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## **Collage of Business and Economics**

### **Department of Accounting & Finance**

**The effect of Corporate Governance on The Independence of  
Internal Audit Function in Private Commercial Banks in Addis  
Ababa**

**A Project Submitted to The school of Post Graduate Studies  
presented in partial fulfillment of The Requirement for The Degree  
of Masters of MSC in Accounting and Auditing**

**By**

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**Nov, 2025**

### Declaration

Dina Belete, the under signed, declare that this project entitled: "The effect of Corporate Governance on The Independence of Internal Audit function in Addis Ababa" is my original work. I have undertaken the research work independently with the guidance and support of the research supervisor. This study has not been submitted for any degree or diploma program in this or any other institutions and that all source of materials used for the project has been duly acknowledged.

Dina Belete  
Name of the student

  
Signature

18/11/2025  
Date

This is to certify that the project entitled: "The effect of Corporate Governance on The Independence of Internal Audit function in Addis Ababa" Submitted in partial fulfillment of the requirements for the degree of masters of Accounting and Auditing of The post graduate studies, Addis Ababa University and is a record of original research carried out by Dina Belete Id /1236/15, under my supervision, and no part of The project has been submitted for any other Degree or Diploma. The assistance and help received during the course of this investigation have been duly acknowledged. Therefore, I recommend it to be accepted as fulfilling the project requirements.

Takele Fufa (PHD.)  
Name of the Advisor

  
Signature

Feb 4/2026  
Date



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## ABBREVIATION AND ACRONYMS

ACCSA	Addis Ababa Chamber of Commerce and sector Association
ACCA	Association of Chartered Certified Accountants.
AICPA	American Institute of Certified public Accountants
BCBS	Basel Committee on Banking Supervision
CGS	Corporate Governance Setting
ECIIA	European Confederation of Institute of Internal Auditor
EAC	Effectiveness of Audit Committee
ERNC	Effectiveness of Remuneration & Nomination Committee
ETA	Effectiveness of Technological Advancement
ESE	Effectiveness of Stakeholder' s Engagement
GAAP	Generally Accepted Accounting Principles
ICAEW	Institute of Chartered Accountants in England & Wales
IIA	Institute of Internal Auditor
IIARF	Institute of Internal Auditors Research Foundation.
IIAF	Independence of Internal Audit Function
ISSAI	International standard of supreme Audit Institution.
ISPPIA	International Standard s for professional Practice for Internal Auditing
IOSCO	International Organization of Securities Commission.
MOFED	Ministry of Finance and Economic Development.
NBE	National Bank of Ethiopia

SMS	Senior Management Support
SPPIA	Standards of The professional practice of Internal Auditing.
SPSS	Statistical package for social sciences

## ***ABSTRACT***

*This study aimed to investigate how various Corporate Governance factors influence the independence of Internal Audit within private commercial banks in Ethiopia. Data was gathered through 117 structured questionnaires distributed among bank management and 10 interview questions directed at the management of six banks, alongside responses from 111 bankers, specifically internal audit department managers. Ultimately, 111 completed questionnaires were obtained from key participants, including Internal Audit managers, heads of inspections, and audit division officers. Utilizing a census approach, the research surveyed the entire target population of Internal Audit managers, heads of inspection, and risk managers from the six selected private commercial banks in Ethiopia, comprising a total of 127 respondents. This method effectively reduced sampling error by encompassing all relevant individuals, thereby ensuring a thorough collection of data regarding the influence of Corporate Governance on Internal Audit independence. The structured questionnaires employed a five-point Likert scale, which provided detailed insights and enhanced the reliability and validity of the results. Data analysis was conducted using The SPSS version 25 statistical software. A regression model was applied to examine the relationship between The Internal Audit function and the level of Corporate Governance factors, with a significance test conducted at a 95% confidence level. The findings indicated a positive linear relationship between the independence of The Internal Audit function and several Corporate Governance factors: Corporate Governance setting (CGS), senior management support (SMS), effectiveness of the audit committee (EAC), impact of the remuneration and nomination committee (ERNC), influence of technological advancement (ETA), and stakeholder engagement (SA) concerning Internal Audit staff within private commercial banks in Addis Ababa, Ethiopia. Based on These findings, The study recommends that The Internal Audit departments of private banks pay attention to the implications of*

*Corporate Governance factors on the independence of Their audit functions. Additionally, it is advised that These departments stay updated on The Corporate Governance elements that affect Their independence to maximize The value-added services provided by Their Internal Audit functions.*

**KEY WORDS:** *Corporate Governance, senior management, independence, Internal Audit, Remuneration & Nomination committee, audit committee effectiveness, Technological advancement Stakeholder's engagement, Internal Audit staff.*

# CHAPTER ONE

## 1. INTRODUCTION

### 1.1. Background of the Study

Corporate Governance refers to the systems and structures that oversee the management of organizations, outlining how they are governed and regulated. It involves key stakeholders such as employees, shareholders, the Board of Directors, and executive management, all of whom play a vital role in this framework (SBB71/19). Effective Corporate Governance is critical for improving financial performance, especially within financial institutions and the banking sector (Ashenafi et al., 2013). It ensures that management, acting as agents, operates in alignment with the interests of one or more stakeholder groups (Malik, 2007).

In addition, Corporate Governance includes the formulation of policies and regulations and considers how the control environment impacts overall economic performance. Strong Corporate Governance is essential for the smooth operation of corporations; it promotes economic efficiency, drives growth, and enhances investor confidence (Sutedi, 2012). In contrast, ineffective Corporate Governance may result from poor leader selection processes, inadequate compensation structures for management, and an imbalanced composition of executive and non-executive board members. Leaders may also lack sufficient experience, training, and qualifications. Recent trends in ownership structures have seen a rise in equity shareholding by institutional investors in companies (Jensen and Meckling, 1976).

Corporate Governance standards define the relationships among shareholders, board members, managers, employees, and other entities with which the company interacts. These standards primarily aim to safeguard the rights of the company and its stakeholders while clarifying their respective responsibilities (Massie, 2000).

Over the past ten years, new approaches to Corporate Governance have emphasized the board's accountability for ensuring the effectiveness of their organization's internal control systems. These theories underscore the crucial role that Internal Audit functions play in assisting boards with oversight of internal controls, thus becoming a fundamental part of a corporation's governance framework. The main objective of Internal Audit is to support the board or its audit committee in meeting their governance obligations. This independent and objective assurance and consulting activity aims to improve organizational operations through problem-solving (Radu Ramona, 2013; IIA, 2004).

In this context, independence means avoiding situations that might compromise objectivity or allow personal biases to influence critical decisions (Hemraj, 2003, as cited by Sandberg, 2012). Therefore, Corporate Governance centers on

how a company is managed and directed, particularly concerning the roles of the board and audit committee as well as the overall control and risk management framework (ACCA, 2005).

## **1.2. Statement of The Problem**

The standards of Corporate Governance delineate the relationships among shareholders, board members, managers, employees, and other stakeholders linked to a company. These standards primarily aim to protect the rights of the company and its participants while clarifying their respective responsibilities. As a result, the principles of Corporate Governance are essential for defining the rights and duties of these groups and for fostering confidence among investors.

The private commercial banking sector is crucial for the development of a country's financial system and acts as a significant catalyst for economic growth (Saci et al., 2009). A breakdown in the banking sector can have widespread repercussions for the entire financial system and the economy at large. Therefore, establishing and implementing robust and effective Corporate Governance is vital to enhancing company performance, promoting economic efficiency and growth, and increasing investor confidence (Saci et al., 2009).

Admassu Assaye (2014) observed that Ethiopia's banking industry is currently in a nascent and precarious state. It remains relatively small, underdeveloped, and largely insulated, with state-owned banks controlling nearly two-thirds of the sector's assets. However, there are signs of expansion within the private banking sector. Unlike other industries, the banking sector faces stringent regulations, with the Corporate Governance framework primarily shaped by the National Bank of Ethiopia. While the independence of Internal Audits is acknowledged as a crucial element for effective Corporate Governance, many organizations fail to design their governance systems in a manner that allows Internal Audits to preserve this independence or contribute significant value. Ethiopian private banks exhibit various shortcomings in Corporate Governance. This study will evaluate whether Corporate Governance influences the independence of the Internal Audit function within private commercial banks in Ethiopia. Previous research, such as that conducted by Mesert W. (2015), indicated that all key factors examined were associated with the effectiveness of Internal Audits in private banks. Essentially, improvements in these factors correlate with enhanced effectiveness of Internal Audits, and vice versa. The most significant determinants of Internal Audit effectiveness in these banks include having an independent organizational structure, a well-defined and approved Internal Audit charter, and a sufficient number of skilled personnel. Additionally, support from management and recognition of the value of Internal Audits by management also play critical roles in boosting their effectiveness.

The standards of Corporate Governance define The relationships among shareholders, board members, managers, employees, and other stakeholders associated with a company. These standards primarily serve to safeguard The rights of The company and its participants while clarifying Their respective obligations. Consequently, principles of Corporate Governance are crucial for establishing the rights and responsibilities of These groups and fostering investor confidence.

The private commercial banking sector plays a pivotal role in developing a country's financial system and serves as a significant driver of economic growth (Saci et al., 2009). A failure in the banking sector can have far-reaching consequences for The entire financial system and The economy. Therefore, to enhance company performance, promote economic efficiency and growth, and bolster investor confidence, it is essential to establish and implement strong, effective Corporate Governance (Saci et al., 2009).

Admassu Assaye (2014) noted that Ethiopia's banking industry is currently in a basic and vulnerable condition. It remains small, underdeveloped, and largely closed off, with state-owned banks holding nearly two-thirds of the sector's assets. However, there are indications of growth in The private banking sector. Unlike other industries, the banking sector is heavily regulated, with The Corporate Governance framework largely dictated by The National Bank of Ethiopia. While The independence of Internal Audits is recognized as a vital tool for effective Corporate Governance, many organizations do not design Their governance systems in a way that allows Internal Audits to maintain this independence or add substantial value. Ethiopian private banks have not been without These Corporate Governance shortcomings. This study will assess whether The Corporate Governance affects independence of Internal Audit function of private commercial banks in Ethiopia. Similar Thesis is prepared previously by some researcher like Mesert w, (2015). Discussed that all the key factors They looked at were linked to how well Internal Audits worked in private banks. Basically, when These factors get better, so does The Internal Audit's effectiveness, and vice versa. The biggest influences on how effective Internal Audits are in These banks, in order, are having an independent organizational structure, a clear and approved Internal Audit charter, and enough skilled staff. Beyond These top three, getting support from management and having management believe in the value of Internal Audits also significantly boost Their effectiveness.

The data clearly indicates that the effectiveness of Internal Audits is enhanced when the organizational structure allows auditors to perform their duties without interference. This effectiveness is further improved by having a sufficient number of qualified Internal Audit staff, the existence of a formal Internal Audit charter, and strong support from management, direct supervisors, and the auditees within the bank. Additionally, the perception of Internal Audit's value

by management significantly contributes to its overall effectiveness. Therefore, this study aims to explore specific variables identified by previous research that influence these outcomes.

### **1.2.1 Research Gaps**

Despite extensive research conducted both globally and locally, there remains a notable lack of understanding regarding how Corporate Governance impacts the independence of the Internal Audit function in private commercial banks in Addis Ababa. While previous studies have explored various aspects of Corporate Governance—such as the effectiveness of senior management, the remuneration and nomination committee, the audit committee, technological advancements, and stakeholder engagement—there is a scarcity of literature addressing factors that specifically influence the independence of Internal Audit within these banks. This study seeks to address these gaps by concentrating on private banks in Addis Ababa and examining a wider array of elements that may affect the independence of their Internal Audit functions. By doing so, this research aims to provide valuable insights and serve as a foundation for future studies on Corporate Governance, offering empirical evidence regarding its mechanisms' effects on the Internal Audit functions of private banks, while considering the unique variables, observations, and sampling methods relevant to Ethiopia's banking governance landscape.

### **1.3. Objective of the Study**

#### **1.3.1. General Objective**

The main objective of the study is to examine the effect of Corporate Governance on the independence of Internal Audit function,

#### **1.3.2. Specific objectives**

Specific objective of the study is:

- To assess the effect of Corporate Governance setting on independence of Internal Audit Function.
- To assess the effect of Senior management support on independence of Internal Audit
- To examine The Effect of audit committee effectiveness on independence of Internal Audit.
- To examine The Effect of remuneration & Nomination committee effectiveness on independency of Internal Audit
- To examine The Effects of Technological Advancement on independency of Internal Audit.
- To Assess the Effect of Stakeholders Engagement on independency of Internal Audit.

## 1.4. Research Hypothesis Formulation

The following hypothesis were test during The Research study:

### Hypothesis 1: Corporate Governance

- **H0:** Corporate Governance has no effect on independence of internal audit function.

While no studies conclusively state that Corporate Governance has no effect on internal audit independence, Anderson (2022) highlights that poor governance practices harm both organizational efficiency and Internal Audit effectiveness, hindering the achievement of objectives.

- **H1:** Corporate Governance has effect on independence of internal audit function.

Internal Audit independence and Corporate Governance share a strong, symbiotic relationship; effective governance enables independent audits, while independent audits strengthen governance by providing critical oversight, reducing risks, and enhancing organizational performance.

**Justification:** Despite The null hypothesis (H0) that Corporate Governance alone has no effect on the independence of The Internal Audit department, this research paper providing empirical evidence to substantiate The alternative hypothesis (H1). By establishing a detailed examination of the dynamics between Corporate Governance and Internal Audit independence.

### Hypothesis 2: Senior Management Support

- **H0:** Senior management support has no effect on independence of internal audit function.

Some studies indicate that management support alone may not suffice for Internal Audit independence, with its effect being moderate or insignificant. Khanam (2024) specifically argues that management support is not essential for enhancing Internal Audit effectiveness, contrasting with the majority viewpoint.

- **H1:** Senior management support has effect on independence of internal audit function

Indeed, senior management has a major impact on the independence and efficacy of Internal Audit, both positively and negatively, according to a number of academics and professional associations. The reporting structure, management's mindset, and the available resources frequently determine the nature of this effect.

**Justification:** The researcher attempted to compare the null hypothesis (H0) and the alternative hypothesis (H1), and despite the hypothesis that senior management support has no effect on Internal Audit independence, the effect of senior management support on the independence of The Internal Audit function is extensively explored in this research paper, as the alternative hypothesis is supported by evidence and has been verified by day-to-day activity.

### **Hypothesis 3: Effectiveness of Audit Committee**

- **H0:** Effectiveness of Audit Committee has no effect on independence of internal audit.
- There are no any scholars about Effectiveness of audit committee has no effect on independence of Internal Audit
- **H1:** Effectiveness of Audit Committee has effect on independence of internal audit.

The audit committee takes key actions to ensure auditor independence by recommending the appointment or renewal of external auditors and approving Their fees. By overseeing These processes, the committee ensures that the fees paid to auditors are fair and transparent, which helps maintain Their objectivity and independence.

**Justification:** The researcher attempted to compare the null hypothesis (H0) with the alternative hypothesis(H1) and found no evidence that the audit committee has no effect on Internal Audit independence. In contrast, the alternative hypothesis is beyond a hypothesis, and has evidence-based and day-to-day activity, so the effect of audit committee on the independence of The Internal Audit function is extensively explored in this Thesis.

### **Hypothesis 4: Effectiveness of Remuneration and Nomination Committee**

- **H0:** Effectiveness of Remuneration and Nomination Committee has no effect on independence of Internal Audit

There isn't a literature stating that The Remuneration and Nomination Committee has no effect on Internal Audit independence.

**H1:** Effectiveness of remuneration & Nomination committee has no effect on independency of Internal Audit

- Through These actions, The Remuneration and Nomination Committee plays a crucial role in strengthening the independence of Internal Audit, ultimately enhancing Corporate Governance and accountability.
- **Justification:** However, existing literature does not specifically support (H0) claim, as the committee is generally viewed as playing a crucial role in enhancing Internal Audit independence through its oversight of compensation policies and the selection of qualified candidates. Conversely, the alternative hypothesis (H1), which asserts that the committee does affect Internal Audit independence, aligns with the perspective that strong governance practices ultimately strengthen corporate accountability and integrity.

## **Hypothesis 5: Effectiveness of Technological advancement**

- **H0:** Effectiveness of Technological advancement has no effect on independence of Internal Audit

There are no any scholars about Effectiveness of Technological advancement has no effect on independence of Internal Audit

**H1:** Effectiveness of Technological advancement has effect on independency of Internal Audit

- Overall, effective technological advancements can strengthen the independence of Internal Audit

by improving efficiency, promoting transparency, and enabling objective evaluations, ultimately leading to more reliable Corporate Governance.

**Justification:** The lack of literature supporting the first hypothesis (H0) indicates an important gap, while the second hypothesis (H1) aligns with the trend of utilizing technology to enhance independence through improved practices. This research seeks to contribute to academic knowledge and practical applications in effectiveness of Technological advancement has effect on independency of Internal Audit

## **Hypothesis6: Effectiveness of Stakeholder's Engagement**

- **H0:** Effectiveness of Stakeholder's Engagement has no effect on independence of Internal Audit

There are no any scholars about Effectiveness of stakeholder's engagement has no effect on independence of Internal Audit

**H1:** Effectiveness of Stakeholder's Engagement has effect on independency of Internal Audit

Stakeholders play a critical role in the success of an Internal Audit function, enhancing the audit's effectiveness. By engaging and collaborating with These stakeholders, Internal Audit can foster a comprehensive approach to identifying risks, improving processes, and ultimately supporting the organization's governance and operational integrity.

**Justification:** Ultimately, this research aims to bridge the identified gap, providing empirical evidence that can inform both academic knowledge and practical applications in The field of Internal Auditing. Overall, effective stakeholder engagement is crucial for maintaining the independence of Internal Audit, enabling auditors to perform Their roles without external pressures and ensuring that Their evaluations contribute positively to governance and operational integrity.

### **1.5. Significance of The Study**

This research enhances the current body of knowledge by offering insights into the relationship between Corporate Governance factors and the Internal Audit function of private commercial banks. The findings will serve as key indicators of Corporate Governance mechanisms, which can aid regulators, management, and business leaders in formulating effective policies and making informed decisions. Additionally, this study may act as a valuable resource for other researchers looking to conduct larger-scale investigations in this area, facilitating comparisons across different banking institutions. Furthermore, it aims to assist practitioners by addressing pertinent questions related to Corporate Governance and Internal Audit independence.

The study will highlight significant findings regarding the Corporate Governance practices within the Ethiopian banking sector that could influence the independence of Internal Audits, paving the way for further research in this domain.

### **1.6. Scope of The Study**

This study is confined to six private banks: Awash Bank S.C., Dashen Bank, Bank of Abyssinia, Wegagen Bank, Hibret Bank, and Nib International Bank. The selection of these banks was informed by the National Bank of Ethiopia's report for the 2021/22 fiscal year, which categorized banks based on their establishment dates. The research aims to investigate how various governance factors—such as the structure of Corporate Governance, support from senior management, the effectiveness of the audit committee, the remuneration committee, the nomination committee, advancements in technology, and stakeholder engagement—impact the independence of the Internal Audit function. The choice of these specific factors was guided by a review of existing literature and prior studies. The target population for this research comprises Internal Audit personnel from the head offices of these banks located in Addis Ababa, as the Internal Audit units are centralized at each bank's headquarters.

### **1.7. Limitation of the Study**

The scope of this study is confined to six selected private commercial banks, with data collection taking place at their head offices in Addis Ababa; therefore, it may not fully capture the broader industry context. Notably, the Research and Development department at the Bank of Abyssinia was unavailable for participation due to building repairs and ongoing training sessions. Additionally, the study is limited to examining only six specific factors that influence the independence of the Internal Audit function within private banks. The research primarily investigates how Corporate Governance affects the effectiveness of the Internal Audit function, focusing on the roles of the audit committee, nomination committee, and remuneration committee, as well as the perception of Internal Audit, support from senior

management, and the overall Corporate Governance framework as independent variables, with the effectiveness of the Internal Audit function serving as the dependent variable.

### **1.8. Definition of The Terminologies**

**Corporate Governance:** encompasses the mechanisms and processes through which companies are directed and controlled, defining the distribution of power, accountability, and decision-making authority. It serves as a framework that aids management and the board in effectively navigating the complexities of running an organization. By establishing sound decision-making procedures and controls, Corporate Governance seeks to balance the interests of all stakeholders, including shareholders, employees, suppliers, customers, and the wider community.

**Independence:** refers to the ability to operate free from influences that could compromise objectivity or give the appearance of compromised objectivity.

**Objectivity:** is characterized by an impartial mindset that enables Internal Auditors to conduct their work with genuine belief in their findings, ensuring that significant quality compromises are avoided. It necessitates that Internal Auditors maintain their own judgment on audit matters without yielding to external pressures.

**Independence of Mind:** (in Fact) refers to a mental state that allows auditors to reach conclusions without being swayed by external factors that might undermine their professional judgment, enabling them to act with integrity while exercising objectivity and professional skepticism.

**Independence in Appearance:** involves steering clear of situations that could lead a reasonable and informed third party to believe that the integrity, objectivity, or professional skepticism of an auditor or audit team member has been compromised.

### **1.9. Organization of The Study**

This research is structured into five chapters. The first chapter provides a general introduction and context for the study. The second chapter reviews existing literature related to the impact of Corporate Governance on the independence of the Internal Audit function. The third chapter details the research methodology employed in this study. The fourth chapter presents and analyzes the collected data. Finally, the fifth chapter concludes with findings and recommendations, along with references and appendices included at the end.

## **CHAPTER TWO**

### **2. LITERATURE REVIEW**

#### **Introduction**

This chapter provides a literature review focused on the independence of the Internal Audit function and its relationship with Corporate Governance. It begins with an overview of the Internal Audit function and Corporate Governance, followed by an analysis of how Corporate Governance impacts the independence of Internal Audit. Overall, this chapter aims to synthesize existing empirical studies on the independence of Internal Audit in relation to Corporate Governance, concluding with a summary of the findings and highlighting gaps in the current literature.

#### **2.1. . THEOROTICAL REVIEW**

##### **2.1.1. Theory of Corporate Governance**

Corporate Governance comprises the systems and processes that direct and manage corporations, with the goal of enhancing shareholder value while ensuring the financial sustainability of the business (Toronto Stock Exchange, annex II). This framework outlines how authority is distributed and establishes accountability among shareholders, the Board of Directors, and management.

Although there is no single widely accepted model for effective Corporate Governance, research from both OECD and non-OECD countries has identified several shared principles that support sound Governance practices. These principles are non-binding and do not dictate specific national laws; rather, they aim to clarify objectives and recommend various strategies for achieving them. The intention is to provide a reference for policymakers in developing legal and regulatory frameworks for Corporate Governance that are tailored to their unique economic, social, legal, and cultural contexts, as well as for market participants in shaping their practices (OECD, 2004).

Corporate Governance involves the relationships and responsibilities among key stakeholders—specifically shareholders, board members, and managers—aimed at optimizing the performance of the banking sector and the

overall economy (OECD). The stability and soundness of banks are essential for maintaining financial stability, and the manner in which these institutions operate is critical to the health of the economy. Governance shortcomings in banks that are key to the financial system can lead to significant issues affecting both the banking sector and the broader economy (Basel Committee Guideline for Banking Supervision, 2014).

### **2.1.2. Corporate Governance in Ethiopia**

Fekadu (2010), as cited by Hussein Ahmed Tura, emphasized the growing gap between ownership and control in Ethiopia, providing empirical support for this claim. Utilizing existing data and research on Corporate Governance, he critiqued the weaknesses of the Commercial Code in protecting the rights of minority shareholders in publicly held companies. He raised critical questions regarding the board's authority, accountability, organizational structure, and standards of liability, among other issues. In his 2011 book, "Ethiopian Company Law," Fekadu further explored various Corporate Governance challenges related to boards of directors (Hussein, 2012). He investigated the legal framework governing share companies in Ethiopia, examining both theoretical principles and regulatory standards of Corporate Governance. His analysis addressed topics such as structural choices, the procedures for appointing and dismissing directors, their powers and responsibilities, compensation, and methods for overseeing board activities.

Historically, share companies were often founded by a small group of individuals; however, there has been a marked trend toward creating companies that offer shares to the wider public. This change has introduced a range of Corporate Governance challenges in Ethiopia (Tewodros, 2011). The separation of ownership and control frequently leads to a concentration of power among a few managers over dispersed shareholders, creating a principal-agent dilemma. In such cases, managers (agents) may take advantage of their informational superiority over shareholders (principals), potentially misusing their investments. Moreover, when only a few major shareholders are present, minority shareholders may face the risk of exploitation by these dominant stakeholders. Hussein (2012) concluded that the agency problems arising between dispersed shareholders and managers or significant shareholders in Ethiopian share companies highlight the pressing need for strong Corporate Governance laws and institutions.

The connection between Internal Auditing and Corporate Governance is increasingly recognized as impactful across various economic activities, with its significance evolving considerably in recent years. Both Internal Auditing and Corporate Governance have emerged as vital areas of public concern. International guidelines indicate that effective collaboration between these two domains enhances organizational performance and offers a competitive edge. The role of Internal Auditing in Corporate Governance is emphasized through its link to essential governance elements.

Additionally, the Board of Directors is recognized as a key figure in Corporate Governance by regulators and governance committees worldwide (US Congress, 2002).

## **2.2. An Overview of Audit Function**

### **2.2.1. Objective and Function of Internal Audit**

The Internal Audit function is tasked with assessing and commenting on the effectiveness of risk management, control, and Corporate Governance processes. According to the Association of Chartered Certified Accountants (2005), and as cited by Jenny et al. (2008), the Institute of Internal Auditors (IIA) defines Internal Auditing as "an independent, objective assurance and consulting activity aimed at adding value and enhancing an organization's operations." This definition highlights that Internal Auditing helps organizations achieve their goals through a systematic and disciplined approach that evaluates and improves the effectiveness of risk management, control, and governance processes.

Furthermore, the definition emphasizes the objectives of Internal Auditing, characterizing it as "a systematic and objective evaluation by Internal Auditors of the various operations and controls within an organization to assess whether: financial and operational information is accurate and reliable; risks to the organization are identified and mitigated; external regulations and acceptable policies and procedures are adhered to; satisfactory standards are achieved; resources are utilized efficiently and economically; and the organization's objectives are successfully met."

### **2.2.2. Independence of Internal Audit Function**

The notion of independence in Internal Auditing pertains to the auditor's capacity to conduct evaluations and assessments impartially and objectively, free from any undue influence that could affect their judgment (Wahid AbuAzza, 2012). The Institute of Internal Auditors (IIA) defines independence in its Standards for Professional Practice of Internal Auditing as the absence of circumstances that could jeopardize objectivity or give rise to a perception of bias. It is crucial for Internal Auditors to manage potential threats to their objectivity across various levels, including on an individual basis, in specific engagements, within functional areas, and at the organizational level (IIA, 2011). Both the IIA and the American Institute of Certified Public Accountants (AICPA) have acknowledged the significance of independence within the Internal Audit function, highlighting its essential role in preserving the integrity of the auditing process.

To uphold independence, the IIA has established multiple attribute standards, particularly Standard 1100, which states that the Internal Audit activity must operate independently in fulfilling its responsibilities. Independence is defined as the absence of conditions that may impede the Internal Audit's ability to perform its duties without bias (IIA, 2011d). For effective audit execution, the chief audit executive should have direct and unrestricted access to senior management and the board, which can be facilitated through a dual-reporting structure. Moreover, potential threats to independence should be addressed at various levels, including individual auditors, specific engagements, functional areas, and the organization as a whole (IIA Guide 1100).

The ongoing discussion regarding reporting structures for Internal Audit functions has led some scholars to propose that assigning complete reporting responsibility to the audit committee may enhance the independence of Internal Auditors (Abbott et al., 2012; Haron et al., 2012). However, the IIA's definition acknowledges both consulting and value-added services, recognizing that Internal Auditors can support organizations in achieving their goals (Ali et al., 2009).

According to guidelines on Internal Auditing in banking provided by Barclays Simpson consultants, complete independence is achieved when Internal Audit refrains from engaging in or authorizing daily operational tasks critical for the bank's functioning. Additionally, it should not be responsible for initiating new actions based on audit recommendations. Nevertheless, Internal Audit should remain available for providing advice and collaboration as needed. The IIA (2020) defines Internal Auditing as an independent and objective assurance and consulting activity aimed at improving organizational operations, stressing the significance of independence and objectivity in both assurance and consulting functions.

Independence and objectivity are closely related concepts within IIA Standards, often used synonymously, which can lead to some confusion. The IIA (2001) recognizes this overlap and emphasizes the need for clarity in differentiating these terms.

### **2.2.3. The Need for Independence of Internal Audit Function**

Auditor independence and objectivity are core principles that form the foundation of the auditing profession. The value and credibility of the assurance services rendered by auditors rely significantly on the fundamental beliefs in both independence of mind and independence in appearance (Stewart et al., 2008).

While historical research has primarily concentrated on the independence and objectivity of external audits, there has recently been an increased focus on the independence and objectivity of Internal Audits. In his research, Travis P. Holt (2009) underscores the necessity of addressing information asymmetry and enhancing governance transparency,

referencing insights from Jensen et al.'s (1976) model of the agency relationship between a company's managers and its shareholders. This relationship presents challenges such as moral hazard and information asymmetry, where managers have insider information that may lead them to make decisions that do not align with the best interests of shareholders (Jensen and Meckling, 1976; Eisenhardt, 1989). As a result, shareholders and regulatory authorities put in place Corporate Governance mechanisms to monitor managerial actions, ensuring that managers act as accountable stewards of corporate assets. The frameworks of accounting, auditing, and governance are critical elements of the capital markets system, as highlighted by Holt (2009).

#### **2.2.4. Internal Audit Function in Banking Business**

Barclays and Simpson Recruitment Consultants have outlined the function of Internal Audit within the banking sector, highlighting its status as an independent department distinct from line management. Its main responsibility is to assess the quality and effectiveness of internal controls established to manage and mitigate risks while protecting the bank's assets. In fulfilling this role, Internal Audit provides management with valuable recommendations and insights regarding issues that require attention (Barclay, 2015).

Generally, Internal Audit develops an annual work plan that concentrates on high-risk areas. This process includes creating structured timelines and specific work programs, such as audit plans for each assignment. Upon completion of each review, an audit report is prepared for senior management's review and necessary action. Moreover, Internal Audit can handle ad hoc requests from senior management to investigate any identified issues or discrepancies further. Engaging Internal Audit in major projects, including system developments, brings significant benefits, as this proactive involvement enables early resolution of audit concerns, thus preventing issues from becoming entrenched (Basel Committee report 2012).

### **2.3. Overview of Banking Industry in Ethiopia**

The banking industry is distinct from other sectors within any country, particularly in relation to the products and services it provides. Banks primarily handle liquid assets and cash equivalents, which often carry substantial risks. Two notable differences in the governance of banks compared to non-financial firms are the larger number of stakeholders involved and the inherent complexity and opacity of banking operations, which can change swiftly (Hamid Mehran & Alan Morrison, June 2011). Banks play a vital role in the global financial system, acting as primary institutions for individuals seeking loans for various purposes, such as buying homes or vehicles, starting businesses, or financing education (Peter et al., 2008).

Given the variations in scale, diversity, complexity, and geographical reach, banks implement diverse management structures tailored to their specific requirements. A critical element of this framework is the Internal Audit function, which aims to address the unique risks encountered by each bank (Mahama, 2009). In Ethiopia, as noted by Admassu et al. (2014), the banking sector has experienced several transformations influenced by varying state systems. Recently, there has been a notable increase in the establishment of private commercial banks throughout the country.

Traditionally, the Ethiopian banking landscape has been largely dominated by the state-owned Commercial Bank of Ethiopia (CBE). Financial intermediation has been constrained, partly due to a lack of public confidence in banks. This skepticism arises from a weak supervisory framework, widespread state ownership, and lending practices often directed by the National Bank of Ethiopia (Admassu et al., 2014).

#### **2.4. Corporate Governance in Private Banks of Ethiopia**

The "Voluntary Code of Corporate Governance for Ethiopia" was adopted on June 3, 2011, under the auspices of the Addis Ababa Chamber of Commerce and Sectorial Associations (AACCSA). This adoption represents a significant step forward in establishing comprehensive Corporate Governance standards in Ethiopia, as noted by Hussein (2012). The banking sector includes one state-owned development bank and 18 commercial banks, two of which are state-owned, with the Commercial Bank of Ethiopia (CBE) accounting for approximately 70 percent of the industry's total assets. The National Bank of Ethiopia (NBE), established in 1963, serves as the country's central bank. Following the enactment of the Monetary and Banking Proclamation No. 83/1994 in May 1991, the NBE was restructured to align with a market-oriented economic policy aimed at promoting monetary stability and fostering a robust financial system that facilitates economic growth (Ayele, 2013).

The adoption of effective Corporate Governance practices within the banking sector is crucial for achieving the NBE's primary goal of ensuring monetary stability and maintaining a sound financial system in Ethiopia (Ayele, 2013). To empower the NBE in its duties, the law grants it the authority to oversee regulatory compliance through both onsite and offsite supervision, as well as to impose penalties on banks that do not adhere to regulations. Notably, as Hussein (2012) indicates, Ethiopian company law does not offer a specific definition of 'Corporate Governance.' Therefore, for the purposes of this study, we define Corporate Governance as a framework of rules and institutions that govern the control and direction of a company while outlining the relationships among its key participants, including the Board of Directors, management, shareholders, and other stakeholders. This definition encompasses both narrow and broad perspectives, highlighting the importance of engaging not just shareholders but also other stakeholders in the governance of share companies.

## **2.5. The Relationship Between Independence of Internal Audit Function and Corporate Governance**

To enhance the status of the Internal Audit function within an organization, it is vital to develop a strong relationship with those responsible for governance, ensuring direct communication with the audit committee (The Institute of Internal Auditors Research Foundation [IIARF], 2013). There is significant evidence that such a reporting structure is increasingly viewed as a best practice among forward-thinking corporations committed to improving their governance frameworks and processes. Principle 13 of the Basel Committee states that the Internal Audit function acts as the third line of defense, following operational and risk management controls. However, some perspectives argue that Internal Audit can also serve as the first line of defense against weaknesses in organizational governance and financial reporting (Njeru, 2011). With appropriate support from the board and the audit committee, Internal Auditors are well-equipped to identify improper accounting practices, inadequate internal controls, and ineffective governance structures (Zekele, 2007). Consequently, they play a vital role in establishing a strong Corporate Governance framework. In conjunction with the board, executive management, and external auditors, the Internal Audit function is essential for effective Corporate Governance.

For true independence within the organization to be achieved, the chief audit executive should functionally report to the board (Institute of Internal Auditors, 2011). This entails monitoring, assessing, and analyzing organizational risks and controls while ensuring compliance with relevant policies, procedures, and laws. By working in partnership with management, Internal Auditors assure the board, the audit committee, and executive management that risks are effectively managed and that Corporate Governance remains strong (Hermanson et al., 2003). When improvement opportunities arise within the organization, Internal Auditors have the responsibility to suggest enhancements to processes, policies, and procedures (Hermanson et al., 2003). The literature clearly indicates a strong connection between the Internal Audit function and various Corporate Governance factors within organizations.

## **2.6. EMPIRICAL STUDIES**

The primary objective of this research is to investigate the impact of Corporate Governance on the independence of the Internal Audit function, analyzing and presenting various perspectives and recommendations from different authors and researchers on this relevant topic.

### **Corporate Governance Factors Influencing the Independence of the Internal Audit Function**

A fundamental principle of Corporate Governance Theory posits that Internal Auditors should collaborate with audit committees, boards, and senior management to establish an appropriate “tone at the top.” They also play a crucial role

in ensuring that ethical behavior is instilled throughout the organization, reaching lower-level employees (IIA, 2003; Brown et al., 2003; Bailey et al., 2003).

### **2.6.1 Corporate Governance Setting**

The International Standards of Supreme Audit Institutions (ISSAI), along with the Institute of Internal Auditors (IIA) and the International Standards for the Professional Practice of Internal Auditing, provide general guidelines that can be adapted to different national contexts. These guidelines stress that their implementation will depend on the specific environment in which Internal Audit activities occur, ensuring adherence to relevant laws and regulations. The IIA's Standards are intended to be universally applicable to all Internal Audit professionals and emphasize the critical need for Internal Auditors to maintain independence and objectivity in their work, whether in public or private sector audits. Furthermore, these Standards advocate for the establishment of a strong internal control system, which should be monitored by a well-resourced Internal Audit function, as a fundamental aspect of effective governance. In the public sector, robust governance is essential for adequate service delivery to the public. Legislative measures intended to establish an Internal Audit function are critical for safeguarding its funding and independence, thereby acknowledging its important role in public sector operations. Legal protections for the independence of Internal Auditors, particularly under civil service law, are key elements of a supportive legislative framework (Intosai, 2015). However, there remains a need for clearly defined Internal Audit standards to better regulate its relationship with Corporate Governance.

In Ethiopia, the importance of Internal Auditing has been recognized since 1991 (Mihret et al., 2009). In 1994, the Ethiopian Prime Minister commissioned a task force to recommend improvements for Internal Auditing in government offices. The recommendations from this task force laid the foundation for legal support through the issuance of the Councils of Ministers Financial Administration Regulation (CMFAR) in 1996. This regulation assigned the Ministry of Finance and Economic Development (MOFED) the responsibility for overseeing and regulating Internal Audits within the public sector, along with developing an Internal Audit manual for all public entities (Mihret et al., 2012).

With regard to Internal Audits in banks, the Basel Committee on Banking Supervision's Principle 2 mandates that a bank's Internal Audit function must operate independently from the activities it audits. This independence requires that the Internal Audit function has sufficient authority and status within the bank to allow auditors to carry out their duties objectively. Accordingly, this study aims to assess how various Corporate Governance elements—such as governance

guidelines, external compliance mandates, and internal bank policies—influence the independence of the Internal Audit function in Ethiopian private banks.

### **2.6.1 Senior Management Support**

Many employees view the Internal Audit department as having strong support from senior management, which aligns with the Standards for the Professional Practice of Internal Auditing (SPPIA). Interestingly, higher-level employees are more likely to perceive this backing than those at lower levels. However, despite this perception of support from senior management, a significant number of employees believe that the Internal Audit function lacks independence. This indicates that, from the employees' viewpoint, backing from senior management does not necessarily enhance the perceived independence of Internal Audit.

A recent survey by Thomson Reuters reveals that Internal Audit practitioners around the globe feel a greater and more visible endorsement from senior management is crucial for their function, especially as changing regulatory and risk landscapes force them to achieve more with limited resources.

Regarding the professional development of employees, Hepworth et al. (2002) highlighted that hiring skilled professionals can improve the effectiveness of Internal Auditing. They advocate for Internal Auditors to pursue continuous professional development by becoming members of national and international professional associations for auditors and accountants and obtaining high-level accreditation. These efforts are vital for enhancing the overall efficiency of the Internal Audit process. Similarly, Shahreri (1999) suggested that recruiting competent and qualified individuals is essential for strengthening Internal Audit functions and departments (SeifObeid et al., 2012).

This research aims to identify various factors that may affect the independence of Internal Audit and assess their impact. Key elements analyzed include responses to audit findings, support for training and development, as well as the recruitment and training of Internal Auditors. These factors were specifically examined within the context of Ethiopian private banks as part of this study.

#### **2.6.1. Effectiveness of Audit Committee as Corporate Governance Tool**

The research conducted by Ramadili et al. (2009) emphasizes that an audit committee can significantly enhance auditor independence, provided its members are truly independent, knowledgeable, and committed to fostering good governance without bias. There is an urgent need for the committee to go beyond mere procedural compliance and tackle fundamental issues related to effective governance, the internal control framework for financial reporting,

concerns surrounding Internal Audit, and the relationship between the head of the accounting and finance division and the Internal Audit (monitoring) division. An effective audit committee is crucial for strengthening the Internal Audit function by creating an independent and supportive atmosphere in which the Chief Internal Auditor (CIA) can bring forth issues that impact management (Braiotta, 1999; Goodwin and Yeo, 2001; Goodwin, 2004).

A key element in evaluating the effectiveness of Internal Audits is the reporting structure, which should involve direct reporting to the audit committee (Krishnamoorthy, 2008; Owolabi Dada, 2011). According to Mu'azu et al. (2014), audit committees have garnered significant attention as an essential aspect of Corporate Governance, particularly in relation to the qualifications of their members. It is vital to include individuals with exceptional independence, qualifications, experience, and knowledge—as highlighted by Alkdai et al. (2012)—to ensure that an audit committee enhances reliable, effective, and efficient Corporate Governance. The formation of such committees has been demonstrated to lead to a decrease in corporate inefficiencies (Mu'azu et al., 2014).

#### **2.6.2. Perception of Independence (Mind and Appearance)**

Auditor independence and objectivity are essential principles within the auditing profession. The value and credibility of the assurance services delivered by auditors rely on the fundamental concepts of both "independence of mind" and "independence in appearance" (Paape, 2007). The International Federation of Accountants (IFAC) distinguishes between these two forms of independence (Quick Warming-Rasmussen, 2005:138). The perception of independence plays a vital role in regulating auditor independence (Geiger et al., 2002). The importance of auditor independence—both in its actual form and as perceived by others—is widely recognized in academic research and regulatory frameworks (Geiger et al., 1999:3; Mathose, 2013).

Independence of mind pertains to the mental state that allows an auditor to issue an opinion without being swayed by factors that might undermine their professional judgment, thereby ensuring integrity, objectivity, and professional skepticism (Mathose, 2013). Conversely, independence in appearance involves steering clear of circumstances significant enough that a reasonable and informed third party might believe the integrity, objectivity, or professional skepticism of the Internal Audit function has been compromised (Quick Warming-Rasmussen, 2005:138). It has been observed that the perceived independence of Internal Audits is comparatively under-explored when set against that of external audits.

This study seeks to identify the factors that may impact independence and assess their effect on perceived independence, given that actual independence cannot be observed directly (Beattie et al., 1999:2). Specifically, the research examines various dimensions of independence, including the ability of the Internal Audit to define its own

scope, the reporting structure of the Internal Audit function, and potential role conflicts arising from interactions with management. These factors were investigated through data collected from private commercial banks in Ethiopia.

**The Basel Supervisory Committee** is releasing updated guidance for assessing the effectiveness of the Internal Audit function in banks. This initiative is part of the Committee's ongoing commitment to address supervisory challenges and improve oversight by promoting sound practices within banking institutions. This new document replaces the 2001 publication titled *Internal Audit in Banks and the Supervisor's Relationship with Auditors*, reflecting advancements in supervisory practices and banking operations, while integrating lessons learned from the recent financial crisis.

1. The Committee's Principles for Enhancing Corporate Governance state that banks must have an Internal Audit function endowed with sufficient authority, stature, independence, resources, and access to the Board of Directors. Independent, competent, and qualified Internal Auditors are essential for effective Corporate Governance.
2. A robust internal control system, which includes an independent and effective Internal Audit function, is integral to sound Corporate Governance. Supervisors need to ensure that a bank's Internal Audit function effectively follows established policies and practices, and that management takes timely corrective actions in response to any weaknesses identified by Internal Auditors. The Internal Audit function plays a critical role in providing assurance to a bank's Board of Directors, senior management, and banking supervisors regarding the quality of the bank's internal control system, thereby helping to mitigate risks of loss and reputational damage.
3. This document addresses the supervisory expectations for the Internal Audit function in banking institutions, as well as the relationship between supervisory authorities and the Internal Audit function, along with the supervisory assessment of that function. The aim is to promote a strong Internal Audit function and provide guidance for its supervisory evaluation.
4. Additionally, this guidance encourages bank Internal Auditors to adhere to and contribute to the development of national and international professional standards, such as those provided by the Institute of Internal Auditors, while emphasizing the importance of considering prudential issues in the development of Internal Audit standards and practices.
5. The document mentions a management structure comprising a Board of Directors and senior management. The Committee acknowledges considerable differences in legislative and regulatory frameworks among countries, which influence the roles and functions of management and governance structures. In some jurisdictions, the Board of Directors primarily oversees the executive body, often referred to as senior management, to ensure it fulfills its responsibilities. Such a board may be termed a supervisory board, as it may not have executive functions. In contrast, in other countries, the board has a broader scope, establishing the general management

framework for the bank. Due to these variations, the terms "Board of Directors" and "senior management" are used in this document not to denote legal entities but rather to describe two distinct decision-making functions within a bank.

6. The principles outlined in this document should be implemented in alignment with the national legislation and Corporate Governance structures relevant to each country.
7. For larger and internationally active banks, an audit committee (or a similar body) typically oversees the bank's Internal Auditors. Such a committee operates within the Board of Directors. Annex 2 provides additional information regarding the responsibilities of audit committees. References to the Board of Directors in this document assume the appropriate involvement of its audit committee when applicable. Consistent with the Committee's Principles for Enhancing Corporate Governance, paragraph 50, this guidance assumes that large and internationally active banks have an audit committee or equivalent. Other banks are strongly urged to establish one.
8. This guidance is relevant to all banks, including those within a banking group, holding companies whose subsidiaries mainly consist of banks, and holding companies subject to prudential oversight with predominant bank subsidiaries. Throughout this document, these entities are collectively referred to as banks or banking organizations. The applicability of this guidance should be proportionate to the significance, complexity, and international presence of the bank (principle of proportionality).

## **2.7. Special Nature of Bank Corporate Governance**

Banks are vital in channeling capital toward productive investments. When managed efficiently and when resources are allocated to their most effective uses, banks play a significant role in driving economic growth (Levine, 2005). However, due to the intricate and opaque nature of banking operations, coupled with extensive government regulations, Corporate Governance in the banking sector functions differently than in other industries. Banks generally exhibit lower transparency compared to non-financial firms, and studies have shown that information asymmetries are more pronounced in this sector. The true value of a bank's loan portfolio can often be challenging to evaluate and may remain hidden for long periods. Moreover, banks can quickly change the risk profile of their assets; they may obscure problems by granting new loans to clients who cannot meet their existing debt obligations (Ayele, A.G., 2013).

Ayele further points out that the unique traits of banking institutions require legal safeguards for both depositors and shareholders. As a result, governments provide explicit deposit insurance and make implicit promises to bail out major banks in order to avert bankruptcies and uphold the stability of the financial system. Independent verification by auditors is critical in achieving this goal.

## **2.8 Regulatory Frame work in Ethiopia Banking Industry**

On August 11, 2008, the government enacted Proclamation No. 591/2008 to strengthen the autonomy of the National Bank of Ethiopia (NBE), clarifying its role as the regulator and supervisor of the banking sector. Despite improvements in the regulatory framework, the NBE's supervisory capacity has historically been constrained by a significant lack of qualified banking supervisors. However, in recent years, the NBE has made concerted efforts to enhance its capabilities. Consequently, public confidence in the banking sector has risen, leading to notable growth in financial intermediation, which had previously been among the lowest in Africa (Admassu, 2014).

In alignment with international standards, the Basel Committee has initiated further measures that approach banking supervision from two perspectives. First, it highlights the necessity for sector-specific "good practices" that take into account the distinct characteristics of banks. The most recent version of their guidelines features 14 principles across six areas designed to improve Corporate Governance within banks. These areas encompass supervisory board practices, the responsibilities of senior management, risk management and internal controls, compensation policies, complex corporate structures, and transparency in information disclosure (BCBS, 2010, October).

Additionally, an extension released by the BCBS in December 2011 provided guidelines for the Internal Audit function within banks, focusing on the establishment of a supervisory board and the evaluation of the Internal Audit function by supervisors. The Revised Bank Risk Management Guidelines from the NBE's Bank Supervision Directorate, published in May 2010, underscore the importance of the board and senior management in ensuring that Internal Audits continually review the systems for managing credit risk, liquidity risk, and interest rate risk.

## **2.9 Summary and Gap in the Existing Literature**

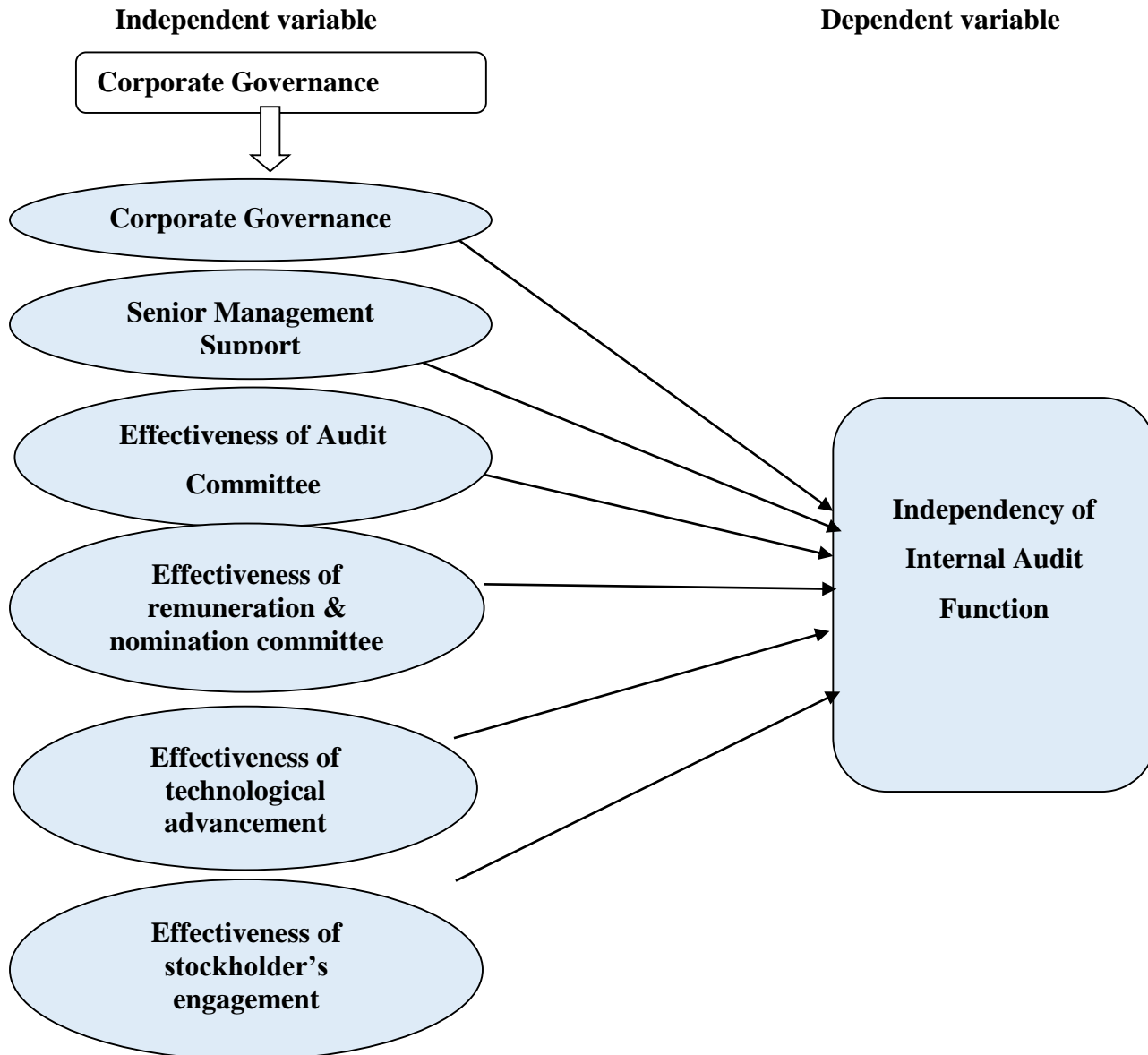
The Board of Directors is widely recognized as an essential element of Corporate Governance by regulators and governance committees worldwide (Cadbury Committee, 1992; Hibret States (US) Congress, 2002; Australian Stock Exchange Corporate Governance Council, 2003). Within this framework, the audit committee acts as a critical sub-committee that significantly improves the quality of financial reporting (McMullen et al., 1996; Davidson et al., 2005). An effective audit committee enhances the Internal Audit function by fostering an independent and supportive environment in which the Chief Internal Auditor (CIA) can raise issues that may affect management (Braiotta, 1999; Goodwin and Yeo, 2001; Goodwin, 2004). Thuweba (2014) explored various factors affecting Internal Audit independence, including limitations on scope, reporting structures, and the involvement of Internal Audits in management activities. It is recommended that Internal Audits report directly to the audit committee to improve their effectiveness.

The Basel Committee on Bank Supervision (2015) emphasizes that Internal Audits should have comprehensive responsibilities without limitations, covering aspects from electronic information management to ensuring the reliability and timeliness of regulatory reports and conducting special investigations. Numerous studies have investigated the relationship between Internal Audit independence and Corporate Governance. The Institute of Internal Auditors (IIA, 2003) notes that the ethical decisions made by Internal Auditors are shaped by the Corporate Governance framework, which delineates the interactions among four key stakeholders: the audit committee, senior management, Internal Audit, and external auditors. The effectiveness of the audit committee is vital in creating an independent support environment for the Internal Audit function and assessing its performance (Ofenoos et al., 2010).

In Ethiopia, the independence of Internal Audits within government ministries was clearly defined in a manual issued by the Ministry of Finance and Economic Development (MOFED) in 2004. A study focusing on the Ethiopian context, which included interviews with directors of Internal Audit functions, indicated that only banks and insurance companies are required by the National Bank of Ethiopia (NBE) to maintain an Internal Audit function (Terdpaopong et al., 2012). Although there are existing studies on the effectiveness of Internal Audits and their role in Corporate Governance (KPMG, 2008; Carl Gabrini, 2013) as well as factors influencing Internal Audit independence (Thuweba, 2014), empirical research specifically examining how Corporate Governance impacts the independence of Internal Audit functions remains lacking. Mesert W. (2015) illustrated the effect of Corporate Governance on Internal Audit independence by discussing key elements such as senior management support, audit committee effectiveness, Corporate Governance structure, and auditors' perceptions. However, her analysis did not incorporate aspects related to the Basel supervisory committee or the role of external auditors.

## 2.8. Conceptual Framework

The Conceptual framework between Corporate Governance Factors and The Independence of Internal Audit Function



Source: Developed from preliminary literature review/SBB/71 National Bank Directive  
*Figure 1 Conceptual Frame work*

## **CHAPTER THREE**

### **3. REASERCH METHEDODOLOGY**

#### **3.1. Description of the Study Area**

This chapter outlines the methodology that will be employed to conduct the research. It encompasses the population, sampling methods, data collection instruments, types of data gathered and their sources, administration of questionnaires, data analysis methods, as well as the scope and limitations of the study. The survey aims to evaluate how Corporate Governance factors influence the independence of the Internal Audit function in the private commercial banks of Ethiopia.

#### **3.2. Research Design**

The study will utilize an explanatory research design, supplemented by qualitative inquiry methods. Combining both quantitative and qualitative approaches provide a more comprehensive understanding of the research issues than either method could achieve on its own. This mixed-methods research will involve both the collection and analysis of quantitative and qualitative data, helping to reduce any biases that might arise from solely using one approach (Creswell, 2003, cited in Amdemikael, 2012).

#### **3.3. Research Approach**

Schweitzer (2009) points out that the quantitative method is particularly suitable for developing research questions and is well-suited for the numerical data required in this study. Thus, both qualitative and quantitative data will be utilized in this research.

#### **3.4. Population and Sampling**

##### **3.4.1. Population**

The target population for this study includes managers from the Internal Audit departments, heads of inspection and audit divisions, and risk managers from selected private banks in Ethiopia. Among the 28 private commercial banks operating in the country, the Internal Audit officers from Awash Bank, Dashen Bank, Nib International Bank, Wegagen Bank, and Hibret Bank have been identified as the target population for this research.

### 3.4.2. Sample and Sampling Technique

This research adopted a census approach for data collection, focusing on a manageable sample size of 127 respondents. According to the National Bank of Ethiopia's 2020/21 annual report, there are 28 private commercial banks, each of which has a single Internal Audit department. Structured questionnaires were distributed to all Internal Audit managers and heads of inspection and audit divisions within these banks, following standard practice. Additionally, risk managers were included as key informants due to their involvement with governance matters and their reliance on Internal Audit reports. A total of 117 questionnaires were distributed to the audit departments of various private commercial banks, while 10 questionnaires were directed at managers and desk officers within the bank supervision directorate, leading to a total of 127 questionnaires being disseminated for the collection of primary data.

**Table 3.1 category of respondent**

Bank's Name	Number of population (N)
Awash Bank	31
Dashen Bank	27
Nib International Bank	25
Wegagen Bank	24
Hibret Bank	20
Total	127

### 3.1. Data Collection Instruments

The questionnaires utilized in this study were meticulously designed and tailored to assess respondents' levels of agreement or disagreement, employing a five-point Likert scale. The ratings on this scale include: Strongly Agree, Agree, Neutral, Disagree, and Strongly Disagree. Responses of 5 or 4 indicate that the item is viewed as important,

while scores of 3 or 2 suggest that the item is considered relatively important but not essential. A score of 1 reflects that the item is deemed unimportant and may be overlooked.

The questionnaires consisted of six sections covering various topics, including general demographic information about the respondents, the independence of the Internal Audit function, the Corporate Governance framework, support from senior management, the effectiveness of the Audit Committee, the performance of the Remuneration and Nomination Committee, the impact of technological advancements, and stakeholder engagement effectiveness. These questionnaires were distributed to Internal Audit managers, risk managers, and heads of audit and inspection divisions, or their equivalents, across six private banks, totaling 127 questionnaires administered within these institutions.

### **3.2. Type of Data and Sources**

The survey primarily involved the collection of primary data through questionnaires from key informants in the private banking sector. Additionally, secondary data was incorporated from authoritative books and credible websites, including pertinent literature such as newsletters, textbooks, standards for the professional practice of Internal Auditing, and ethical guidelines from the Institute of Internal Auditors (IIA).

### **3.3. Data Analysis and Presentation**

The primary data collected from the questionnaires was summarized and analyzed using descriptive statistics, which included proportions, percentages, means, and frequency distribution tables. Data analysis was performed using the Statistical Package for the Social Sciences (SPSS Version 25). A linear regression model was employed to examine the relationship between Internal Audit independence and the level of influence of Corporate Governance factors within private commercial banks, with a significance test conducted at a 95% confidence level.

### **3.4. Model Specification**

The study adopted the following conceptual model, where the Independence of Internal Audit Function (IIAF) serves as the dependent variable, influenced by various factors: Corporate Governance Setting (CGS), Senior Management Support (SMS), Effectiveness of the Audit Committee (EAC), Effectiveness of the Remuneration and Nomination Committee (ERNC), Effectiveness of Technological Advancement (ETA), and the Effectiveness of Stakeholder Engagement (ETA) alongside Internal Audit Staff (IAS).

$$\text{IIAF} = \beta_0 + \beta_1 \text{CGS} + \beta_2 \text{SMS} + \beta_3 \text{EAC} + \beta_4 \text{ERNC} + \beta_5 \text{ETA} + \beta_6 \text{ESE} + \epsilon$$

Where;

IIAF = Independence of Internal Audit Function;

CGS = Corporate Governance Setting;

SMS = Senior Management Support;

EAC = Efficiency of Audit Committee;

ERNC= Effectiveness of Remuneration & Nomination committee

ETA= Effectiveness of Technological Advancement

ESE = Effectiveness of Stakeholders Engagement

$\epsilon$  = Error term

$\beta_0$  = Constant term

### 3.1. Reliability and Validity of the Data

The reliability of the data was assessed using parallel measures and a triangulation approach, which involved cross-checking information gathered from key informant interviews, documents, and personal observations, complemented by adequate contextual descriptions. All respondents held positions of responsibility and possessed at least a bachelor's degree, eliminating the need for translation of the interviews into their native language.

To evaluate the rationality of the questionnaire, the researcher leveraged the expertise of professionals in the study area, took into account employees' perspectives, and conducted an items validity test using the SPSS program. Consequently, the use of varied sources of information enhances both the reliability of the data and the credibility of the results (Creswell, 2012). The researcher assessed reliability through Cronbach's Alpha ( $\alpha$ ), which is an internal consistency test measuring how well the items consistently reflect the underlying construct. As shown in Table 3.1, the value of Cronbach's Alpha was found to be 0.803.

Table 3.1 Reliability Statistics

Cornbrash's Alpha	No of Items
.703	32

Source: - own survey (SPSS, 2025)

### 3.1. Ethical Considerations

The study will be conducted in accordance with ethical principles, ensuring respect for all aspects of gender, religion, and language. Proper citation practices will be followed, and respondents will be informed about the study's objectives and the intended use of their information. The findings will be reported ethically, with all gathered data treated with strict confidentiality and used exclusively for research purposes. Participants will receive sufficient information to make informed choices regarding their participation, and any ethical issues related to consent and confidentiality will be transparently addressed. The researcher is dedicated to maintaining high ethical standards, which include safeguarding the confidentiality and dignity of participants, ensuring integrity in research practices, avoiding plagiarism, and refraining from the fabrication or destruction of data.

## **CHAPTER FOUR**

### **3. DATA ANALYSIS, RESULTS AND DESCUSSION**

#### **4.1 Introduction**

This chapter centers on the analysis and interpretation of data gathered from participants, with the intent of addressing the research questions and discussing the study's findings. The research examines the impact of Corporate Governance on the independence of the Internal Audit function, particularly in private commercial banks in Ethiopia. Data was collected through questionnaires, interviews, and observations. This chapter presents an analysis of the response rate, profiles of the respondents, and an assessment of how Corporate Governance influences the independence of the Internal Audit function based on relevant measurement factors.

#### **4.2 Response Rate Analysis**

The questionnaires were distributed to auditors in private banks, with a total of 127 questionnaires sent to individuals directly involved in audit activities within their organizations. Out of the 127 distributed questionnaires, 111 were returned, while 10 were not retrieved from respondents; 6 of these were discarded due to incomplete or improperly filled responses

##### **4.2.1 Socio-Demographic Characteristics of Respondents**

This section addresses the socio-demographic characteristics of the respondents, which include their gender, age, educational background, work experience, and their respective fields of study.

**Table 4.2.1 Demographic profile of respondents**

<b>Variables (N=111)</b>	<b>Categories</b>	<b>Frequency</b>	<b>Percentage</b>
<b>1. Gender</b>	Male	88	79.3
	Female	23	20.7
	<b>Total</b>	<b>111</b>	<b>100</b>
	26 – 35	51	45.9
	36 – 45	47	42.3
<b>2. Age</b>	Above 45	13	11.7
	Total	111	100
	Diploma	1	0.9
<b>3. Educational level</b>	Degree	57	51.4
	Masters	53	47.7
	PhD	0	0
	<b>Total</b>	<b>111</b>	<b>100</b>
<b>4. Position in The organization</b>	Manager	10	9
	Audit	38	34.2
	Senior Auditor	33	29.7
	Junior Auditor	29	27
	Total	111	100
<b>5. Year of Experience</b>	1– 2years	0	0
	3-4 years	15	13.5
	Above 4	96	86.5
	Total	111	100
Work position	Manager	10	9
	Audit	38	34.2
	Senior Auditor	33	29.7
	Junior Auditor	29	27
	Total	111	100
Field of study	Accounting	99	89.2
	Management	8	7.2
	Other related field	4	3.6
	Total	111	100

Source: Questionary Results (2025)

The gender distribution of respondents reveals that there were 88 male respondents (79.3%) and 23 female respondents (20.7%). This analysis indicates that the majority of employees within the organization are male auditors, suggesting a need to increase the proportion of female auditors to achieve better gender balance.

Regarding age, the majority of respondents are relatively young. Specifically, 51 respondents (45.9%) are between the ages of 26 and 35, 47 (42.3%) are aged 36 to 45, and 13 (11.7%) are over 45 years old. The data shows that most auditors in the organization fall within the 26 to 35 age range, which could imply a more dynamic workforce capable of performing their duties effectively.

In terms of educational background, 57 respondents (51.4%) hold a Bachelor's Degree, 53 (47.7%) have a Master's Degree, and none (0%) possess a Ph.D. These results demonstrate that the respondents are well-educated, which is likely to enhance their understanding of the questions and their ability to fulfill their responsibilities effectively. Nevertheless, many participants, while degree holders, could benefit from furthering their education to become more skilled and knowledgeable auditors.

Most respondents have more than four years of work experience, with 15 (13.5%) having between 3 to 4 years of experience. Notably, there are no respondents with less than 2 years of work experience within the organization. This indicates that a significant portion of employees possess considerable experience. Among respondents, 10 (9.0%) were managers, 38 (34.2%) were auditors, 33 (29.7%) were senior auditors, and 29 (27.0%) were junior auditors. This distribution suggests that the organization employs a qualified, competent, and skilled auditing team.

In terms of fields of study, 99 respondents (89.2%) are from accounting backgrounds, 8 (7.2%) are from management, and 4 (3.6%) come from other related fields. This data indicates that the majority of auditors in the organization have academic backgrounds relevant to their profession. A degree in accounting is evidently preferred for those aspiring to be auditors, further reinforcing that most auditors within the organization have studied accounting.

**Table 4.2.2 Descriptive Statistics**

<b>Dependent Variable</b>	<b>N</b>	<b>Mean</b>	<b>Std.Deviation</b>
CGS	111	3.6865	.50713
SMS	111	3.5354	.56077
EIAC	111	3.6595	.37620
ERNC	111	3.5518	.64237
ETA	111	3.5075	.73560

SE	111	3.6577	.62152
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Table 4.2 presents the mean and standard deviation values for Corporate Governance, which were found to be 3.68 and 0.507, respectively. The mean score for senior management support was 3.53, with a standard deviation of 0.56. The effectiveness of the audit committee had a mean of 3.65 and a standard deviation of 0.37. For the effectiveness of the remuneration and nomination committee, the mean was 3.55, accompanied by a standard deviation of 0.64. The indicator for the effectiveness of technological advancement recorded a mean of 3.50 and a standard deviation of 0.73. Lastly, stakeholder engagement showed a mean of 3.65 and a standard deviation of 0.62. The results for each variable, along with their frequency and valid percentages, are detailed below.

**Table 4.2.3. Corporate Governance Setting**

No	Items	Responses	Frequency	Percent	Mean	STD.
Cs1	There are established applicable laws & regulations for carrying out audit responsibilities independently.	SD	4	3.6	3.61	.96
		D	6	5.4		
		N	39	35.1		
		A	42	37.8		
		SA	20	18.0		
		Total	111	100		
Cs2	There are standards & codes of ethics that recognize the importance of internal auditor's independence & objectivity when performing the work.	SD	4	3.6	3.77	.87
		N	34	30.6		
		A	53	47.7		
		SA	20	18.0		
		Total	111	100		
Cs3	There is a strong system of internal control that is monitored by well-resourced independent internal audit activity as a fundamental feature of corporate governance.	SD	8	7.2	3.49	1.02
		D	7	6.3		
		N	32	28.8		
		A	51	45.9		
		SA	13	11.7		
		Total	111	100		
Cs4	There is well developed Internal audit standards to guide the internal auditor relationship with management.	D	23	20.7	3.52	1.01
		Neutral	26	23.4		
		Agree	43	38.7		
		S A	19	17.1		

		Total	111	100		
Cs5	It is the responsibility of board directors to ensure The intensity of The composition's accounts and financial reports and The independence of Internal Auditors.	SD	4	3.6	3.85	.90
		Neutral	31	27.9		
		Agree	50	45.0		
		Strongly Agree	26	23.4		
		Total	111	100		

Source: Questionary results (2025)

Table 4.2.3 provides an analysis within the context of Corporate Governance, highlighting important insights regarding the independence of the Internal Audit function in private commercial banks in Ethiopia.

The first question examined whether there are established laws and regulations that allow auditors to perform their duties independently. Responses varied: 4 respondents (3.6%) strongly disagreed, 6 (5.4%) disagreed, 39 (35.1%) were neutral, 42 (37.8%) agreed, and 20 (18.0%) strongly agreed.

The second question focused on whether standards and codes of ethics recognize the necessity for Internal Auditors to maintain their independence and objectivity. In this case, 4 respondents (3.6%) strongly disagreed, while no disagreements were recorded. A total of 34 respondents (30.6%) remained neutral, 53 (47.7%) agreed, and 20 (18.0%) strongly agreed.

The third question assessed whether a robust internal control system, overseen by a well-resourced Internal Audit function, is a crucial component of Corporate Governance. Responses included 8 respondents (7.2%) who strongly disagreed, 7 (6.3%) who disagreed, 32 (28.8%) who were neutral, 51 (45.9%) who agreed, and 13 (11.7%) who strongly agreed.

The fourth question inquired about the presence of well-defined Internal Audit standards that guide the relationship with Corporate Governance. Here, 23 respondents (20.7%) disagreed, 26 (23.4%) were neutral, 43 (38.7%) agreed, and 19 (17.1%) strongly agreed.

Finally, the fifth question explored the role of board directors in ensuring the integrity of financial reporting systems and the independence of Internal Auditors. The findings indicated that 4 respondents (3.6%) strongly disagreed, while 50 (43.0%) agreed, 31 (27.9%) remained neutral, and 26 (23.4%) strongly agreed.

Overall, These findings indicate that The Corporate Governance setting (CGS) significantly influences The independence of The Internal Audit function in private commercial banks in Ethiopia.

Table 4.2.4 Senior Management support

No	Items	Responses	Frequency	Percent	Mean	Std.dev
SMS1	The independence of Internal Audits is supported by senior management.	SD	5	4.5	3.74	.89
		D	5	4.5		
		N	35	31.5		
		A	44	39.6		
		SA	22	19.8		
		Total	111	100		
SMS2	Senior management supports The Internal Audit function by recruiting competent and well-qualified staff.	D	10	9.0	3.26	1.27
		N	32	28.8		
		A	46	41.4		
		SA	23	20.7		
		Total	111	100		
SMS3	Senior management safeguards auditor independence.	SD	20	18.0	3.61	.96
		D	4	3.6		
		N	29	26.1		
		A	43	38.7		
		SA	15	13.5		
		Total	111	100		
SMS4	Senior management members are well knowledgeable, skilled & committed to improve organizational governance.	SD	4	3.6	3.47	.93
		D	6	5.4		
		N	39	35.1		
		A	42	37.8		
		SA	20	18.0		
		Total	111	100		
SMS5	Senior management is committed to supporting Internal Auditors in discharging Their responsibilities..	D	21	18.9	3.49	1.02
		N	30	27.0		
		A	47	42.3		
		SA	13	11.7		
		Total	111	100		
SMS6	Senior management has The responsibility of measuring The performance of The audit function and appointing and dismissing The heads of The Internal Audit	SD	8	7.2	3.52	1.01
		D	7	6.3		
		N	32	28.8		
		A	51	45.9		
		SA	13	11.7		

	department.	Total	111	100		
SMS7	Senior management is definitely enhancing reliable, dependable, effective and efficient corporate governance.	D	23	20.7	3.44	1.02
		N	26	23.4		
		A	43	38.7		
		SA	19	17.1		
		Total	111	100		

Source: Questionnaire results (2025)

Table 4.2.4 deals with senior management support. The independence of The Internal Audit function is significantly influenced by the support provided by senior management. In this context, responses to the first statement revealed that 5 respondents (4.5%) expressed strong disagreement or disagreement, while 35 respondents (31.5%) remained neutral. Conversely, 44 respondents (39.6%) agreed, and 22 respondents (19.8%) strongly agreed with the assertion. The second statement addressed whether senior management supports The Internal Audit function by recruiting competent and qualified staff. Here, 10 respondents (9.0%) disagreed, 32 respondents (28.8%) were neutral, while a majority of 46 respondents (41.4%) agreed, and 23 respondents (20.7%) strongly agreed. The third item focused on the extent to which senior management safeguards auditor independence. In this case, 20 respondents (18.0%) strongly disagreed, 4 respondents (3.6%) disagreed, 29 respondents (26.1%) were neutral, while 43 respondents (38.7%) agreed, and 15 respondents (13.6%) strongly agreed. The fourth statement assessed whether senior management members possess the knowledge, skills, and commitment necessary to enhance organizational governance. The results showed that 4 respondents (3.6%) strongly disagreed, 6 respondents (5.4%) disagreed, 39 respondents (35.1%) remained neutral, while 42 respondents (37.8%) agreed, and 20 respondents (18.0%) strongly agreed. The fifth item examined the commitment of senior management to support Internal Auditors in fulfilling Their responsibilities. Here, 21 respondents (18.9%) disagreed, 30 respondents (27.0%) were neutral, while 47 respondents (42.3%) agreed, and 13 respondents (11.7%) strongly agreed. The sixth statement emphasized that senior management is responsible for measuring the performance of the audit function and for appointing or dismissing heads of The Internal Audit department. In this regard, 8 respondents (7.2%) strongly disagreed, 7 respondents (6.3%) disagreed, while a significant number of 32 respondents (28.8%) agreed, and a majority of 51 respondents (45.9%) strongly agreed. Lastly, the seventh item reiterated the responsibilities of senior management regarding the performance measurement of The audit function and The appointment or dismissal of The head of The Internal Audit department. The responses indicated that 4 respondents (3.6%) strongly agreed, 23 respondents (20.7%) disagreed, 26 respondents (23.4%) were neutral, while 43 respondents (38.7%) agreed, and 19 respondents (17.1%) strongly agreed.

Overall, These findings suggest that senior management support plays a crucial role in influencing The independence of The Internal Audit function within private commercial banks in Ethiopia to a significant extent.

**Table 4.2.5 Effectiveness of internal audit committee**

NO	Item	Responses	Frequency	Percent	Mean	STD
IAC1	There is an audit committee which undertakes an independent, objective assurance and consulting activity designed to add value and improve The independency of auditors.	SD	8	7.2	3.81	.68
		D	7	6.3		
		N	32	28.8		
		A	51	45.9		
		SA	13	11.7		
		Total	111	100		
IAC2	There is an audit committee that helps the bank accomplish its objectives by bringing a systematic, disciplined approach to evaluating & improving the effectiveness of risk management control & the governance process of internal auditor.	N	38	34.2	3.52	1.00
		A	56	50.5		
		SA	17	15.3		
		Total	111	100		
IAC3	The audit committee contributes to the bank's compliance with applicable laws & regulations & facilitates the work of auditors.	D	23	20.7	3.61	.96
		N	26	23.4		
		A	43	38.7		
		SA	19	17.1		
		Total	111	100		
IAC4	The Audit committee enhance Corporate Governance structure	SD	4	3.6	3.64	.90
		D	6	5.4		
		N	39	35.1		
		A	42	37.8		
		SA	20	18.0		
		Total	111	100		
IAC5	Internal Audit effectiveness increases when The audit committee is involved in The Internal Auditor's activities.	D	13	11.7	3.49	1.02
		N	33	29.7		
		A	46	41.4		
		SA	19	17.1		
		Total	111	100		

Source: Questionnaire results (2025)

Table 4.2.5 examines the effectiveness of internal audit committee. The first statement addressed whether There is an audit committee that conducts independent, objective assurance and consulting activities aimed at enhancing the independence of auditors. In response, 8 respondents (7.2%) strongly disagreed, 7 respondents (6.3%) disagreed, 32 respondents (28.8%) remained neutral, while a majority of 51 respondents (45.9%) agreed, and 13 respondents (11.7%) strongly agreed. The second statement inquired whether the audit committee aids the bank in achieving its objectives by employing a systematic & disciplined approach to evaluate & enhance the effectiveness of risk management, control, and governance processes related to Internal Auditors. Here, 38 respondents (34.2%) indicated neutrality, while 56 respondents (50.5%) agreed, and 17 respondents (15.3%) strongly agreed. The third item focused on the role of the audit committee in ensuring The bank's compliance with relevant laws and regulations while facilitating The work of auditors. In this context, 23 respondents (20.2%) disagreed, 26 respondents (23.4%) were neutral, 43 respondents (38.7%) agreed, and 19 respondents (17.1%) strongly agreed. The fourth statement assessed whether the audit committee enhances The Corporate Governance structure. Regarding this, 4 respondents (3.6%) strongly disagreed, 6 respondents (5.4%) disagreed, 39 respondents (35.1%) were neutral, while 42 respondents (37.8%) agreed, and 20 respondents (18.0%) strongly agreed.

The fifth item explored whether the involvement of the audit committee in Internal Auditor activities increases the effectiveness of Internal Audits. In this case, 13 respondents (11.7%) disagreed, 33 respondents (29.7%) remained neutral, while 45 respondents (41.4%) agreed, and 18 respondents (17.1%) strongly agreed. Overall, these findings suggest that The effectiveness of The audit committee significantly influences The independence of The Internal Audit function within private commercial banks in Ethiopia.

**Table 4.2.6. Effectiveness of Remuneration & nomination committee**

NO	Statement	Responses	Frequency	Percent	Mean	Std.Dev
EOR1	There is an attractive payment for Internal Auditors to discharge Their responsibilities efficiently and effectively.	D	10	9.0	3.74	.89
		N	32	28.8		
		A	46	41.4		
		SA	23	20.7		
		Total	111	100		
EOR2	There is internal regulation & supervision for managing the benefits of internal auditors.	SD	18	16.2	3.33	1.28
		D	7	6.3		
		N	23	20.7		
		A	46	41.4		
		SA	17	15.3		

		Total	111	100		
EOR3	There are audits and risk subcommittees, a remuneration subcommittee, and a main board management subcommittee to follow up on & monitor internal auditor's remuneration.	D	23	20.7	3.52	.10
		N	26	23.4		
		A	43	38.7		
		SA	19	17.1		
		total	111	100		
EOR4	There is a system to align managers' and shareholders' interests, mitigating agency costs and providing a link between managerial action and The performance of Internal Auditors.	SD	4	3.6	3.61	.96
		D	6	5.4		
		N	39	35.1		
		A	42	37.8		
		SA	20	18.0		
		Total	111	100		
ENC1	There is a delegation of highly qualified managerial personnel who are able to monitor, support, & follow up with the internal auditors.	D	10	9.0	3.74	.89
		N	32	28.8		
		A	46	41.4		
ENC2	The assigned personnel have a better position and can timely address the critical problem of the independence of internal auditors.	SA	23	20.7	3.61	1.28
		Total	111	100		
		SD	4	3.6		
		D	6	5.4		
		N	39	35.1		
		A	42	37.8		
ENC3	Frequent meeting create & strength cohesive boards among directors.	SA	20	18.0	3.63	.90
		Total	111	100		
		D	14	12.6		
		N	31	27.9		
		A	48	43.2		
		SA	18	16.2		
		Total	111	100		

Source: Questionnaire results (2025)

Table 4.2.6 examines the effectiveness of remuneration in the context of internal auditing, summarizing findings based on various statements aimed at assessing respondents' perceptions.

The first statement assessed whether attractive compensation for Internal Auditors enables them to effectively fulfill their responsibilities. In this case, 10 respondents (9.0%) disagreed, 32 (28.8%) were neutral, while a majority of 46 (41.4%) agreed, and 23 (20.7%) strongly agreed.

The second statement explored the existence of internal regulations and oversight concerning the management of benefits for Internal Auditors. Here, 18 respondents (16.2%) strongly disagreed, 7 (6.3%) disagreed, 23 (20.7%) were neutral, 46 (41.4%) agreed, and 17 (15.3%) strongly agreed.

The third item evaluated whether there are audits and risk sub-committees, as well as a remuneration sub-committee, dedicated to monitoring and reviewing the remuneration of Internal Auditors. In this case, 23 respondents (20.7%) disagreed, 26 (23.4%) remained neutral, while 43 (38.7%) agreed, and 19 (17.0%) strongly agreed.

The fourth statement assessed whether a system is in place to align the interests of managers and shareholders, thereby reducing agency costs and linking managerial actions to the performance of Internal Auditors. Responses indicated that 4 respondents (3.6%) strongly disagreed, 6 (5.4%) disagreed, 39 (35.1%) were neutral, 42 (37.8%) agreed, and 20 (18.0%) strongly agreed. These findings highlight the significant influence of the effectiveness of the remuneration committee (ERC) on the independence of the Internal Audit function in private commercial banks in Ethiopia.

In contrast, the effectiveness of the nomination committee was also assessed. The first item considered whether there is a delegation of highly qualified managerial personnel capable of monitoring, supporting, and following up with Internal Auditors. In response, 10 respondents (9.0%) disagreed, 32 (28.8%) were neutral, while 46 (41.4%) agreed, and 23 (20.7%) strongly agreed.

The second statement examined whether the assigned personnel occupy positions that enable them to promptly address critical issues affecting the independence of Internal Auditors. Here, 4 respondents (3.6%) strongly disagreed, 6 (5.4%) disagreed, 39 (35.1%) were neutral, 42 (37.8%) agreed, and 20 (18.0%) strongly agreed.

The third item considered whether frequent meetings foster greater cohesion among board directors. In this context, 14 respondents (12.6%) disagreed, 31 (27.9%) were neutral, while 48 (43.2%) agreed, and 18 (16.2%) strongly agreed. Overall, these results suggest that the effectiveness of the nomination committee (ENC) significantly impacts the independence of the Internal Audit function in private commercial banks in Ethiopia.

#### Table 4.2.7 Qualification & Competency

NO	Statements		Frequency	Percent	Mean	Stan Dev.
QC1	Board directors were qualified at education qualifications of the board directors help them to make decisions.	SD	16	14.4	3.18	1.2
		D	16	14.4		
		N	24	21.6		
		A	42	37.8		
		SA	13	11.7		
		Total	111	100		
QC2	The qualification of the board directors help to create diverse perspective to make a decision.	SD	8	7.2	3.49	1.0
		D	7	6.3		
		N	32	28.8		
		A	51	45.9		
		SA	13	11.7		
		Total	111	100		
QC3	Director's qualifications are central to effectively interpreting & utilizing the information generated by management.	SD	2	1.8	3.31	1.00
		D	27	24.3		
		N	28	25.2		
		A	43	38.7		
		SA	11	9.9		
		Total	111	100.0		
QC4	The directors are well qualified, innovative, creative, and produce better strategies for decision-making	D	13	11.7	3.59	.82
		N	30	27.0		
		A	57	51.4		
		SA	11	9.9		
		Total	111	100.0		
		Total	111	100		

Source: Questionnaire results (2025)

Table 4.2.7 highlights the importance of the qualifications and competencies of board directors in the decision-making processes. The first item assessed whether the educational qualifications of board directors contribute to effective decision-making. In this context, 16 respondents (14.4%) disagreed (including those who strongly disagreed), while 24 respondents (21.6%) remained neutral. A majority of 42 respondents (37.8%) agreed, and 13 respondents (11.7%) strongly agreed.

The second item evaluated if the qualifications of board directors promote diverse perspectives in decision-making. Here, 8 respondents (7.2%) strongly disagreed, and 7 respondents (6.3%) disagreed, while a notable 32 respondents (28.8%) were neutral. Conversely, 51 respondents (43.9%) agreed, and 13 respondents (11.7%) strongly concurred.

The third item focused on the role of directors' qualifications in effectively interpreting and utilizing information provided by management. Responses included 2 respondents (1.8%) who strongly disagreed, 27 (24.3%) who disagreed, and 28 (25.2%) who were neutral. Additionally, 43 respondents (38.7%) agreed, while 11 respondents (9.9%) strongly agreed.

The fourth item assessed whether directors are well-qualified, innovative, and capable of formulating effective strategies for decision-making. In this instance, 13 respondents (11.7%) disagreed, 30 (27.0%) were neutral, while a substantial 57 respondents (51.4%) agreed, and 11 respondents (9.9%) strongly agreed.

Overall, these findings suggest that the qualifications and competencies of board directors have a significant impact on the independence of the Internal Audit function within private commercial banks in Ethiopia.

Table 4.2.8 Independency of Internal Audit Function

NO	Statement		Frequency	Percent	Mean	Stan Dev.
IIAF1	Auditor independence is a cornerstone of the independence of internal audit function.	D	10	9.0	3.54	.84
		N	32	28.8		
		A	46	41.4		
		SA	23	20.7		
		Total	111	100		
IIAF2	Management's perception of internal auditors has an impact on the effectiveness of their function.	SD	8	7.2	3.49	1.02
		D	7	6.3		
		N	32	28.8		
		A	51	45.9		
		SA	13	11.7		
		Total	111	100		
IIAF3	Internal Audit independence exceeds all The factors that affect an organization's operation	D	23	20.7	3.52	1.00
		N	26	23.4		
		A	43	38.7		
		SA	19	17.1		
		Total	111	100.0		
IIAF4	Adequate & competent internal audit staff placement is vital in any organization.	SD	4	3.6	3.11	.96
		D	6	5.4		
		N	39	35.1		
		A	42	37.8		
		SA	20	18.0		
		Total	111	100.0		

Source: Questionnaire results (2025)

Table 4.2.8 emphasizes that auditor independence is crucial for the effectiveness of the Internal Audit function. In this context, 10 respondents (9.0%) disagreed with the statement, while 32 respondents (28.8%) were neutral. A majority, 46 respondents (41.4%), agreed, and 23 respondents (20.7%) strongly agreed.

The second item evaluated management's perception of the Internal Auditor's role and its subsequent effect on the effectiveness of the Internal Audit function. In this case, 8 respondents (7.2%) strongly disagreed, and 7 respondents (6.3%) disagreed. A notable 32 respondents (28.8%) remained neutral, while a significant 51 respondents (43.9%) agreed, and 13 respondents (11.7%) strongly concurred.

The third item assessed whether Internal Audit independence is the most critical factor influencing an organization's operations. In response, 23 respondents (20.7%) disagreed, 26 respondents (23.4%) were neutral, while 43 respondents (35.7%) agreed, and 19 respondents (17.1%) strongly agreed.

The fourth item focused on the necessity of having adequate and competent Internal Audit staff in any organization. Here, 4 respondents (3.6%) strongly disagreed, and 6 respondents (5.4%) disagreed. A significant number, 39 respondents (35.1%), remained neutral, while 42 respondents (37.8%) agreed, and 20 respondents (18.0%) strongly agreed.

Overall, these findings highlight the critical role of auditor independence and management perceptions in enhancing the effectiveness of the Internal Audit function within organizations.

#### **4.3.1. Correlation Analysis**

The study aimed to identify the relationship between independent and dependent variables. To accomplish this, Pearson Correlation analysis was employed at a 95% confidence level ( $\alpha = 0.05$ ). Correlation analysis is a widely used method in research for assessing the relationship between two distinct variables, determining the significance and strength of their association. This approach effectively summarizes these relationships with a single value that ranges from -1 to +1.

A correlation analysis utilizing Pearson's correlation coefficient ( $r$ ) was performed on all variables included in this study to investigate their interrelationships. The correlation coefficient  $r$  serves as a statistical measure of the degree or strength of this relationship. As noted by Pallant (2003), a perfect positive correlation is indicated by  $r = 1.00$ , while a perfect negative correlation is indicated by  $r = -1.00$ . If  $r = 0.00$ , it suggests no correlation exists; a weak relationship is

indicated by r values between 0.10 and 0.29, or between -0.10 and -0.29. A moderate association is present when r values range from 0.30 to 0.49 or -0.30 to -0.49, while a high correlation is identified when r values are between 0.50 and 1.00 or -0.50 and -1.00. The results will be interpreted and discussed based on these criteria for each dependent and independent variable, with findings presented as follows.

**Table 4.3.1 Correlation**

		<b>Correlations</b>						
		CGS	SMS	EAC	ERC	ENC	QC	IIF
Corporate Governance setting	Pearson Correlation	1						
	Sig. (2-tailed)							
Senior Management support	Pearson Correlation	.763**	1					
	Sig. (2-tailed)	.000						
	N	111	111					
Effectiveness of Audit committee	Pearson Correlation	.731**	.713**	1				
	Sig. (2-tailed)	.000	.000					
	N	111	111	111				
Effectiveness of Remuneration & Nomination committee	Pearson Correlation	.589**	.659**	.676**	1			
	Sig. (2-tailed)	.000	.000	.000				
	N	111	111	111				
Effectiveness of Technological advancement	Pearson Correlation	.456**	.616**	.557**	.739**	1		
	Sig. (2-tailed)	.009	.000	.000	.000			
	N	111	111	111	111	111		
Stakeholder's engagement	Pearson Correlation	.549**	.581**	.602**	.537**	.402**	1	
	Sig. (2-tailed)	.000	.000	.039	.000	.000		

	N	111	111	111	111	111	111	
Independency of Internal Audit function	Pearson Correlation	.762**	.798**	.823**	.855**	.773**	.645**	1
	Sig. (2-tailed)	.000	.000	.000	.000	.000	.000	
	N	111	111	111	111	111	111	111
**. Correlation is significant at The 0.01 level (2-tailed).								

Source: Questionnaire results (2025)

There exists a positive and statistically significant relationship between the Corporate Governance setting and the independence of the Internal Audit function, with a correlation coefficient of  $r = 0.613$  and  $p < 0.01$ . Similarly, there is a positive and statistically significant association between Senior Management support and the independence of the Internal Audit function, represented by  $r = 0.440$  and  $p < 0.01$ . Additionally, the correlation between the Effectiveness of the Audit Committee and the independence of the Internal Audit function is also positive and statistically significant, with  $r = 0.626$  and  $p < 0.01$ . The relationship between the Effectiveness of the Remuneration & Nomination Committee and the independence of the Internal Audit function is notably strong, showing a correlation of  $r = 0.895$  and  $p < 0.01$ . Furthermore, there is a positive and statistically significant correlation between the Effectiveness of Technological Advancement and the independence of the Internal Audit function, indicated by  $r = 0.708$  and  $p < 0.01$ . Lastly, a significant positive relationship is found between Stakeholders Engagement and the independence of the Internal Audit function, with  $r = 0.825$  and  $p < 0.01$ .

#### 4.4. Diagnostic Test

##### 4.4.1 Multicollinearity

The multicollinearity test for a regression model is essential for detecting the presence of highly correlated variables. In cases where data reflect the outcomes of uncontrolled experiments, variables may change together in predictable patterns. When multiple variables are involved, these issues are referred to as collinearity or multicollinearity (Hair et al., 1998). As multicollinearity increases, interpreting the variables becomes more complex, making it difficult to ascertain the effect of any single variable due to their interrelationships.

According to Hair et al. (1998), caution is advisable when considering the inclusion of two variables that show a bivariate correlation of 0.95 or higher. In our study, the correlations between independent variables are all below 0.95, indicating that multicollinearity is not an issue. Consequently, regression analysis can be conducted without concern.

#### 4.4.2. Multicollinearity Testing using VIF

Variance Inflation Factor (VIF) can be calculated using the formula  $VIF = 1 / (1 - R^2)$ . The tolerance of a variable is expressed as  $1 - R^2$ . If the tolerance value is low, it suggests that the variable is nearly a perfect linear combination of the independent variables already included in the equation, and thus should not be incorporated into the regression model. Further investigation is warranted if the tolerance value falls below 0.1. The table below shows that the VIF values are all below 10, and the tolerance values exceed 0.1, indicating that there is no multicollinearity issue among the independent variables.

**Table 4.4.1. Multi collinearity test**

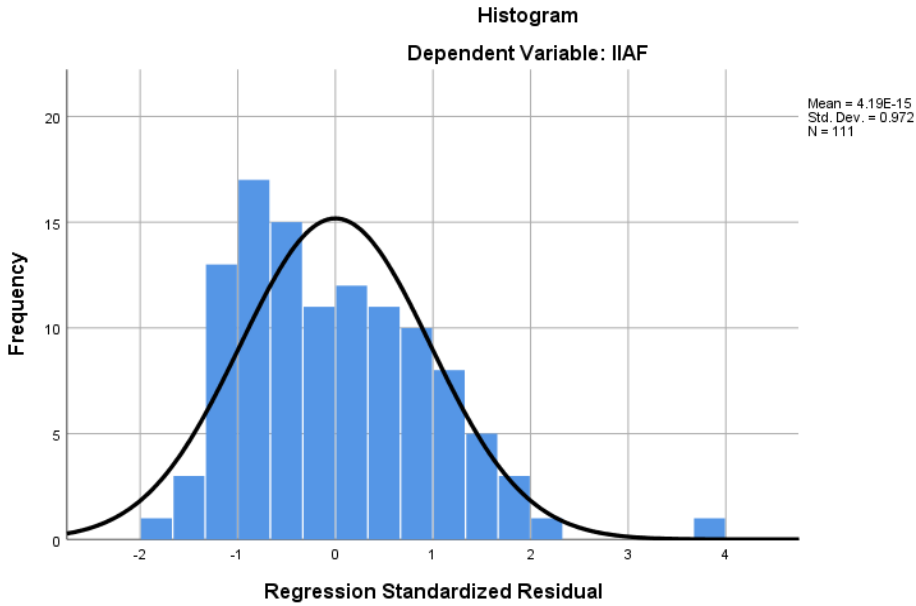
Model		Collinearity Statistics	
		t	VIF
1	(Constant)		
	CGS	0.335	2.981
	SMS	0.3	3.337
	EIAC	0.338	2.956
	ERNC	0.331	3.023
	ETA	0.409	2.443
	SE	0.572	1.749

(Source: Survey data analysis, 2025)

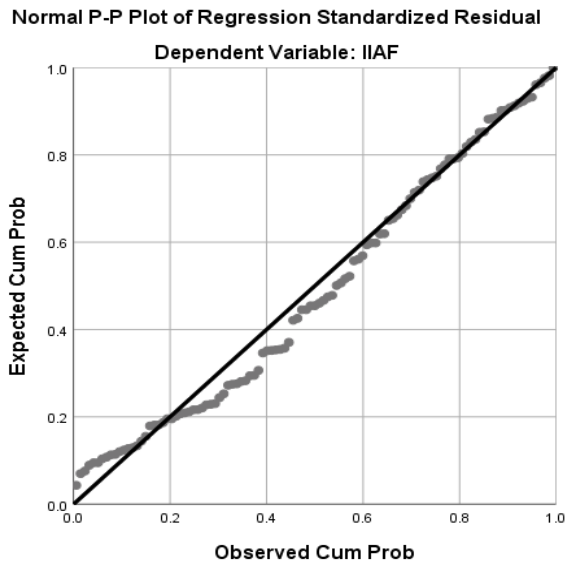
#### 4.4.3. Normality Test

A number of tests can be run to determine whether a data set is normal. Visual examination of the histogram in Figure 3 validated this study. The histogram should have a bell shape if the residual is regularly distributed. Additionally, the bell-shaped points in the image below show that the model is free of the normality problem.

**Figure 2 Normality Test**



*Figure 3. Linearity Test*



#### 4.4.4. Test for model

The researcher employed the ANOVA test to assess the assumption of linearity. This test is beneficial for comparing group means and evaluating variance estimates to determine whether the means of different groups are identical. Additionally, the ANOVA test can be utilized to calculate both linear and non-linear components between a pair of

variables. If the estimated probability value for the non-linear component is found to be less than 0.05, it indicates significant non-linearity.

**Table 4.4.2 ANOVA**

ANOVA <sup>a</sup>						
Model		Sum of Square	df	Mean Square	F	Sig.
1	Regression	41.069	6	6.845	171.341	.000 <sup>b</sup>
	Residual	4.155	104	0.04		
	Total	45.224	110			

Source: Questionnaire results (2025)

**4.4.5. Tests of Independence (Autocorrelation)**

The independence of error terms was assessed using The Durbin- Watson test that implies the observations are independent. The Durbin Watson model assures the residuals of the model are not auto correlated. DW values from 1.5 to 2.5 reflect independent observations (Kinuya, 2015)

**Table 4.4.3. Test for independence**

Model Summary					
Model	R	R Square	Adjusted R Square	Std. error of the Estimate	Durbin-Watson
1	.953 <sup>a</sup>	0.908	0.903	0.19987	2.409
a. Predictors: (Constant), QC, ENC, CGS, EIAC, ERC, SMS					
b. Dependent Variable: IIAF					

**4.5. Regression Analysis**

The study aimed to determine how independent variables impact dependent variables through multiple linear regression analysis. The regression model used in the analysis was:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + \epsilon$$

In this model, Y represents the independence of the Internal Audit function,  $\beta_0$  denotes the regression constant, and  $\beta_1$  through  $\beta_6$  are the regression coefficients. The independent variables are defined as follows: X1 is the Corporate Governance setting, X2 is Senior Management support, X3 is the Effectiveness of the Audit Committee, X4 is the Effectiveness of the Remuneration and Nomination Committee, X5 is the Effectiveness of Technological Advancement, and X6 is Stakeholder Engagement. Lastly,  $\varepsilon$  signifies the error term of the model.

**Table 4.1.5 Model Summaries**

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of Estimate
1	.953 <sup>a</sup>	.908	.903	.19987
a. Predictors: (Constant), Corporate Governance Setting, Effectiveness of Audit Committee, Senior Management Support, Effectiveness of Remuneration, Effectiveness of Nomination Committee, Effectiveness of Technological Advancement, Effectiveness of Stakeholders Engagement				
b. Dependent Variable: Independency of Internal Audit Function				

Source: Questionnaire results (2025)

Table 4.5.1 indicates that the adjusted R-squared value (coefficient of determination) was 0.908, suggesting that 90.8% of the variation in the independence of the Internal Audit function (IIAF) can be attributed to changes in the Corporate Governance setting (CGS), senior management support (SMS), the Effectiveness of the Audit Committee (EAC), the Effectiveness of the Remuneration and Nomination Committee (ERNC), the Effectiveness of Technological Advancement (ETA), and Stakeholder Engagement (SE).

Additionally, the study found a strong relationship between the independence of the Internal Audit function (IIAF) and the aforementioned factors, evidenced by a correlation coefficient of 0.953.

**Table 4.5.2 Coefficients**

Coefficients <sup>a</sup>						
Model		Unstandardized Coefficient		Standardized Coefficient	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.1.044	.162		-6.462	.000
	Corporate Governance Setting	.229	.062	.189	3.678	.000

Senior Management support	.103	.062	.090	1.657	.100
Effectiveness of Audit committee	.322	.073	.225	4.408	.000
Effectiveness of Remuneration & Nomination committee	.300	.052	.300	5.809	.000
Effectiveness Technological advancement	.249	.047	.247	5.307	.000
Stakeholder's engagement	.087	.037	.093	2.360	.020
R <sup>2</sup> – 908					
a. Dependent Variable: independency of Internal Audit function					

Source: Questionnaire results (2025)

The regression Equation was Thus, from The above finding The equation would be

$$Y = -1.044 + .229X_1 + .322X_3 + .300X_4 + .249X_5 + .087X_6$$

According to the findings, if the Corporate Governance setting, Effectiveness of the Audit Committee, Senior Management support, Effectiveness of the Remuneration and Nomination Committee, Effectiveness of Technological Advancement, and Stakeholder Engagement are all held constant at zero, the independence of the Internal Audit function would be -1.044.

A unit increase in the Corporate Governance setting would result in a 0.229 increase in the independence of the Internal Audit function. Likewise, a unit increase in Senior Management support would lead to a 0.103 increase in that independence. An increase of one unit in the Effectiveness of the Audit Committee would correspond to a 0.322 rise in the independence of the Internal Audit function. Similarly, a unit increase in the Effectiveness of the Remuneration and Nomination Committee would yield a 0.300 increase, while a unit increase in the Effectiveness of Technological Advancement would cause a 0.249 rise in the independence of the Internal Audit function. Finally, a unit increase in Stakeholder Engagement would lead to a 0.087 increase in the effectiveness of the Internal Audit function's independence.

**Table 4.5.3 ANOVA**

<b>ANOVA<sup>a</sup></b>
--------------------------

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	41.069	6	6.845	171.341	.000 <sup>b</sup>
	Residual	4.155	104	.047		
	Total	45.224	110			
a. Dependent Variable: Effectiveness of Internal Audit Function						
b. Predictors: (Constant), Corporate Governance Setting, Effectiveness of Audit Committee, Senior Management Support, Effectiveness of Remuneration, Effectiveness of Nomination Committee, Effectiveness of Technological Advancement, Effectiveness of Stakeholders Engagement						

Source: Questionnaire results (2025)

Table 4.5.3 presents the results of the ANOVA analysis, which revealed an F-value of 171.341, significantly greater than 0.000. Additionally, the p-value was 0.000, indicating it is less than 0.05. Thus, the model is considered significant.

### 4.3.3 Hypothesis Testing

Following the data analysis and the application of correlation and regression methods, the researcher conducted further tests to evaluate the hypotheses developed. The hypotheses are as follows:

#### **Hypothesis I: Corporate Governance Setting**

The computed t-value for Corporate Governance setting (CGS) is 3.678, while the critical value at the 0.05 confidence level supports rejecting the null hypothesis. This leads to the acceptance of the alternative hypothesis, indicating that Corporate Governance settings (CGS) in private commercial banks in Ethiopia significantly impact the independence of the Internal Audit function.

#### **Hypothesis II: Senior Management Support**

The calculated t-value for Senior Management Support (SMS) is 1.657, with the critical value at the 0.05 confidence level. Consequently, this results in accepting the null hypothesis and rejecting the alternative hypothesis, suggesting that Senior Management Support (SMS) does not significantly affect the independence of the Internal Audit function in private commercial banks in Ethiopia.

#### **Hypothesis III: Effectiveness of Audit Committee**

The t-value for the Effectiveness of the Audit Committee (EAC) is 4.408, and the critical value falls at the 0.05 confidence level. Therefore, this test leads to the rejection of the null hypothesis and the acceptance of the alternative hypothesis, indicating that the effectiveness of the Audit Committee (EAC) in private commercial banks in Ethiopia affects the independence of the Internal Audit function.

#### **Hypothesis IV: Effectiveness of Remuneration & Nomination Committee**

The computed t-value for the Effectiveness of the Remuneration and Nomination Committee (ERNC) is 5.809, with the critical value at the 0.05 confidence level. Accordingly, this leads to the rejection of the null hypothesis and acceptance of the alternative hypothesis, confirming that the effectiveness of the Remuneration and Nomination Committee (ERNC) in private commercial banks in Ethiopia significantly impacts the independence of the Internal Audit function.

#### **Hypothesis V: Effectiveness of Technological Advancement**

The t-value for the Effectiveness of Technological Advancement (ETA) is 5.307, while the critical value is determined at the 0.05 confidence level. Thus, this results in the rejection of the null hypothesis and acceptance of the alternative hypothesis, suggesting that the effectiveness of Technological Advancement (ETA) in private commercial banks in Ethiopia affects the independence of the Internal Audit function.

#### **Hypothesis VI: Stakeholder Engagement**

The calculated t-value for Stakeholder Engagement (SE) is 2.360, with the critical value at the 0.05 confidence level. This leads to the rejection of the null hypothesis and acceptance of the alternative hypothesis, indicating that Stakeholder Engagement (SE) in private commercial banks in Ethiopia significantly impacts the independence of the Internal Audit function.

#### **4.3.4 Interview results with Bank Management**

In addition to The regression analysis, this study incorporates qualitative insights from interviews conducted with selected six private bank management, Awash Bank., Dashen Bank, Bank of Abyssinia, Wegagen Bank, Hibret Bank, and Nib International Bank. Their perspectives provide a deeper understanding of the effect of Corporate Governance on the Independence of Internal Audit Function in private commercial Banks in Addis Ababa help reinforce findings from The quantitative analysis as follows; -

- They believe that strong Corporate Governance frameworks contribute to better organizational performance and accountability by establishing clear reporting lines, ensuring the independence of audit functions, and effectively assessing internal controls.
- Most of the interviewee believe that Senior management support are more likely to be experienced than inexperienced ones, and therefore that they have a greater ability to help The Internal Audit department independency by sharing Their experience & guidance to younger audit managers.
- The other is as the interviewees explained the audit committee is critical to provide unbiased assessments of internal control & Governance process while maintaining Internal Audit Independence, transparency, and a culture of ethics by providing and developing necessary resources.
- The interviewee underlined that The Remuneration and Nomination Committee is a key part of the corporate governance structure, it primarily focuses on overseeing executive compensation and ensuring effective succession planning. If the internal audit function does not gain the compensation or other benefits it deserves, it may be exposed to undue influence that could compromise its independence.
- They believe that Technological advancements are enhancing data analytics, ensuring secure data access, and providing flexible audit options that keep pace with the times. They believe that by facilitating continuous skill development and strengthening the independence of the Internal Audit Function, Internal Auditors will be able to more easily identify and effectively assess risks and create proactive prevention capabilities.
- Finally, most audit professionals believe that The Internal Audit function should be strengthened to enhance transparency, strengthen internal controls, and empower the audit committee. They believe that stockholder's engagement is crucial to fostering an audit culture and building strong Internal Audit governance within The organization to uphold audit ethics.

### **The linkage of qualitative & quantitative Results**

#### **Hypothesis I: Corporate Governance Setting**

The quantitative analysis revealed a statistically significant relationship between Corporate Governance Settings (CGS) and the independence of the Internal Audit function, as indicated by a t-value that supports rejecting the null hypothesis. This conclusion is further backed by qualitative insights from bank management, who assert that strong Corporate Governance frameworks enhance accountability and the effectiveness of audit functions. Together, these analyses highlight the crucial role of robust governance structures in fostering audit independence.

## **Hypothesis II: Senior Management Support**

While the quantitative results suggested no significant impact of Senior Management Support (SMS) on Internal Audit independence, qualitative feedback from interviewees presents a different perspective. Many managers indicated that experienced senior leaders are better positioned to offer guidance and support to the Internal Audit department, thereby enhancing its independence. This discrepancy points to the potential influence of context-specific managerial behaviors that may not be fully captured through quantitative measures.

## **Hypothesis III: Effectiveness of Audit Committee**

The analysis demonstrated a strong positive effect of the Effectiveness of the Audit Committee (EAC) on audit independence, leading to the rejection of the null hypothesis. Qualitative responses corroborate this finding, as interviewees emphasized the committee's essential role in providing impartial assessments and maintaining transparency within governance processes. Together, these findings affirm the critical importance of audit committee effectiveness in promoting autonomy within Internal Audit functions.

## **Hypothesis IV: Effectiveness of Remuneration & Nomination Committee**

The quantitative analysis indicated a significant effect of the Effectiveness of the Remuneration and Nomination Committee (ERNC) on Internal Audit independence. Insights from bank management reinforced this finding, highlighting that equitable compensation is vital for ensuring unbiased oversight. This correlation suggests that the effectiveness of this committee can directly impact the independence and integrity of the Internal Audit function.

## **Hypothesis V: Effectiveness of Technological Advancement**

Quantitative findings demonstrated that the Effectiveness of Technological Advancement (ETA) significantly enhances Internal Audit independence, a conclusion further supported by qualitative comments regarding technology's role in improving audit processes. Interviewees noted that advancements in technology facilitate ongoing skill development and proactive risk assessments, which in turn strengthen the independence of the Internal Audit function. This synergy illustrates the complementary relationship between technology and audit effectiveness.

## **Hypothesis VI: Stakeholder Engagement**

The t-value analysis indicated a significant effect of Stakeholder Engagement (SE) on Internal Audit independence. Qualitative feedback affirmed this view, with professionals underscoring the importance of stakeholder involvement in fostering a culture of transparency and effective governance. Both quantitative and qualitative insights suggest that active stakeholder engagement is essential for maintaining ethical standards and enhancing Internal Audit practices.

## **4.6 Discussion**

As highlighted by Bhavik M. (2012), Corporate Governance encompasses a wide array of topics, and its definitions and effective practices are influenced by various factors such as the economic scale, legal and regulatory differences, institutional frameworks, capital market status, and stakeholder perceptions. Despite these differences, the fundamental importance and meaning of Corporate Governance are consistent on a global scale.

The definitions and principles of Corporate Governance defined by the Organization for Economic Cooperation and Development (OECD) have received widespread acceptance from numerous countries and multinational organizations, including the World Bank Group, the United Nations, the Basel Committee for Banking Supervision, the International Organization of Securities Commissions (IOSCO), the Asian Development Bank, and the Islamic Financial Services Board. The significance of Internal Audit independence is further emphasized by the growing demand for credible and high-quality services across organizations, along with the rapid growth of its professional body, the Institute of Internal Auditors (IIA). However, there is a scarcity of research focusing on this function and its connection to Corporate Governance.

This study aimed to investigate the extent to which Corporate Governance affects the independence of the Internal Audit function within private commercial banks in Ethiopia. Data were collected from 111 respondents across six private commercial banks.

### **4.6.1 Descriptive Analysis**

The study utilized a census methodology involving Internal Audit managers, heads of inspection and audit divisions, and designated officers and managers as specified in the research methodology. The descriptive statistics reveal that the study encompassed a balanced representation of both male and female genders, avoiding gender bias and focusing solely on the job positions held in six private commercial banks in Ethiopia.

### **4.6.2 Regression Analysis and Hypothesis Testing**

From the regression analysis presented in Table 4.5.1, the adjusted R-squared value (coefficient of determination) was found to be 0.903, indicating that 90.3% of the variation in the dependent variable, independence of the Internal Audit function (IIAF), is attributable to changes in the following independent variables: Corporate Governance setting (CGS), senior management support (SMS), effectiveness of the audit committee (EAC), effectiveness of the remuneration and nomination committee (ERNC), effectiveness of technological advancement (ETA), and stakeholder engagement (SE). Although the model is based on a limited number of variables, it demonstrates a high explanatory power, accounting for 90.3% of the variance, while the remaining 9.7% is attributable to factors not considered by the researcher.

Both the overall F-test for significance and individual significance tests indicated a strong causal relationship between the dependent variable, independence of the Internal Audit function, and the various Corporate Governance factors.

Though there are no strict guidelines on what VIF value should prompt concern, Myers (1990) suggests that a value of 10 is a threshold for caution. If the VIF exceeds 10, it may indicate multicollinearity that could skew the regression model (Bowerman & O'Connell, 1990). The tolerance statistic, being the reciprocal of VIF ( $1/VIF$ ), should also remain above 10.

The data analysis revealed a positive linear relationship between the dependent variable, Independence of the Internal Audit function (IIAF), and the independent variables, namely Corporate Governance setting (CGS), senior management support (SMS), effectiveness of the audit committee (EAC), effectiveness of the remuneration and nomination committee (ERNC), effectiveness of technological advancement (ETA), and stakeholder engagement (SE).

### **4.6.3 Alignment of Major Findings with Previous Studies**

Numerous studies have produced findings that resonate with the conclusions of this research. For example, Abdul et al. (2014) determined that Corporate Governance significantly affects the independence of the Internal Audit function. Extensive research has explored the relationship between Corporate Governance and Internal Audit independence, uncovering significant correlations between the characteristics of the audit function and those of Corporate Governance. Specifically, the traits of both the audit committee and management play a substantial role in enhancing the overall quality of Internal Auditing and its specific features. Ensuring a high level of independence and expertise within the audit department is crucial for improving the quality of Corporate Governance and the effectiveness of both the audit and Internal Audit functions in promoting governance standards.

Additionally, Meseret (2015) confirmed a strong positive correlation between the independence of the Internal Audit function in private commercial banks and various Corporate Governance factors, including Corporate Governance

setting (CGS), senior management support (SMS), effectiveness of the audit committee (EAC), and perceptions of Internal Audit independence (POI). The findings of this study not only support previous research but also contribute to a deeper understanding of this significant topic.

## **CHAPTER FIVE**

### **5. CONCLUSION AND RECOMMENDATIONS**

#### **5.1 Conclusions**

Internal Audit plays a vital role in the success of an organization; the presence of an effective Internal Audit function is essential. Organizations with a robust Internal Audit capability can detect fraud more efficiently than those lacking such a function. Recognizing this aspect, the study identified key factors that influence Corporate Governance and the independence of Internal Auditors.

The findings regarding Corporate Governance settings indicate that applicable laws and regulations are in place to ensure auditors can perform their responsibilities independently. Standards and ethical codes emphasize the necessity for Internal Auditors to maintain their independence and objectivity during their work. A strong internal control system, regularly monitored by a well-resourced independent Internal Audit activity, is fundamental to effective Corporate Governance. Established Internal Audit standards guide the relationship with Corporate Governance and hold board directors responsible for ensuring the accuracy of financial reports and the autonomy of Internal Auditors.

Regarding the effectiveness of the Internal Audit committee, the presence of an independent audit committee provides objective assurance and consulting activities aimed at adding value and enhancing audit independence. This committee supports the bank in achieving its objectives by systematically evaluating and improving the management of risk controls and governance processes. Furthermore, the audit committee aids the bank's compliance with relevant laws and facilitates auditors' operations, while Internal Audit effectiveness is heightened when the audit committee is actively involved in Internal Audit activities.

On the aspect of the effectiveness of the remuneration and nomination committee, fair compensation for Internal Auditors is ensured through internal regulations and supervision. Various subcommittees—such as audits and risk, remuneration, and main board management—monitor and manage the remuneration of Internal Auditors. This subcommittee helps align the interests of managers and shareholders, reducing agency costs and linking managerial actions to the performance of Internal Auditors. Management properly acknowledges audit findings as essential tools for assessing current financial performance and internal control mechanisms.

In terms of the effectiveness of the nomination committee, there is a delegation of highly qualified managerial personnel capable of monitoring, supporting, and following up with Internal Auditors. These qualified personnel are in a better position to promptly address critical issues regarding the independence of Internal Auditors. Consultative workshops and meetings are regularly organized, inviting representatives who can manage the discussions, provide refreshments, and handle the payment of Internal Auditors.

Technological advancements significantly enhance the Internal Audit function by enabling advanced data analysis to swiftly identify trends and risks, automating routine tasks for improved efficiency, and facilitating real-time control monitoring. Sophisticated risk assessment tools offer data-driven insights for prioritization, and dynamic reporting improves communication with stakeholders. Collaborative platforms streamline interactions between audit teams and management, while enhanced cybersecurity measures safeguard sensitive data. Additionally, technology supports remote auditing, increasing flexibility and access to expertise. These advancements collectively make Internal Audits more effective, efficient, and aligned with organizational objectives.

The study findings indicate that stakeholder engagement plays a significant role in enhancing the Internal Audit function by providing valuable insights into organizational risks, ensuring alignment with goals, and fostering trust through open communication. This engagement leads to a greater acceptance of audit recommendations, improved decision-making, and a culture of accountability and continuous improvement. Furthermore, stakeholders can help

identify blind spots that auditors might overlook, ultimately strengthening the audit process and leading to more favorable organizational outcomes.

## **5.2 Recommendations**

Based on the findings from the analysis of the collected data, the following recommendations are proposed to enhance Internal Audit effectiveness:

- The boards of banks should focus on Corporate Governance to ensure the independence of the Internal Audit function. Additionally, an appropriate number of auditors should be hired to distribute the workload evenly. Auditors must receive fair compensation and motivation from upper management and directors. They should have unrestricted access to information, perform their duties fairly in accordance with the established audit manual, and retain qualified staff. A proper budget must be allocated to address the financial resource challenges faced by Internal Auditors. Their benefits should be measured against established performance standards.
- Management should prioritize the experience of Internal Audit staff as a key factor affecting the independence of the Internal Audit function. Experienced auditors can deliver high-quality audits and valuable recommendations.
- Bank management, boards, and relevant authorities should conduct studies to identify weaknesses within the audit committee and work towards forming an effective committee.
- Guidelines should be developed to enable senior management to support the independence of the Internal Audit function, as their backing is critical for promoting audit independence.
- The bank management, boards, and relevant authorities should strengthen the remuneration and nomination committee by establishing effective rules and regulations that foster Corporate Governance, thus creating an environment conducive to the independence of Internal Audit functions.
- It is essential for bank management to leverage advanced technology for data analysis and real-time monitoring. Implementing feedback mechanisms for continuous improvement and fostering a culture of accountability are crucial. Additionally, developing performance metrics to evaluate the effectiveness of Internal Audits in achieving governance objectives will enhance oversight and overall organizational efficacy.
- Clear communication channels should be established by bank management to ensure regular updates and involve stakeholders early in the audit planning phase. Workshops should be organized to educate stakeholders on the audit process and its advantages, while soliciting their feedback to enhance audit practices. Regularly showcasing the value and outcomes of Internal Audits in addressing stakeholder concerns and contributing to organizational goals is also recommended.

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## **Appendix I**

### **Interview questions**

1. How is the effect of Corporate Governance on Internal Audit independence described?  
Strong Corporate Governance frameworks contribute to better organizational performance and accountability by establishing clear reporting lines, ensuring The independence of audit functions, and effectively assessing internal controls.
2. How do senior management support for the Internal Audit function independency?  
Senior management support is more likely to be experienced than inexperienced ones, and therefore that they have a greater ability to help The Internal Audit department independency by sharing Their experience & guidance to younger audit managers.
3. Is audit committee independence important for Internal Audit work? How?  
Yes, the audit committee is critical to provide unbiased assessments of internal control and Governance processes while maintaining Internal Audit independence, transparency, and a Culture of ethics by providing and developing necessary resources.
4. What is the relationship of Remuneration & Nomination committee with Internal Audit independency?  
The Remuneration and Nomination Committee is a key part of the company's Corporate Governance structure, it primarily focuses on overseeing executive compensation and ensuring effective succession planning. If the Internal Audit function does not gain the compensation or other benefits it deserves; it may be exposed to undue influence that could compromise its independence.
5. Do technological advancements have an impact on Internal Audit independency? How?  
Yes, Technological advancements are enhancing data analytics, ensuring secure data access, and providing flexible audit options that keep pace with the times. Facilitating continuous skill development and strengthening the independence of the Internal Audit function, Internal Auditors will be able to more easily identify and effectively assess risks and create proactive prevention capabilities.

6. What are the stakeholders' contributions to Internal Audit independence?

The Internal Audit function should be strengthened to enhance transparency, strengthen internal controls, and empower the audit committee. stockholder's engagement is crucial to fostering an audit culture and building strong Internal Audit governance within the organization to uphold audit ethics.

7. How do you assess the independence of Internal Audit in your organization?

Although there is a perception that The Internal Audit department is independent, in practice, its independence is seen to be compromised for various reasons. For example, due to lack of awareness, an incorrect perception given to the profession, and oTher reasons, Internal Audit independence has not reached the desired level audit independence has not reached the desiredlevel

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## **Appendix II Questionnaire**

**Addis Ababa University**

**College of Business and Economics**

**Department of Accounting & Finance MSC in Accounting & Auditing**

### **Questionnaire to be filled by Managements**

**Dear sir/ Madam,**

The main aim of this study is to determine how Corporate Governance influences the independence of the Internal Audit function in private banks. The findings from the survey will be documented anonymously, ensuring that your individual responses remain confidential. I sincerely appreciate your genuine cooperation in answering the questions thoughtfully, as your honest and willing contributions will be crucial in enhancing the effectiveness and credibility of this research.

This questionnaire is for educational purposes only. Please use this "X" symbol in The box to indicate your response.

**For further comments, please use 09 11 34 16 22**

Thank you

#### **Part I: Demographic Information of Respondents**

The following questions concern about your personal information. Completion of this information is voluntary and its confidentiality is assured. No individual data will be reported.

1. Age: -

A. 18-25 years  B. 26-35 years  C. 36-45 years  D. Above 45

2. Sex

A. Male  B. Female

3. Educational level: -

A. Diploma  B. Degree  C. Masters  D. PhD

4. Your work experience at in The Bank

A. 1-2 years       B. 3-4 Years       C. above 4 years

**Part II: General Questions**

Key SD= strongly Disagree D= Disagree N= Neutral A= Agree SA= strongly agree

For The following statement put your level of agreement By putting (X) on The space provided.

No	Statements	SD	D	N	A	SA
	<b>Corporate Governance Setting</b>					
CS1	There are recognized laws and regulations in place that ensure the independent execution of audit responsibilities.					
CS1	Standards and ethical codes exist that highlight the significance of independence and objectivity for Internal Auditors during their work.					
CS3	A robust internal control system is in place, overseen by a well-resourced independent Internal Audit function, which serves as a key element of Corporate Governance.					
CS4	Additionally, well-defined Internal Audit standards guide the relationship between Internal Auditors and management.					
CS5	It is the duty of board directors to guarantee the accuracy of financial accounts and reports while safeguarding the independence of Internal Auditors.					
	<b>Senior Management Support</b>					
SMS1	The independence of Internal Audits is reinforced by the backing of senior management.					
SMS2	Senior management enhances the Internal Audit function by hiring capable and qualified personnel.					
SMS3	They are dedicated to maintaining auditor independence.					
SMS4	Senior management members possess strong knowledge, expertise, and a commitment to enhancing organizational governance.					
SMS5	They are devoted to aiding Internal Auditors in fulfilling their					

	responsibilities.					
SMS6	Additionally, senior management is accountable for evaluating the performance of the audit function as well as for appointing and removing the heads of the Internal Audit department.					
SMS7	Overall, senior management plays a crucial role in promoting reliable, effective, and efficient Corporate Governance.					
	<b>Effectiveness of Internal Audit Committee</b>					
IAC1	An audit committee exists that provides independent and objective assurance and consulting services aimed at adding value and enhancing auditor independence.					
IAC2	This committee assists the bank in achieving its objectives by employing a systematic and disciplined approach to assess and improve the effectiveness of risk management controls and the governance processes of Internal Auditors.					
IAC3	The audit committee plays a vital role in ensuring the bank’s compliance with relevant laws and regulations while also supporting auditors in their tasks.					
IAC4	Moreover, the audit committee strengthens the Corporate Governance framework.					
IAC5	The involvement of the audit committee in Internal Auditor activities significantly boosts the effectiveness of the Internal Audit function.					
	<b>Effectiveness of Remuneration &amp; Nomination Committee</b>					
ERNC1	Internal Auditors receive competitive compensation to carry out their responsibilities both efficiently and effectively.					
ERNC2	There are internal regulations and oversight mechanisms in place to manage the benefits provided to Internal Auditors.					
ERNC3	A team of highly qualified managerial personnel is designated to monitor, support, and follow up with Internal Auditors.					
ERNC4	Internal Auditors receive competitive compensation to carry out their responsibilities both efficiently and effectively.					

	<b>Effectiveness of Technological Advancement</b>				
ETA1	The Internal Audit function is well-organized, dependable, and employs the latest technology.				
ETA2	Corporate Governance facilitates the use of modern technology in the Internal Audit function.				
ETA3	The integrity of audit results is safeguarded through the use of integrated technological solutions.				
	<b>Effectiveness of Stakeholders Engagement</b>				
ESE1	Stakeholder feedback has contributed to enhancements in Corporate Governance practices and the Internal Audit function.				
ESE2	Engagement with stakeholders influences the perceived independence of Internal Auditors within the bank.				
ESE3	Stakeholders play a crucial role in preserving the independence of the Internal Audit function.				
	<b>Independence of Internal Audit Function</b>				
IIAF1	Auditor independence is fundamental to the overall autonomy of the Internal Audit function.				
IIAF2	Management's view of Internal Auditors significantly influences the effectiveness of their operations.				
IIAF3	The independence of Internal Audit is paramount, surpassing all other factors that affect an organization's performance.				
IIAF4	Proper placement of skilled and capable Internal Audit staff is essential for any organization.				

**Statistical Data Analysis Tables**

<b>Descriptive Statistics</b>			
	Mean	Std. Deviation	N
IIAF	3.5901	0.64119	111
CGS	3.6468	0.52774	111
SMS	3.5354	0.56077	111
EIAC	3.6144	0.44860	111
ENRC	3.5518	0.64237	111
ETA	3.6607	0.63561	111
ESE	3.3919	0.68226	111

<b>Correlations</b>
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		CGS	SMS	EIAC	ERC	ENC	QC	IIAF
CGS	Pearson Correlation	1	.763**	.731**	.589**	.456**	.549**	.762**
	Sig. (2-tailed)		0.000	0.000	0.000	0.000	0.000	0.000
	N	111	111	111	111	111	111	111
SMS	Pearson Correlation	.763**	1	.713**	.659**	.616**	.581**	.798**
	Sig. (2-tailed)	0.000		0.000	0.000	0.000	0.000	0.000
	N	111	111	111	111	111	111	111
EIAC	Pearson Correlation	.731**	.713**	1	.676**	.557**	.602**	.823**
	Sig. (2-tailed)	0.000	0.000		0.000	0.000	0.000	0.000
	N	111	111	111	111	111	111	111
ERNC	Pearson Correlation	.589**	.659**	.676**	1	.739**	.537**	.855**
	Sig. (2-tailed)	0.000	0.000	0.000		0.000	0.000	0.000
	N	111	111	111	111	111	111	111
ETA	Pearson Correlation	.456**	.616**	.557**	.739**	1	.402**	.773**
	Sig. (2-tailed)	0.000	0.000	0.000	0.000		0.000	0.000
	N	111	111	111	111	111	111	111
ESE	Pearson Correlation	.549**	.581**	.602**	.537**	.402**	1	.645**
	Sig. (2-tailed)	0.000	0.000	0.000	0.000	0.000		0.000
	N	111	111	111	111	111	111	111
IIAF	Pearson Correlation	.762**	.798**	.823**	.855**	.773**	.645**	1
	Sig. (2-tailed)	0.000	0.000	0.000	0.000	0.000	0.000	
	N	111	111	111	111	111	111	111

\*\* . Correlation is significant at The 0.01 level (2-tailed).

Variables Entered/Removed			
Model	Variables Entered	Variables Removed	Method
1	ESE, ERNC, CGS, EIAC, ETA, SMS <sup>b</sup>		Enter

Model Summary <sup>b</sup>										
Model	R		Adjusted R Square	Std. Error of the estimate	Change Statistics					Durbin-Watson
		R Square			R Square Change	F change	df1	df2	Sig.F Change	
1	.953 <sup>a</sup>	0.908	0.903	0.19987	0.908	171.341	6	104	0.000	2.409

Coefficients <sup>a</sup>						
Model			t	Sig.	Collinearity Statistics	
					Tolerance	VIF
1	(Constant)	-1.044	-6.462	0.000		
	CGS	0.229	3.678	0.000	0.335	2.981
	SMS	0.103	1.657	0.100	0.300	3.337
	EIAC	0.322	4.408	0.000	0.338	2.956
	ERNC	0.300	5.809	0.000	0.331	3.023
	ETA	0.249	5.307	0.000	0.409	2.443
	ESE	0.087	2.360	0.020	0.572	1.749