



Received 16 April 2019; Accepted 10 June 2019

Assessment of Internal Auditing Position in the Nigerian Private Sector: An Applied Study

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Abstract: The significance of quality internal auditing has received serious attention in both regulatory and public fora in recent years. Essential elements of organisation internal auditing are competency, independence, quality of work performed, risk-based internal audit, internal control activities and coordination between internal and external auditors. The objective of this study is to examine the position of these quality attributes of IA in the Nigerian private sector following the recent regulatory changes. The questionnaire was administered on internal auditors using a sample of ninety-seven organisations listed on the Nigerian Stock Exchange (NSE) to collect information for the period December 2018 to July 2019. The findings show that all the variables are free from multicollinearity and the results of the descriptive statistics of mean and standard deviations provide that all the respondents seem to agree with the statements regarding the variables. Finally, the paper provided limitation of the study and direction for future research.

Keywords: competency, independence, work performance, risk-based audit, internal control activities, internal auditing

JEL Classification: M40, M42, M49

Paper Type: Research

1. INTRODUCTION

Internal auditing (IA) task is believed to be as one of the functions that gain tremendous attention at local and international level at both private and public sectors organisations. This worldwide attention given IA was generally as a result of higher corporate and financial scandals such as Lehman Brothers, Arthur Anderson, HH Insurance, Enron and WorldCom. This has led to various organisations both private and public to admit the relevance of IA particularly after it has become clear that lack of effective internal control system is viewed as one of the contributing factors of major corporate failures (Lewington, 1996; Verschoor, 2002).

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In recent years, IA has become an essential part of organisational structures as a value-adding service (Al-Twairy, Brielrley, & Gwilliam, 2003; Arena & Azzone, 2009; Mihert & Woldeyohannis, 2008). The importance of IA has also been acknowledged in various legislation such as the Blue Ribbon Committee (BRC, 1999); King Committee 2009, Sarbanes-Oxley Act (SOX, 2002), Committee of Sponsoring organisation (COSO, 2011) integrated framework.

In Nigeria, several regulations and codes of best practices have been released to take an interest in IA at private-sector levels, such as Financial Reporting Act (FRA, 2012) and private sectors Code of Corporate Governance (CCG, 2016). Similarly, IA has also attracted professional attention of the Institute of Chartered Accountants of Nigeria (ICAN) by issuing Technical Guidance to Report on Internal Audit over Financial Reporting (TGRIAFR, 2015) and the setting up the Nigerian Institute of Internal Auditors. Among the objectives of the institute is to develop IA in Nigeria and to provide international best practices in IA and proper direction relating to IA practices.

The objective of this study is to assess the IA position in terms of competency, independence, work performed, risk-based internal auditing, internal control activities and coordination between internal and external auditors in Nigerian private sector pursuant to what has been listed in the FRA 2012 and CCG 2016 issued by Financial Reporting Council (FRC) relating to these quality factors. In Nigeria, private sector organisations are classified into two, listed and non-listed organisations. The present study focused on listed organisations because the listed organisations are under strict regulations to establish and maintain IA compare to non-listed.

This study was motivated for several reasons: Firstly, the topic is particularly relevant for Nigeria characterised with inadequate enforcement mechanisms and poor accounting and an auditing infrastructure. Further, the quality of IA in Nigeria has been questioned in recent years because of the increasing number of accounting scandals and corporate failures (Iyoha, 2011; Kantudu & Samaila, 2015; ROSC, 2011). Secondly, IA tends to vary among organisations and countries level depending on the regulatory framework put in place (Alhajri, 2017; Alqudah, Amran & Hassan, 2019; Goodwin & Yeo, 2001). As a result, several studies have suggested for further research in this area at both country and organisational levels from both developed and developing countries, especially where CG changes have taken place to assess the effectiveness of such changes (Endaya & Hanefah, 2016; Mihert & Yismaw, 2007).

The rest of the paper is organised as follows: section two presents the literature review, section three provided the methodology of the study, section four presents the result and analysis findings and section five presents discussion and conclusions of the study.

2. LITERATURE REVIEW

Internal auditing is continuously becoming more critical in the present governance structure. In spite of that, it remains a field that is seen as not sufficiently studied to gain the maximum benefit of the function in academic study (Sarens, Lenz, & Decaux, 2016). Several studies on internal audit quality have focused on a number of attributes as of particular interest such as objectivity, work performed, independence, and competency (Al-Qadasi, Abidin, & Al-Jaifi, 2019; Ali, Gloeck, Ali, Ahmi, & Sahdan, 2007; Arena & Azzone, 2009; Christopher, Sarens, & Leung, 2009; Dalmas & Barac, 2018; Goodwin & Yeo, 2001; Jachi & Yona, 2019). For example, Goodwin and Yeo (2001) evaluated the quality of IA departments using independence and objectivity of internal audit function (IAF).

The second stream of IA literature consists of cluster of studies that considers how other stakeholders such as audit committee, senior management and external auditors evaluate the quality of IAF (Abdallah, 2018; Adel & Maissa, 2013; Cooper, Leung & Matthews, 1996; Goodwin-Stewart & Kent, 2006; Khlif & Samaha, 2016; Krishnanmoorthy, 2002; Mohamed, Zain, Subramaniam, Fadzilah, & Yusoff, 2012; Page & Spira, 2004; Tušek, 2015). Cooper et al. (1996) indicated that IA stands as support devices to the senior management with regards to examining the operation efficiency, organisational finances, and providing an understanding of business operations.

Additionally, considerable archival studies have concentrated on the relationship between IA and financial reporting quality (FRQ) (Abbott, Daugherty, Parker & Peters, 2016; Al-Shetwi, Ramadili, Chowdury & Sori, 2011; Coram, Ferguson & Moroney, 2008; Davidson, Goodwin-Stewart & Kent, 2005; Gras-Gil, Marin-Hernandez & Garcia-Perez de Lema, 2012; Gros, Koch & Walker, 2017; Johl, Johl, Subramaniam & Cooper, 2013; Lakovic, Smolovic & Stanovic, 2016; Prawitt, Smith & Wood, 2009). Abbott et al. (2016) indicated that the joint existence of independence and competence are essential ingredients in effective IA financial monitoring. Gras-Gil et al. (2012) studied IA from the proxies of coordination between internal and external auditors, and the type of audit performed by IA and the study reported enhanced FRQ when IA is involved in the annual audit.

Nonetheless, there has been a relatively limited study on IA that has predominantly focused on Nigeria private sector organisations. Hence, IA remains under-researched in the context of Nigeria. Given the limited studies on IA, this study attempts to provide insights into IA in Nigeria regarding whether the scope of IA is sufficiently wide-ranging to be considered value-adding. By carrying out a study on IA in Nigeria, this study will enhance the understanding of IA practices in this country where the environment differs from developed countries. Thus, in this setting, a study of IA improves knowledge of the profession and is also timely because Nigeria cannot lag behind the increasing interest in corporate governance practices in several developing countries.

3. METHOD

3.1 Participants and Data Collection Process

The population of the present study is all chief audit executives (CAEs) of Nigerian listed organisations as at December 2018 to July 2019. Questionnaires were distributed to 149 CAEs or their representatives. At the end of the data collection process, 109 questionnaires were returned completed. 97 out of the 109 questionnaires were found to be usable for further analysis.

3.2 Variable Measurement

A 5-point Likert Scale questionnaire designed was used to obtain the opinion of the participants. The questionnaire design is based on the review of relevant literature regarding internal audit competency, internal audit independence, internal audit work performance, risk-based internal auditing, internal control activities and coordination between internal and external auditors.

Internal audit competency: This was proxy using nine items adapted from Endaya and Hanefah (2016); Kabuye, Nkundabanyanga, Opiso and Nakabuye (2017) and Schneider (1984): CAEs have an in-house training; CAE have current knowledge of audit practices; CAE has knowledge of the organisation policies, operations and procedures; in recruiting CAE emphasis in giving to professional certification; CAE have sufficient knowledge of

internal auditing standards; CAE has support for continuing professional training; there is adequate induction training for new CAE; CAE are trained in data processing system; CAE educational background is relevant to auditing and accounting.

Internal audit independence: This was measured using 11 items adapted from Johl et al. (2013), Prawitt et al. (2009), Endaya and Hanefah (2016): CAE have unrestricted access to all sections of the organisation; AC evaluate the performance of CAE; AC approves the remuneration of CAE; CAE meet with AC without management presence; CAE is free from duties that conflict with their roles as internal auditors; CAE have authorization and unrestricted access to investigate any area; CAE is not assigned to areas where close friends or relatives are employed; CAE is at liberty to choose audit approach, procedures and technique to use; reports and recommendations made by CAE is free from management interference; AC has the authority to appoint/dismiss CAE; AC determines/approve internal audit budget,

Internal audit work performance: This was proxy using 12 items adapted from Schneider (1984); Johl et al. (2013); Desai, Roberts & Srivastava (2010): annual internal audit plans are prepared every year in line with applicable internal audit standards; annual internal audit task is accomplished in accordance with the plan; internal audit findings are backed up with appropriate evidence; findings from the fieldwork are recorded in the audit working papers; there are continued follow-up procedures on the audit findings to ensure that corrective measures are taken; CAE activities include ensuring that financial operations are carried out correctly; CAE performs periodic quality review of internal audit working papers; internal audit work manual is available for use by all internal auditors; activity reports measuring performance with department goals and work schedule are submitted periodically to management and AC; CAE ensure post-audit assessments are adequately carried out; there is proper job description for each level of internal auditor; CAE audit reports are prepared in a clear and concise manner.

Risk-based internal auditing: This was measured using 6 items adapted from Ackermann and Marx (2016), Abdullatif and Kawuq (2015) with modification to suit the study objectives: CAE assess the risk exposure affecting reliability and integrity of financial and operational information; CAE identify risk that can prevent the attainment of financial reporting objectives; CAE was aware of potential material misstatements due to fraud in evaluating risk to the achievement of financial reporting objectives; CAE assess risk exposures affecting the effectiveness and efficiency of operations and programs; CAE have more comprehensive understanding of the risk practices of the organisation; CAE have clear strategies for dealing with significant risks that have been identified.

Internal control activities: This was measured using nine items adapted from Utami (2016); Wah (2011): organizational philosophy supports the attainment of effective internal control over financial reporting; management assigns appropriate level of authority to CAE to facilitate the internal control over financial reporting; CAE assess controls contributing to the attainment of reliability and integrity for financial and operational information; CAE identify internal control weaknesses in a timely manner to those parties responsible for taking corrective actions; there is continuous evaluation by CAE to determine whether or not internal control over financial reporting are functioning; CAE assess the controls contributing to the attainment of strategic objectives of the organisation; CAE promote the continuous improvement of internal control process; CAE prepare an internal audit plan allowing for control testing; CAE state their opinion on the status of the internal control system.

Coordination between internal and external: This was measured using 8 items adapted from Gras-Gil et al. (2012): internal and external auditors (IEA) hold periodic meeting to discuss audit matters; IEA collaborate in the preparation of annual audit; IEA have free access to each other's audit programs and working papers; IEA exchange audit

reports and management letters; IEA discuss their audit plans and findings; internal auditor display a kind of assurance to external auditor that comply with relevant professional standards; IEA collaborate in the area of work schedule and audit coverage; IEA have common understanding of audit approaches, techniques and terminologies.

To control for non-response bias, each questionnaire was accompanied by an explanation and assurance that all individual responses would be treated confidentially. We developed a short survey length, ensured concise and clear wordings of the questions, conduct several follow-up visits and call reminders up a maximum of four times for prolonging to answer the questionnaire. The current study conducted a missing value analysis because missing information may minimise the accuracy of calculated statistics because there is less information than initially planned

4. RESULTS AND ANALYSIS

This study used the Statistical Package for Social Sciences (SPSS) version 22.0 to verify the data descriptively. Following various steps in establishing the frequencies, percentages, ranges, means and standard deviations for the variables, the information was coded into SPSS software and proceed for the data screening to identify the treatment of outliers, missing value and replacement of missing values normality test multicollinearity test, descriptive statistic test and any other associated checks (Tabachnick & Fidell, 2007).

Then normality analysis of the individual variables was undertaken, normality test in the method of categorising the data for individual constructs and their association to the standard categorisation for statistical approach (Hair, Anderson & Tatham, 2010). To assess the normality of the variables and check possible deviations, this study employed multivariate normality to evaluate the data categorisation using kurtosis and skewness (Hair et al. 2010). West, Aiken and Todd (1993) suggested cut-off scores for assessing data categorisation, where kurtosis scores <7 and skewness scores <2. Table 1 present the result of normality test: kurtosis and skewness.

Table 1. Normality Test: Skewness and Kurtosis Statistics (n=97)

Constructs	Min	Max	Mean	SD	Skewness		Kurtosis	
					Sta	SD.	Sta	Std
IAC	2.78	4.78	4.18	.319	-1.02	.245	2.82	.485
IAI	2.64	5.09	4.03	.488	-.861	.245	.763	.485
IAW	3.58	5.00	4.46	.297	-.307	.245	.237	.485
RBA	2.50	5.00	4.27	.373	-1.11	.245	4.54	.485
ICA	3.22	5.00	4.32	.355	-.979	.245	1.21	.485
IEA	2.38	5.00	4.08	.515	-.892	.245	1.43	.485

Furthermore, the study evaluates the multicollinearity through the investigation of tolerance and VIF via the regression findings presented by SPSS collinearity diagnostic results. Ringle and Sarstedt (2011) viewed this investigation as the most important and most dependable analysis for multicollinearity. The presence of multicollinearity can affect the scores of the estimation of coefficient and statistical significance (Chatterjee & Yilmaz, 1992; Tabachnick & Fidell, 2007). Multicollinearity was defined as the association between two or more variables when the variables show a small relationship with one another (Hair et al. 2010; Pallant, 2010). Table 2 present the result of multicollinearity test.

Table 2. Multicollinearity Test: Correlation Matrix (n=97)

CONSTRUCTS	IAC	IAI	IAW	RBA	ICA	IEA
IAC	1					
IAI	.338**	1				
IAW	.201*	.315**	1			
RBA	.399**	.143	.286**	1		
ICA	.298**	.292**	.496**	.378**	1	
IEA	.438**	.371**	.319**	.437**	.437**	1

Table 3. Multicollinearity Test: Tolerance and VIF (n=97)

Variables	Collinearity Statistics	
	Tolerance	VIF
Internal Audit Competency	0.67	1.47
Internal Audit Independence	0.69	1.43
Internal Audit Work Performed	0.70	1.42
Risk-Based Internal Auditing	0.66	1.5
Internal Control Activities	0.55	1.79
Internal and External Auditors Coordination	0.59	1.69

In this part, descriptive statistics of individual variables were provided. The mean (that is aggregate of all surveyed result from the sample divided by the sum number of occurrences) and standard deviation (that is SD, the measure utilized to estimate the extent of dispersion of series of data values) were expected to arrive at the descriptive statistics of the variables as provided in Table 4.

Table 4. Descriptive Statistics of Study Variables: Mean and Standard Deviation (n=97)

Constructs	(M)	(SD)
Internal Audit Competency (IAC)	4.18	.31
Internal Audit Independence (IAI)	4.03	.48
Internal Audit Work Performed (IAW)	4.46	.29
Risk-Based Internal Auditing (RBA)	4.27	.37
Internal Control Activities (ICA)	4.32	.35
Internal and External Auditors Coordination (IEA)	4.08	.51

5. DISCUSSION AND CONCLUSION

The study examined the factors that might influence the IA position and these quality factors were built based on PCAOB (2007), AICPA (1991), CCG (2016) and FRA (2012), SAS No.65 and COSO (2006) integrated framework. The factors include six independent dimensions, namely: IA competency, IA independence, IA work performed, risk-based internal auditing, IA internal control activities and internal and external auditor’s coordination.

The study is also supported by the assumption of agency theory which postulates that quality dimensions are needed to achieve high IA positions in an organisation. In this regard, quality of the IA can be achieved by appropriate competency, independence, quality of work performed, internal control activities, risk-based internal auditing and internal and external auditor’s coordination.

Regarding the normality test of variables, the results show that both kurtosis and skewness are within the average range of satisfactory scores of <2 and <2. Thus, indicating that the data is free from bootstrapping standard error (Chernick, 2011). Concerning the multicollinearity test, the results provided that tolerance and VIF scores have proved that the variables are free from multicollinearity as the findings show VIF scores of all the variables are below 5, and the tolerance scores are high than .20 indicating the non-existence of multicollinearity among the variables. Thus, the variables are free from providing meaningless information that could strengthen standard error in the analysis.

Concerning descriptive statistics, the findings show the mean and SD for IAC are 4.18 and .31 while mean and SD for IAI stood at 4.03 and .48 respectively. Also, IAW mean and SD is 4.46 and .29, and the mean and SD for RBA are 4.27 and .37. Similarly, ICA and IEA mean and SD are 4.32 and .35 and 4.08 and .51 respectively. This indicates that respondents in the survey seem to agree with the statements concerning all the variables.

The present study has some implications for future studies in this field. First, the study shows different levels of IA factors that could lead to a different level of the IA position. Further, as against other studies on IA position in developing countries (Alktani & Ghareeb, 2014; Obeid, 2007), the results of the study are entirely unexpected. The findings of the study suggest that factors influencing the position of IA can strongly be affected by the different level of competency, independence, work performed, risk-based internal auditing, internal control activities, and coordination between internal and external auditors. Thus, decision-makers who are keen on improving the private sector IA should take into consideration the different levels of the quality factors. Further, the decision-makers need to focus on developing policies to enhance IA positions in organisations.

However, the present study is not free from limitations. First, the study focused on the environmental setting of the private sector listed organisations. Thus, future studies could look at these factors within the context of private sector non-listed organisations that establish IAF. Future studies could also incorporate other quality factors of IA that were not included in the current study such as senior management support to IA and audit committee interaction with IA. Finally, it should be noted with caution that the findings of this study are based on the Nigerian private sector IA setting. Hence, a generalisation of the results to other sector or counties should be made with caution.

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