "government" and "governance" are interchangeably used, both denoting the exercise of authority in an organisation, institution or state. Government is the name given to the entity exercising that authority. Authority can most simply define as legitimate power. Whereas power is the ability to influence the behaviour of others, authority is the right to do so. Authority is therefore the based on an acknowledged duty to obey rather than on any form of coercion or manipulation. Weber distinguished between three kinds of authority, based on the different grounds upon obedience can be established; traditional authority is rooted in history, charismatic authority stems from personality and legal-authority is grounded in a set of impersonal rules. To study government is to study the exercise of authority (Heywood, 1997).

Governance has been defined in some circles as follows;

- "The exercise of economic, political, and administrative authority to manage a country's affairs at all levels. It comprises mechanisms, processes, and institutions through which citizens and groups articulate their interests, exercise their legal rights, meet their obligations, and mediate their differences" UNDP (1997a).
- In governance, citizens are rightly concerned with a government's responsiveness to their needs and protection of their rights. In general, governance issues pertain to the ability of government to develop an efficient, effective, and accountable public management process that is open to citizen participation and that strengthens rather than weakens a democratic system of government. "The USAID, Office of Democracy & Governance

Overview of the Organisational Structure of the Local Government Service in Ghana

The objective of the Local Government Service is to secure the effective administration and management of local Government in the country. The Local Government Service Secretariat seeks to improve delivery of quality of service through the appointment, development and promotion of adequate numbers of competent staff in their right mix to fill vacancies at the national, regional and district levels. The secretariat charges itself with the core values accountability, client-oriented, creativity, diligence, discipline, equity, integrity, innovativeness, timeliness and transparency in the discharge of their activities. In keeping with the mandate of the Local Government Service Secretariat to ensure that the Local Government Service of Ghana is well structured and adequately staffed to provide excellent services to its stakeholders and clients, the LGSS is structured as below

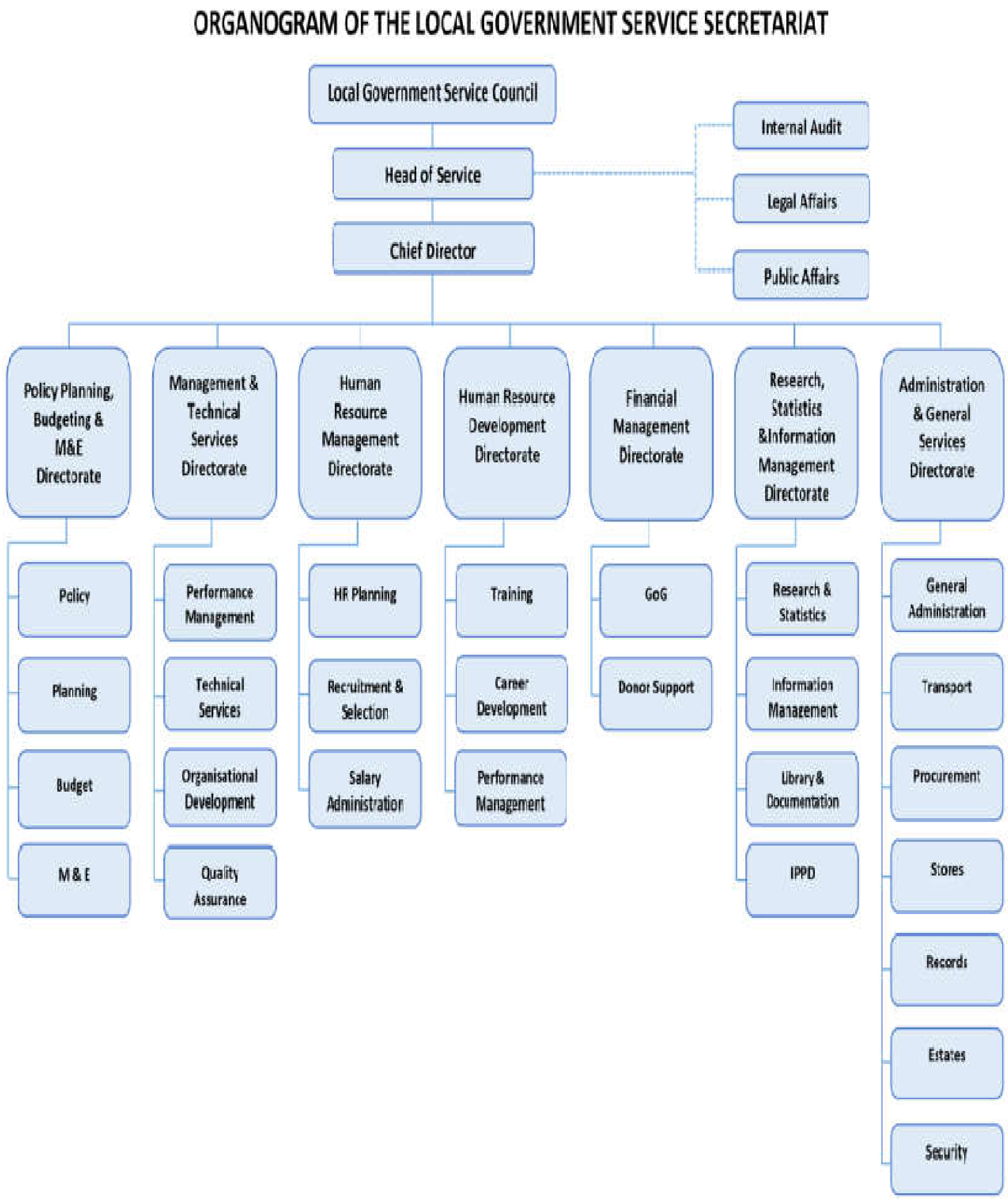

Figure 2 **Organogram of Local Government Secretariat**

Source: lgs.gov.gh/our_structure/ 30th July, 2016

At the apex of the governance structure of the Local Government Service is the Local Government Service Council (LGSC). The governing body for the Service consists of fifteen (15) members. The chairperson and other members of the Council are appointed by the President in consultation with the Council of State. Among the functions of the LGSC includes;

- Recommending to the Minister matters of policy relating to the management of the service;
- Ensuring the implementation of the functions of the Service;
- Developing professional standards and guidelines for the various categories of staff who are members of the Service;
- Monitoring and evaluating the performance standards of District Assemblies and Regional Co-ordinating Councils;
- Recommending to the minister a scheme of service prescribing the terms and conditions of service as well as the remuneration of the employees of the Service;

The Head of the Local Government Service is responsible for the efficient organisation and management of the Service and the day-to-day operation of the Secretariat. He also provides leadership and guidance in the efficient and effective performance of the LGS in implementing sectoral and cross-sectoral policies of Government. The units under the office of the head of service includes the Internal Audit. This Unit ensures transparency and accountability in the use of state resources through compliance with financial management and accounting practices and regulation laid down by the Procurement Authority, Internal Audit Agency, Audit Service and the Financial Administration Act.

Agency Theory

Agency theory having its roots in economic theory was exposited by Alchian and Demsetz (1972) and further developed by Jensen and Meckling (1976). Agency theory is defined as "the relationship between the principals, such as head of service and agents such as the employees of the local management". Employees of the LGS can be seen as agents of the Heads of Service (the principal) because they are required to produce a certain level of public output, including the quality of this output, in exchange for their rewards. In this theory, Head of Service who are the head or principals of the Local Government secretariat hires the agents to perform work. Principals delegate the running of institution to the directors or managers, who are the shareholder's agents Clarke, (2004). The agency theory shareholders expect the agents to act and make decisions in the principal's interest. On the contrary, the agent may not necessarily make decisions in the best interests of the principals (Padilla, 2000). Such a problem was first highlighted by Adam Smith in the 18th century and subsequently explored by Ross (1973) and the first detailed description of agency theory was presented by Jensen and Meckling (1976). Indeed, the notion of problems arising from the separation of ownership and control in agency theory has been confirmed by Davis, Schoorman and Donaldson (1997).

In agency theory, the agent may be succumbed to self-interest, opportunistic behaviour and falling short of congruence between the aspirations of the principal and the agent's pursuits. Even the understanding of risk defers in its approach. Although with such setbacks, agency theory was introduced basically as a separation of ownership and control Bhimani (2008). Holmstrom and Milgrom (1994) argued that instead of providing fluctuating incentive payments, the agents will only focus on projects that have a high return and have a fixed wage without any incentive component. Although this will provide a fair assessment, it does not eradicate or even minimize corporate misconduct. The positivist approach is used where the agents are controlled by principal made rules, with the aim of maximizing principals' value. Hence, a more individualistic view is applied in this theory (Clarke, 2004). Indeed, agency theory can be employed to explore the relationship between the ownership and management structure.

However, where there is a separation, the agency model can be applied to align the goals of the management with that of the owners. Due to the fact that in a family firm, the management comprises of family members, hence the agency cost would be minimal as any firm's performance does not really affect the firm performance (Eisenhardt, 1989). The model of an employee portrayed in the agency theory is more of a self-interested, individualistic and are bounded rationality where rewards and punishments seem to take priority Jensen & Meckling, (1976). This theory prescribes that people or employees are held accountable in their tasks and responsibilities. Employees must constitute a good governance structure rather than just providing the need of the head of service, which maybe challenging the governance structure.

Institutional Theory

According to institutional theory by Fogarty, (1996), an organisation is designed and functions to meet social expectations in so far as its operations are visible to the public. Therefore organisational internal operations, which are often complex and difficult to identify, may take second place to the issue of external legitimacy. It is suggested that the external image of the organisation may be loosely coupled with its operating processes and the kind of technology it adopts.

Fogarty, (1996) developed this, asserting that the contribution of institutional theory is in the insight that the actual accomplishments of an organisation and what its structure suggests should accomplish are often different. The organisation operates with internal processes that are not normally visible to those external to it, while other structures maintained for outsiders do not significantly add to output. Fogarty (1996) observes that scrutiny by outsiders can be avoided if the right structures are adopted by organisations. Loose technological coupling enables organisations to show success in external problems whilst allowing flexibility in operational processes. Thus the institutions should be ready to meet the high cost of adopting various technologies in the internal audit department and ensure that the staffs are trained in order for the department to operate efficiently.

Stakeholder Theory

Stakeholder theory can be defined as “any group or individual who can affect or is affected by the achievement of the organisation’s objectives”. Unlike agency theory in which the managers are working and serving for the stakeholders, stakeholder theorists suggest that managers in organisations have a network of relationships to serve – this include the suppliers, employees and business partners. This group of network is important other than owner-manager-employee relationship as in agency theory Freeman (1999). On the other end, Sundaram and Inkpen (2004) contend that stakeholder theory attempts to address the group of stakeholder deserving and requiring management's attention.

Whilst, Donaldson and Preston (1995) claimed that all groups participate in a business to obtain benefits. Nevertheless, Clarkson (1995) suggested that the firm is a system, where there are stakeholders and the purpose of the organisation is to create wealth for its stakeholders. Freeman (1984) contends that the network of relationships with many groups can affect decision making processes as stakeholder theory is concerned with the nature of these relationships in terms of both processes and outcomes for the firm and its stakeholders. Donaldson and Preston (1995) argued that this theory focuses on managerial decision making and interests of all stakeholders have intrinsic value, and no sets of interests are assumed to dominate the others.

Expectancy Value Theory

Expectancy Value Theory has been used to understand motivations underlying individuals' behaviours. Focus has been placed on intent, as the immediate precursor to a particular behaviour. This theory proposes that if one can determine the elements that impact intention, then one can more accurately predict whether an individual will engage in a particular behaviour. Likewise, it proposes that by changing an individual's perceptions of potential outcomes, one can alter the individual's intent. The basis of the theory is that "individuals choose behaviours based on the outcomes they expect and the values they ascribe to those expected outcomes" (Borders, Earleywine, & Huey, 2004). The level of one's willingness to perform a particular behaviour is dependent on;

a) The extent to which the individual believes a consequence will follow and
b) The value the individual places on the consequence (Mazis, Ahtola, & Kippel, 1975).

The more attractive a particular outcome is to the individual, the more likely the person will engage in the behaviour. Similarly, as the number of positive outcomes increase, the motivation to engage in the behaviour will increase. Expectancy itself is defined as "the measurement of the likelihood that positive or negative outcomes will be associated with or follow from a particular act" (Mazis et al, 1975). Thus, the individual's outcome expectations affect one's attitudes towards the behaviour. In addition to the expected outcome, the value the individual places on the outcome influences the individual's intentions.

The potential negative impact of a particular action may act as a barrier to a civil servant's recommended action. Thus a cost-benefit analysis of benefits and costs takes place in which the civil servant weighs the action's expected effectiveness against the perceptions that it may be expensive, dangerous (negative side-effects), and unpleasant (painful, upsetting). Civil servants will take action only if the benefits of taking the action outweigh the costs. Civil servants' readiness to take action is influenced by other factors, which serve as cues to initiate an action. These factors could be some environmental events such as media publicity.

Even though the Expectancy Value Theory has been used to predict the intentions that will impact behaviour, there are a number of limitations to the theory. One of the main weaknesses of the theory is the focus on limited cognitive processes. Borders, Earleywine, and Huey (2004) found that individuals choose from a variety of alternatives and thus must examine a variety of expectancies before choosing to engage in behaviours. Among the potential alternatives of decisions that can be made, some appear more attractive than others. For example, it appears individuals are likely to intend behaviours that have been positively reinforced by successful outcomes and by other individuals in social networks (Bandura, 1977)

Corporate Governance

Corporate governance has been defined as a manner in which the business of an enterprise is directed and controlled, how the corporate objectives are set and how corporate activities and expectations of the stakeholders are aligned (Coyle, 2003). Corporate governance involves the combination of the body of directors, management and controls that guide the firm. Borerwe (2004) consented to Deal and Kennedy (1982)'s views and defined corporate governance from the banking industry as a manner in which boards of directors govern the business affairs of individual institutions and senior management, affecting how the banks:

- run the day to day operations of the business;

- align corporate activities and behaviours with the expectation that banks will operate in safe and sound manner, compliance with laws and regulations; and
- set corporate objectives (including generating economic returns to shareholders and protect the depositor's interests.

Borerwe (2004) reiterated that corporate governance is concerned with holding goals. The aim is to align as near as possible the interest of individuals, corporate and society which can be ensured by having effective internal control system. Magaisa (2004) supported this view when he says that effective internal control is an attempt to encourage employees, managers, board members to think about and make decisions through the doctrine of shared values.

According to the King Report (2002) the corporate discipline, transparency, independency of board members and committees, fairness, accountability and social responsibility are the essential pillars of good corporate governance. For a corporate to achieve good corporate governance it must adopt a clear stance on the following: Strategy, Stewardship, Corporate culture, Corporate reporting, IT systems and Board operations. Pheysey (1993) added another dimension to the above definition by defining corporate governance as the way business is conducted in accordance with the shareholders desire which generally is to make as much money as possible.

According to the Reserve Bank of Zimbabwe (RBZ) a corporate governance guideline protect the integrity of the sector and cultivates confidence within investors and deposited, conditions that result in free circulation of funds thus making it easy for banks to undertake their day to day operations without difficulties. This entails economic development as a result of free circulation of money within the economy. Magaisa (2004) substantiated the RBZ governor's statement by indicating that poorly governed financial institutions are a liability to the economy and are a functional equivalent of circulatory problem in human beings.

Harvey and Brown (1998) are of the view that the exclusive focus of corporate governance should maximize shareholder wealth to the extent that wealth maximization conflicts with the interests of other stake holder's interests. Those interests should be ignored unless management is legally required to take interests into account. Coyle (2003) added that the main corporate governance problem is rooted in the Blake and Mouton (1985) paradigm of separation of shareholders ownership and management's control in institutions. This resulted in the emergence of the agency problem, which is the need of ensuring that management is always acting in the best interest of the shareholders rather than theirs (Davis & Militelo, 1994).

Buchanan (1975) views the firm as a system of stakeholders operating within a larger system of a host of society that provide necessary legal and market infrastructure for the firm's activities. Khan (1994) supported this view by stating that the goal of directors and management should be maximizing total wealth creation by the firm. Reserve Bank of Zimbabwe, (2004) recommended that boards of commercial banks and building societies must have at least five directors. The major reason for this recommendation was that large boards are for corporate performance because they have a range of expertise to help make quality decisions and makes it difficult for powerful CEOs to dominate.

Blake and Mouton (1985) indicated that monitoring by boards could deal with at least some problems of corporate governance. Johnson (1992) proposed that board of directors could solve agency problems if the company under performs in a health industry because under this situation boards would find it easier to evaluate performance of the management. Weibach (1988) tested hypothesis advanced by Fama (1980) and discovered that outside directors behave differently from inside directors and behave differently from inside directors and boards dominated by outside directors performed better that firms with boards dominated by insider directors to remove the chief executive officer.

Definition of Internal Auditing

With changing times, the concept of internal auditing has undergone significant changes with regard to its definition, scope of coverage and approach. In some institutions, the scope of modern internal auditing has been broadened from financial issues to include value for money, evaluation of risk, managerial effectiveness and governance processes. In 1978, the Institute of Internal Auditors (IIA) defined internal auditing as: "An independent appraisal activity established within an organisation as a service to the organisation. It is a control, which functions by examining and evaluating the adequacy and effectiveness of other controls. The objective of internal auditing is to assist members of the organisation in the effective discharge of their responsibilities.

The modern scope and focus of internal auditing are reflected in the current definition that was formally adopted by the IIA in 1999: "An independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes". According to Asare (2008), the difference between the definitions of 1978 and 1999 (as repeated in IIA 2008) that is worthy of note is the prominence of objectivity in internal audit activities and also the emphasis on the evaluation and improvement of the effectiveness in risk management and governance processes. The current definition also contemplates two main internal audit services: assurance and consulting services.

Assurance services, according to IIA (2008): Involve the internal auditor's objective assessment of evidence to provide an independent opinion or conclusions regarding an entity, an operation, a function, a process, system, or other subject matter. The nature and scope of the assurance engagement are determined by the internal auditor. There are generally three parties involved in assurance services: (1) the person or group directly involved with the entity, operation, function, process, system, or other subject matter - the process owner, (2) the person or group making the assessment - the internal auditor, and (3) the person or group using the assessment - the user.

Consulting services, according to the same source: Are advisory in nature, and are generally performed at the specific request of an engagement client. The nature and scope of the consulting engagement are subject to agreement with the engagement client. Consulting services generally involve two parties: (1) the person or group offering the advice - the internal auditor, and (2) the person or group seeking and receiving the advice - the engagement client. When performing consulting services, the internal auditor should maintain objectivity and not assume management responsibility (IIA, 2008).

According to IIA (2008), even though the above differences in definition may affect the practice of internal auditing in each environment, adhering to the IIA International Standards for the Professional Practice of Internal Auditing (Standards) would ensure that the responsibilities of internal auditors and the internal audit activity are met.

Roles of Internal Audit

The role of internal auditing have been identified as involving three main elements, namely the evaluation and improvement of risk management, control and governance processes. These elements are sometimes referred to as the "three pillars" of internal auditing.

Figure 3 **Three pillars of internal auditing**

Source: Asare (2008)

Risk management, control and governance encompass the policies and procedures established to ensure the achievement of objectives and include the appropriate assessment of risk, the reliability of internal and external reporting and accountability processes, compliance with applicable laws and regulations, and compliance with the behavioural and ethical standards set for public organisations and employees. The three elements are further discussed below as reinforcements of the fundamentals of an internal audit function in the public sector (Asare, 2008).

Internal Audit and Corporate Governance

The audit function has become an integral part of government financial management and an instrument for improving performance in the public sector. The need for good governance and accountability has compelled governments to demonstrate a stronger sense of responsibility in the use of public funds and efficiency in the delivery of services. Management of national economies today is more complex and demands greater competency and professionalism from internal auditors, if they are to be able to assist government in ensuring that scarce resources are deployed in a more efficient manner and to also effectively deal with the associated risks. Effective internal oversight and monitoring are crucial to good governance and effective Public Financial Management (PFM). Internal oversight includes the internal audit function that must be effective and should comply with generally accepted auditing standards with regards to practice and approach. The focus of internal auditing is to determine whether public funds have been spent for the purposes for which they were earmarked and thereby promoting accountability.

Internal audit undertakes reviews of individual systems and processes and consequently makes recommendations to heads of public sector entities on how internal controls could be improved. An internal audit function is an essential part of any public expenditure management system and should ensure that public spending is within budgetary provisions; disbursements comply with specified procedures, provides for the timely reconciliation of accounts and effective systems for managing and accounting for physical and financial assets (Commonwealth Secretariat 2005). Van Gansberghe (2005) puts forward the case that "Management must recognize the value added role of internal audit and contribute towards its effectiveness.", and that "As internal auditing in the public sector assumes a status of professional practice, management would benefit from its recommendations in improving its decision-making and thus would be playing a more proactive and foresight role.

Internal audit function provides internal consulting service to the management in public sector institutions and hence the executive arm of government for smooth and efficient functioning and for reviewing and improving its performance. It also ensures that there are efficient controls and greater transparency in the decision and policy-making processes of government functionaries and institutions, in delivering services successfully and in carrying out development programs in an efficient and appropriate manner. Public Sector controls cover all aspects of activities including financial, managerial and operational policies and are intended to safeguard assets, ensure the accuracy and reliability of financial information and promote operational efficiency. The internal audit function is in a good position to help senior management of public institutions to identify risks, suggest risk management strategies and, ultimately, provide assurance that the risks are being managed appropriately. Thus, the internal auditing function evaluates the effectiveness of public institutions in achieving agreed objectives and thereby promoting strong governance and accountability regime. Deloitte (2005) noted that without internal audits" efforts and expertise in companies" organisational operations, "the business landscape would likely be littered with significantly more disclosures of material weaknesses and revelations of noncompliance with."

Based on the Audit Committee, on the one hand internal auditing contribute to corporate governance by: Bringing best practice ideas about internal controls and risk management processes to the audit committee; providing information about any fraudulent activities or irregularities (Rezaee and Lander, 1993); conducting annual audits and reporting the results to the audit committee and encouraging audit committee to conduct periodic reviews of its activities and practices compared with current best practices to ensure that its activities are constituent with leading practises (Sawyer, 2003).

From the other hand, an effective audit committee strengthen the position of the internal audit function by providing an independent and supportive environment and review the effectiveness of the internal audit function. External audit is also regarded as an important cornerstone of corporate governance, particularly with respect to the prevention and detection of fraud and errors in financial statements (Davidson et al., 2005).

Internal Auditing and Internal Control

According to Harvey and Brown (1998), the major components of internal controls are control environment, accounting system and control procedures. Smircich (1983) subscribes to the same sentiments by highlighting that the tone at the tog has implications on the direction taken by employees. Furthermore, Jansen (1998) pointed out that historically internal controls, has focused conforming employees' actions to the desires of management.

An internal control system available to a firm according to Grieves (1998) consists of: management oversight and the control culture; risk recognition and assessment; control of activities and segregation of duties; information and communication and monitoring activities and correcting deficiencies. Control environment reflects the overall attitude, awareness and actions of the board of directors, management and stockholders. The accounting system consists of the methods, records and report on entity's transactions to provide complete, accurate and timely financial information. Finally the control procedures are essentially specific procedures put in place by management to provide assurance that the company's objectives will be met. They usually come in the form of authorizations, segregation of duties, design and use of adequate documentation and records, adequate safeguards or access to assets and independent checks on performance.

The control environment reflects the overall attitude, awareness and actions of the Board of Directors, management and stockholders. Robbins (1992) defines internal control systems as the whole system of controls, financial and otherwise, established by management in order to carry out the business of the enterprise in an orderly and efficient manner, ensure adherence to management, safeguard the assets and secure as far as possible the completeness and accuracy of the records. According to Khan (1994), internal controls are designed to protect an institution from loss or misuse of its assets. They also ensure that all transactions are properly authorized and thus guarantee or foster good corporate governance.

Cook and Wincle (1976), however finds that the Internal Control System resembles the human nervous system which is spread throughout the business carrying orders and reactions to and from the management. In this concept, by measuring and evaluating the effectiveness of organisational controls, internal auditing, itself, is an important managerial control device, which is directly linked to the organisational structure and the general rules of the business (Cai, 1997). In today's business environment internal auditors are now providing *management* with a far broader range of information concerning the organisation's financial, operational and compliance activities to improve effectiveness, efficiency, and economy of management performance and activities.

The internal auditors are expected to provide recommendations for improvement in those areas where opportunities or deficiencies are identified. While management is responsible for internal controls, the internal audit activity provides assurance to management and the audit committee that internal controls are effective and working as intended. The internal audit activity is led by the Chief Audit Executive (CAE). The CAE delineates the scope of activities, authority, and independence for internal auditing in a written charter that is approved by the audit committee. An effective internal audit activity is a valuable resource for management and the board or its equivalent, and the audit committee due to its understanding of the organisation and its culture, operations and risk profile. The objectivity, skills, and knowledge of competent internal auditors can significantly add value to an organisation's internal control, risk management, and governance processes.

Corporate governance developments around the world have reaffirmed the responsibility of the board in the process of ensuring the success and efficiency of the internal control framework of the company. As a result, the key role of the internal audit is vital in order to support the board in order to ensure sufficient oversight of internal control as well as in the process of doing so form in the integral aspect of the corporate governance framework of the organisation. Thus the key role of the internal audits focuses on the process of assisting the board and/or its audit committee in the process of discharging its governance responsibilities by focusing on the following: an objective assessment of the existing risk and internal control framework; methodical examination of business processes and connected controls; reviews of the subsistence and value of assets; a source of information on major frauds and irregularities; unplanned and informal reviews of other areas of concern, including unacceptable levels of risk; reviews of the agreement framework and specific compliance issues; reviews of operational and financial performance; suggestions for more helpful and competent use of resources; appraisals of the achievement of corporate goals and objectives and finally advice and comment on devotion to the values and code of conduct/code of ethics of the organisation (Deloitte, 2005).

Internal Audit Role in Risk Management

The demand for proper risk management strategies in the public sector emanates from the complexity and dynamism of the operating environment, ever-increasing needs of society coupled with general unpredictability pattern and dwindling of resources for national development. According to the Australian Department of Finance and Deregulation, risk management is an important responsibility for any public sector entity for effective and efficient use of resources. It defines risk management as the possibility of an event or activity impacting adversely on an organisation, preventing it from achieving organisational outcomes. Risk management comprises the activities and actions taken to ensure that an organisation is conscious of the risks it faces, makes informed decisions in managing these risks, and identifies and harnesses potential opportunities. Managing risk well requires careful consideration of the key concepts of minimising loss, maximizing opportunity and preparing for uncertainty (Commonwealth of Australia, 2008).

The internal auditor's role in risk management involves assessing and monitoring the risks that the organisation faces, recommending the controls required to mitigate those risks, and evaluating the trade-offs necessary for the organisation to accomplish strategic and operational objectives. Griffiths (2006) "internal auditing provides independent and objective assurance to an organisation's management that its risks are being mitigated to an acceptable level, and reports where they are not". Fraud and corruption are key risks that need to be managed in the public sector. Surveys by KPMG in the US (KPMG, 1999) and Deloitte and Touché Tohmatsu in New Zealand (2000) suggest that, in general, internal auditors are more optimistic about the extent of their potential contribution to risk assessment and management than are senior executives.

Management has the responsibility to put in place systems and processes that will prevent and detect fraud within an organisation. However, it is internal audit that gathers sufficient objective information for management to carry out its stewardship function and to be well informed on the risks of fraud and effectiveness of fraud control procedures and to enable them to understand the complexities of fraudulent activities. Internal audit adds value through improving the control and monitoring environment within organisations to detect fraud (Coram, 2007). The very presence of internal audit review in an institution serves as a deterrent measure on the assumption that any fraud perpetuated may be uncovered. Good governance principles require that audit committees or similar oversight bodies, work closely with internal auditors in fraud risk evaluation and investigations especially when recent trends suggest perpetration by senior management in collusion with other employees.

Khan (2006) identified the useful role internal audit could play in the investigation process and made the following suggestion: “Internal auditors can play a vital role assisting the agencies responsible for investigation of alleged cases of corruption in public sector organisations by way of interpretation of various rules, explanation of various practices, and the sharing some of the confidential information that they may possess as they usually have more diversified and detailed knowledge of the operations in different parts of the organisation than the investigating agency staff that are deployed only for a particular case”. The challenge of public sector internal audit, however, is to avoid becoming compliance based due to the presence of a strict legal framework that sets out the public financial controls and internal auditing processes. Moving towards risk-based internal audit will require a foresight function of monitoring and advising on the improvement of program efficiency and effectiveness and mitigating risks that hinder the achievement of organisational objectives. Internal auditing professional standards require the function to monitor and evaluate the effectiveness of the organisation's Risk management processes.

Risk management relates to how an organisation sets objectives, then identifies, analyzes, and responds to those risks that could potentially impact its ability to realize its objectives. Griffiths' study (1999) within 92 Financial Times Stock Exchange (FTSE) of 200 companies reveals that financial director‟s perception of internal audit is by no means universally positive. However, their main concerns were that the function was too low key and basic (and therefore insufficiently operationally or business risk oriented) or that the function was lacking in skills (or had a poor mix of skills/staff). Following the financial directors in his study, internal audit needs to become much more business (risk) and operationally oriented, be more proactive, responsive and innovative and enhance the skills within the function as well as a the quality of the staff.

In general, providing a more constructive contribution via involvement in the assessment and management of business risk would enhance financial directors‟ perception of the internal audit function. More specifically, managing the control and risk self-assessment process or having a significant involvement in its delivery provides the opportunity to directly support the financial directors‟ requirements and responsibilities in this regard.

Empirical Studies

An effective internal audit function plays a key role in assisting the board to discharge its governance responsibilities. The study of O'Leary and Stewart (2007) used exploratory study; this had been done by presenting the five ethical dilemmas for 66 internal auditors. For each scenario, a key element of corporate governance was operated in order to assess its influence on ethical decision making. These were audit committee support; management truthfulness regarding different accounting policies; management integrity regarding pressure on internal audit; external auditor characteristics; and organisational code of conduct. As a result, the researcher had been able to show the different ethical decision-making related to internal audit and corporate governance.

On the other hand, Spira and Page (2003) explored the change in internal control using sociological perspectives on risk and its conceptualization to frame the debate about internal control and risk management within the United Kindom corporate governance arena. By using this method, the paper had been able to show that progresses in corporate governance reporting requirements offer chances for the misappropriation of risk and its management by groups, at the same time, enables to evaluate the current changes in internal audit.

Keitany (2000) in his study "the internal audit control function and its implication for risk assessment by the external auditor: A case of quoted companies" aimed at establishing whether the existence of an adequate internal audit function translates into a strong internal system that can be relied upon by the external auditor. The study adopted an exploratory research design and the population was all companies active in the National Stock Exchange (NSE) and their external auditors. The sample was 100% of the population. Primary data was collected using semi structured questionnaires with close ended questions. The data was analyzed using descriptive statistics such as mean, standard deviations and percentages. It was concluded that though the extent of reliance of internal controls is not sensitive to the strength of internal audit departments, companies should not do away with it. This is because as a management tool, it should assist management in its day to day operations and not necessarily of relevance to the external auditor.

Kibet (2008) in his study “a survey on the role of internal audit in promoting good corporate governance in Statement Of Expenditures (SOEs)” aimed to explore the role and the use of internal audit function in promoting good corporate governance in public sector enterprises and the challenges faced by the internal auditors in SOEs. The study followed an exploratory research design and the population comprised of all SOEs with government equity of over 50% located in Nairobi. A sample of 43 state corporations was selected by way of geographical location and government shareholding. Data collection was by way of questionnaires and the respondents were the heads of internal audit departments. Data collected was analyzed using the SPSS and the output presented in frequency distribution tables, pie and bar charts. The study concluded that internal audit function played a role in corporate governance.

Krishnan and Visvanathan (2005) in their study sought to address the role of audit committees and auditors in the reporting of internal control deficiencies after the passage of the Sarbanes-Oxley Act (SOX). The study sample comprised of firms selected from the Compliance week and covered a period from November 15, 2004 till March 1, 2005. Compliance Week reported that 164 firms mentioned internal control issues in their filings with SEC during the sample period. To represent auditor attributes the study examined size of the auditor, tenure, auditor changes, and audit fees. The study found that a higher number of meetings of the audit committee, lesser proportion of "financial experts" in the audit committee, and more auditor changes characterize firms that report weaknesses in their internal controls compared to firms with no weaknesses. Prior restatements of financial statements are also higher for firms not reporting such weaknesses. The results were robust to controlling for a variety of firm characteristics such as complexity of operations, profitability, and growth. It underscored the importance of governance characteristics beyond general firm characteristics in examining the reporting of internal control weaknesses.

Zhang, Zhou and Zhou (2006) in their paper “Audit committee, auditor independence and internal control weaknesses” investigated the relation between audit committee quality, auditor independence, and the disclosure of internal control weaknesses after the enactment of the SOX. The study concluded that Firms are more likely to be identified with an internal control weakness, if their audit committees have less financial expertise or, more specifically, have less accounting financial expertise and non-accounting financial expertise, as well. They are also more likely to be identified with an internal control weakness, if their auditors are more independent. In addition, firms with recent auditor changes are more likely to have internal control weaknesses.

Ausitn (2011) in an unpublished thesis examined the current practices and involvement of Internal Audit Agency in budgetary control among MDAs and MMDAs of public sector in Ghana. As an exploratory study the researcher made use of both primary and secondary data which include face - to - face interviews; structured and unstructured questionnaires administered to fifty (50) respondents of the Management and Staff of the Internal Audit Departments and Finance, and budget offices in some selected MDAs and MMDAs in Accra, Greater Accra Region. She found that The results on current practices reveal that audit work by IAA is not limited to only pre-audit and financial compliance as suggested by World Bank (2006) but has extended to budgetary control audits in the MDAs and MMDAs. She therefore suggested that Internal Auditors should plan and perform their audit procedures, evaluate and report on the results, recognizing that non-compliance by the entity with law or regulations may materially affect the financial statements.

Conceptual Framework

There is no doubt that internal audit as a process within the public institutions has increased in profile during the past decade to ensure that institutions worked within their job description. It could be argued that in the past it was the external auditors who took the limelight for ensuring accountability, but in recent years, thanks to reports relating to corporate governance the role and importance of internal auditing in ensuring that good governance processes are adhered to.

The new definition of internal audit shifts the focus its function from one of assurance to that of value added and attempts to move the profession toward a standards-driven approach with a heightened identity (Bou-Raad, 2000). To add value to an institution, management takes into consideration the five components of an adequate and effective internal control defined in the

Committee of Sponsoring Organisations of the Treadway Commission (COSO) report (Rezaee, 1995). These five components are (Messier, 1997):

- control environment,
- risk assessment,
- control activities,
- information and communication, and
- monitoring.

Furthermore, internal control system, and consecutively internal audit, is a significant part of the modern enterprise system, and also an important way that enterprises emphasize management and enhance economic benefit, substantially embodying the self-restraint system of enterprises (Jou, 1997). Generally speaking in recent years, internal audit can add value. In the modern business environment internal audit promotes:

- The effectiveness of goods and material supply
- The efficiency of productive organisation.
- Technological effectiveness
- The effectiveness of resource utilisation.
- Cost-benefit.
- The effectiveness of economic contracts.
- The effectiveness of product sales

Conclusion

The audit function has become an integral part of government financial management and an instrument for improving performance in the public sector.

Internal audit undertakes reviews of individual systems and processes and consequently makes recommendations to heads of public sector entities on how internal controls could be improved. The internal audit function is in a good position to help senior management of public institutions to identify risks, suggest risk management strategies and, ultimately, provide assurance that the risks are being appropriately managed.

Based on the Audit Committee, internal auditing contribute to corporate governance by: Bringing best practice ideas about internal controls and risk management processes to the audit committee; providing information about any fraudulent activities or irregularities (Rezaee & Lander, 1993); conducting annual audits and reporting the results to the audit committee and encouraging audit committee to conduct periodic reviews of its activities and practices compared with current best practices to ensure that its activities are constituent with leading practices. Most of the reviewed literature is from the developed countries whose strategic approach and financial footing is different from that of Ghana. Thus, there is a literature gap on the subject matter in the Ghanaian situation. This study therefore will seek to fill this gap by establishing the effectiveness of internal audit in promoting good governance in the public sector in Ghana with reference to the MDAs and MMDAs.

CHAPTER THREE

RESEARCH METHODS

Introduction

This chapter is totally devoted to the description of the methodology employed in the conduct of the study. The chapter opens with the research design, followed by the target population, the sampling technique, data collection, data analysis and estimation technique. The chapter also captures the justification and measurement of the study variables and a brief description of the study area. Data description followed and the chapter ends with unit and method of analysis.

Research Design

Research design refers to the procedures to be employed to achieve the objectives of the research (Mutai, 2001). According to Cooper and Shinder (2007), the research design constitutes the blueprint for the collection, measurement and analysis of data. The study adopted a both descriptive research design and regression analysis in investigating the relationship between internal controls and governance in MDAs and MMDAs in Ghana. The method is chosen since it is more precise and accurate and it involves description of events in a carefully planned way (Babbie, 2004). The descriptive research, also known as statistical research, describes data and characteristics about the population or phenomenon being studied.

Target Population

According to Mason et a1. (2007), the population of a study is the collection of all possible individuals, objects or measurements of interest. The target population for the study is management and staff of the Internal Audit Departments and Finance, Accounts, budget offices in MDAs in Kumasi, Ashanti Region. The study uses the Kumasi Metropolis due to the researcher's familiarity together with the easy accessibility. They also have the background knowledge in the field of study.

Sampling Technique

In selecting the respondents, purposive sampling technique was used to select from the different categories of personnel. In purposive sampling, also known as judgmental sampling, the researcher picks the respondents that will deliver the best information in order to satisfy the research objectives in question or with a purpose in mind. The researcher deemed it important to use purposive sampling technique as the study needed to reach out to people with knowledge of the research area hence the forty (40) staff at the internal audit, claims and finance departments was used for the study.

Data Collection

The study collected primary data on the current state of affairs of the government agencies. The main instrument for data collection was questionnaire with both structured and open-ended questions. Structured questions allow for uniformity of responses to questions. Questionnaires give the researcher comprehensive data on a wide range of factors. It allows greater uniformity in the way questions are asked, ensuring greater compatibility in the responses.

A five point non-comparative Likert scale will be used for the structured questions with the intent of the Likert being that, the statements represents different aspects of the same attitude. Likert scale is simple to construct, and easy for the respondents to read, understand and respond appropriately to the statements put across. The Likert scale enhances the production of highly accurate results during analysis. Secondary data was collected from government reports, magazines, newspapers and journals.

Data Analysis

The questionnaires were coded and analysed using the Statistical Programme for the Social Sciences (SPSS) version 19.0. Tables, charts, graphs, frequencies and averages (mean) will be used to demonstrate the response that was obtained from the respondents. Both qualitative and quantitative methods of investigations were employed in the analysis and interpretation of data for the study. The researcher will also use a multivariate regression analysis to estimate the relationship between the independent variables and the dependent variable. This will be done by using the logistic model estimation technique.

Estimation Technique

This study explores the relationship between governance and internal audit as well as risk management, internal control and compliance and consulting. Since good governance is assumed in this study to be good or bad, the logistic regression is deemed most appropriate for the study. That is, the econometric estimation of the model is based on the extensively applied logistic model.

It is assume that the probability that internal audit and the other independent variables ensure good governance can be expressed in a logistic function which is produced below:

$$P_i = \frac{1}{1 + e^{-(\beta_1 + \beta_2 X_i)}} \tag{1}$$

P_i was not observed but $Y = 1$ indicating good governance. If $Y = 0$, it indicates bad governance.

Since Y_i is a Bernoulli random variable, it can be written

$$\Pr(Y_i = 1) = P_i \tag{2}$$

$$\Pr(Y_i = 0) = (1 \quad P_i) \tag{3}$$

Supposing we have a random sample of n observations. Letting $f_t(Y_t)$ denote the probability that $Y_t = 1$ or 0, the joint probability of observing the Y values, i.e. $f(Y_1, Y_2, \dots \dots Y_n)$ is given as:

$$\ln\left(\frac{P_i}{1 \quad P_i}\right) = \beta_1 + \beta_2 X_i \tag{4}$$

Hence the regression equation

$$Y = \beta 0 + \beta 1X1 + \beta 2X2 + \beta 3X3 + \beta 4X4 \ \varepsilon$$

Where;

Y= Corporate governance in Kenyan government ministries (Discipline, Transparency, Independence, Accountability, Responsibility, Fairness, Social responsibility)

$\beta0$ = Constant Term

$\beta1$, $\beta2$, $\beta3$and $\beta4$, = Beta coefficients

X1= Risk Management (Risk Identification, Risk Assessment, Risk Mitigation and Risk Monitoring)

X2- Internal Controls (monitoring, control activities, accounting information and communication)

X3= Compliance and Consulting (compliance with specified procedures, provision for the timely reconciliation of accounts, promoting accountability, fraudulent activities or irregularities, ensure effectiveness and efficiency of operations, reviews of operational and financial performance)

X_4= Other independent variables

ε = Error term

Data Validity and Reliability

The researcher has carried out a pilot study to pretest the validity and reliability of data to be collected using the questionnaire. According to Berg and Gall (1989), validity is the degree by which the sample of test items represents the content of test is designed to measure. The researcher employed content validity which measures the degree to which data collected using a particular instrument represents a specific domain or content of a particular concept.

CHAPTER FOUR

RESULTS AND DISCUSSION

Introduction

This study aims at investigating the effect of internal audit on good corporate governance by determining how internal control systems have been effective or otherwise in ensuring good corporate governance in the MMDAs and MDAs in Ghana. Therefore, the purpose of this chapter is to present and discuss the empirical findings of our study. This chapter presents data and analysis on internal control practices, problems with internal control practices and respondents' perception in the performance of the internal audit section. In addition to this, the socio – demographic characteristics of respondent were also examined. The regression analysis follows the descriptive statistics of the factors under study.

Response Rate

Table 1 presents the response rate of the study. From the purposive sampling technique used, a total of forty (40) respondents were sampled and forty (40) questionnaires were issued out to the staff of MMDAs and MDAs. From table 1, out of the 40 questionnaires, 30 were returned representing a response rate of 75%, which the study considered adequate for analysis. The completed questionnaires were edited for completeness and consistency.

Table 1: *Response rate*

Questionnaire	Frequency	Percentage
Completed	30	75%
Uncompleted	10	25%
Total	100	100%

Source: Survey, Boateng (2016)

Socio – Demographic Characteristics of Respondents

The following socio – demographic characteristics were looked at as part of the analysis, age of respondents, sex of respondents, educational attainment level of respondents, years of services of the respondent and whether a respondent belonged to any of the professional association.

Age of Respondents

The study categorized the age distribution of respondents into persons aged 19 or lower, from 20 to 29, 30 to 39, 40 to 49 and persons aged 50 and above as represented in table 2. Out of the 30 respondent used in the study, 14 representing 46.7% were within the ages of 20 and 29. 11 respondents representing 37.7% were aged between 30 and 39. Those aged between 40 and 49 were the least of the age distribution, accounting for 5 out of the 30 respondents, representing 16.7%. However there were no respondents below the age of 20 years. The details are represented in the table below.

Table 2: *Age distribution of respondents*

Age	**Frequency**	**Percentage**
19 or <	0	0%
20 – 29	14	46.7%
30 – 39	11	36.7%
40 – 49	5	16.7%
Total	30	100%

Source: Field Survey, Boateng (2016)

Gender of Respondent

Table 3 represents the gender distribution of respondents. It was found that majority of the respondent are male (60%) while the remaining (40%) are female. This suggests that most of the staff dealing with audits and internal controls practices are males. The details are presented in table below.

Table 3: *Gender distribution of respondents*

Gender	**Frequency**	**Percentage**
Male	18	60%
Female	12	40%
Total	30	100%

Source: Survey, Boateng (2016)

Education Level

Table 3 presents the educational level of respondents as the study sought the highest education level of respondent. This was categorized as secondary, diploma, bachelor's degree, master's degree and higher degree. It was found that majority of respondents are having bachelor's degree as their highest level of education. This was evident as 23 out of the 30 respondents representing 76.7% were holding bachelor's degree. The secondary and higher education level were the least among the respondents with one (1) each representing 3.3%. There were three (3) respondents with master's degree representing 10% whereas there were two (2) diploma holders representing 6.7% of the total respondents. These findings go a long way to emphasize the level of skill needed in the accounting and auditing field. Below are the details.

Table 4: *Educational level of respondents*

Education	**Frequency**	**Percentage**
Secondary	1	3.3%
Diploma	2	6.7%
Bachelor's degree	23	76.7%
Master's degree	3	10%
Higher degree	1	3.3%
Total	30	100%

Source: Field Survey, Boateng (2016)

Years of Service

The study also sought to find the working experience of respondents. This was done through finding the number of years the respondent has worked in his current office. The study categorized the years of service into 1- 5 years, 6-10 years, 11- 15 years, 16- 20 years and over 20years of service. It was found that majority of respondent had worked for five (5) or less years. From table 5 it was evident that 19 out of the total 30 respondents representing 63.3% had worked for less than five years (5) in present position. Only two (2) respondents representing 6.7% of total respondents had worked for 11 – 15 years whereas nine (9) respondents representing 30% had worked for 6 – 10 years. None of the respondents had worked for 16 years and over. Below are the details of the year of service of respondents.

Table 5: *Distribution of respondents' years of service.*

Years of Service	**Frequency**	**Percentage**
5 or <	19	63.3%
6 – 10	9	30.0%
11 – 15	2	6.7%
16 – 20	0	0%
20 or >	0	0%
Total	30	100%

Source: Field Survey, Boateng (2016)

Professional Association

The study also sought to find out if respondents belong to any of the professional associations on their field of work. This was done by asking respondents to respond "yes" if they belonged and "no" if they do not belonged to a professional association. From table 6, it was found that a minority 7 out of the 30 respondents representing 23.3% belonged to a professional association in the work field whereas the remaining 23 representing 76.6% did not belong to a professional association. Below are the details

Table 6: *Distribution of professional status of respondents.*

Professional	Frequency	Percentage
No	23	76.7%
Yes	7	23.3%
Total	30	100%

Source: Field Survey, Boateng (2016)

Effectiveness of Internal Audit on Risk Management

The study sought to find out the effectiveness of internal control on risk management. Risk management was assessed by this study on three parameters of risk assessment, risk mitigation and risk monitoring. For easier understanding the study provided a scale of 1 – 5, with 1 representing ineffective and 5 representing very effective. From the data collected, many respondents indicated that risk assessment, risk mitigation and risk monitoring are effective. Risk assessment, risk mitigation and risk monitoring had 3.57, 3.47 and 3.30 means respectively. The standard deviation for the responses of the three risk management strategies were 1.040 for risk assessment, 0.860 for risk mitigation and 0.915 for risk monitoring.

These statistics indicate that internal audit is deemed effective in ensuring risk management in MDAs and MMDAs in Ghana. This is in line with Griffiths (2006) who found that internal auditing provides independent and objective assurance to an organisation's management that its risks are being mitigated to an acceptable level, and reports where they are not. Keitany (2000) also concluded in his study of "the internal audit control function and its implication for risk assessment by the external auditor: A case of quoted companies" concluded that the internal audit departments in companies should not be done away with as it assists management in its day to day operations.

Table 7: *Effectiveness of Internal Audit on Risk Management*

Risk Management	**Min**	**Max**	**Mean**	**St. dev**
Risk Assessment	2	5	3.57	1.040
Risk Mitigation	2	5	3.47	.860
Risk Monitoring	2	5	3.30	.915

Source: Field Survey, Boateng (2016)

Effectiveness of Internal Audit on Internal Control

Table 8 below depicts the summary of the findings on the effectiveness of internal audit in internal control. Respondents were asked to rate the level of effectiveness of some internal control activities on a scale of 1 – 5, with 1 representing ineffective and 5 representing very effective. According to the findings, respondents rated review of individual systems and process as moderately effective with a mean of 3.30. Control of information within the organisation had similar rating with mean of 3.33 as did accounting information and communication with a mean of 3.37. Managerial controls and operational controls had means of 3.17 and 3.47 respectively whereas provision of financials controls had the highest ratings with mean of 3.73.

These statistics indicate that respondents saw internal audit as effective on internal controls. This is supported by Zhang, Zhou and Zhou (2006) in their paper "Audit committee, auditor independence and internal control weaknesses" which concluded that firms are more likely to be identified with an internal control weakness, if their audit committees have less financial expertise or, more specifically, have less accounting financial expertise and non-accounting financial expertise, as well. Mihret and Yismaw (2007) as well in a study on Ethiopia public sector found that internal audit's lack of authority on budgets reduces its control of resource acquisition and utilization.

Table 8: *Effectiveness of Internal Audit on Internal Control*

Internal Control	**Min**	**Max**	**Mean**	**St. Dev**
Review of individual systems and processess	1	5	3.30	0.952
Providing financial controls	2	5	3.73	1.015
Managerial controls	1	5	3.17	1.206
Operational controls	1	5	3.47	0.973
Control information within the organisation	1	5	3.33	1.155
Accounting information and communication	2	5	3.37	0.964

Source: Field Survey, Boateng (2016)

Effectiveness of Internal Audit on Compliance and Consulting

The study further sought to investigate the effectiveness of internal auditing to compliance and consulting. For easier understanding, the study provided a scale of 1 – 5, with 1 representing ineffective and 5 representing very effective. From the findings many respondents indicated that ensuring that public spending was within budgetary provisions and disbursement comply with specified procedures are the most effective. This is depicted by the high mean ratings of 3.77 and 3.80 respectively. Elsewhere, promoting of accountability and compliance with laws, regulation and contracts were also deemed effective by respondents with mean ratings of 3.57 and 3.67 respectively.

Review of operational and financial performance and provision information about any fraudulent activities or irregularities were seen to be moderately effective by respondents with average ratings of 3.40 and 3.47 respectively. This is consistent with literature as Bostan and Grosu (2010) in their study of the role of internal audit in optimization of corporate governance at groups of companies concluded that internal audit ensures compliance with legislation and recommendations in matters of corporate governance and also transparency, efficiency and friability in internal communication.

Also Ljubisavljevic and Jovanovic (2011) in a research on the internal audit position of Serbian companies concluded that Internal audit determines the reliability, reality, and integrity of financial and operational information that comes from different organisational units, on which appropriate business decisions at all levels of management are based. Wangui (2012) also concluded in a similar study in the ministries in Kenya that internal audit effectively ensured that advice and comment on devotion to the values and code of conduct or code of ethics of the ministries were adhered to.

Table 9: *Effectiveness of Internal Audit in Compliance and Consulting*

Compliance and consulting	Min	Max	Mean	St. Dev
Promoting accountability	1	5	3.57	1.223
Provide information about any fraudulent activities or irregularities	1	5	3.47	1.137
Ensure public spending is within budgetary provisions	1	5	3.77	1.165
Ensure disbursement comply with specified procedures	1	5	3.80	0.961
Compliance with laws, regulation, and contracts	2	5	3.67	0.884
Review of operational and financial performance	1	5	3.40	0.894

Source: Field Survey, Boateng (2016)

Attributes of Corporate Governance in various Ministry in the Last five Years

The study aimed at investigating the rating of corporate governance attributes in various MDAs and MMDAs over a period of five years preceding the study. For easier understanding the study provided a scale of 1 – 5, with 1 representing greatly decreased and 5 representing greatly improved. From the findings, accountability earned the highest ratings of 4.11 whereas fairness recorded the least ratings of 3.20. This therefore indicates that accountability had improved over the last five year whereas it is somehow constant in terms of fairness. Transparency, responsibility and discipline had also improved as depicted by mean score of 3.63, 3.75 and 3.85 respectively. However social responsibility, fairness and independence seem to have not shown significant improvement with average ratings of 3.25, 3.20 and 3.24 respectively.

Table 10: *Attributes of Corporate Governance in various MDAs aand MMDAs in the last five years*

Attributes	**Mean**	**Std. Dev**
Discipline	3.85	0.657
Transparency	3.63	0.574
Independence	3.24	0.890
Accountability	4.11	0.605
Responsibility	3.75	0.553
Fairness	3.20	0.701
Social responsibility	3.25	0.623

Source: Field Survey, Boateng (2016)

Coefficient of Correlation

Table 11: *Correlation Coefficients*

		Corporate Governance	Risk Management	Internal Control	Compliance and Consulting
Corporate Governance	Pearson correlation	1			
Risk Management	Pearson correlation	0.074	1		
Internal Control	Pearson correlation	0.025	0.853**	1	
	Sig	0.897	0.000		
Compliance and Consulting	Pearson correlation	0.042	0.795**	0.874**	1
	Sig	0.825	0.000	0.000	

NB: ** indicates significance at 95% confidence interval

The study computed the Pearson correlation coefficient to measure the strength and direction of the linear relationship between the variables. From the findings, it was ascertained that there is a strong positive relationship between Internal Control and Risk Management as indicated by a correlation coefficient of 0.853. Compliance and Consulting and Internal Control also have a strong positive correlation with a correlation coefficient of 0.847. However, even though there was a positive relationship between Corporate Governance and risk management, internal controls and compliance and consulting, there extent of the relationship is not strong as indicated by correlation coefficients of 0.074, 0.025 and 0.042.

Multiple Regression Analysis

The study further conducted a multiple regression analysis so as to identify effectiveness of internal audit in promoting good governance in the public sector in Ghana with special focus on MDAs and MMDAs. Multiple regression is a statistical technique that allows the study to predict a score of one variable on the basis of the scores of several other variables. The main purpose of multiple regression is to learn more about the relationship between several independent or predictor variables and a dependent or criterion variable. The study used the statistical data analysis tool STATA to code the variables and estimate the multiple regressions for the study. The dependent variable, corporate governance, was recoded into a binary variable with ratings of 3 to 5 representing good governance and 1 to 2 representing bad governance. The table below is the output of the multiple regression.

Table 12: *Regression output of corporate governance on risk management, internal control and compliance and consultant.*

		Marginal effect	**P-value**
Risk_man		0.562**	0.047
Int_Control		-0.329	0.269
Comp_Cons		-0.046	0.843
Contant		0.565	0.130
No. of observations	**30**		
Pseudo R^2	**0.1546**		

NB: ** indicates significance at 95% confidence interval.

The regression equation for the study was stated as;

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \alpha$$

Where Y is the dependent variable (corporate governance), X_1 is Risk Management, X_2 is internal controls, X_3 is compliance and consulting. The study estimated the marginal effect of the regression as;

$Y = 0.562X_1 \quad 0.329X_2 \quad 0.046X_3 + 0.565$

From the regression equation, it was found that only Risk management has a positive effect on good corporate governance as indicated by a positive marginal effect of 0.562. This indicates that risk management is about 56 percent more likely to lead to good governance. However, the study found that an improvement in the ratings of internal controls and compliance and consultancy is less likely to lead to good governance. This is indicated by the marginal effects of -0.329 and -0.046. With the marginal effect of -0.329 for internal controls, it implies that internal control is about 33 percent less likely to ensure good corporate governance.

Also, marginal effect of -0.046 of compliance and controls indicates compliance and consulting is about 4 percent less likely to ensure good corporate governance. In relation to literature, Wangui (2012) affirms the effectiveness of risk management on good corporate governance within Kenya government ministries. The findings of this study is also in agreement with earlier findings by Prawitt et al., (2006) that the internal audit function plays a unique role in corporate governance by monitoring organisational risks and ensuring that organisational processes are efficient and effectively controlled. Spira and Page (2003) found that the internal audit activity evaluates risk exposures relating to the organisation's governance, operations and information systems, with regards to the effectiveness and efficiency of operations, reliability and integrity of financial and operational information.

However, in contrast to the findings of this study, Njanike, Mutengezanwa and Gombarume (2011) found in their study of “Internal Controls in Ensuring Good Corporate Governance in Financial Institutions” done in Zimbabwe, that effectiveness of internal control systems contributed to a greater extent to good corporate governance in financial institutions in Zimbabwe. On the impact of internal control on corporate governance, Olumbe (2010) in a study of the relationship between internal controls and corporate governance in commercial banks in Kenya, found internal control to positively impact on corporate governance which is in contrast to the findings of this study.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

Introduction

The objective of this study is to investigate the effectiveness of internal audit on good governance. In addressing this objective, the study examined the relationship between internal audit and good corporate governance by investigating the effect of internal audit on good corporate governance in MDAs and MMDAs in Ghana.

Summary of Findings

From the findings of the study, it was clear that internal auditing is effective in risk management in risk assessment, risk monitoring and risk mitigation. This is in agreement with earlier findings by Prawitt et al., (2006) that the internal audit function plays a unique role in corporate governance by monitoring organisational risks and ensuring that organisational processes are efficient and effectively controlled. This is also consistent with Spira and Page (2003). They found that the internal audit activity evaluates risk exposures relating to the organisation's governance, operations and information systems, with regards to the effectiveness and efficiency of operations, reliability and integrity of financial and operational information. Jackson (2000) also found that risk management had become essential to corporate governance through its connection with the idea of internal control.

Further, the study found that assessment of internal control framework through, accounting information and communication and reviews of individual systems and processes were effective. Also financial controls, operational policies controls and managerial controls were found to be effective aspect in internal control due to application of internal auditing. This is supported by Cai (1997) who indicated that by measuring and evaluating the effectiveness of organisational controls, internal auditing, itself, is an important managerial control device, which is directly linked to the organisational structure and the general rules of the business. Herdman (2002) also asserted that an effective internal audit function is "crucial to the success of a company in stemming fraud and abuse, and in the preparation of accurate financial statements.

On the effectiveness of internal auditing on compliance and consulting, the study found that internal audit is effective in promoting accountability, providing information about fraudulent activities or irregularities. The study also found internal audit to be effective in ensuring that public spending is within budgetary provisions and also disbursement comply with specified procedures. Furthermore compliance with laws, regulations and contracts and review of operational and financial performances were effectively influenced by internal auditing. These findings are consistent with Roe (2004), whose study focused on internal audit independence and corporate governance. He stated that compliance and consulting in the internal audit function is a first line protection against insufficient corporate governance and financial reporting. Gramling and Myers (2003) also found that internal auditing help corporate governance by reviewing the organisation's code of conduct and ethics policies to ensure they are current and are communicated to employees for compliance.

On the ratings of the attributes of corporate governance in various ministries for the last five years, the study revealed that discipline, transparency and accountability, responsibility, independence and fairness had improved within government ministries. It was found that accountability is the most improved whereas fairness had the least improved ratings.

Conclusions

The study sought to find out effectiveness of internal audit in promoting good governance in the public sector in Ghana with special focus on the MDAs and MMDAs. This was achieved by investigating the effectiveness of internal audit on risk management, internal controls and compliance and consultancy.

Based on the findings, the study concludes that internal auditing is effective in risk management. Even though it was found that internal audit was effective on risk assessment, risk mitigation and risk monitoring, it was more effective on risk assessment than on risk mitigation and risk monitoring.

Internal audit was found to be effective on the review of individual systems and processes and also the control of information within the organisation. On the aspect of internal auditing to compliance and consulting, the study concludes that internal audit effectively promoted accountability and provided information about fraudulent activities and irregularities. It also effectively ensured that public spending is within budgetary provisions and that disbursement complies with specified procedures. The study also concludes that internal audit effectively ensured compliance with laws, regulations and contracts and reviews of operational and financial performance.

Furthermore, the study concludes that discipline, transparency and accountability, responsibility, independence and fairness had improved within the MDAs and MMDAs. However, accountability is the most improved and independency is the least improved. From the regression analysis, the study concludes that improving risk management is more likely to lead to good governance whereas improving internal controls and compliance and consultancy is less likely to lead to good corporate governance.

Policy Recommendations

From the findings of the study, the researcher recommends that in order for the government to be effective in its operation and service delivery they should recognize the contribution of internal auditing. Additionally, the study recommends that for the public institutions to effectively asses, mitigate and monitoring risk they should apply internal auditing in its operation. On effectiveness of internal auditing on internal control, the study that the MDAs and MMDAs and other government institutions should embrace internal auditing as an effective tool on internal control so as to realize their objectives set with ease.

On the compliance and consult, the study recommends that the MDAs and MMDAs should put much importance on internal auditing services in order to improve on their performance and ensure they gain the trust of the people they serve. Inclusively, the study recommended that for effective service delivery government ministries should comply with the internal auditing policies to create transparency in the use of the public resources.

On ensuring good corporate governance, the study recommends that public institutions especially MDAs and MMDAs should ensure improvement on risk management, as this is more likely to lead to improvement in corporate governance. This can however be achieved through effective internal auditing.

Limitations of the Study

The researcher encountered various limitations that were likely to hinder access to information that the study was looking for. The main limitation of study was its inability to include more public institutions across the country. This study could have been enriched by covering more institutions across public sector so as to provide a broader based analysis from diverse public institutions. However, time and resource constraints placed this limitation. The time frame allocated for the study was also not adequate as it impacted on the coverage and in-depth study and analysis of objectives. The researcher also faced the challenge of non-co-operating staff, loss of questionnaires and some staff not answering certain questions raised in the questionnaire. The small size of the sample could have limited confidence in the results and this might limit generalizations to other situations.

Suggestions for Further Study

Future researchers should consider the inclusion of other public institutions to give a broader view of public institutions in Ghana. Also, future researchers can consider other factors that influence good governance of public institutions in Ghana.

The study suggests that further research can consider replicating this study in the private sector to highlight the impact of internal audit of governance in privately managed organisations in Ghana. This will present an opportunity for the comparison of internal audit's effect on the public and private sector organisations in Ghana.

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APPENDICES A

Questionnaire

Personal Data

1. Sex: Male [ ] Female [ ]

2. Age: 19 or less [ ] 20—29 [ ] 30—39 [ ] 40—49 [ ] 50 or more [ ]

3. Which level of education are you?

   SHS/Secondary [ ]

   Diploma [ ]

   Bachelors' [ ]

   Masters' [ ]

   Others (Specify)……………..........................

4. Current Job Title/Office……………………………………………………………

5. How long have you been in your current office?

   5 or less years [ ]

   6 – 10years [ ]

   11 – 15years [ ]

   16 – 20 years [ ]

   21 years or more [ ]

6. Do you belong to any professional association on your job area?

Yes [ ] No [ ]

Internal audit in promoting good governance

1. How effective are the following functions of internal audit (risk management, internal controls and compliance and consulting) in promoting good governance in your ministry?

Use a scale of 1- 5 where 5=very effective, 4=effective, 3=Moderately effective, 2= Slightly effective and 1= ineffective

	1	2	3	4	5
Risk Management					
Risk Assessment					
Risk Mitigation					
Risk Monitoring					
Suggest risk management strategies					
Provide assurance that the risks are being appropriately managed					
Assess ethics and values within the organszation					
Assess performance management					
Assess communication of risk					
Unplanned and informal reviews of other areas of concern, including unacceptable levels of risks					

INTERNAL CONTROLS					
Reviews of individual systems and processes					
Provide Financial controls					
Managerial controls					
Operational policies controls					
Controls information within the organisation					
Accounting Information and communication					
Assessment of internal control framework					
Methodical examination of business processes and connected control					
Provision of independent verification of a sufficient sample of transactions to ensure integrity of the decision making process					
Ongoing and independent reconciliation of all balances					
COMPLIANCE AND CONSULTING					
Ensure that public spending is within budgetary provisions					
Ensure disbursement comply with specified procedures					
Provides for the timely reconciliation of accounts					

Provides effective systems for managing and accounting for physical and financial assets					
Promoting accountability					
Providing information about any fraudulent activities or irregularities					
Ensure effectiveness and efficiency of operations					
Ensure reliability and integrity of financial and operational information					
A source of information on major frauds and irregularities					
Reviews of the agreement framework and specific compliance issues					
Reviews of operational and financial performance					
Suggestions for more helpful and competent use of resources					
Appraisal of the achievement of corporate goals and objectives					
Compliance with laws, regulation, and contracts					
Advice and comment on devotion to the values and code of conduct/code of ethics of the organisation					

2. How would you rate the following attributes of corporate governance in your ministry in the last five years?

	Greatly improved (5)	Improved (4)	Constant (3)	Decreased (2)	Greatly decreased (1)
Discipline					
Transparency					
Independence					
Accountability					
Responsibility					
Fairness					
Social esponsibillity					

Thank you for your cooperation.