EFFECTS OF INTERNAL AUDIT PRACTICE ON ORGANIZATIONAL PERFORMANCE OF REMITTANCE COMPANIES IN MODADISHU-SOMALIA

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ABSTRACT

The purpose of the study was to conduct a survey of internal audit practice factors affecting in the performance of remittance companies in Mogadishu-Somalia. The study design was used is descriptive survey, the target population of the study was remittance companies locate in Bakara market, and they are 15 remittance companies, the employees worked that 15 remittance companies are 402 employees. A sample size of 200 respondents was selected using Slog van's formula. Data collection methods used included questionnaire. The selection sample technique was purposive or judgmental approach. Data was analyzed using SPSS version 22. The key findings were that internal audit practice drivers individually had a positive influence on the organizational performance of remittance companies in Mogadishu-Somalia. The overall results indicated that there was a significant linear relationship between internal audit independence, internal audit quality, internal control system and audit risk assessments have positive significant relationship with Remittance Company's performance in Somalia. The conclusions were established that internal audit practice drivers were found to significantly and positively influence organizational performance of remittance companies in Mogadishu, Somalia. It is recommended that managers should study and select the driver that best suits their companies in order to achieve maximum performance.

Keywords: internal audit independence, internal audit quality, internal control system audit risk assessments, organizational performance, Mogadishu- Somalia

1. Introduction

Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization to accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes (International Professional Practices Framework, 2013). .). The study of (Carton, 2004) define organizational performance the measurement of the change of the financial state of an organization, or the financial outcomes that results from management decisions and the execution of those decisions by members of the organization. Auditor Independence refers to the auditor's ability to express his conclusions honestly and impartially. Auditor's independence is the primary justification of the existence, and thus the hallmark of the auditing profession. It is recognized as the primary attribute to be maintained by auditors in all circumstances. (Abu Bakar, 2009).

The study of (Jeong, 2005) state if the auditors find accounting irregularities in previous financial statements, it is assumed that high quality auditors are more likely to make corrections and report the changes in current financial statements. However, if the economic environment and institutional setting does not demand high-quality audit services, auditors may not restrict the opportunistic behavior of management but rather may behave opportunistically themselves to attract more clients. According to (Turner, 2013) internal control system is a process effected by an entity's board of directors', management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in three categories. According to (Anderson, 2012) audit risk is the risk the auditor faces in issuing an audit opinion when the audited financial statements contain a material misstatement. The auditor plans and carries out the audit to minimize this risk.

1.2 Statement of the Problem

The financial statement audit is an important tool for reducing information asymmetries and maintaining an efficient market environment, also it improves organizational performance (Farouk & Hassan, 2014). Internal Audits are an essential management tool to be used for verifying objective evidence of processes, to assess how successfully processes have been implemented, for judging the effectiveness of achieving any defined target levels, to provide evidence concerning reduction and elimination of problem areas to improve overall organizational performance (Mahzan & Binti Hassan, 2015).

As organizations pursuing objectives in an economic environment, the company is the meeting place of a wide range of stakeholders interested in its performance. They can be the directors of the company as shareholders and other third parties. This complex situation has prompted us to seek to understand more precisely. Internal audit can contribute to corporate performance, it can also help employees keep their place in the company the state to consider recovery of taxes, financial institutions take steps to recover their debt, the shareholders or partners should ensure the profitability of their investment. It could help all the actors of the company in every level to make the company get better and themselves in the same way. Internal audit is a method of controlling which allows different business partners such as shareholders, personnel, financial institutions the state to ensure the quality and reliability of the information provided. (Saud, 2012).

According to the study of (Ojong, 2014) internal auditing serve as an important connection in the business and financial reporting processes of corporations and not-for-profit organizations. Internal auditors play a key role in monitoring a company’s risk profile and identifying areas to improve risk management. The aim of internal auditing is to improve organizational performance. Although remittance companies practice internal audit but still they does not performing well according literature remittance companies practice internal audit but how practicing internal audit effect performance of remittance companies. So this study would investigate the effect of internal audit practice on the performance of remittance companies in Mogadishu-Somalia.

1.3 Specific Objectives of the Study

I. To assess the effects of internal audit independence on organizational performance of remittance companies in Mogadishu-Somalia.

II. To investigate the effects of internal audit quality on organizational performance of remittance companies in Mogadishu-Somalia.

III. To examine the effects of internal control system on organizational performance of remittance companies in Mogadishu-Somalia.

IV. To determine the effects of audit risk on organizational performance of remittance companies in Mogadishu-Somalia.

2. Literature Review

2.1 theoretical frameworks

According to (Carmichael, 2005), the need for theory in auditing, as with any other discipline, is associated with the willingness of the interested parties (shareholders, managers, bankers, auditors, analysts and so on) to form a solid basis for making financial decisions. Each of these parties is considered as an economic actor seeking to maximize its wealth and in doing so; they want to know all the possible ways to achieve this goal. To acquire the necessary knowledge about these options requires a thorough understanding of the economic variables and of the relationship between them. This can only be done through the use of a theoretical framework, which provides sufficient explanation and reasoning of the variables, their association with each other and the environment in which the economic action is taking place.

2.1.1 Theory of Inspired Confidence (Theory of Rational Expectations)

In 1926 Professor Theodore Limperg of the University of Amsterdam developed a theory, known as the Theory of Inspired Confidence (Theory of Rational Expectations), which, eventually, became known as the Theory of Rational Expectations. The theory holds that the value of the auditor's report derives from the expert nature of the auditor as an independent, competent professional. Broadly, this is a dynamic theory which holds that as the business community changes so the expectations it has of the auditors' function also changes. Limperg held that the work carried out by the auditor should be governed by the rational expectations of those who use their reports so auditors should not disappoint those expectations. Further, auditors should not seek to raise those expectations by any more than the work they do justifies, (Millichamp & Taylor, 2012).

2.2 Conceptual Framework

Conceptual framework is a scheme of variables which the study operationalizes in order to achieve the set objectives. A variable being the measurable characteristic that assumes different values among the subjects, independent variables are the ones that the study manipulates in order to determine their effects on another variable. The dependent variable attempts to indicate the total influence arising from the effects of the independent variables. It therefore varies as a function of the independent variables (Mugenda & Mugenda, 2003).

Independent variable, according to (Mugenda & Mugenda, 2003) is the presumed cause of changes in the values of the dependent variable; the dependent variable is expected to be influenced by the independent variable. This is illustrated in figure 2.1 below. The independent variables in this study are internal audit independence, internal audit quality, internal control system and audit risk assessments how they affect organizational performance of remittance companies in Somalia.

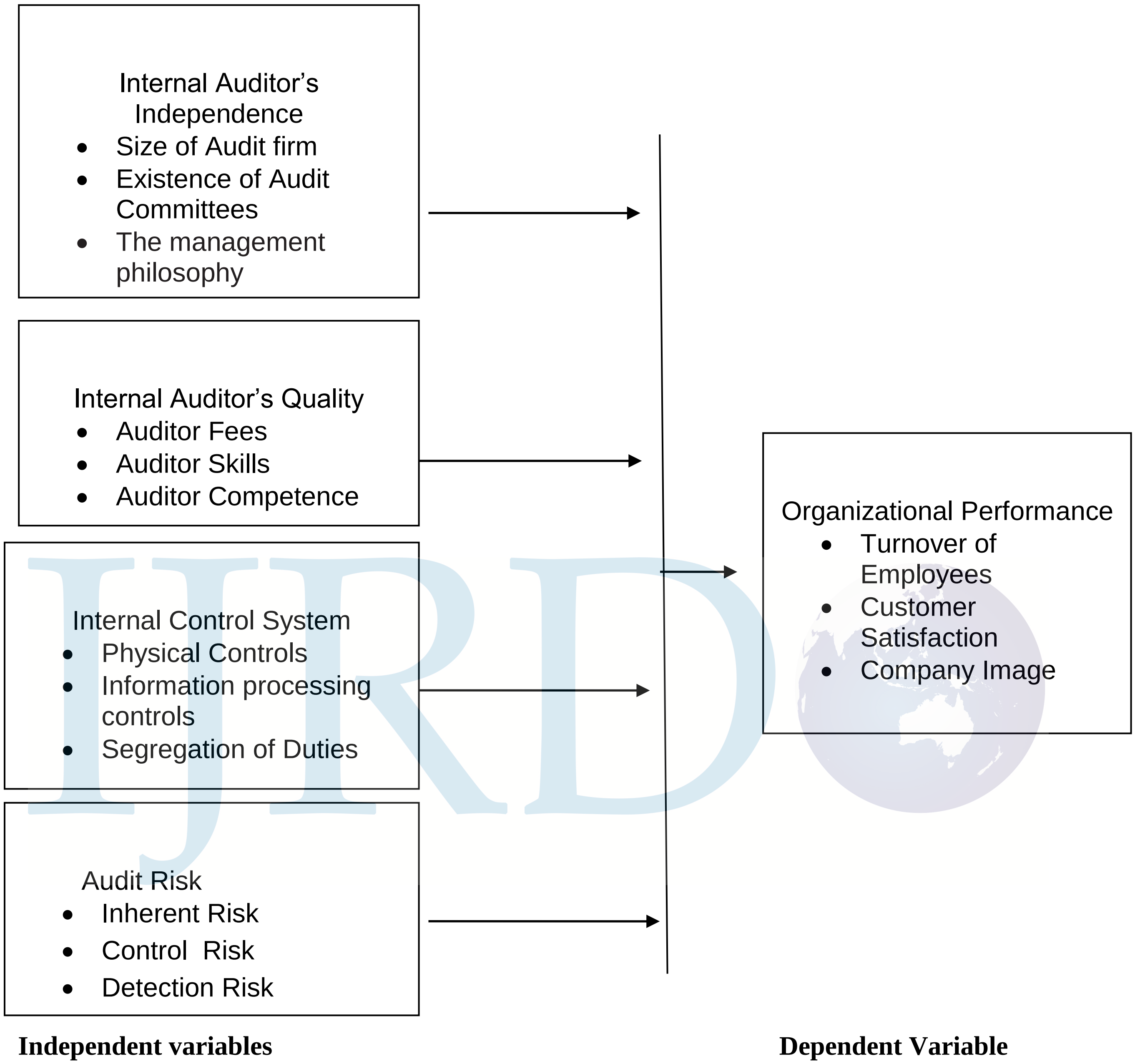

Figure 2.1: Conceptual Framework

2.3 Internal Auditor's Independence

Independence is the freedom from conditions that threaten objectivity or the appearance of objectivity. Such threats to objectivity must be managed at the individual auditor, engagement, functional and organizational levels. Auditor independence and objectivity are the cornerstones of the profession. The assurance services provided by auditors derive their value and credibility from the fundamental assumptions of independence of mind and independence in appearance. in more recent years, there has been heightened interest in issues associated with the independence and objectivity of internal audit. The motivation for research growth in the area is related to the evolving and expanding role of internal audit as a key corporate governance mechanism as well as an internal consultancy service and also performance of organizations. In this regard, internal auditors are in a unique situation as providers of both assurance services within the organization and consultancy services to managers (Stewart & Subramaniam, 2008).

2.4 Internal Auditor's Quality

Audit quality plays an important role in maintaining an efficient market environment; an independent quality audit underpins confidence in the credibility and integrity of financial statements which is essential for well functioning markets and enhanced organizational performance. Internal audits performed in accordance with high quality auditing standards can promote the implementation of accounting standards by reporting entities and help ensure that their financial statements are reliable, transparent and useful (Farouk & Hassan, 2014).

Sound audits can help reinforce strong corporate governance, risk management and internal control at firms, thus contributing to organizational performance. Management can improve organizational performance of their firms by increasing the quality of internal audit Although, this might seem like a profit reducing decision in the short run, the benefits that will accrue to the firm far outweighs the cost. This will help ensure that all financial transactions are in order; give the users of the financial statements more trust and confidence in terms of the quality of audited reports (Farouk & Hassan, 2014).

2.5 Internal Control System

Internal controls refer to the measures instituted by an organization so as to ensure attainment of the entity's objectives, goals and missions. They are a set of policies and procedures adopted by an entity in ensuring that an organization's transactions are processed in the appropriate manner to avoid waste, theft and misuse of organization resources. Internal Controls are processes designed and affected by those charged with governance, management, and other personnel to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of the financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations. Organizations establish systems of internal control to help them achieve performance and organizational goals, prevent loss of resources, enable production of reliable reports and ensure compliance with laws and regulations. An internal control system comprises the whole network of systems established in an organization to provide reasonable assurance that organizational objectives will be achieved (Nyakundi, Nyamita, & Tinega, 2014).

2.6 Audit risk

According to (Jones, 2009) audit risk is the risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of material misstatement and detection risk. Audit risk is fundamental to the audit process because auditors cannot and do not attempt to check all transactions. It would be impossible to check all of these transactions, and no one would be prepared to pay for the auditors to do so, hence the importance of the risk based approach toward auditing. Traditionally, auditors have used a risk-based approach in order to minimize the chance of giving an inappropriate audit opinion, and audits conducted in accordance with International Standards Auditing must follow the risk based approach, which should also help to ensure that audit work is carried out efficiently, using the most effective tests based on the audit risk assessment. Auditors should direct audit work to the key risks sometimes also described as significant risks.

2.7 Organizational performance

In general, the concept of organizational performance is based upon the idea that an organization is the voluntary association of productive assets, including human, physical, and capital resources, for the purpose of achieving a shared purpose. Those providing the assets will only commit them to the organization so long as they are satisfied with the value they receive in exchange, relative to alternative uses of the assets. As a consequence, the essence of performance is the creation of value. So long as the value created by the use of the contributed assets is equal to or greater than the value expected by those contributing the assets, the assets will continue to be made available to the organization and the organization will continue to exist. Therefore, value creation, as defined by the resource provider, is the essential overall performance criteria for any organization. How that value is created is the essence of most empirical research in management. Conversely, how that value is measured is the essence of this research (Carton, 2004).

3. Data and Methodology

This study would adopt a descriptive study design. Descriptive research studies are those studies which are concerned with describing the characteristics of a particular individual, or of a group, studies concerned with specific predictions, with narration of facts and characteristics concerning individual, group or situation. Descriptive studies are concerned with what, where and how of a phenomenon hence more placed to build a profile on that phenomenon (Kothari, 2004). Descriptive research is more appropriate because the study seeks to build a profile about the effect of internal audit on the performance of remittances companies in Mogadishu-Somalia.

According to (Lavrakas, 2008) define a population as any finite or infinite collection of individual elements. Target population refers to the entire group of individuals or objects to which researchers are interested in generalizing the conclusions (Ngumi, 2013), this research would target the employee of all remittance companies in Bakara market, the biggest market in Mogadishu. The exact number of all remittance companies in this area is 14 remittance companies. They are Dahabshil, Taaj, Amal, Tawakal, Amano, Juba, Mustaqbal, Kaah, Olimbic, Najma, Iftin, Muna, Horyal and Al falah. The area was selected because the majority of remittance companies in Mogadishu are located in Bakara market.

Sampling is the process of selecting a number of individuals for a study. A sampling design is a defined plan determined before any data is collected for obtaining a sample from a given population. The selected number of individuals will be as a representative of the whole population under study. Non probability sampling is a sampling procedure which does not afford any basis for estimating the probability that each item is the population has of being included in the sample. In purposive sampling, items for the sample are selected deliberately by the researcher; however, this design is adopted because of the relative advantage of time and money inherent in this method of sampling. Therefore this type of sampling is very convenient and is relatively inexpensive (Kothari, 2004). Slovin's formula will be used to this study to determine the sample size, because according (Tejada, 2012) Slovin's formula is applicable only when estimating a population proportion and when the confidence coefficient is 95%. Additionally, it is optimal only when the population proportion is suspected to be close to 0.5. Hence, it is not advisable to use Slovin's formula if any of the abovementioned assumptions do not hold. Sloven's formula for obtaining the sample size. Denoting by **n** the sample size,Slovin's formula is given by

$$n = \frac{N}{1 + Ne^2}$$

Where *N* is the population size and *e* is the margin of error (Lavrakas, 2008).

$$\boldsymbol{n} = \frac{\mathbf{402}}{\mathbf{1 + 402(0.05)^2}}$$

$= \frac{402}{1+402(0.0025)} = \frac{402}{2.005} = 200.4 \approx 200$. So the sample would be 200

Data collection methods used included questionnaire**.** Data will be analyzed quantitatively and presented descriptively and illustrated by using of tables and charts. The selection of these tools have been guided by the nature of data to be collected, the time available as well as by the objectives of the study. Kothari (2004) defines a questionnaire as a document that consists of a number of questions printed or typed in a definite order on a form or set of forms.

4 DATA ANALAYSIS AND PRSENTATION RESULT

Response rate is the percentage of people who responded to a survey. According to (Orodho, 2003), response rate is the extent to which the final data sets include all sampled members and is calculated as the number of respondents with whom interviews are completed and divided by the total number of respondents of the entire sample including none respondents. The study sample consisted of 200 remittance companies. The researcher distributed two hundred (200) questionnaires. Among the 200 questionnaires distributed, 190 were returned and 10 were not returned. The overall response rate was 95%. According to Kothari (2004), a response rate of 50% is considered average, 60-70% is considered adequate while anything above 70% is considered to be excellent response rate. This response rate was, therefore, considered good representative of the respondents to provide information for analysis and derive conclusions.

4.1 Reliability Analysis

In evaluating the survey constructs, reliability test was done. Reliability test is said to examine the degree to which individual items used in a construct are consistent with their measures. The widely used Cronbach's coefficient alpha was employed to assess internal consistency (Fien, 2006). Bryman and Cramer (1997) stated that 56 reliability of 0.70 is normally acceptable in basic research (Fien, 2006).According to (Zikmund, 2003) posits that a Cronbach alpha of 0.60 as a minimum is acceptable. All the alpha coefficients ranged between 0.65 and 0.95. Internal audit independence had Cronbach's alpha coefficient of 0.871, internal audit quality had 0.881, internal control system had 0.927, audit risk assessment had 0.873 while organizational performance had 0.761, Based on the coefficient values, the items tested were deemed reliable for this study.

4.2 Regression Analysis

In order to answer the research questions, a standard multiple regression analysis was conducted using organizational performance as the dependent variable, and the four independence variables: Internal audit independence, internal audit quality, internal control system and audit risk assessments as the predicting variables. The research used statistical package for social sciences (SPSS V 22) to code, enter and compute the measurements of the multiple regressions.

Table 4.1 model summary

Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**
1	0.795[a]	0.633	0.625	0.36114
a. Predictors: (Constant), audit risk, auditor quality, auditor independence, internal control system				

Adjusted R squared is coefficient of determination which tells us the variation in the [i]dependent variables due to change in the independent variables. From the findings in the above table the value of adjusted R squared is 0.625 and indicates that there was variation of 62.5% on organizational performance of remittance companies in Mogadishu due to changes in Internal audit independence, internal audit quality, internal control system and audit risk assessments at 95% confidence interval. This shows the significant that 62.5% of the variations in the organizational performance of remittance companies in Mogadishu are accounted for by the variations in the independent variables and the remaining 37.5% are accounted by other factors contained in the standard error.

R is the correlation coefficient which shows the relationship between the study variables. From the findings shown in the table above there was a strongly positive relationship between the study variables as shown by 0.795.

4.3 Analysis of Variations

Table 4.2 ANOVA of multiple regressions

	Model	Sum of Squares	Df	Mean Square	F	Sig.
	Regression	43.772	4	10.943	83.903	.000[a]
1	Residual	25.433	185	0.130		
	Total	69.205	189			
a. Predictors: (Constant), audit risk, auditor quality, auditor independence, internal control system						
b. Dependent Variable: organizational performance						

From the ANOVA statistics shown in table, the processed data, which is the population parameters, had a significance level of 0.5% which shows that the data is ideal for making a[ii] conclusion on the population's parameter as the value of significance (p-value) is less than 5%. The F critical at 5% level of significance was 2.42. Since F calculated (83.903) is greater than the F critical (2.72), this shows that the overall model was significant and that Internal audit independence, internal audit quality, internal control system and audit risk assessments significantly affect the organizational performance of remittance companies in Mogadishu-Somalia.

4.3 Coefficients of Stepwise Multiple Regression

Table 4.3 Coefficients of multiple regressions

Model		Un standardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	T	Sig.
1	(Constant)	1.978	.075		26.302	.000
	Auditor independence	.293	.090	.603	3.238	.001
	Auditor quality	.053	.075	.110	.705	.002
	Internal control system	.152	.171	.315	.885	.003
	Audit risk assessments	.455	.158	.943	2.871	.005

a. Dependent Variable: performance

From [iii]the above regression equation it was revealed that holding internal auditor independence, internal auditor quality, internal control system and audit risk assessments to a constant zero, organizational performance of remittance companies in Mogadishu would be at 1.978. A unit increases in internal auditor independence would lead to increase in the organizational performance of remittance companies in Mogadishu by a factor of 0.293. A unit increases in internal auditor quality would lead to increase in the organizational performance of remittance companies in Mogadishu by a factor of 0.053, A unit increases in internal control system would lead to increase in the organizational performance of remittance companies in Mogadishu by a factor of 0.152 and a unit change in audit risk assessments would lead to increase in the organizational performance of remittance companies in Mogadishu by a factor of 0.455.

5 Conclusions

From the findings of the regression analysis, the study found that there was a variation of 62.5% indicating that a combination of internal audit independence, internal audit quality, Internal control system and audit risk assessments explained 62.5% of the variation in the organizational performance of the remittance companies in Mogadishu-Somalia.

This is an indication that 62.5% changes in organizational performance of the remittance companies in Mogadishu could be accounted for by internal audit independence, internal audit quality, Internal control system and audit risk assessments while the remaining percentage is explained by other factors contained in error terms. The study further revealed that there was positive strong relationship internal audit independence, internal audit quality, Internal control system and audit risk assessments and organizational performance of change as shown by strong positive correlation coefficient. From the finding on analysis of variance, the study found that the overall model had a significance value of 0.05% which shows that the data is ideal for making a conclusion on the population's parameter as the value of significance (p-value) is less than 5%. The study further revealed that internal audit independence, internal audit quality, Internal control system and audit risk assessments significantly affects the organizational of remittance companies in Mogadishu. The established regression equation was

$Y = 1.978 + 0.293X1 + 0.053X2 + 0.152\ X3 + 0.455X4$.

6 Recommendations

1) There is need for the remittance companies in Mogadishu to increase their internal auditor quality as it was founded that internal auditor quality positively affects the organizational performance of remittance companies in Mogadishu.
2) There is need for the regulator to introduce internal control system that will be applied across all the organizational performance of remittance companies. This will go way further towards increased internal control system in the sector and contributes towards better organizational performance in the sector.
3) There is need for the remittance companies in Mogadishu to increase their audit risk assessments as it was founded that audit risk assessments positively affects the organizational performance of remittance companies in Mogadishu.
4) The study further recommends the need to strengthen this study via a longitudinal study and compare the performance of different categories of businesses as well. The implications from the findings point to a configuration approach on the implementation of internal audit practice by remittance companies.

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