

ADDIS ABABA UNIVERSITY
SCHOOL OF GRADUATE STUDIES
DEPARTMENT OF ACCOUNTING AND FINANCE



FACTORS THAT DETERMINE INTERNAL CONTROL EFFECTIVENESS IN INTERNATIONAL NON-GOVERNMENTAL ORGANIZATIONS WORKING IN HEALTH SECTOR IN ADDIS ABABA.

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A thesis submitted to Addis Ababa University College of Business and Economics in partial fulfillment of the requirements for the Degree of Masters of Science in Accounting and Finance.

June, 2016

Addis Ababa, Ethiopia

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Declaration

I, the undersigned, declare that this thesis is my original work and has not been presented for adgree in any other university, and that all source of materials used for the thesis have been duly acknowledged.

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ABBREVIATION AND ACRONYMS

AARP: American Association of Retired Persons
ACCA: Association Chartered Certified Accountants
AICPA: American Institute of Certified Public Accountants
CEO: Chief Executive Officer
CFO: Chief Finance Officer
ChSA: Federal Charity and Society Agency of Ethiopia
CIA: Certified Internal Auditor
COSO: Committee of Sponsoring Organizations
CPA: Certified Public Accountants
ERM: Effective Risk Management
GAO: General Accounting Office
IA: Internal Audit
IAE: Internal Audit Effectiveness
IAF: Internal Audit Function
IC: Internal Control
ICS: Internal Control System
IIA: Institute of internal Auditor
INGO: International Non-Governmental Organizations
NGO: Non-Governmental Organization
OLS: Ordinary Least Square
SAP: Statement on Auditing Practice
SPSS: Statistical Package for Social Science

ABSTRACT

NGO'S internal control effectiveness involves the capability of an organization to deliver services to its people in the most efficient manner while ensuring high quality of its services and support. The focus of the study was guided by the following objectives; to assess internal controls effectiveness in non-governmental organizations to identify the possible areas of deficiencies in the system. The study would be significant to the NGOs' as it would give insights to them on the importance of integrating internal control effectiveness their operational efficiency. The target population of the study was all internal audit/control staff all in all 90 working in the 30 selected non-governmental organizations working in health sector using multistage sampling methodology through questionnaires. Data was collected using questionnaires distributed to those individuals. Data was analyzed using descriptive statistics and inferential statistics using SPSS results. The findings revealed that there is insignificant internal control effectiveness. Particularly, there is negative insignificant relationship between the management support and internal control, though there is insignificant positive relationship between adequate and competent internal control staff and internal control. However there is significant relationship between organizational independence and internal control effectiveness. The study recommends that internal controls should be used to support in achieving its objectives the organizations in achieving its objectives by managing independence of internal control staff and by employment of adequate and competent staff that fosters operational performance of the organizations.

Key Words: Internal Control effectiveness; International Non-Governmental Organizations; Determinants of internal control Effectiveness.

Chapter One

1.1. Introduction

In every country there is now a big issue of accountability in the use of public money especially in relation to effectiveness, efficiency and cost of service delivery. To achieve government objectives, applying internal control function is a major mechanism for exercising and oversight in the use of scarce resources. Even more larger and complex systems require greater competitiveness, thus internal control has to become ever more critical and professional (Cecilia Nordin Van Gansberghe, 2003).

Internal control is also an integral part of Non-Governmental Organizations (NGOs) the financial policies and procedures, for them Internal control consists of all the measures taken for the purpose of protecting resources against waste, fraud and inefficiency. Internal controls ensure accuracy and reliability in accounting and operating data, securing compliance with the policies of the organization and evaluating the level of performance in all units of the organization (DeVries, D., and Lin, J. 2010).

Internal controls are simply good business practices. A firm's internal controls should include finance, operations and administration. Quality control is a type of internal control mechanism generally used by manufacturing and engineering firms to assure that products and services meet or exceed customer requirements and expectations. However quality controls should not be a tool used only by manufacturing or engineering firms but rather a tool used by any firm that provides services to customers or clients (Borg W and Gall, J. 1997).

Operational efficiency involves the capability of the organization to deliver services to its people in the most cost-effective manner possible while still ensuring the high quality of its products, services and support. Operational efficiency is often achieved by streamlining a company's core processes in order to more effectively respond to continually changing market forces in a cost-effective manner (De Vries, and Lin, 2010). In order to attain operational efficiency and for a company to achieve higher profit margins or is more successful in highly competitive markets. It is the vision of every company to improve operational effectiveness. Significant expertise is

required in areas of cost reduction; sourcing and shared services analyses, IT effectiveness, as well as crisis management in ones for companies achieve best performance and operational effectiveness.

In addition, development in internal control brings change in the scope and functions of internal audit customers. Previously internal auditors were seen mere assistants to accountants. Recently, however internal audit is certainly is considered an independent profession, in view of the significant they play in the management of organizations. Besides, the independence of internal auditors has always been a sensitive issue since they are also employees of an organization. This is compounded by the fact that there is no clearly organized structure, or reporting line, in many offices (Rolandas Rupsys, 2005).

According to The Committee of Sponsoring Organizations of the Tread way Commission (COSO, 1992) internal control is a major part of managing an organization. It comprises the plans, methods, and procedures used to meet missions, goals, and objectives; in doing so, support performance-based management. Though the functions of internal control makes it wider, the American Institute of Certified Public Accountants (AICPA), General Accounting Office (GAO) and other sources, broadly define internal accounting control as a series of procedures and practices designed to promote and protect sound management practices, both general and financial. Thus an effective internal control procedure will significantly increase the likelihood that financial information is reliable, so that management can make informed accurate information decision so that assets and records of the organization are not stolen, misused, or accidentally destroyed, the organizations policies and government regulations are met, and overall organization objective is achieved.

In recent years, funding constraints, calls for accountability, media exposure and the development of a contract culture have all brought increased demand for performance measurement within the development sector. Donors place greater emphasis on effectiveness and sustainability. As a consequence, NGOs are currently under pressure to undertake increased monitoring and evaluation, and to present measurable indicators of output, impact and capacity (Edwards, 1999; Lewis, 2001; Hailey, 2000; 2003). There is need for greater attention to the management challenges NGOs face today. Many NGOs command significant economic resources yet the accounting literature have largely ignored this sector. Consequently knowledge

of the effectiveness and efficiency of these organizations is poor. This study attempts to fill this lacuna by studying control systems in an NGO. It is against such background that I have decided to undertake this kind of research.

1.2. Statement of the Problem

Ideally, the use of internal controls measure in NGOs supposed to help them; to accomplish specific goals or objectives. NGOs are supposed to integrate internal control systems to ensure that resources are directed, monitored, and measured. For sound internal control, it is important that there be a segregation duties between individuals involved in a given process; in order to avoid the risk of someone controlling the process from beginning to end. Small NGOs with limited staff typically should implement a double-checking procedure. This ensures that each step is properly done and that no errors occur in the process. There are several measures an NGO can take to assure good control over the expenditures. Such control measures ensures that NGOs are operating in its mandate and achieves its goals and objectives.

Despite the various measures put in place to enhance proper management of NGOs in Ethiopia, there are significant policy risks and challenges that NGOs currently face. (ChSA report 2013). Therefore, the need to keep implementing, monitoring and evaluation of internal controls, should not be left to the public and private sectors, but should also be instituted by NGOs as well. It is against this background therefore that the study sought to investigate the influence of internal control measures employed by NGO's in enhancing their operational efficiency.

The purpose of this study was to assess the determinants of internal control effectiveness of INGOs. Specifically, this will involve managements' perception of internal control (IC's) value, management support, organizational independence, adequate competent internal audit staff. It is against this background that there is a need to undertake this kind of research to address the knowledge gap.

1.3. General objective of the Study

The general purpose of this study is to examine what factors determines internal control effectiveness of INGOs; in particular, those working in the health sector in Addis Ababa.

1.3.1. Specific Objective

- a) To examine the contributions of management support for internal control effectiveness in selected NGOs.
- b) To evaluate the extent to which organizational controls influence operational efficiency in selected NGOs; and
- c) To assess the extent to which periodic reviews influence the internal control effectiveness of selected NGOs Addis Ababa.

1.4. Research Questions

- 1. Does the management perception of internal control matter for organizations operational performance?
- 2. Does organizations independence of internal auditors affect operational performance of the organizations?
- 3. Does having competent internal control staff impacts better internal control effectiveness of the organizations?
- 4. To what extent have the approved internal audit charter contributed to the IAE in the NGOs offices

1.5. Significance of the Study

It is hoped that the study would make significant contribution to understanding how NGOs strengthening internal controls measures, and the implements of this on their operations efficiency. The study would also be significant in that it would form a useful foundation against which future studies could be undertaken. The study findings would also contribute literature on the influence of internal control measures on operational efficiency in NGOs.

Therefore, this research will be very essential to the effectiveness of internal control by assessing the factors which determines the NGOs internal control effectiveness in measuring of

performance. In addition this research will be important for the empirical evidences for the NGOs offices to examine their policies and procedures, because the internal auditors have a significant impact to control any non-compliance activity in line with the established policies, plans, procedures, laws and regulations, set by the government which could have a significant impact on the organization's operations. The internal auditors are also essential to add or create value to the organizations, to avoid failure and to save the operating and administration costs in accordance with the organization's policies and procedures and for the future researchers also important to develop a conceptual literature development.

1.6. Limitations of the Study

The limitation faced during the study in past, related to unwillingness of respondents to sacrifice their time to give information. The researcher however reassured them that the research was confidential and for educational purpose only. The anticipated limitations were inadequate and capital to conduct the research. The researcher nonetheless dedicated much time for the study to be conducted.

1.7. Scope of the Study

The study was conducted for the four months from February – May 2016 on the effectiveness of internal control of non-governmental organizations. The study was conducted in International non-governmental organization those working in the health sector only of Addis Ababa. The main data collection instrument was the questionnaire. The target population was for the study was finance heads, internal control employees and project staff. Though it will important to include all these areas because of infeasibility from resource time perspectives, the focus of this study was only on the effectiveness of internal control on non-governmental organizations working in the health sector. The study used 30 NGOs of existing of all 120 international Non-governmental Organizations involved in the health sector.

The expected threat of the study was related to inherent limitations of internal control will focus on the determinants of internal audit effectiveness and operating performances would be more successful if it is conducted in all NGO offices, and also on all privately owned organizations.

But due to time and financial constraints it is out of the touch of the individual researcher, and due to this the NGOs offices which are cover under this research work are limited to our purposively selected NGO will be expected to show the effects of all the rest untouched offices.

1.8. Organization of the Study

In addition to the preliminary pages, this theses will consists of five chapters. The first chapter with its sub topics will be introductory; incorporating the introduction, statement of the problem, research objectives, research questions, research hypotheses, significant of conducting the study, scope of the study. The second chapter will provide detailed review of relevant literatures; especially those related to performance measurement and the internal control effectiveness and the variables which affect the internal control effectiveness. The third chapter will be expressing the information regarding the sampling techniques used to conduct the research thus the methodology used to collect data. The fourth chapter will be the analysis, discussions and presentation part of the research findings and finally, the last chapter will be the conclusions and recommendations of the study followed by the references and appendixes.

Chapter Two

2. Review of Literature

2.1. Performance Measurement and Management Practices in NGOs

In the literature on performance measurement among NGOs, the significance and advantages of utilizing performance measurement and management to different organizational management structures, techniques and processes have been broadly proved (Teelken, 2008).

Performance measurement and management in NGOs is extremely vital since it focus is on how organizations use performance information in their decision making processes. This implies that managing and assessing performance is a pre-requisite for strategic planners in NGOs to improve their functions. Moreover, it is closely associated with the budgetary system inside NGOs since these organizations are considered to be fundraising-oriented. A further reason of the necessity of performance measurement and management in NGOs is the need for transparency and accountability toward different stakeholders. This is due to the fact that there is a sort of pressure from stakeholders on NGOs to demonstrate how they perform their operations.

In NGOs literature, many authors offered a number of definitions of measuring performance.

For instance, Poister (2003) mentioned that performance measurement is a method of identifying, controlling and utilizing different objective measures of the organization's performance and its programs on regular basis. Furthermore, Lindblad (2006) considered performance measurement as the utilization of objectives, indicators and information to assess NGOs interventions and services. Ferreira and Otley (2009) treated it as a mechanism of assessing people, teams and the overall organization. Miller (2007) viewed performance measurement as a program assessment method that evaluates efficiency and effectiveness of a program and its impact. While Carman (2007) claimed that performance measurement is a systematic evaluation of a program's outputs, inputs and impacts. Still, there is still little consensus over how to define and measure performance in NGOs since many of them typically lack clear goals and uncertain relationship between programs' activities and outcomes (Newman and Wallender, 1978; Fottler, 1981; Kanter and Summers, 1987). Performance of NGOs has been defined by Yuchtman and Seashore (1967), Yuchtman and Seashore (1967) performance.

Kareithi and Lund (2012) argued that the primary mission of NGOs is focused on goals desired by their targeted beneficiaries and their communities, so the performance of these organizations should be assessed by their effectiveness and efficiency to achieve mutually identified social goals. One important part of NGOs performance measurement, that has been a concern for a long period, is to understand the appropriate indicators that should be taken into account when measuring and evaluating NGOs performance (Herman and Renz, 1999; Gill et al., 2005). The research on NGOs performance measurement examined two main issues: internal indicators and external indicators. According to Argyris (1964) and Bennis (1966), the internal indicators of measuring NGOs performance are related to "Organizational Health". These indicators concern the financial performance of NGOs including access to funding, budgeting efficiency, expenses and costs (Ritchie and Kolodinsky 2003; Gill et al., 2005). On the opposite, the external indicators address the link between the NGO and the environment. For instance, Yuchtman and Seashore (1967) proposed a system resource framework which defines NGOs performance as the capability to derive benefits from the surroundings toward the best acquisition of the financial needs and requirements for their survival. Their framework is based on the idea of NGOs ability to sustain a good connection with the environment (Keeley, 1978; Miles, 1980; Connolly et al., 1980; Boschken, 1994).

Ammons (1996) introduced two more indicators essential to performance productivity and workload; on the bases of Benjamin and Misra (2006) focused on measuring performance in NGOs inputs, outputs, outcomes and impact. While Fine and Snyder (1999) defined the relationship between inputs utilized and outputs achieved as efficiency, while effectiveness is considered as a measure used to determine up to what extent is an organization achieving its planned goals and targets. Other authors relied on the notion "outcomes" to refer to effectiveness. For instance, Morley et al. (2001) defined outcomes as a certain result or quality of an organization's program or project. Efficiency is the optimal use of financial and other non-financial resources (labor, time and expertise) to achieve the planned results. It is the extent to which a program has converted or is expected to convert its resources/inputs economically into results in order to achieve the maximum outputs. Usually the relationship between input measures and output measures produces efficiency. The inputs measures track mainly a program or project's inputs such as staff, time and funds, while the output measures are results generated

from the utilization of a program's inputs mainly related to the number of beneficiaries served and number of products provided in comparison with the planned objectives of that program. On the other hand, outcomes or effectiveness measures refer to those indicators that explain a qualitative difference in the lives of the beneficiaries targeted by an NGO or its intervention (Lindgren, 2001). In other words, it mainly examines the extent to which the stated objectives of a program have been met. (Zimmerman & Stevens, 2006). These measures include participation of the stakeholders and beneficiaries' satisfaction. Beneficiaries' satisfaction measures give another vital mean for assessing NGOs performance and may serve as one outcome or one indicator of effectiveness. Niven (2008) said that beneficiaries' satisfaction can be measured through access, timeliness, selection and availability. Finally, the impact performance addresses the extent of achieving the overall objective of a program (such as community building, sectors development, standard of living and changes in people life). The impact usually considers the long term consequences of achieving objectives and bigger socio-economic change. It tries to identify the whole influence of a program or intervention on communities or people outside the immediate targeted beneficiaries.

In general, NGOs can assess their performance by creating performance indicators and then gathering information related to these indicators. Carman (2007) saw that the most utilized performance beneficiaries' satisfaction. Teelken (2008) used four performance indicators to evaluate NGOs operations: efficiency, effectiveness, economy and efficacy. Similarly, Fine and Snyder (1999) stressed that performance measurement in NGOs includes identifying and assessing indicators which mainly address efficiency and effectiveness.

2.2. Review on Performance Measurement and Management Frameworks in NGOs

Many authors have developed performance measurement frameworks for the NGO sector in the recent years. In general, there are not many models and frameworks for assessing the performance of NGOs as much as the frameworks available for the private sector. Moreover, the reliance on the traditional financial-based indicators of performance, like return on assets, liabilities or profitability ratios cannot be applied to NGOs (Herman and Renz, 1997). The

literature review reveals a number of performance measurement frameworks in NGOs. For instance, Ritchie and Kolodinsky (2003) proposed a framework for assessing the financial performance of NGOs. The framework involves fundraising efficiency, public support, expenses and cost efficiency.

Similarly, Standards for Charity Accountability of the Better Business Bureau proposed a framework for measuring NGOs performance in which the performance measures include the financial aspect, effectiveness and governance. In their model, the financial aspect is not only represented by fundraising efficiency but involves also managing and producing clear and accurate financial statements and budgets. Another framework has been offered by AARP (American Association of Retired Persons) which is the biggest NGO membership institution for people who exceed the age of fifty in USA (Datar et al., 2007).

2.2.1. Definition of Internal Control

The large number of accounting scandals during the early part of the 21st century resulted in the Sarbanes-Oxley Act of 2002. Sections 302 and 404 of this Act require companies to maintain, assess, and disclose internal control over financial reporting. The disclosures of internal controls intended to provide financial statement users with an early warning about potential future problems that could result from deficiencies in internal controls (PCAOB, 2004)

Internal Control is a process affected by a college or university's governing board, administration, faculty, and staff designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

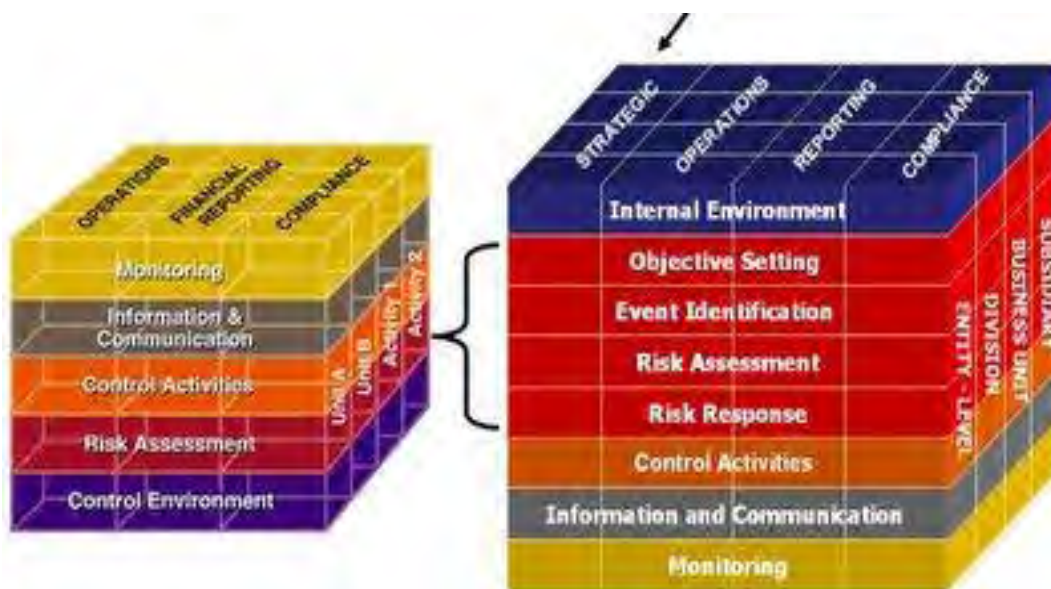
- Effectiveness and efficiency of operations.
- Reliability of financial reporting.
- Compliance with applicable laws and regulations.

This definition reflects certain fundamental concepts that internal control is a process and is a means to an end, not an end in itself. Internal control is affected by people. It's not merely policy manuals and forms, but people functioning at every level of the institution. Internal control is

geared to the achievement of objectives in several overlapping categories. Internal control can be expected to provide only reasonable assurance to an institution's leaders regarding achievement of operational, financial reporting, and compliance objectives. Administration involves planning, executing, and monitoring. Internal control is a tool used by administrators to accomplish these processes.

2.2.2. Components of Internal Control

Internal control consists of five interrelated components (derived from basic college and university operations and administrative processes) as follows: **Internal Control concepts – Brown university, <http://www.brown.edu>**



Source: Internal Control concepts – Brown University, <http://www.brown.edu>

- **Control Environment** - The core of any organization **institution** is its people. They are the engine that drives the organization. Their individual attributes (integrity, ethical values, and competence) and the environment in which they operate determine the success of the institution.
- **Risk Assessment** – Non-governmental organizations must be aware of and deal with the risks they face. They must set objectives that integrate key activities so the total

organization operates in concert. They also must establish mechanisms to identify, analyze, and manage the related risks.

- **Control Activities** - Control policies and procedures must be established and executed to help ensure that actions necessary to achieve the institution's objectives are effectively carried out.
- **Information and Communication** - Surrounding these activities are information and communication systems. These enable the organization's people to capture and exchange the information needed to conduct, manage, and control its operations.
- **Monitoring** - The entire process must be monitored and modified as necessary. Thus, the system can react dynamically to changing conditions.



Source: Internal Control concepts – Brown University, <http://www.brown.edu>

Effective I/C or ERM means that management has a "flow of reliable information" about each component of control for all the objectives, from all areas of the organization. And "Soft Controls" relate to the people performing the work to meet the objectives of the organization; "hard control" relates to the processes and activities those people do.

2.3. Theoretical Review

2.3.1 Internal Audit and Related Literature

A simple and more traditional meaning of internal auditing is defined as that of an independent appraisal function established within an organization to examine and evaluate its activities as a service to the organization. Later on, the new Institute of Internal Audit (IIA, 2001), defined internal audit as: An independent, objective assurance and consulting activity designed to add 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. According to this definition the major scope of the internal auditors are making assurance to the organization and giving consultant services to the overall managements of the corporate governance. By providing the independent opinion and conclusions regarding the operation, function, system and wellbeing of the organization the IA can provide assurance services; and by giving the advisory service based on the specified requests of an engagement client the internal auditor can give the consulting service to the organization. Internal audit are the mechanism through which information about the effectiveness of the quality system is gathered by auditors selected from within the company but, who are independence of the area, function or procedures being audited. Or the Internal Audit Function (IAF) is the mechanism through which the operation of the quality management system is formally monitored and in accordance with the documented quality system is assured (MoFED, 2004).

The Statement on Auditing Practice (SAP-6) of the Institute of Chartered Accountants of India describes internal audit as “the plan of organization and all the methods and procedures adopted by the management of an entity to assist in achieving management's objective of insuring, as far as possible, the orderly and efficient conduct of its business, including adherence to management policies, the safeguarding of assets, prevention and detection of fraud and error, the accuracy and completeness of accounting records and timely preparation of reliable financial information.

On the other hand, internal audit is a critical appraisal of the function of various operations of an enterprise involving system of internal check. Exceptions from normal functioning of internal

check system are exposed in internal audit. Accuracy, completeness, reliability and timeliness of accounting information are tested and reported for remedial action.

Non-accounting areas with the operational side of enterprise are critically studied, analyzed and weakness of the system or practice with inefficiency, wastage and frauds are brought to the notice of the management. Suggestions for increasing the effectiveness of the system, for improving the productivity and profitability of business practices are offered. Internal audit is the independent appraisal of activity within an organization for the review of accounting, financial and other business practices as a protective and constructive arm of management. It is a type of control which functions by measuring and evaluating the effectiveness of other types of control (B.N. Tandon 14 edition, p “112-115”).

2.3.2 Types of Audits Performed by Internal control staff

A variety of audits are performed in the review of programs and projects. These audits include: Operations Audits: These audits examine the use of resources to determine if resources are being used in the most effective and efficient manner to fulfill the organization’s mission and objectives. Financial Audits: These audits review accounting and financial transactions to determine if commitments, authorizations, and receipt and disbursement of funds are properly and accurately recorded and reported. This type of audit also determines if there are sufficient controls over cash and other assets and that adequate process controls exist over the acquisition and use of existing resources.

Compliance Audits: These audits determine if entities are complying with applicable laws, regulations, policies and procedures. Examples include federal and state laws, and Trustee policies and regulations. Information Systems Audits: These audits review the internal control environment of automated information processing systems and how people use these systems. The audits usually evaluate system input, output; processing controls; backup and recovery plans; system security; and computer facilities.

Internal Control Reviews: These audits focus on the components of the major business activities, such as payroll and benefits, cash handling, inventory and equipment, physical security, grants and contracts, and financial. The International Standards for the professional Practice of Internal Auditing Institute of Internal Auditors.

2.3.3 Internal Audit Effectiveness

Different authors were defined the term “effectiveness” as follows; for instance, Arena and Azzone (2009) defined effectiveness as “the capacity to obtain results that are consistent with targets”. While Dittenhofer (2001) “Effectiveness is the achievement of internal auditing goals and objectives using the factor measures provided for determining such factors”. In Mihret and Yismaw, (2007) internal audit effectiveness is defined as “the extent to which an internal audit office meets its supposed objective or the extent to which it meets the intended outcome”.

All the three authors defined effectiveness in terms of achieving the IA goals and objectives, though interpreted in different ways. Mihret and Yismaw (2007) described the characteristics of effective internal audit unit from the internal audit point of view. Effective Internal Audit (IA):

- Undertakes an independent evaluation of financial and operating systems and procedures;
- Contributes to the achievement of organizational goals;
- Needs management’s commitment to implement recommendations;
- Provides useful recommendations for improvements as necessary;
- Affected negatively by lack of attention from management which in turn adversely affects the auditee attributes; and
- Management support is a natural quid pro quo for effective internal audit.

While; Sarens and Beelde (2006) point out the contribution and roles of internal audit in organizations or corporate governance from the senior management’s expectation point of view.

Senior management expects internal audit:

- To compensate for management’s loss of control resulting from increased organizational complexity,
- To be the safeguard of corporate culture through personal contacts with people in the field,
- To be a supportive functions in the monitoring and improvement of the risk management and internal control system,

- To be laid a training ground for future managers, and
- To collaborate actively with the external auditors to increase total audit coverage.

This indicates that internal audit and management is the interdependent unit that should be collaborated to achieve organizational goals. While doing their activities, there is some value that internal audit unit seeks from management (such as management support, commitment, expectation, etc.) and that the management wants from the internal audit like adding value in decision making by providing sufficient information and reducing information asymmetry, monitoring and improvement of the risk management and internal control system.

2.4. Empirical Review

As the main aim of this research is to assess the effectiveness of internal audit in the public business sector enterprise, different authors and researcher's idea and recommendations regarding the related topic of internal audit are presented. Although internal auditing in Ethiopia dated back to 1940s the same time the United States and most European countries; the effectiveness of internal audit in the public sector are challenged because of the factors that hinder the development of IA in Ethiopia. For ease of presenting the literature the main determinants/factors/ that influence the effectiveness of internal audit in the public business enterprise sector; such as the perceptions of the management, management support, organizational independence of internal auditors, adequate competent of IA staff and the presence of IA charter reviewed from different researchers are included in these literature.

2.4.1. Management Support

Internal auditors have a close relationship with organization's management in their day to day activities. They need good support and perception from their management to be more effective and to achieve the audit objectives. Management support is expressed in terms of supporting the auditing process by fulfilling the necessary resources, finance, transport if required, providing training, introducing auditors with new technology and procedures, budgeting funds for certification and other facilities that facilitate the internal auditing works.

Management support has a far-reaching consequence on IA effectiveness in organizations. For

example, Mihret and Yismaw (2007) in their case study of IA effectiveness on public sector shows that the component of management support consists of the response to audit finding and the commitment to strength internal audit which has significance influence on IA effectiveness.

Given the fact that internal audit activities are performed in dynamic management process and more supportive environment, internal auditor expects senior management to take the first steps to support the IA process. Because, Sarens and Beelde (2006) argue that the overall acceptance and appreciation of IA within the company is strongly dependent upon the support they receive from senior management. Internal audit actively seeks management support with resources, commitment to promote and communicate their added value.

The management support is very crucial to the operations and internal auditing; because all other determinants of IA effectiveness derive from the support of top management, given that hiring proficient IA staff, developing career channels for IA staff, and providing organizational

Independence for IA work is the results of decisions made by top management (Cohen & Sayag, 2010). This means it is the interest of management to maintain a strong internal audit department (Adams, 1994; Mihret and Yismaw, 2007).

In addition implementation of audit recommendations is highly relevant to IA effectiveness (Sarens and Beelde, 2006; van Gansberghe, 2005) which is the component of management support (Mihret and Yismaw, 2007). The management of an organization is viewed as the customer receiving IA services. As a result, management's commitment to use audit recommendations and its support in strengthening internal audit is vital to IA effectiveness.

Therefore, audit finding and recommendations would not serve much purposely unless management is committed to implement them. Furthermore, Belay, (2007) find that to curb corruption and inefficiency in the public sector of Ethiopia, it is mandatory to have effective internal audit function (IAF) that in turn needs appropriate governance structure, mobilizing sufficient and appropriate resource and competent personnel.

2.4.2. Management's Perception of IA's Value

Perception is the process of attaining awareness or understanding of sensory information or it is the mental image or intuitive recognition of experience when aware of the elements of the

environment (Woodard III, 2002). To function effectively, internal auditors and the customers of audit services should possess a similar understanding of what makes internal auditing a value added activity. The failure to reach this understanding could result in the perception that internal audit is simply an obstacle to achieving production objectives. This can result in underutilized audit services and ignored audit recommendations (Flesher and Zanzig, 2000) which adversely influence the effectiveness of IA (Arena and Azzone, 2009).

When employees at all levels perceive that the top management assigns importance to the function of IA, they will cooperate and support these processes (Cohen & Sayag, 2010). This implies that internal audit staffs are more motivated and encouraged to perform audit activities given good management's awareness of IA values. Sarens and Beelde (2006) used a case study approach of five Belgian firms to explore the expectations and perception of both senior management and internal auditors with respect to the relationship between these two parties. They find that, when internal audit operates primarily in a management support role, there is a lack of perceived objectivity and the relationship the audit committee is weak. However, senior management's expectations significantly influence internal audit and that the perception of senior management is critical to the acceptance and appreciation, to promote value added and to the maturity of internal audit function with the organization.

2.4.3. Organizational Independence

Independence has no single meaning and interpretation; hence the concept is subject to ambiguity and uncertainty (Wines, 2012). However, for the purpose of the study, independence refers to the state of being free from any management influence while internal auditors perform audit activities and issue audit report (Ahmad & Taylor, 2009; Belay, 2007; MoFED, 2004). Independence is fundamental to the reliability of auditor's reports. Those reports would not be credible, and investors and creditors would have little confidence in them, if auditors were not independent both in fact and appearance. The assurance services provided by auditors derive their value and credibility from the fundamental assumptions of independence of mind and independence in appearance (Wines, 2012; Stewart and Subramanian, 2010).

While the internal audit typically the whole management process, to maintain objectivity, to increase the reliability of information, to be free from unacceptable risk of material bias, and to

issue reasonable and credible audit opinion, it is required to be independent (IIA,2001). However, due to an often strong direct or indirect relationship between IA and the Chief Executive Officer (CEO) and/or chief Finance Officer (CFO), it is reasonable to expect that senior management is in a position to exert a significance influence over IA (Sarens and Beelde, 2006; Van Peurseem, 2005).

Independence in fact exists when auditors are actually able to act with objectivity, integrity, impartiality and free from any conflict of interest. While the concept of independence in appearance is the auditor should be perceived by others (the public or other third party) to be independent. In this case, conflict of interest will also exist when a reasonable person, with full knowledge of all relevant facts and circumstances, would conclude that the auditor, or a professional member of the audit team, is not capable of exercising objective and impartial judgment in relation to the conduct of the audit of the audited body.

Auditors should be sufficiently independent from those they are required to audit in order to conduct their work without interference. Coupled with objectivity, organizational independence contributes to the accuracy of the auditor's work and gives employers confidence that they can rely on the results and the reports (Cohen & Sayag, 2010). However, Hellman N. (2011) suggested that CFOs seek to influence audit planning, particularly with regard to internal controls and the selection and scope of entities subject to audit; and this in return impairs the independence of internal auditors.

In order to maintain their independence internal auditor's organizational status and position is also critical which is related to management perception. This is because it enables them to exercise their tasks independently and act objectively. As Stewart and Subramanian (2010) review under organizational status the IAF should be given the appropriate status in the organization to enable the function to exercise organizational independence and individual internal auditors to act objectively since internal auditors found in a unique position as employees of an organization with responsibility to asses and monitor decisions made by management and also to the management. Furthermore, many auditors have been argued that in order to achieve audit objectives and become effective organizational independence is very important. For instance, the independence of internal audit department and the level of authority

to which the internal audit staff report are the important criteria influencing the objectivity of its work, and added that organizational independence is more crucial to the effectiveness of the internal auditors, as it protects the auditor from pressure or intimidation, and increases the objectivity of the auditing work (Cohen & Sayag, 2010; Van Peurse, 2005; Boa-Read, 2000).

2.4.4. Conceptual framework

The current study was guided by the following conceptual framework, which was used to explain the interrelationship between the variables. A conceptual framework is a scheme of variables a researcher operationalizes in order to achieve the set objectives (Oso & Onen 2002).

Independent variable

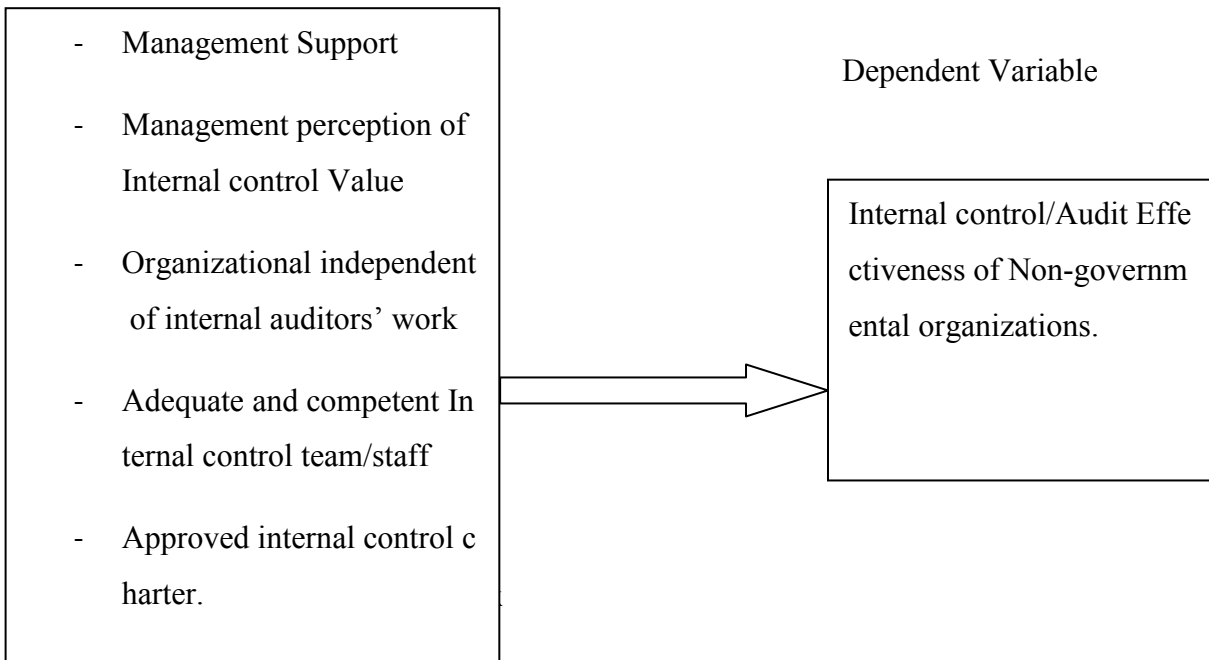


Figure 1: Conceptual Framework

Source: Research Data (2016)

The conceptual framework shows the correlation between internal control measures and the operational efficiency of non-governmental organization (NGO's). Internal controls are simply processes, policies and procedures, effected by people that ensure our internal proceses, designed to

modify risk, work the way we want them to so that we achieve what we want. An organization will have hundreds if not thousands of internal controls in place.

The operational efficiency of an organization is dependent on internal control measures employed by an organization. Internal controls of the organization are dependent on industry analysis, organizational management and firm effects in the form of resources and the strategies developed. From an environmental management perspective, internal control measures are important predictors to the organization's operational efficiency.

The quality of internal control is directly related to the quality of the personnel operating system that affects the operational efficiency of an organization. The entity should have sound personnel policies for hiring, orienting, training, evaluating, counseling, promoting, compensating and taking remedial action. For example, in hiring a standard should be sought only to hire the most qualified person, with prior working experience and evidence of integrity and ethical behaviour.

2.4.5. Gap in Literature

According to the studies of internal control measures and operational efficiency, (Long, 2007) it is clear that most NGO's have integrated internal control measures in every unit of the organization to ensure that operational efficiency is achieved at every unit. Such units include administration where it involves approval by the supervisor of employee's attendance entries. The purpose of this control mechanism is to ensure adherence to time and attendance procedures. However, this study, will examine whether effective internal control measures has implications beyond that of firm operational efficiency. In addition, inadequate physical security, inadequate segregation of duties and inadequate documentation further allow the misappropriation of inputs by employees. Furthermore, ineffective internal control measures may result in erroneous internal management reports, and managers relying on such reports are more likely to make suboptimal operational decisions. Finally, ineffective internal control measures relating to information technology not only further results in erroneous internal reports, but also reduce NGOs' effectiveness in monitoring the usage of resources and leads to inefficient use and wastage of resources. This then is the knowledge gap that the study seeks to reveal by carrying out an assessment of the internal control measures employed by NGOs in enhancing operational efficiency.

Chapter Three

3. Research Methodology

3.1. Introduction

The Chapter describes the research design as well as the methods that were used to sample the population and the target population to bringing out the sample size. The chapter further looked at methods of data collection, research instruments, their validity and reliability, operational definition of variables and methods of data analysis.

3.2. Research Design and Methodology

An important part of the research activity was to develop an effective research design which shows the logical link between the data collected, the analysis and conclusions to be drawn. This design used to satisfy the most suitable methods of investigation, the nature of the research instruments, the sampling plan and the types of data (De Wet, 1997).

Research design refers to the way a study was planned and conducted. It entails choosing the subjects who participate in the study. The techniques and approaches for collecting data for the subject and procedures (Kumssa, 2011). The main objective of a research design is to enhance the validity (degree to which the results obtained from the analysis of the data actually represent the phenomenon under study) Mugenda and Mugenda (2003).

While carrying out the study, the researcher adopted a descriptive and inferential statistics for the research design. This design investigates the current status and nature of the phenomena. Orodho (2003) defines descriptive as a method of collecting information by interviewing or administering a questionnaire to a sample of individuals. Descriptive research, describes data and characterist

ics about the population or phenomenon designed studied. According to Coopers and Schindler (2004) descriptive studies were more formalized and typically structured with clearly stated hypothesis or investigative questions. The descriptive analysis approach was chosen for the study, because it seeks to gain insight into a phenomenon as a means of providing basic information in the area of study (Koul, 1993). The descriptive research design was adopted in the study based on the conceptual relationship between the independent variable and the dependent variable.

3.3. Target Population

The target population refers to the group of people or study subjects who are similar in one or more ways and which forms the subject of the study in a particular survey (Orodho, 2003). The target population of the study was internal control/audit staff working in the International NGOs in the health sector in Addis Ababa as per the source of Federal Charities and Societies Agency (ChSA).

Table 3.1 Target Population

Category	Target Population
Internal controllers/Auditors	116

Source: 30 NGOs Human Resources Department March/April (2016)

3.4. Population, Sample Size and Sampling Techniques

The minimum sample size depends on the type of research involved. Some cite a sample size of 30 as a guideline for correlational, causal-comparative, and experimental research. Thus, for correlational studies at least 30 participants are needed to establish the existence or nonexistence of a relationship. For causal-comparative and true experimental studies, a minimum of 30 participants

in each group is recommended, although in some cases it might be difficult to attain this number for each group.

I used cluster multi stage sampling where the samples is carried out in stages. Dividing the population into groups (clusters), then one or more clusters are chosen at random and appropriate as explained below targeted for sampling.

First stage sampling was applied to study Sample Size refers to the number of observations or replicates to include in a statistical sample. The total number found was 120 non - governmental organization involved in the health sector (ChSA) and the sample size of 30 was based on Gay, L. R. and P. Airasian (2003 p“112”) and those 30 INGOs' selected by the use of a random number generator from <http://www.psychicscience.org>. and the researcher first list all 120 INGOs those are working in the health sector in Addis Ababa, based on the random numbers generated the researcher select those 30 international NGOs'. After that the researcher request HR departments of those NGOs' to list of employees of thier internal Audit departments. Then, from all of those 30 NGOs' the researcher found a total number of 116 internal control/ Audit department employees. Therefore by using a sample size calculator in <http://www.raosoft.com/samplesize.html> by considering the the margin of error 5% and the level of distribution 50% therefore I have reached a sample size of 90. By the time I conducted the research 86 of them respondes which is about 74% of the 116 in total found in selected NGOs.

The selected NGO offices were as follows:

Action Contre la Faim, Save the Children international, Child Fund ETHIOPIA, World Vision, Path Finder International, DKT Ethiopia, Family health international, Care Ethiopia, Marie Stopes Internaional, Population Service International, Mercy Corps, A Glimmer of hope foundation, I-T

ECH Ethiopia, Medecens Sans Frontiers Spain, Goal Ethiopia, Johns Hopkins university centre for communication programs, Christian Children's Fund of Canada, International Medical Corps, Endegeer Heath Inc, Merlin Medical Emergency Relief International, IPAS Ethiopia, CAFOD, Norwegian Church Aid, CRS, IRC, GIZ, SNV NETHERLANDS, GERMAN AGRO ACTION, TROCAIRE, MEDICOS DEL MUNDO ESPANA.

3.5. Data Collection Instrument

The primary data were used to accomplish the study, and to collect the data from the respondents included in the sample questionnaires were distributed. The questionnaires were distributed to the internal auditors/controls of the those selected non governmental offices. The questionnaire deals about the effectiveness of independence of internal auditors.

The questionnaires were adopted and modified from the prior author and literature review (Mihret and Yismaw, 2007; Cohen & Sayag, 2010; Arena and Azzone, 2009), an approach which is recommended in methodological literature for studies of this nature (Bryman and Bell, 2007) and these questionnaires are prepared in the form of Likert-Scale type (showing respondents agreement or disagreement) by constructing into five point scale where the lowest scale represent strongly disagree and the highest scale represent strongly agree (Likert, 1932). The questionnaires distributed to the respondent are organized in to two parts; the first part comprises the demographic questions regarding the respondents, and the second part contains items relating to the effectiveness of IC and its determinants.

3.6. Variables used in the Research

3.6.1. Dependent Variable

The dependent variable for this research was internal audit effectiveness. In here the internal control effectiveness was measured in terms of internal auditors' ability to identify non-compliance activities with the offices procedures and policies, and the contributions added by IA to the public offices.

Compliance audit is a type of audit service that mostly performed by internal auditors of the organization (Fadzil, F.H et al, 2005). Compliance is defined as 'adhering to the requirements of laws, industry and organizational standards and codes, principles of good governance and accepted community and ethical standards'. Compliance also involves ascertaining the extent of compliance with established policies, plans, procedures, laws and regulations, which could have a significant impact on the organization's operations (Fadzil, F.H et al, 2005; MoFED, 2004).

Therefore, IC is responsible to regularly assess and verify internal operations conformance with organization's policies and procedures, and then issue compliance report to the concerned body (MoFED, 2004).

The added contribution by IC to organizations can be measure in terms of value creation (e.g. its role in the avoidance of corporate failures) and cost saving (Soh and Bennie, 2011; Cohen & Sayag, 2010). Through cost saving of funds will create implementing more works than normally used to implement.

In this study the researcher measured the IC effectiveness by implementing the internal audit effectiveness of the Non-governmental offices with the country's auditing environment in which the

internal auditor's ability in identifying non-compliance activities and the added contribution by the IA to the NGOs offices. Compliance audit is the most audit services implemented in Ethiopian public bodies (Mihret and Woldeyohanes, 2008; MoFED, 2004) while the added contributions by the IA to organization was used by Cohen and Sayag (2010) to measure the IA effectiveness.

Therefore, both dimensions will be measured IA effectiveness against the perception of NGOs offices managers (CEO and CFO). To understand the level of the manager's perception of IA effectiveness a 5-scale point Likert-type of 15 different item questionnaires will be constructed and distributed to the respondents. The researcher will be used the summative score technique for the questions in each factor for each participant. This is because Likert scale is the common summative scores (Balnaves and Caputi, 2001).

3.6.2. Independent Variable

This study will be focused on five independent variables that might have an impact on the internal control effectiveness in the NGOs offices. Those predicted variables investigated in this research will be: the managements support for the IA activity, the management's perception of IA's value, organizational independence of the IA work, the adequate and competent internal audit staff and the presence of approved internal audit charter. It should be noted that the data for the independent variables were collected from the internal auditors/controls of the selected Non-governmental offices. Therefore, the independent variables will be representing the perceptions of the internal auditors about these concepts.

Similarly with the dependent variable items, all of the independent variables items will be measured on a five point Likert-scale where the lowest scale represent strongly disagree and the highest scale represent strongly agree (Likert, 1932).

3.7. Data Analysis Method

Data analyses was conducted through a descriptive and inferential statistics to provide details regarding the demographic question and the various factors that affect the effectiveness of IC in the NGOs. To evaluate the effects of various factors on the effectiveness internal auditors in the NGOs offices the correlation analysis were used. And also, the Statistical Package for Social Sciences (SPSS) version 20 was used for the data analysis. In order to assess the reliability and consistency of the instrument the Cronbach's Alpha (α) analysis was conducted. Whereas, to determine the relationship among the variables and to test the research hypothesis correlation and regression analysis method was used by meeting the ordinary least square (OLS) assumptions of the linear regression.

3.8. Model Specification

The following model was formulated for this research in order to test the research hypothesis set earlier. Most of the independent variables included in the model are extensively used in prior audit researchers (Mihret and Yismaw, 2007; Cohen & Sayag, 2010; Arena and Azzone) except the management perception of IA's value and the adopted internal audit charter. So the reliability and validity of the model was being recognized and used in this research is to analyze and interpret the result of the study.

$$IAE = a + \sigma_1 MS + \sigma_2 MP + \sigma_3 OIN + \sigma_4 ACIAS + \sigma_5 AIAC + e_i$$

Where:

IAE: the effectiveness of internal auditors' in identifying non-compliance activities and the added contributions of IA to the NGO offices,

MS : The Managements Support,

MP : The management's perception of IA's value,

OIN: The organizational independence,

ACIAS: The adequate and competent internal audit staff,

AIAC: The existence of approved internal audit charter.

$\tilde{\alpha}$ is a constant, represents the effectiveness of IA when every independent variables are zero.

α_1 is the coefficient, in which every marginal change in variables on internal auditor's

Effectiveness affects correspondingly.

e_i = the error term

Chapter Four: Data Analysis, Results and Discussion

4.1. Introduction

This chapter presents the data analysis, the research findings (results), and based on the results the researcher gives discussion on the findings and also gives some interpretation of the result. In order to presents findings and the discussion about the relationship between internal control and operational performance in the studied NGOs' in Addis Ababa; the researcher uses different form of tables and figures and qualitative analysis done in prose.

4.2. Response rate

A total of 90 questionnaires were administered to employees of 30 international NGO's currently operating in health sector in Addis Ababa, out of which 86 were completely filled and returned. The remaining 4 questionnaires were not collected due to refusal to give response for the questionnaires. This gave a response rate of 95.56% According to Mugenda the statistically significant response rate for analysis should be at least 50%. (Mugenda, 2003)

Table 4.1: Response Rate

	No of Questionnaire	Percent
Completed	86	95.56%
Not Completed	4	4.44%
Total	90	100%
Source: Research data (2016)		

4.3. General Information about respondents in the study

4.3.1. Gender and Age Bracket of Respondents

From Table 4.2, we can see that from the total 86 respondents 62.80 % or 54 of them are Males the remaining 37.20% or 32 of respondents were Females. This indicates the majority of internal auditors in those international NGO's who are working in the health sector are Males. When we see the age distribution of this research respondents from a total 86 respondents at those selected international NGO's 3 of them or 3.5% were found at the age bracket 20-29years, 57 or 66.3% were in the age bracket 30-39 years, 20.19% or 18 of them are found in the age bracket 40-49 Years and the remaining 8 respondent or 9.3% of the respondent were found at the age bracket 50-59 years. This indicates most of employees are found in the age group 30-39 i.e. they are matured. Therefore the researcher believes they were well versed with relevant information for this study.

Table 4.2: Gender and Age Group of Respondents

		Frequency	Percent	Valid Percent	Cumulative Percent
Gender	Male	54	62.8	62.8	62.8
	Female	32	37.2	37.2	100.0
	Total	86	100.0	100.0	
Age Group	20 - 29 Years	3	3.5	3.5	3.5
	30 - 39 Years	57	66.3	66.3	69.8
	40 - 49 Years	18	20.9	20.9	90.7
	50 - 59 Years	8	9.3	9.3	100.0
	Total	86	100.0	100.0	

4.3.2. Respondents of Educational Level and Fields of Study

From Table 4.3 the educational Level of respondents in total 77% or from a total of 86 respondents 66 of them have 1st degree, 21% that is from a total of 86 respondents 18 of them have 2nd degree or master's degree and the remaining 2 respondent which is 2% from the total respondents have Diploma. This indicates most of internal audit department staffs in those

selected NGO's are middle level professionals, this suggests our respondents give relevant and accurate information needed for the study. When we see the respondents' field of study the majority of them study accounting i.e. 58 or 68% of our respondents' education background is accounting; next 26 or 30% of respondents have Management qualification and the remaining 2 respondents' field of study is economics. Therefore those respondents educational background is very related to their position in those selected NGO's and the researcher believes those respondents give relevant information for the study.

Table 4.3: Field of Study and Level of Education

	<i>Level of education</i>						Total	
	<i>Diploma</i>		<i>Bachelor's Degree</i>		<i>Master's Degree</i>			
<i>Your field of study</i>	No.	%	No.	%	No.	%	No.	%
Accounting	0	0%	46	70%	12	67%	58	68%
Management	2	100%	18	27%	6	33%	26	30%
Economics	0	0%	2	3%	0	0%	2	2%
Total in No.	2	100%	66	100%	18	100%	86	100%
Total in %	2%		77%		21%		100%	

4.3.3. Reliability of Research Instruments

Reliability refers to the measure of the degree to which a research instrument yields consistent results on across time and across the various items of the instrument (Sekaran, 2003). It is the extent to which an instrument is predictable, stable, accurate and dependable to yield the same results every time it is administered. The measures of independent variable had Cronbach's alpha coefficient of 0.891 (Table 4.5) while those of the dependent variable had Cronbach's alpha coefficient of 0.892 (Table 4.4). The study measures were found to be highly reliable in that they all had alpha coefficient greater than the minimum accepted Cronbach's alpha coefficient of 0.70 (Santos, 1999).

Table 4.4: reliability statistics for the dependent variable

Reliability Statistics

Cronbach's Alpha	N of Items
.892	15

Table 4.5: Reliability Statistics for independent Variable

Reliability Statistics

Cronbach's Alpha	N of Items
.891	30

4.3.4. Professional Certifications of Respondents

From table 4.6 we can see that from a total of 86 respondents we have only 17 or 20% of respondents with a professional certification i.e. the majority of our respondents are not professionally certified (69 or 80% of respondents). Among 17 certified professionals 12 or 71% of them have a professional certification called Certified Internal Auditor (CIA), 3 or 18% of those professionally certified respondents have a certification from Association of Chartered Certified Accountant (ACCA) and the remaining 2 or 12% of respondents are Certified Public Accountant (CPA). This indicates the majority of internal auditors in those international NGOs' do not have a professional certification.

Table 4.6: Professional certification					
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Certified Internal Auditor (CIA)	12	14%	71%	71%
	Certified Public Accountant (CPA)	2	2%	12%	82%
	Association of Chartered Certified Accountant (ACCA)	3	3%	18%	100%
	Total	17	20%	100%	
Missing	System	69	80%		
	Total	86	100%		

4.3.5. Respondents Number of years of experience as Internal Auditor

From table 4.7; we can see that the majority of our respondents i.e. from a total of 86 respondents 46 or 53% of them have 4 to 6 years work experience as internal auditor, next we have 34 or 40% of our respondents have a work experience 1 to 3 years and the remaining 7% or 6 respondents have more than 6 years' work experience as internal auditor. This indicates the research respondents are experienced and the researcher believes they gave the correct and accurate information the researcher needed for the study.

Table 4.7: Respondents years of experience as an internal auditor					
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	1 to 3 years	34	40%	40%	40%
	4 to 6 years	46	53%	53%	93%
	Above 6 years	6	7%	7%	100%
	Total	86	100%	100%	

4.3.6. Availability of Audit committee

For the question “Does your organization have audit committee?” from table 4.8, we can see that 68 or 79% of respondents answer quire “Yes” this indicates the majority of those international NGO’s who are currently working in the health sector has audit committee.

Table 4.8: Availability of Audit committee

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Yes	68	79%	79%	79%
	No	18	21%	21%	100%
	Total	86	100%	100%	

4.3.7. Activities carried out by Internal Auditors

Here respondents are asked to give answer for “What are the activities carried out by IA in your office/sector? You can select more than one.” And the researcher gives the following choices for the respondents.

1. Compliance audit
2. Financial audit
3. Operational/performance audit
4. Internal control system evaluation
5. Risk assessment (analysis) audit

From table 4.9; we can see that from a total of 86 respondents the majority of respondents say all of the above activities were carried-out by the internal audit department i.e. 60 or 70% of the respondents say they do all activities mentioned above. 10 or 12% of respondents say except Operational/performance audit they do all of the mentioned activities, 7 or 8% of respondents says except compliance audit they do all of the above activities and the remaining 6 respondents say there internal audit department work only compliance audit and financial audit. This implies the majority of those internal audit departments in those selected international NGO’s who are

working in the health sector carry out all of those activities i.e. Compliance audit, financial audit, Operational/performance audit, internal control system evaluation and Risk assessment (analysis) audit.

Table 4.9: Activities carried out by Internal Auditor

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 1 &2	6	7%	7%	7%
1,2 &4	3	3%	3%	10%
All	60	70%	70%	80%
Except 3	10	12%	12%	92%
Except 1	7	8%	8%	100%
Total	86	100%	100%	

4.3.8. Current position of respondents in their office

From table 4.10, the majority of respondents are junior auditors i.e. 50 or 58.1% of respondents, 32 or 37.2% of respondents are senior auditors and the remaining 4 respondents are Audit managers. This indicates all respondents are auditors in different levels and the researcher believes the data is collected from the right persons and the information we get from those professionals are relevant.

Table 4.10: Current position in your office

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Junior Auditor	50	58.1	58.1	58.1
Senior Auditor	32	37.2	37.2	95.3
Audit Manager	4	4.7	4.7	100.0
Total	86	100.0	100.0	

4.4. Regression Analysis

The researcher carried out a regression analysis to show the association between the independent variables with the dependent variable i.e. how the dependent variable “the effectiveness of internal control in identifying non-compliance activities and the added contributions of IC to the NGO offices” affected by those five independent variables i.e. The management support, The management’s perception of IA’s value, the organizational independence, the adequate and competent internal audit staff and the existence of approved internal audit charter managements. From the below table 4.11 we can see that there is significant association between the dependent variable and the independent variable the organization independence since the p-value for this independent variable in the below table is less than 0.05. And those other independent variables have insignificant relationship with the dependent variable. And the resulting regression equation is as follows;

$$\text{ICE} = -0.457 - 0.297\text{MS} - 0.90\text{MP} + 1.006\text{OIN} + 0.213\text{ACIAS} + 0.175\text{AIAC} + e_i$$

Where:

- ICE: The effectiveness of internal control in identifying non-compliance activities and the added contributions of IC to the NGO offices,
- MS : The Managements Support,
- MP : The managements perception of IA’s value,
- OIN: The organizational Independence,
- ACIAS: The adequate and competent internal audit staff,
- AIAC: The existence of approved internal audit charter.
- α is a constant, represents the effectiveness of IA when every independent variables are zero.
- $e = \beta_1 - 5$ is the coefficient, in which every marginal change in variables on internal auditor’s effectiveness affects correspondingly.

Coefficients^a

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	-.457	.310		-1.472	.145
The Managements Support	-.297	.158	-.193	-1.878	.064
The management's perception of IA's value	-.090	.137	-.092	-.659	.512
The organizational independence	1.006	.124	.955	8.105	.000
The adequate and competent internal audit staff	.213	.183	.133	1.159	.250
The existence of approved internal audit charter	.175	.113	.127	1.550	.125

a. Dependent Variable: the effectiveness of internal control in identifying non-compliance activities and the added contributions of IC to the

Table 4.11 Regression coefficient

From the above model and the table 4.11; we can see that the regression equation above show as by taking all factors into account constant at zero, the dependent variable (the effectiveness of internal control in identifying non-compliance activities and the added contributions of IC to the NGO offices) will have value -0.457. And this finding also show by taking all other independent variables at zero a unit increase in the value of the dependent variable Management Support (MS) will decrease the dependent value by 0.297 since this variable has a –ve coefficient i.e. the dependent and the independent variable has a –ve association; here the same is true for the independent variable called The management’s perception of IA’s value (MP) here the dependent variable will decreased by 0.090. For the remaining three independent variables a unit increase for each of that variable will have a positive or an increase effect by considering the reaming variables with zero value. Since all of those variables have positive associations with the dependent variable ICE.

4.5. Model Summary for Dependent Variable ICE

From table 4.12 below; R-Square which is the coefficient of determination is a commonly used statistic to evaluate model fitness. The adjusted R^2 , is also called the coefficient of multiple determination, is the percentage of the variation in the dependent variable explained uniquely or jointly by the independent variables. Here 87.3% of the variations in ICE in those selected NGO's which are found in the health sector in Ethiopia can be attributed to the combined effect of the five predictor variables. This means that 12.7% of the changes in the Dependent variables can be attributed to other factors.

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.938 ^a	.880	.873	.24051

a. Predictors: (Constant), The existence of approved internal audit charter, The Managements Support, The organizational independence, The adequate and competent internal audit staff, The management's perception of IA's value

Table 4.12: Model Summary of the Dependent variable ICE

ANOVA^a

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	34.043	5	6.809	117.707	.000 ^b
	Residual	4.628	80	.058		
	Total	38.671	85			

a. Dependent Variable: the effectiveness of internal control in identifying non-compliance activities and the added contributions of IC to the

b. Predictors: (Constant), The existence of approved internal audit charter, The Managements Support, The organizational independence, The adequate and competent internal audit staff, The management's perception of IA's value

Table 4.13: ANOVA Result for ICE

Table 4.13; show the P-value of 0.000 indicates that the regression relationship is significant in predicting how the five independent variables ICE: the effectiveness of internal control in identifying non-compliance activities and the added contributions of IC to the NGO offices, MS :

The Managements Support, MP : The management’s perception of IA’s value, OIN: the organizational independence, ACIAS: The adequate and competent internal audit staff, and AIAC: the existence of approved internal audit charter influence the effectiveness of internal control in identifying non-compliance activities and the added contributions of IC to the NGO offices (ICE) in those NGOs who are currently working in health sector in Ethiopia. The F critical at 5% level of significance is 2.33. Since F calculated is 117.71 is greater than the F critical (value = 2.33) thus showing that the model is significant.

4.6. Internal control effectiveness in the studied INGOs in Addis Ababa

Chi-Square Tests

	Value	Df	Asymp. Sig. (2-sided)
Pearson Chi-Square	272.619 ^a	248	.136
Likelihood Ratio	183.084	248	.999
Linear-by-Linear Association	.553	1	.457
N of Valid Cases	86		

a. 288 cells (100.0%) have expected count less than 5. The minimum expected count is .03.

Table 4.14: Chi Square Test for the relationship b/n internal control and operating performance

From the top row of the above table, Pearson Chi-Square statistic, $\chi^2 = 272.62$, and $p > 0.001$; i.e. Here there is very small probability (insignificant relationship) between the internal control and operating performance. Since the p-value is above 0.05.

Chapter Five: Summary, Conclusion and Recommendations

5.1. Introduction

This chapter gives the summary of the findings, conclusion as well us recommendations. As stated in chapter one of this research paper the overall aim of this study was to examine

effectiveness of internal control on operating performances in the selected NGOs offices in Addis Ababa. To explore the relationship between the dependent and the independent variables and specifically to give answer for the following research questions:

- To what extent does management support contribute to the internal control in the NGOs offices?
- To what extent is the organizational independence of internal auditors for internal audit function in the NGOs offices?
- To what extent the management perception contribute to the internal control effectiveness in the NGOs offices?
- To what extent having audit charter will contribute to the internal control effectiveness?

5.2. Summary of the Findings

- ✓ Gender distribution employees in those selected NGOs' are not balanced since from the total sample collected 62.80% are males which is almost double the number of female respondents i.e. 32 in number and 37.20%.
- ✓ 69.8% of respondents were found in the age bracket 30 to 39 years, next to this we have found 20.9% of our respondents in the age bracket 40 to 49 and in the remaining age brackets we are found less than 10% of our respondents this indicates most of our respondents are matured.
- ✓ In the educational Level our respondents have 1st Degree (77%), 2nd Degree (21%) and the remaining 2% of our respondents have Diploma. This indicates most of internal audit department staffs in those selected NGO's are middle level professionals, this suggests our respondents give relevant and accurate information needed for the study.
- ✓ When we see the respondent's field of study the majority of them study accounting i.e. 58 or 68% of our respondent's education background is accounting; next 26 or 30% of respondents have Management qualification and the remaining 2 respondent's field of study is economics. Therefore , those respondents educational background is very related

to their position in those selected NGO's and the researcher believes those respondents give relevant information for the study.

- ✓ From a total of 86 respondents we have only 17 or 20% of respondents with a professional certification i.e. the majority of our respondents are not professionally certified (69 or 80% of respondents). This indicates the majority of internal auditors in those international NGO's do not have a professional certification.
- ✓ The majority of respondents are junior auditors i.e. 50 or 58.1% of respondents, 32 or 37.2% of respondents are senior auditors and the remaining 4 respondents are Audit managers. This indicates all respondents are auditors in different level and the researcher believes the data is collected from the right persons and the information we get from those professionals are relevant
- ✓ From the regression equation in chapter four Management Support (MS) and the management's perception of IA's value (MP) have a –ve association with the dependent variable ICE since both of those variables have a –ve coefficient and for the remaining three independent variables a unit increase for each of that variable will have a positive or an increase effect by considering the remaining variables with zero value. Since all of those variables have positive associations with the dependent variable ICE.
- ✓ The model summary for the dependent variable ICE indicates 87.3% of the variations in ICE in those selected NGO are which are found in the health sector in Addis Ababa can be attributed to the combined effect of the five predictor variables. This means that 12.7% of the changes in the dependent variable can be attributed to other factors.
- ✓ Pearson Chi-Square statistic, $\chi^2 = 272.62$, and $p > 0.001$ shown in chapter for analyzing the relationship between internal control and operating performance indicates there is no significant relationship between the internal control and operating performance. Since the p-value is above 0.05.

5.3. Conclusion

From Chapter four and the summary in the previous section we can conclude that a management support has insignificant negative association with the internal control in NGOs' in Addis Ababa i.e. Since the beta coefficient for the regression equation is negative here the same is true for the

management's perception of IA's value but the other two variables have insignificant positive association i.e. The adequate and competent internal audit staff and the existence of approved internal audit charter but the organizational independence has significant positive association with the internal control. Finally internal control effectiveness is insignificant on those stated factors in the studied INGOs working particularly in the health sector.

5.4. Recommendations for future research

Some recommendations are provided to solve the limitations encountered in this research and improve the related research studies conducted by other researchers in the future. In this research, future researches are recommended not only focus in selected NGO's but also include other government bodies which has authority in verifying expenditures of those NGO's. and this study can be done by including other NGO's which are currently engaged in various sectors both in the development and Emergency since there is huge resource allocated in those sectors. By doing so, the research can be conducted in a much more specific way and researchers are able to track to most significant factors that could influence ICE in the NGO's sector. And also the researcher recommends that the future research can be done by focus on other related factors; since in this research, the main factor that affects effectiveness of internal control is the organization independence.

Therefore the findings from this research can be useful for the future research especially for the managers and other government bodies who take into account the effectiveness of the Internal control. This study can also help in improving the commitment of internal Auditors in those selected NGOs' as well as others in both similar sectors or in other sectors to accomplish their goals.

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Appendix A: Questionnaire

Addis Ababa University

College of Business and Economics

School of Graduate Studies

Department of Accounting and Finance

Dear Participant:

The intent of this questionnaire is to explore information regarding effectiveness of Internal Control (IC) on operational performance to conduct Master Thesis (Research) for the partial fulfillment of Master's Degree in accounting and finance at Addis Ababa University. The questionnaires are distributed to the non-governmental organizations offices that found in Addis Ababa city. The results of the study are expected to contribute to identify the determinants of internal audit effectiveness.

The conclusions of the study will be drawn in aggregate terms, without any reference to specific offices or individual respondents. Please, do not write your name on the questionnaire.

I would also like to assure you that the information you provided will be treated as strictly Confidential and used only for the purpose of this research only.

Your honest and thoughtful response is valuable
Thank you in advance for your support and participation.

With best regards,

Getu Mohammed, Mobile: +251- 910 67 62 54, Email: getumohammed@gmail.com

Personal Profile:

1. What is your gender/sex?

Male

Female

2. What is your age in years?

20–29

30–39

40–49

50–59

60 and above

3. What is your field of training??

Accounting

Management

Economics

Other specify.....

4. What is your highest completed academic level?

TVET certificate

Diploma

Bachelor

Masters

Others, please specify.....

5. Which of these professional certifications do you have?

Certified Internal Auditor (CIA),

Certified Public Accountant (CPA)

Certified Management Accountant (CMA)

Other (specify).....

6. For how many years have you worked as an Internal Auditor?.....

7. Does your organization have an Audit committee?

No

Yes

8a. Identify the organizational controls that are commonly used in the organization to enhance operational efficiency?

i) Marketing controls

ii) Human Resource control

iii) Computers and information controls

iv) Financial Controls

8b. what are the effects of organizational controls you have identified above in enhancing operational efficiency?

.....

.....

.....

.....

9. What are the activities carried out by IC in your office/sector? You can select more than one.

- A. Compliance audit
- B. Financial audit
- C. Operational/performance audit
- D. Internal control System evaluation
- E. Risk assessment (analysis) audit

10. Identify the operating controls that are commonly used in the organization to enhance operational efficiency

- i) Planning
- ii) Budgeting
- iii) Policies and procedures
- iv) Project monitoring and evaluation

11. Choose ONE of the internal controls that you consider the most vital in achieving operational efficiency in your organization

- a) Organizational Controls
- b) Operating Controls
- c) Personnel Controls
- d) Periodic Reviews

The Questionnaire is prepared in Likert-scale form with five (5) point scales. I ask you to tick (v) the appropriate scale (point) that indicates your opinion in table below. The values of scales are 5= strongly agree, 4= Agree, 3= Neutral, 2= Disagree, 1= strongly disagree,

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Statements					
(a) Operational control such as good planning system ensure that day-to-day actions are consistent with established plans and objectives					
(b) Budgeting is done to ensure that all expenses are catered for					
(c) There are clearly laid down policies and procedures with regard to operations to be followed within the organization					
(d) The office/sector supports me to introduce me with new technology, policy or procedures whenever it is necessary.					
(e) All records of the organization are effectively documented for efficiency of controls.					
Management's perception of internal audit function					
(f) The office/sector has enough awareness					

and good perception about internal auditing roles.					
(g) The office/sector considers internal auditing practices as a value adding activity and I work smoothly & regularly with the management.					
(h) The office/sector encourages me to implement my recommendations, to promote value-added activities and to strength internal audit function.					
(i) The position/status of internal audit is clearly recognized by the management in my office/sector.					
(j) The office/sector see internal auditing as providing internal assurance through investigations, check & assessment, and consultants & adviser particularity into controls associated to management performance and internal operations.					
Organizational independence					
(k) I perform the auditing activities without any interference from anybody and without any influence from the office/sector.					
(l) I freely decide the scope, time and extent of auditing procedures based on auditing standards and the office's/sector's policy.					
(m) I objectively examine auditing issues only meeting on reliable audit evidence and no					

management interest is involved for adjustment beyond auditing standards & values.					
(n) I feel free to include any audit finding in my audit work and report directly to responsible body.					
(o) I can freely access necessary documents, information and data about the organization/sector for my audit work.					
The adequate competent internal audit staff					
(p) My office/sector has sufficient skilled internal auditors. Most of them have certification in auditing.					
(q) It is possible to audit and review each activity on time, and cover the planned scope of auditing activities.					
(r) The audit procedures and evidence collections are completed on time, since enough and skilled internal auditors are available or employed.					
(s) The internal audit staff number & their skill matches the scope of office's/sector's internal operations.					
(t) The work of internal audit is performed with modern technology that uses computerized data tools and specific IA					

software					
The approved internal audit charter					
(u) Internal audit charter is maintained (available) in my office /sector.					
(v)The purpose and authority of internal audit is clearly defined in charter.					
(w)The purpose and authority of internal audit charter is in line with “Standards for the Professional Practice” formulated by the Institute of Internal Auditors					
(x)The IA charter specifies the internal audit activity’s position within the office; authorized access to records, personnel, and physical properties relevant to the performance of engagements, and the defined scope of IA activities.					

Concerns have been expressed on accountability issues (Gray et al, 1987; Tinker, 1991; Tower, 1993). For example, why is accountability necessary? How is accountability determined? To whom is accountability due? How is control systems linked to accountability? What information should be communicated for accountability purpose? These issues in relation to NGOs are discussed below: NGOs have special legal and operational privileges and hence should act in accordance with the norms of their community (Birkett, 1988). Normally communities or donors should receive periodic assurances from the recipients on the use and effect of such resources.

Performance evaluation questions:

	Strongly	Agree	Neutral	Disagree	Strongly Disagree
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	Agree				
(1) Do you make field visits after reviewing financial documents to check to see the physical structure?					
(2) Do your organization make accountable for donors through continuous evaluation, half- yearly performance reports, annual activity reports, and audit reports.					
(3) There is efficiency in the organization to deliver services to its people in the most cost-effective manner?					
(4) Do beneficiaries participate in the evaluation and monitoring of your project that are implemented by your organization?					
(5) Is it adequate for NGOs to be accountable to the government and donors?					

Thank you for participating in this research.

