EFFECT OF INTERNAL AUDIT PRACTICES ON CORPORATE GOVERNANCE OF THE HEALTH SECTOR IN KENYA

BY

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DECLARATION

Declaration by Candidate

I declare that with the exception of references to other people's work which have been duly acknowledged, this thesis is my own work and has not been presented for another degree elsewhere.

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DEDICATION

This thesis is dedicated to my dear wife, Esther Rotich and our children Faith, Naomi, Amos, Mercy, Victor and Benjamin for their patience, encouragement, support and understanding during my pursuit of higher education and career development. My wife deserves accolades for the resolve to run our home during this period.

ABSTRACT

One of the most important keystones and foundations of corporate governance is that internal auditors are anticipated to work with audit committees, boards and senior management to assist put the right tone at the top and helps to guarantee that ethical behavior flows down all the way through the ranks to lower level employees. A viable internal audit function is one of the most grounded devices to screen and improve organization performance. Internal auditing and corporate governance have now become a matter of major public concern. It is against this realization that the study investigated effect of internal audit practices on corporate governance with focus on health sector in Kenya. The specific research objectives were to determine the influence of risk management, internal environment audit practices, control activities and monitoring activities on corporate governance of the health sector in Kenya. The study adopted Agency theory and Stewardship theory. An explanatory research design was employed. The study sought the views from internal auditors and risk managers of the health sector. The target population of this study was 110 auditors of referral hospitals in Kenya of which sample sizes of 86 respondents were selected. The research instruments that were used in this study were questionnaires and interview schedule. The validity of the instrument was determined by the researcher using expert judgment. Cronbach's Coefficient Alpha was used to determine the reliability of the research instrument. The data were then coded and entered in the computer for analysis using the Statistical Package for Social Sciences (SPSS). The descriptive analyses that were used include mean, percentages, standard deviation and frequencies. Inferential statistics were used to analyze relationship between variables. This was done using Pearson product moment correlation and multiple regression analysis. From the model, (R^2 = .874) showing that the factors account for 87.4% variation in corporate governance in health sector. The predictors used in the model captured the variation in the corporate governance in health sector. The β-value for risk management, internal environment audit practices, control activities and audit monitoring activities had a positive coefficient, depicting positive relationship with corporate governance in health sector in Kenya. There was a significant positive relationship between risk management (β_1=0.370), internal environment audit practices (β_2=0.613) and audit monitoring activities (β_4=0.112; $p <0.05$) and corporate governance in health sector. There was no significant relationship between control activities (β_3=0.153 and p value >0.05) and corporate governance in health sector. The risk management, internal environment audit practices and audit monitoring activities influenced the corporate governance in health sector, while control activities do not. The study recommended that risk assessment should be led at the level of individual organizations and over the wide range of exercises and auxiliaries of the solidified association.

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DEFINITION OF KEY TERMS

Audit Monitoring Activities: It is the ongoing evaluations, built into business processes at different levels of the entity, provide timely information. Separate evaluations, conducted periodically, will vary in scope and frequency depending on assessment.

Control activities: A system that assesses the way of the structure's execution after some time. Constant watching happens in the ordinary course of operations, and joins reliable organization and supervisory activities and diverse moves staff make in playing out their commitments that assess the way of inside control system (Colbert and Bowen, 1996)

Corporate governance: Most often viewed as both the structure and the relationships which determine corporate direction and performance (Gatamah, 2008).

Internal audit practices: plays a unique role in corporate governance by monitoring organizational risks and ensuring that organizational processes are efficient and effectively controlled. There has been advance in achieving accord on what audit standards, governments and government offices ought to apply (Spencer, 2008).

Internal auditing is a self-governing, objective and consulting activity that is designed in order to add value and develop the operations of an organization. It helps an organization to carry out its objectives by bringing an organized, disciplined approach in order to assess and develop the effectiveness of risk management, control and governance processes.

Internal environment audit practices: Whittington and Pany (2001) characterized internal environment audit practices as the tone of the association by impacting the control awareness of individuals.

Risk Management: The internal audit activity evaluates risk exposures relating to the organization's governance, operations and information systems, in relation to; effectiveness and efficiency of operations, reliability and integrity of financial and operational information, safeguarding of assets and compliance with laws, regulations, and contracts.

ABBREVIATIONS

COSO	The Committee of Sponsoring Organizations
EMS	Environmental Management System
IAD	Internal Audit Departments
ICAEW	Institute of Chartered Accountants in England and Wales
IFAC	International Federation of Accountants
IFRSs	International Financial Reporting Standards
IIA	Institute of Internal Auditors
IIAM	Institute of Internal Auditors Malaysia
INTOSAI	International Organization of Supreme Audit Institutions
IPSASs	International Public Sector Accounting Standards
IRCA	International Register of Certificated Auditors
ISAs	International Standards on Auditing
KPMG	Klynveld Peat Marwick Goerdeler
MIA	Malaysian Institute of Accountants
MSWG	Minority Shareholder Watchdog Group
ROA	Return on Assets
ROE	Return on Equity
SEC	Securities and Exchange Commission
TSA	Treasury Single Account

CHAPTER ONE

1.0 Introduction

This chapter provides an imminent into the background of the study, statement of the problem, objectives of the study, research hypothesis, justifications of the study, significance of the study, scope of the study and limitations of the study. It also sets the tone for basic ideas and arguments for the study.

1.1 Background to the Study

Corporate governance has been reflected upon since the beginnings of the modern corporation (Kim and Nofsinger, 2007), (International Journal of Accounting and Financial Reporting ISSN 2162-3082 2018, Vol.8, No. 4) The Organization for Economic Corporation and Development (OECD) defines corporate governance as a set of relationships; it certainly has received increased attention and scrutiny over the last two decades. In this period, corporate governance issues have become important not only in the academic literature, but also in public policy debates.

Corporate governance issues are in general receiving greater attention as a result of the increasing recognition that a firm's corporate governance affects both its economic performance and its ability to access long-term, low investment capital (Mordelet, 2009). Corporate governance affects both its economic performance and its ability to access long-term, low investment capital (Mordelet, 2009). Corporate governance ranges throughout countries and firms. A higher quality of corporate governance allows firms to gain access to capital markets more easily, which is greatly significant for firms, which mean to boost their funds. Simultaneously, Cohen and Hanno (2000) using the Public Oversight Board's perspective, defined corporate governance as "those oversight activities undertaken by the board of directors and audit committee to ensure the integrity of the financial reporting process". This view of governance focuses on the control environment and control activities.

According to Institute of Internal Auditors (IIA) (2009) internal auditing can be defined as a self-Governing objective and consulting activity that is designed in order to add value and develop the operations of an organization. In the world over, it is acknowledged that the Internal Audit practices can possibly provide unparalleled administration to management in the behavior of their obligations. It is basic knowledge to note that both the International Organization of Supreme Audit Institutions (INTOSAI) and the Institute of Internal Auditors (IIA) have issued guidelines to manage inspection in the general population area. On account of inside review and Audit Committees, rules must be in conformance with the Institute of Internal Auditors- International Standards for the Professional Practice of Internal Auditing (Sayag, 2010).

The role of an internal auditor varies from providing independent assurance to acting as management advisor (Deloitte, 2010). Another area gaining importance in the business community is the support given by internal auditors to Accounts Committees in the assessment of risk management and risk processes (Soh & Martinov-Bennie, 2011). Based on the roles outlined above, internal auditing has had some impact on good governance, which is the particular interest of this study. The citizens (the principals) have contributed resources through taxes and other duties to national budget for economic and social development. They need an independent third party to lend credibility to the stewardship accounts rendered by the agents, that is, the government. They rely upon the auditor to provide an independent, objective evaluation of the accuracy of the agent's accounting and to report on whether the agents have used the resources in accordance with the principal's wishes (Al-Matarneh, 2011 and Al-Shammari, 2010).

For a long time, internal audit was considered as an administrative unit aimed at checking documents, counting assets, and reporting on past events for management purpose. However, these days, many factors have led to an improvement in internal audit practices in private and public entities. In the global economy of the twenty-first century, good governance has become a central issue. In the context of preventing corporate failure, questions have been raised about the performance of internal audit and other forms of auditing (Imhoff, 2003; Mohamad & MuhamadSori, 2011). It is worldwide practice for the internal auditors to report to the Audit Committees, not to management (except for administrative interface), in order to maintain their independence (The Institute of Internal Auditors [IIA], 2012b; Verschoor, Barrier, & Rittenberg, 2002).

The effective relationship between internal auditors and the Audit Committee is crucial in ensuring good governance (MIA Professional Standards & Practices [MIA], 2012). There is, therefore, potential for better functioning of business in Kenya to optimize the internal audit functions and audit committee interaction. Presumably, an effective internal audit would depend on the understanding of the internal audit process and, importantly, of the impact of internal audit on corporate governance. Moreover, the Institute of Internal Auditors (IIA), the professional body for internal auditors based in USA, prescribes that internal audit be consultative in nature to add value and improve an organization's operations (2010b).

The call for integral audit by Khemakhe is in line with the Institute of Internal Auditor's prescription. The Institute of Internal Auditors has also identified combined assurance as a new area to be studied, but the institute has not yet defined combined assurance. However, the term combined audits has been used when two or more different management systems are audited simultaneously (International Register of Certified Auditors, 2011). The adoption of the ISO standard for risk management by the Institute of Internal Auditors (2010a) suggests that combined assurance, such as incorporating audit criteria for quality audits into process audits, is the new direction for internal audit.

The complexities in internal audit relate to the objective and scope of the audit. There are various internal audits such as management audit, operational audit, systems audit, compliance audit, computer audit, probity audit, value-for-money audit, and quality audit (Pickett, 2003; Whittington & Pany, 2004). These various types of audits create pressure for management and employees, giving them the perception that they are constantly being audited. This poses the question of effectiveness of the audits and how such audits would aid the organization in its corporate governance and risk assessment framework.

Questions surrounding the effectiveness of internal audits need to be addressed in the light of reliance placed on the Internal Audit Function as one of the mechanisms of corporate governance. To achieve its objectives, government develops strategies that could help in effective management of public funds, and the internal audit function is one of those strategies (a governance tool) which help it to effectively manage and achieve its objectives (Cohen & Sayag, 2010). The tasks, functions and roles of internal auditing have expanded, changed and shifted more to management-oriented matters than accounting matters; reporting lines have also been transformed and in many countries its structure has been transformed (Feizizadeh, 2012 and Hellman, 2011).

In Rwanda, the scope of internal audit changed after 1994 Rwandan Tutsis genocide. The current trend in Rwanda is that each public institution reports annually to the Office of the Auditor General of Public Finance (OAG). The critical situation is that local public institutions in Rwanda are still challenged by improper management of public funds, lack of fair financial reporting and yet they have the services of the internal audit. The office of Auditor-General reports to the parliament public finance commission every year that some public institutions do not comply with rules and regulations for public finance management (Biraro, 2016).

The 2013 report clearly mentioned that local government entities do not have adequate mechanisms of enhancing public funds accountability, have persistent weaknesses in preparation and presentation of financial statements, breaking rules and regulations of funds management, existence of fraudulent cases and misappropriation of assets (Biraro, 2016). In journey for more grounded responsibility environment, Kenya keeps on creating solid bookkeeping and evaluating frameworks (Rutto, 2011). For instance, it embraced a globally perceived reporting system.

In 1999 it embraced the International Financial Reporting Standards (IFRSs) and International Standards on Auditing (ISAs) for the Private Sector and generally, the International Public Sector Accounting Standards (IPSASs) in 2014. The Country rebuilt the general population segment and embraced execution contracting, organized screening of State Officers, set up Independent Commissions and Offices and different changes that keep on strengthening corporate administration and with current talks with the World bank to establish a Financial Oversight Authority to monitor

Public Interest Entities (Sayag, 2010). Even where public services are neither publicly neither provided nor financed, for social and political reasons they are usually subjected to regulation going beyond that applying to most economic sectors.

A public service in Kenya have the characteristics of a public good (being non-rivalrous and non-excludable), but most are merit goods, that is, services which may (according to prevailing social norms) be under-provided by the market. Empirically, a study directed by KPMG (2011) established that internal audit review in a firm, contributes impressively to execution change and help in distinguishing benefit prove in corporate fiascos, especially monetary extortion reliably reports a relationship between powerless administration (fewer independent boards or nonattendance of an internal audit system) and the incidence of problems (Beasley, 2000), (Effect of Internal Audit practices on organization performance: A case of regulatory Bodies in Kenya) KCA university 2016.

Internal audit works as a guard dog and prevents an organization from misconduct and anomalies subsequently empowering the association to accomplish its destinations of guaranteeing abnormal state of profitability and benefit. Greenlay and Foxall (2012) pointed out that despite the fact that studies have found a relationship between bookkeeping control frameworks and performance hypothesis, predicts that these organizations will be impacted by external environmental impacts.

1.2 Statement of the Problem

Within the globalized economy, internal auditing is established as an essential means for the exact management of any business economic resources. Simultaneously, corporate governance has received wide attention in recent years both in practice and in academic research because of the major accounting scandals and large-scale corporate failures. Recent corporate scandals and earnings restatements have resulted in an increased emphasis on the need for strong corporate governance to ensure financial reporting quality (Cohen Davidson., 2004; Carcello *et al*., 2005) and Effect of corporate Governance on Accounting Information Quality (Survey on Publicly listed companies in Indonosia Stock exchange 2011-2016).

Over the years, the public sector has been experiencing massive corruption and fraud related cases where public funds end up in the hands of corrupt individuals (Adari, 2007). Recent corporate accounting scandals and the resultant outcry for transparency and honesty in reporting have given rise to two desperate yet logical outcomes. First, Internal Auditing skills have become crucial in untangling the complicated accounting maneuvers that have mystified financial statements. Second, public demand for change and subsequent regulatory action has transformed corporate governance. Increasingly, firm's internal audit officers and directors as well as board members are under ethical and legal scrutiny. Both trends have the common goal of responsibly addressing concerns about the financial reporting system and thus the need for this study.

Weak internal controls also provide avenues for fraud in organizations. These risks need to be identified and mitigated to ensure that imminent threats are controlled (Wagacha & Ngugi, 2009). A question is left unanswered as to whether internal auditors should be among the ones to blame when organizations are at the point of collapsing. Some scholars have found positive effects while others have established minimum or adverse effects of the internal audit function on corporate governance. In attempting to adequately discharge their responsibilities, internal auditors often find themselves in an anomalous position.

Otieno (2012) researched on impacts of corporate governance and financial performance of commercial banks in Kenya. He found that corporate governance elements represent 22.4 % of the budgetary execution of commercial banks. Chepkorir (2010) established that internal audit helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes. Ruto (2011) researched on Relationship between internal audit independence and corporate governance in commercial banks in Kenya and Wanyoike (2007) studied about internal audit department's role in enterprise risk management.

The internal audit activity evaluates risk exposures relating to the organization's governance, operations and information systems. The internal auditors are expected to provide recommendations for improvement in those areas where opportunities or deficiencies are identified. However, there has been laxity in implementation of internal audit findings and recommendations. Following the complexity of the internal audit function, there are conflicting findings on the different roles played by internal audit in enhancing organization performance.

From the above studies, no study has looked at the effect of internal audit practices on health sector in Kenya. It is against this realization that the current study investigated effect of internal audit practices on good governance with focus on public health sector in Kenya. This study seeks to fill this gap by looking at the effect of internal audit practices on.

1.3 Objective of the Study

The overall research goal was to establish the effect of internal audit practices on corporate governance of the health sector in Kenya. The following were the specific research objectives:

i) Determine the influence of risk management on corporate governance of the health sector in Kenya.

ii) Establish the effect of internal environment audit practices on corporate governance of the health sector in Kenya.

iii) To find out the influence of control activities on corporate governance of the health sector in Kenya.

iv) Establish the relationship between audit monitoring activities and corporate governance of the health sector in Kenya.

1.4 Justification of the Study

Internal auditing assumes a basic part in the administration and operation of an association. At the point when viably executed, worked and overseen, it is considered as a vital component in helping an association accomplish its goals. Associations that adequately utilize Internal audit in evaluating their operations can recognize business dangers, processes and framework, wasteful aspects and make fitting remedial move and at last bolster ceaseless change.

Internal audit function has helped keep bad things from happening, assure good things can happen and help management understand where their risks are, whether the risks are under control and whether the risks are worth taking. It is against this background that the current study aimed to investigate effect of internal audit practices on corporate governance of the health sector in Kenya.

1.5 Significance of the Study

This study shall provide critical information to the various stakeholders in the corporate world. The study helps management to appreciate the role played by internal auditing function in their organizations and to understand the challenges they face in carrying out their roles and solve them. It enables them to know whether their investment in strong Internal Audit Department (IAD) is worthwhile. Governing bodies and senior management in the public sector need the services of internal audit to be effective and efficient.

At the same time the legitimacy of internal audit activity and its mission should be understood and supported by senior management of government entities to enhance its effectiveness in promoting good public sector governance, control and risk management systems. Modern internal audit practice has transformed into a professional discipline of its own and as a partner to governance bodies with strategic focus of contributing towards the improvement of organizational governance and risk management strategies.

The internal auditors understand their role in organizations and the challenges they face as they carry them out. The findings help the government in particular to learn a lot about accountability, efficiency and effectiveness of service delivery. To academicians and scholars, the study contributes significantly to the internal auditing debate as well as the existing literature regarding the effect of internal audit on corporate governance and also to identify research areas that have advantage for further study.

1.6 Scope of the Study

The research seeks to determine the effect of internal audit practices on corporate governance of the public health sector in Kenya. This was achieved by looking at the risk management, internal environment audit practices, control activities and audit monitoring activities within the health sector in Kenya.

1.7 Limitations of the Study

The study encountered a number of limitations. Responses limited the study results particularly the freedom which respondents felt in disclosing their internal audit practices. However, the use of questionnaires and interviews gave additional information that led to valid conclusions. The respondents for this study who were the auditors and risk managers were always very busy so getting them to cooperate and participate in the study was a challenge. However, the researcher had to book appointment with them and clarified the intentions of the study.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter presents the review of related literature with respect to the objectives of the study, from global, regionally and local perspectives.

2.1 Concept of Corporate Governance

More recently, Roe (2004) defines corporate governance as the relationships at the top of the firm-the board of directors, the senior managers, and the stockholders. In his opinion, institutions of corporate governance are those repeated mechanisms that allocate authority among the three and that affect, modulate and control the decisions made at the top of the firm. The above definition of corporate governance indicates idea of objectives correspondence, incentives, monitoring and control.

The best way to define the concept is to adopt the definition shared by the Organization for Economic Cooperation and Development (OECD, 2004) countries is that the Corporate governance is the system by which a business corporation (or a nonprofit organization) is directed and controlled, at its senior level, in order to achieve its objectives, performance and financial management, but also accountability, integrity and openness. The World Bank has defined governance as 'the manner in which power is exercised in the management of a country's economic and social resources for development (World Bank 1991).

At the micro level, corporate governance relates to how well an organization is managed to ensure its sustainability as a going concern. Governance is the system by which organizations are directed and controlled. It includes the rules and procedures for making decisions on corporate affairs to ensure success while maintaining the right balance with the stakeholders' interest. Evidence for poor governance includes failure to establish a legal framework, a tendency for pursuing private gains and non-transparent decision-making (World Bank, 1991).

Simultaneously, Cohen and Hanno (2000) using the Public Oversight Board's perspective, defined corporate governance as "those oversight activities undertaken by the board of directors and audit committee to ensure the integrity of the financial reporting process". This view of governance focuses on the control environment and control activities. The key dimensions in corporate governance identified by the World Bank are: legal framework; improvements in management; accountability; and, information and transparency. Under the first dimension — legal framework or corporate policies — the World Bank states that there should be known rules or policies and the related change procedure, for rules application and enforcement, as well as conflict resolution.

In applying this requirement to an organization, these rules or policies may relate to the company policies on various business processes including human resource management, which could be evidenced through standard operating procedures. Further, to avoid abuse of rules and policies, review systems or monitoring mechanisms are required. Where conflicts arise on enforceable agreements, the resolution must be binding and made by independent parties. This position is crucial and needs to be understood within the organizational structure as there will be occasions where internal auditors are asked to perform certain tasks that may undermine their independent status. The reporting requirements for the internal audit function and the specific reference to the audit committee in certain legislation, specifically, the listing rules, emphasize the important roles of internal auditors and audit committee members in the corporate governance framework. One of the areas that need to be reviewed by the internal audit function is risk management (Bursa Malaysia, 2009b). A brief account on the risk management policies is readily available in the annual reports of Malaysian public listed companies. Next, improvement in management is viewed from the perspectives of management of revenue, expenditure and personnel. Revenue needs to be even, expenditure controlled and the placement of staff based on competencies and appropriate compensations. The World Bank's emphasis here is on capacity and efficiency.

The third dimension, accountability means holding a person responsible for his/her actions and is gauged from financial and economic performances, and voice mechanism. Financial accountability involves the use of accounting and auditing covenants. External audits act to reinforce expenditure control and assist in fraud prevention. Internally, the organizations would enforce the monitoring mechanism for all processes by internal audits in the legal framework. In economic performance, value-for-money reviews are made on expenditures. Voice mechanisms relate to disseminating information on services, getting feedback and dealing with complaints. For effective accountability assessments, the World Bank advocates focusing on the reviews of audit reports and the action taken to contend with identified corruption and waste (World Bank, 1991).

The final dimension in the World Bank framework on corporate governance is information and transparency. Availability and access to adequate information together with transparency of decision-making are critical to accountability and the legal framework. Transparent decision-making safeguards against corruption, wastage and abuse of authority. Corruption prevention through transparent expenditure management apart from reporting and monitoring systems should be in place. The organization should analyze its data and its information system in the evaluation of its capabilities to disseminate information.

All the dimensions in the World Bank's governance framework could be linked to the sub-elements of internal control. Internal control is the management's control mechanism to achieve an organization's operating objectives and to meet reporting obligations (Gill & Cosserat, 1993). There are three elements in internal control, namely, control environment, information system and control procedures (O'Leary *et al*., 2006). The control environment encompasses management's philosophy and operating style, organizational structure, human resource and levels of authority, internal audit, audit committee and the use of information technology.

For control procedures, there should be segregation of duties, authorization procedure, safeguards for assets and documentation. An alternative to the World Bank's framework is that proposed by the Organization of Economic Co-operation and Development (OECD). The key principles of corporate governance by the OECD (2004) relates to mechanisms in ensuring the basis for an effective corporate governance framework; rights of shareholders and key ownership functions; equitable treatment of shareholders; stakeholders role in corporate governance; disclosure and transparency, and responsibilities of the board of directors. These principles can be grouped into four main areas: mechanism of business ethics, mechanism of decision-making, adequate disclosure and transparency, and lastly, mechanism of book keeping and final accounts (Abu-Tapanjeh, 2008).

The World Bank and OECD do not work independently. Both parties have collaborated in establishing the regional Corporate Governance Roundtables to identify areas of reform in corporate governance (Jesover & Kirkpatrick, 2005). Although there are four main areas that can be used to evaluate an organization's corporate governance, the OECD principles are more focused on rights and duties of shareholders and board of directors. Further, the disclosure and transparency requirement is directed towards financial performance, composition of ownership and governance. The OECD corporate governance principles are used as part of the listing requirements by Bursa Malaysia (Bursa Malaysia, 2009b).

The Malaysian listing requirements are discussed further in the next section. As internal audit deals with the processes in their organization and the way these processes are managed such as compliance to procedures and good business practice; operational practices for economy, efficiency and effectiveness (Dittenhofer, 1997; Moeller, 2009; Ziegenfuss, 2000); a framework that looks at these activities is needed to gauge the performance of internal audit. As such, using the World Bank's framework would facilitate the investigation into areas of improvements on the business processes arising from internal audit recommendations.

Arguden (2010) argued that corporate governance is not just compliance and the purpose of measuring it is for improvements. The notion on improvements augurs well with the second dimension in the World Bank's framework of management improvements in business processes. An ideal measure for corporate governance however is difficult to achieve. This situation is fairly recognized when discussing measures of corporate governance (Romano, Bhagat, & Bolton, 2008; Wan, 2010). There seems to be a consensus that measurement of corporate governance needs to correlate with performance, the premise for formulating governance scores or indices. A number of proxies have been used in the creation of indices. For example, the

Governance Index used the strength of shareholder rights in the provisions for takeovers to measure the impact of governance on firm performance (Gompers, Ishii, & Metrick, 2003). The measures used are mainly on anti-takeover provisions and would not be appropriate for measuring on-going governance, which is of multi dimensions.

Another study to measure accountability in corporate governance was done using data envelopment analysis or DEA (Feroz, Goel, &Raab, 2008). The researchers argued that the board of directors in discharging their monitoring role, use market based measures such as return on equity (ROE) in business performance analysis, as an approach to review the quality of decision-making relative to their competitors. DEA decomposes ROE into measures of profitability, asset utilization and equity multiplier so that responsibility can be assigned to the relevant business unit. They argued that an income efficient organization produces maximum total revenue while using the minimum of resources. A survey on corporate governance in Japan also uses ROE and return on assets (ROA) as part of corporate governance index, a measurement from the shareholders' perspective (JCGR, 2006).

In Malaysia, the governance index for public listed companies also uses ROE in addition to the Malaysian Code of Corporate Governance, Malaysian listing requirements and disclosures in annual reports (MSWG, 2011; MohamadAriff *et al*., 2007). Yet, another proxy is used to measure overall firm level or internal governance by referring to relationship of governance mechanism – board of directors – with information risk (Strydom, Navissi, Skully, &Veeraraghavan, 2009). The rationale given was that good internal governance is present when monitoring, disclosure and control mechanism as prescribed by best practices, are implemented. The proxy for information risk used is the quality of working capital accruals and cash flows from operations of US listed companies.

The use of indices provides one summary number of multiple dimensionalities (Romano *et al*., 2008). Romano insisted that corporate performance could not be consistently related to the governance index and such indices should not be the main criteria for stock investments. The above indices are very much linked to reported financial performance. The quality of information for market purposes, including computation of ROE and ROA, is dependent on the disclosure of financial information via the audited accounts and annual reports. Availability of information and transparency could reduce uncertainty and transaction costs, which together with mechanisms to analyze and disseminate information lead to better accountability (World Bank, 1991).

The work of internal auditors in reviewing and ensuring reduced transaction errors and efficiency in business processes ultimately leads to improvements or better firm performance. Administrative controls need to minimize the opportunities for corruption, for example through transparent budgets and procurement procedures as well as performing environmental assessments (World Bank, 1991). Although the World Bank did not mention risk, this recommendation on administrative controls is in line with the steps in risk management – another review area of internal auditing.

In this study, rather than using the index as a measure of corporate governance as mentioned by Gompers, *et al*. (2003) or the governance index, the impact on corporate governance of internal audit performance will be assessed by the recommendations made by internal audit on the dimensions in the World Bank's corporate governance framework. This measure is in agreement with the suggestion by the World Bank in using the reviews of audit reports as effective accountability assessments. Further, this measure also followed one of the measures of IAF's effectiveness by using the acceptance and adoption of IAF recommendations (Soh & Martinov-Bennie, 2011; Ziegenfuss, 2000).

2.2 Concept of Internal Audit

Internal audit is defined as an objective assurance with the aim 'to evaluate and improve the effectiveness of risk management, control and governance processes' (IIA, 2010b). 'Assurance' is also used by the international accounting body in tandem with auditing standards (IFAC, 2010). Although auditing standards are applicable for audits of financial information, the assurance standards are for other engagements. Internal audit has also been described as an independent appraisal of the effectiveness of internal control within an entity of its management process in achieving set objectives and goals (Gill &Cosserat, 1993; Haron *et al*., 2010).

Fadzil *et al*. (2005) looked at the internal auditing practices and its effect on the quality of internal control. They summarized the services performed by the IAF to cover four areas: Review of adequacy and effectiveness of the control systems (accounting, financial, operational) ascertain the compliance to policies, rules and regulations which could impact significantly on the business operations. Review the means of safeguarding the company's assets including efficiency and economy of resources employed and review operations or programs to determine that the results are as established by management. Upon the conclusion of an audit, the report presented should give a 'reasonable assurance' on the state of matter that was investigated. 'Reasonable assurance' is clarified as the degree of confidence the user of the audit report has that due professional care has been exercised in the audit (Chambers, 2006; ICAEW, 2011).

Although the concept of reasonable assurance is linked to external audits, the basis for the opinions made on the outcomes of internal audits, should be traceable to the supporting documents or analyses made during the audits. Confirmation of factual content with the auditee is essential (Dittenhofer, 1997). The reliance on the reports or other opinions of internal auditors is very important as these reports will be referred to by management when they undertake continuous improvements.

The work of internal auditors will also be assessed by external auditors who would determine whether reliance will be placed on such work in the conduct of financial audits or other engagements (AUASB, 2010). Upon the agreement of the process owners to take corrective actions or improvements, customarily the follow-up audit made by the internal auditors will also assess the effectiveness of such corrective actions in ensuring the root causes for the weaknesses have been addressed. The report on the initial audit findings and the results of the corrective actions would be indicative of the effectiveness of the internal audit.

Institute of Internal Auditors (IIA) (2009) referred internal auditing as an independent, goals and consulting activities that is intended to add imperative value and build up the operations of an organization. It assists any firm to complete its targets through bringing a composed, restrained approach that will build up the adequacy of hazard administration, control and administration forms. In this way, interior evaluating is being performed by experts with a careful comprehension of the business culture, frameworks and procedures, the inner review movement which offers and ensure that inside controls set up are adequate keeping in mind the end goal is to ease the dangers, administration procedures are useful and equipped, and authoritative objectives and targets are being met (IIA, 2004). This pronunciation recommends internal control as a system that brings a unique experience to organizations and an outlook change from an accentuation on responsibility about the past to enhancing future result which helps evaluators work in more compelling and effective way (Nagy & Cenker, 2002).

Internal Audit is a target and independent appraisal benefit in risk management, control and administration by measuring and assessing their viability in accomplishing the organization concurred goals (Committee, 2002). Likewise, internal audits results are basic to the Board of Directors and line administration in the inspected units. The administration applies the master capacities of inward examining through exact and controlled evaluation of the techniques, strategies and operations that administration set up to ensure the achievement of the association's objectives and through proposals for development (Dumitrescu, 2004).

According to Institute of Internal Auditors (2009) internal auditing is a self-overseeing, objective and consulting function that is intended to add value and develop operations in organizations. Internal audit practices help organizations to accomplish their objectives by setting up a sorted out and taught way to deal with surveying the adequacy of risk control and management and in addition processes within organizations. As a result, internal auditing should be performed by professionals with a proper comprehension of the business culture, systems, and procedures. According to Institute of Internal Auditors (2004) internal audit is an activity that guarantees that interior controls of an organization are sufficient to alleviate risks. It also ensures that governance processes are helpful and competent and that the organization' goals and objectives are met.

Internal auditing is a profession that involves prompting organizations on the most proficient methods to accomplish their objectives through overseeing risks and upgrading internal control systems (Nagy & Cenker, 2002). It additionally includes using a deliberate technique to dissect business methods or issues and recommending solutions. The essential part of the internal auditing activity is to guarantee effective application of official management controls. The internal audit function, despite the fact that it is not obligatory, exists in most private or corporate agencies, and in public sector including national and county governments.

The quality and quantity of an internal audit functions varies according to organizations and sectors depending on traditions of companies and the approach of top managers. Cai (2007) suggests that by accessing and evaluating the ability of definitive controls, internal audit is looking at shapes, a key managerial control mechanical assembly that is clearly associated with the structure and general standards of an affiliation. Internal audit function has a few points and standards which is vital to adhere to. It is the top managerial staff of any organization, however which bears last obligation that the organizations management applies a proper and viable arrangement of internal audit.

Internal audit offers a system of evaluating banking activity risk and risks concerning organization capital, appropriate strategies for checking consistence with laws, measures and internal methods. Internal control involves five parts; the internal environment audit practices, the risk assessment, advanced information communication systems, control activities and audit monitoring controls (Hayes, 2005). Internal auditing is a professional and movement required in prompting associations with respect to how to better accomplish their goals through overseeing dangers and enhancing internal control. Internal auditing involves the utilization of a systematic methodology for analyzing business processes or organizational problems and recommending solutions.

The main role of the internal audit practices is to ensure that administration official controls are being connected in a successful way. Internal audit function, although it is not compulsory, subsists in majority of private venture or firm's substances, and public sector are not excluded, state, and national and city governments. The errand, quality and solid purpose of an inward review capacity might be distinctive broadly inside the approach of top officials and conventions of organizations and associations.

Internal Audit function (IAF) has been referred to as the department that performs internal audit (Johl*et al*., 2013; Mat Zain &Subramaniam, 2007; IIAM, 2009). Even though, the Malaysian listing requirements specify the presence of the IAF in the corporate governance structure, the IAF could be outsourced (Ahmad & Taylor, 2009; Haron*et al*., 2004; Johl*et al*., 2013). As such, in this study, IAF refers to the internal audit process and its reporting structure, notwithstanding whether the IAF is in-house or outsourced.

The internal audit process can be divided into four dimensions: planning, execution or fieldwork, reporting, monitoring and follow-up on findings (Beckmerhagen, Berg, Karapetrovic, &Willborn, 2004; Dittenhofer, 2001a, 2001b; Fadzil*et al*., 2005; Moeller, 2009). In planning the audit, major items to be considered are: scope and objective of audit, rules and regulations, potential risks, independence and competencies of internal auditors, and audit programs. While executing the audit, internal auditors obtain reliable information including process performance data as audit evidence. They also ensure good documentation and easy retrieval of audit findings. Reporting of audit findings to the relevant management level is done for appropriate corrective actions to be taken by the auditee to eliminate root causes of weaknesses found. Monitoring of internal audit process through self-assessments and peer reviews of audit teams should be conducted for performance improvement, for example, to identify training needs for internal auditors in areas such as information technology or risk management. Following-up on audit findings is crucial to ensure that corrective actions by management are effective and changes to organizational processes are aligned to targeted improvements.

Internal auditors have taken specific strategies, including combined audits and collaborations, to perform their monitoring role for management. An initial step towards a combination of internal audit activities is a comprehensive audit. In a comprehensive audit, the activities encompass attesting financial statements, checking legal and administrative compliance, ensuring probity of decisions by management and conducting a performance audit (Gill & Cosserat, 1993).

Another suggestion made to auditors performing value-for-money and comprehensive audits is to include the evaluation of the quality of strategic planning and how the services were provided (Khemakhe, 2001). Khemakhe called this type of audit integral auditing. The risk or impact assessments made are also important in ensuring accountability of policy or program undertaken by an organization. By performing an integral audit, Khemakhe claims that auditors have gone beyond the role of controller to that of facilitator, thereby providing a better performance assessment on corporate governance.

2.2.1 Risk Management and corporate governance

The internal audit function plays a unique role in corporate governance by monitoring organizational risks and ensuring that organizational processes are efficient and effectively controlled. This unique role has been noted in both research and practice. For example, studies have found that the presence of an internal audit function has a deterrent effect on financial reporting irregularities and employee theft. Gordon and Smith (1992) found that a control function, such as that performed by internal audit, can lead to better firm performance. Furthermore, Prawitt et al., (2006) found that the internal audit function moderates the level of earnings management in companies.

The internal audit activity evaluates risk exposures relating to the organization's governance, operations and information systems, in relation to; effectiveness and efficiency of operations, reliability and integrity of financial and operational information, safeguarding of assets and compliance with laws, regulations, and contracts. Based on the results of the risk assessment, the internal auditors evaluate the adequacy and effectiveness of how risks are identified and managed in the above areas. They also assess other aspects such as ethics and values within the organization, performance management, communication of risk and control information within the organization in order to facilitate a good governance process (IIA Research Foundation, 2004).

The study of Spira& Page (2003) explores the changes due to the fundamental redefinition of Turnbull guidelines about the nature of internal control as an attributes of corporate governance in the UK. The paper focused on sociological standpoints regarding risks as well as other conceptualization in order to outline the discussion regarding the internal control and risk management within the UK corporate governance. Corporate governance replicates the power relations and political resolutions between shareholders, creditors, management and labor as they are personified in a given institutional history (Jackson 2000). For this reason, the idea of risk had become essential to corporate governance and become connected to the idea of internal control. In the process, the significance had changed. Internal control was under assessment, partially because of well-publicized corporate failures and partially as a result of moves towards professionalization of the internal audit function.

Express changes in IT and decision-making practices in many organizations were motivating moves away from strict, recognized control to situations where liability for control was being pushed down the organization hierarchy and where mistakes by management could not be attained through conventional, fulfillment based internal audit. The study had been able to show an observation that within the corporate governance policy, risk management has become closely aligned with internal control which proposes the amount to which risks are administered has now been captured as a form of accountability, rather than its focus – considered as an index against which a measurement of performance is being calculated. Thus, the redefinition enables to offer a new vision of risk management as part of the accountability process, which involves an alteration which shadows the difference between responses to risk, through risk management systems and accountability of risk (Spira & Page, 2003).

An organization management of internal control has a key part in the administration of dangers that are noteworthy to the satisfaction of its business targets. A sound arrangement of inward control adds to protecting the shareholders venture and the organization's advantages. Internal control encourages the adequacy and effectiveness of operations, guarantees the dependability of interior and outside reporting and helps consistence with laws and directions (Whittington and Pany, 2010). An organization arrangement of inward control has a key part in the administration of dangers that are noteworthy to the satisfaction of its business targets.

A sound arrangement of internal control adds to shielding the shareholders venture and the organization's advantages. Internal control encourages the viability and productivity of operations, guarantees the unwavering quality of inward and outer reporting and helps consistence with laws and directions (Whittington & Pany, 2010). Organizations understand risk and need valuing the significance of hazard administration to an association. Great corporate administration codes require the board to introduce an arrangement of hazard administration and educate their shareholders regarding this framework (Pickett, 2003).

An organization cannot get smaller in its ways on approach of any issues to any extent. It must create, and one of the key methods to fruitful development is pointing out any danger to the administration. Chance affects an association's capacity to content with and to keep up its money related quality and the nature of its items and administration. It is the interior examiner's business to recognize all auditable exercises and important hazard figures and to evaluate their noteworthiness. Effective internal control structure requires that the material perils that could unfavorably impact on the achievement of the bank's destinations are being perceived and constantly surveyed.

As indicated by Beyanga (2011) this evaluation ought to cover all dangers confronting the bank and the combined keeping money association (that is, credit hazard, nation and exchange chance, showcase chance, financing cost chance, liquidity chance, operational hazard, legitimate hazard, and reputational chance). Inward controls should be modified to fittingly address any new or beforehand uncontrolled dangers (Radu and Ramona, 2013). Subsequently it is basic that, as a major aspect of an inner control framework these dangers are being perceived and ceaselessly surveyed. From an inside control point of view, a hazard appraisal ought to recognize and assess the inward and outward components that could antagonistically influence the accomplishment of the administrative bodies' execution, data and consistence objective.

Effective risk assessment identifies, perceives and considers internal parts, (for instance, the multifaceted way of the affiliation's structure, the nature of the bank's activities, the nature of the work constrains, various level changes and agent turnover) and what's more outside components, (for instance, fluctuating fiscal conditions, changes in the business and mechanical advances) that could inimically impact on the achievement of the firm’s objectives. This hazard evaluation ought to be led at the level of individual organizations and over the wide range of exercises and backups of the combined managing an account association. This can be refined through different strategies (Pickett, 2010). Successful hazard appraisal addresses both quantifiable and non-quantifiable parts of dangers and measures expenses of controls against the advantages they give.

The risk assessment process also figures out risks which are controllable by the firm and which are most certainly not. For those dangers that are controllable, the bank must survey whether to acknowledge those dangers or the degree to which it wishes to relieve the dangers through control techniques. For those dangers that can't be controlled, the bank must choose whether to acknowledge these dangers or to pull back from or lessen the level of business action concerned. According to Birkett

(2009) risk refers to the probability that an occasion, condition, or activity may unfavorably influence an association or its activities. Certain factors in events, conditions, or actions may be seen as posing risks for an organization or its activities.

In order for risk assessment, and in this manner the arrangement of internal control, to stay viable, senior administration needs constantly to assess the dangers influencing the accomplishment of its objectives and respond to changing conditions. Internal audit controls may be amended to suitably address any new or beforehand uncontrolled dangers. For instance, as money related development happens, a bank needs to assess new budgetary instruments and market exchanges and consider the dangers connected with these exercises. Risk assessment system is divided into three steps: risk identification, risk analysis and evaluation, risk control and report. Risk identification deals with finding out how the enterprise judges and analyzes risks, including its nature, types and reasons of the occurrence.

On the other hand, risk analysis and evaluation needs quantitative analysis of digital information collected by mathematical method in order to make the risk management based on scientific basis. The result of risk analysis and risk evaluation is the probability of occurrence and size of the risk so as to provide a dependable basis for decision-making. When dealing with risk control and report, management involvement is required to consider how to control risk. The method of controlling risk usually is to avoid, loss prevention, loss reduction, separation duplication and diversification.

2.2.2 Internal environment audit practices

Internal environment audits are the regular examination of your business' actual operating methods - comparing them against those set out in your environmental management system (EMS) manual. These can be reviews of procedures and areas of operation, and are designed to assess effectiveness. Whittington and Pany (2001) characterized internal environmental audit practices as the tone of the association by impacting the control awareness of individuals. They encouragingly affirm that controlled environment is seen as the establishment for the various segments of inner control.

Administration state of mind ought to be focused on moral business honest and to taking after the set up control techniques (Fish, 2001). This is the establishment for each other piece of internal control, giving request and structure. Inside environment control sharpens components which include Integrity and good values; the devotion to wellness, organization hypothesis and working style as well as the way organization distributes power and commitment, deals with and develops its family.

The Internal environmental control practices are the establishment of the five components in the inner control system. Its assignment and operation influence the venture' general action, as well as the other four components. In this way control environment specifically influences the impact of execution of interior control system and the advanced ventures ought to build up a reasonable internal environment control (Eden, 2006). Internal environment audit practices have a few components, nonetheless, for some reasons this exploration and the survey will concentrate on administration rationality and working style, the trustworthiness and moral estimations of staff that make and regulate controls, and review councils and directorate.

For motivations behind the study, governing body will be spoken to by the Board of Management and the different advisory groups of the Board (Verschoor, 1999).

Whittington and Pany (2001) likewise trust that these variables set a premise whereupon the other inward control parts can be manufactured. They additionally give a structure inside which alternate segments work. Be that as it may, these attestations have not generally remained constant, since administration in associations has dependably superseded these controls and the absence of tutoring. The internal environment audit practices usually include the following context. To begin with, there is personnel integrity and quality.

The staff assume a double part: on one hand, they are the subjects of inward control in the association and control the execution of their task; then again, they are the objects of interior control in the association and regulated and controlled by the other. Anything of inner control framework might not go past the staffs' trustworthiness and quality that makes, oversees, actualizes and administers the framework. Besides, there is the administration style and administration thought (Eden, 2006). The leadership administration style and administration thought impact the method for overseeing of the undertakings, particularly the supervisor singular marvelousness and the capacity to settle on choice. Directors control the endeavor principally by planning the association and administration component, approving and outlining the framework. What's more, in conclusion there is the association structure which including association structure settings, duties portion, what position of the individual in the association is and what power and obligation he has. Association structure is the grantee for the undertaking to accomplish generally speaking.

Internal environment audit practices have variables incorporate, trustworthiness and moral estimations of work force in charge of making, managing and checking the controls, duty and skill of people performing doled out obligations, top managerial staff or review panels, management philosophy and operating style and authoritative structure (which might be an all-around sorted out structure that accommodates appropriate arranging, coordinating and controlling operations or a disordered structure that may just

2.2.3 Control activities and corporate governance

Ray and Pany (2010) referred control exercises as another part of inner controls. They observe that control activities are methodologies and frameworks that certification which organization commands are finished. Control exercises in an association essentially involve; execution surveys (contrasting genuine execution and spending plans, gauges and earlier period execution), data preparing (important to check exactness, culmination and approval of exchanges), physical controls (important to give security over both records and different resources), and isolation of obligations (where no individual ought to handle all parts of an exchange from the earliest starting point to the end).

Internal control ought to be successful when looking at outline and can amazingly be helpful and is as a rule for association administration and broadly to budgetary articulations at present. An extensive variety of business firms have used internal controls through the advancement of ways to deal with certification and protecting assets and profitable business environment especially accounting course of action, organization procedure, and operational approach (Ogneva, Subramanyam and Raghunandan, 2010). Thus, internal control ought to be all the time survey in all parts of the organization and embed inside controls that will reinforce the organization and increment benefit (Skaife, 2009).

Control activities and the Inside control structures ought to be watched - a system that assesses the way of the structure's execution after some time. Constant watching happens in the ordinary course of operations, and joins reliable organization and supervisory activities, and diverse moves staff make in playing out their commitments that assess the way of inside control system execution (Colbert and Bowen, 1996). The expansion and repeat of specific evaluations depend basically on an examination of perils and the feasibility of advancing checking systems (Anduuru, 2005).

Internal control inefficiencies should be represented upstream, with bona fide matters reported quickly to top association and regulating sheets. Internal control systems change after some time (Dumitrescu, 2004). The way controls are associated may progress once suitable frameworks end up being less convincing being a direct result of the arrival of new staff, fluctuating sufficiency of planning and supervision, time and resources necessities, or additional weights. Also, conditions for which control structure was at first sketched out furthermore may change. Corporate governance developments around the world have reaffirmed the responsibility of the board in the process of ensuring the success and efficiency of the internal control framework of the company. As a result, the key role of the internal audit is vital in order to support the board in order to ensure sufficient oversight of internal control as well as in the process of doing so form the integral aspect of the corporate governance framework of the organization.

The key role of the internal audits focuses on the process of assisting the board and/or its audit committee in the process of discharging its governance responsibilities by focusing on the following: an objective assessment of the existing risk and internal control framework; methodical examination of business processes and connected controls; reviews of the subsistence and value of assets; a source of information on major frauds and irregularities; unplanned and informal reviews of other areas of concern, including unacceptable levels of risk; reviews of the agreement framework and specific compliance issues; reviews of operational and financial performance; suggestions for more helpful and competent use of resources; appraisals of the achievement of corporate goals and objectives and finally advice and comment on devotion to the values and code of conduct/code of ethics of the organization (Deloitte, 2005). In this publication, we will be looking at the final two of the five The Committee of sponsoring organization (COSO) components and the related principles

2.2.4 Audit Monitoring Activities

Monitoring refers to the process of assessing the quality of internal control structure overtime. Since internal control is a process, it is usually accepted that they need to be adequately monitored in order to assess the quality and the effectiveness of the system's performance over time. By monitoring, the organization gets provided with assurance that the findings of audits and other reviews are promptly determined (Theotanis *et al.*, 2011). Amuda and Inenga (2009) add that monitoring of operations ensures effective functioning of internal control system.

In addition, monitoring can be achieved by regularly supervising and managing activities like monitoring of customers complain and feedback and audits conducted directly by internal auditors. Monitoring of internal control is performed through application of both ongoing evaluations and separate evaluations. These evaluations ascertain whether other components of internal control continue to function as designed and intended. The evaluation facilitates identification of internal control deficiencies and communicates them to appropriate officials responsible for taking corrective action.

A monitoring process must be capable of addressing the need for revisions in the design of controls based on changing risks at an acceptable level to ensure effective and efficient operations. Ongoing basis monitoring is a process of assessing risks linked to achieving operational objectives. The Committee of sponsoring organization (COSO) model requires establishing a monitoring foundation consisting of procedures of evaluating risks. Monitoring activities include assessment of controls and reporting the results of the assessment together with any required corrective action. A key benefit of internal control monitoring is to provide assurance regarding effective and efficient operations and compliance with applicable laws and regulations.

2.3 Effect of Internal Audit on Corporate Governance

Well performing internal audit function is one of the strongest means to monitor and promote good governance system in an organization. Internal auditing is an integral part of the corporate governance mosaic in both the public and the private sectors (Cohen *et. al.*, 2002). As a result, in many countries it has received an increasing attention as an important component of government financial management and as a tool for improving the performance of the government sector.

According to the professional guidance of the Institute of Internal Auditors (IIA), public sector governance encompasses the policies and procedures used to direct an organization's activities to provide reasonable assurance that objectives are met and that operations are carried out in an ethical and accountable manner. Good governance is considered as a tool that is used in order to achieve strategy of an organization (Belay, 2007). Thus, a growing number of finances restatements by government institutions joined with allegations of financial statement fraud and lack of accountable corporate governance of many government departments. This has helped to grind the ever increasing attention on corporate governance in wide-ranging role and the audit committee in particular. As a result, the function of the committee had changed over the years (Rezaee & Olibe, 2003). Other recent research shows the assurance, compliance and consultant roles of internal auditing are now being recognized at board level in many organizations as valuable contributors to good governance practices.

Most internal audit specialists point out that successful internal audit practices relate with enhanced organizational performance. As indicated by Bejide (2009) an internal audit administration can, particularly, decrease overhead, distinguish approaches to enhance proficiency and increase presentation to conceivable misfortunes from minimal defended organization resources all of which can significantly affect achievement of the organization goal. Additionally, Venables and Impey (2010) expressed that internal audit is a significant instrument of administration for enhancing organization performance.

Fadzil (2005) likewise noticed that internal auditors run an organization proficiently and viably to maximize shareholders' expectations. Hermanson and Rittenberg (2008) pointed out that the presence of a viable internal audit capacity is connected with effective firm performance. Internal oversight includes the internal audit function that must be effective and should comply with generally accepted auditing standards with regards to practice and approach. The focus of internal auditing is to determine whether public funds have been spent for the purposes for which they were appropriated and thereby promoting accountability. Internal audit undertakes reviews of individual systems and processes and consequently makes recommendations to heads of public sector entities on how internal controls could be improved.

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

Internal audit function provides internal consulting service to the management in public sector institutions and hence the executive arm of government for smooth and efficient functioning and for reviewing and improving its performance. It also ensures that there are efficient controls and greater transparency in the decision and policy-making processes of government functionaries and institutions in delivering services successfully and in carrying out development programs in an efficient and appropriate manner. Public Sector controls cover all aspects of activities including financial, managerial and operational policies and are intended to safeguard assets, ensure the accuracy and reliability of financial information and promote operational efficiency.

The internal audit function is in a good position to help senior management of public institutions to identify risks, suggest risk management strategies and, ultimately, provide assurance that the risks are being appropriately managed. Thus, the internal auditing function evaluates the effectiveness of public institutions in achieving agreed objectives and thereby promoting strong governance and accountability regime. Additionally, recent speeches from Securities and Exchange Commission (SEC) officials (Herdman, 2002; Richards, 2002) emphasize the significance of internal audit to a company's governance structure. The vital role that the internal audit function played in the implementation of the reporting requirements of the Sarbanes-Oxley Act of 2002 (SOX) highlights the importance of the function to maintaining strong corporate governance (Rosenstein and Rose, 2006).

Deloitte (2005) noted that without internal audits efforts and expertise in companies 'organizational operations, the business landscape would likely be littered with significantly more disclosures of material weaknesses and revelations of noncompliance with. Based on the Audit Committee, on the one hand internal auditing contribute to corporate governance by bringing best practice ideas about internal controls and risk management processes to the audit committee.

Providing information about any fraudulent activities or irregularities Rezaee and Lander (1993) conducting annual audits and reporting the results to the audit committee and encouraging audit committee to conduct periodic reviews of its activities and practices compared with current best practices to ensure that its activities are constituent with leading practices (Sawyer, 2003). On the other hand, an effective audit committee strengthens the position of the internal audit function by providing an independent and supportive environment and reviews the effectiveness of the internal audit function. External audit is also regarded as an important cornerstone of corporate governance, particularly with respect to the prevention and detection of fraud and errors in financial statements (Davidson et al., 2005).

In the past, managers in the public sector had a narrower range of expectations for the role of internal audit than managers in the private sector. This explains why the internal audit function in the public sector was dominated by pre-payment audits. Thus internal auditors devoted most of their time to the checking on individual transactions before the payments were made. However, in recent years internal auditing has assumed a strategic dimension that underscores an essential component of public sector governance and financial management reforms in many developing countries (Barrier, 2003).

It is now generally accepted that the correlation between internal auditing and corporate governance affects all kinds of economic activities and that the perceived implications and consequences of this interaction have changed considerably in the recent years. Internal auditing and corporate governance have now become a matter of major public concern. Internal auditing is involved in many of the current discussions taking place on corporate governance practices (Mordelet, 2009). The ethical standing of any profession is critical to its reception in the society (Mintz, 1995).

According to Armstrong (1993), ethical conduct focuses at the center of each cause for survival of work. This is the case for the auditing profession where ethical failings can have far-reaching economic influences and result to the extensive financial agony. Ethical values are fundamental for the internal auditors because of two important reasons. First, internal auditors are regularly faced with various ethical problems which can confront their standards (Goodwin & Yeo, 2001). They may face cases which involve and oblige them to speak out and this is not always simple, for the most part when pressure is being exercised by senior management to go with the flow and not to make waves (Thompson, 2003).

Second, with the existing emphasis on corporate governance, it is becoming more and more familiar that internal auditors can play a key function in increasing business ethics and corporate honesty (Moelle, 2004). As one of the important keystones and foundations of corporate governance, internal auditors are anticipated to work with audit committees, boards and senior management to assist put the right tone at the top and helps to guarantee that ethical behavior flows down all the way through the ranks to lower level employees.

2.4 Empirical Studies

An effective internal audit function plays a key role in assisting the board to discharge its governance responsibilities. The study of O'Leary & Stewart (2007) used exploratory study; this had been done by presenting the five ethical dilemmas for 36 internal auditors. For each scenario, a key element of corporate governance was operated in order to assess its influence on ethical decision making. These were audit committee support, management truthfulness regarding different accounting policies, management integrity regarding pressure on internal audit, external auditor characteristics, and organizational code of conduct.

As a result, the researcher had been able to show the different ethical decision-making related to internal audit and corporate governance. On the other hand, Spira & Page (2003) explored the change in internal control using sociological perspectives on risk and its conceptualization to frame the debate about internal control and risk management within the UK corporate governance arena. By using this method, the progresses in corporate governance reporting requirements offer chances for the misappropriation of risk and its management by groups, at the same time, enables to evaluate the current changes in internal audit.

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

Kibet (2008) in his study a survey on the role of internal audit in promoting good corporate governance in State Owned Enterprises (SOEs’) aimed to explore the role and the use of internal audit function in promoting good corporate governance in public sector enterprises and the challenges faced by the internal auditors in state Owned Enterprises (SOEs). The study followed an exploratory research design and the population comprised of all State Owned Enterprises (SOEs) with government equity of over 50% located in Nairobi. A sample of 43 state corporations was selected by way of geographical location and government shareholding. The study concluded that internal audit function played a role in corporate governance.

Krishnan and Visvanathan (2005) in their study sought to address the role of audit committees and auditors in the reporting of internal control deficiencies after the passage of the Sarbanes-Oxley Act (SOX). The study sample comprised of firms selected from the Compliance week and covered a period from November 15, 2004 till March 1, 2005. Compliance Week reported that 164 firms mentioned internal control issues in their filings with Securities and Exchange Commission (SEC) during the sample period. To represent auditor attributes the study examined size of the auditor, tenure, auditor changes, and audit fees.

The study found that a higher number of meetings of the audit committee, lesser proportion of "financial experts" in the audit committee, and more auditor changes characterize firms that report weaknesses in their internal controls compared to firms with no weaknesses. Prior restatements of financial statements are also higher for firms not reporting such weaknesses. The results were robust to controlling for a variety of firm characteristics such as complexity of operations, profitability, and growth. It underscored the importance of governance characteristics beyond general firm characteristics in examining the reporting of internal control weaknesses.

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

Organizations now demands for incredible competency and polished methodology from internal audit, and uncommon resources must be sent all the more capably to minimize and regulate risks (Ramamoorti, 2003). Mechanical progression makes it conceivable to track and examine information with consistently expanding speed therefore making it key for organizations to be very much prompted by the internal audit department (Fish, 2012). Internal audit differs starting with one association then onto the next, and rolling out improvement in modern environment can be a generous undertaking. The move from simply guaranteeing consistence with tenets and directions to relay or convey information worth including requires more than simply organizational changes.

A viable internal audit functions is one of the most grounded devices to screen and improve organization performance. Cohen (2002) pointed out that internal auditing practices are a crucial part of an organization performance in both private and public sectors. Internal control refers to the measures founded by an association in order to guarantee achievement of the substance's targets, goals and operations. These are terms and conditions employed by a firm in guaranteeing that organizations exchanges are prepared in the suitable way to maintain a strategic distance from waste, burglary and abuse of organization assets.

Internal Controls are procedures composed and influenced by those accorded with governance, management, administration, and other staff to give sensible certification about the accomplishment of an element's targets as to unwavering quality of the money related reporting, viability and effectiveness of operations and consistence with pertinent laws and directions (Mwindi, 2008). As indicated by Hayes (2005) internal controls provide sensible yet not outright confirmation to a firm management and board of directors that the organization targets will be accomplished. The probability of accomplishment is influenced by constraints intrinsic in all frameworks of internal control practices. Organizations develop some procedures to ensure its goals and objectives are attained effectively which help them accomplish execution and hierarchical objectives, avoid loss of assets, empower creation of dependable reports and guarantee consistence with laws and directions.

2.5 Theoretical Framework

According to (Carmichael, 2005), the need for theory in auditing, as with any other discipline, is associated with the willingness of the interested parties (shareholders, managers, bankers, auditors, analysts and so on) to form a solid basis for making financial decisions. To acquire the necessary knowledge about these options requires a thorough understanding of the economic variables and of the relationship between them. This can only be done through the use of a theoretical framework, which provides sufficient explanation and reasoning of the variables, their association with each other and the environment in which the economic action is taking place. This study will adopt Agency theory as propounded by Adams (1994) and stewardship theory by (Davis and Donaldson 1997).

2.5.1 Agency theory

Agency theory and the internal audit as propounded by Adams (1994) is one of the theoretical framework that guided this study. Agency theory also provides a useful theoretical framework for the study of internal auditing function. Adams (1994) proposed that agency theory not only helps to explain and predict the existence of internal audit but that it also helps to explain the role and responsibilities assigned to internal auditors by the organization and that agency theory predicts how the internal audit function is likely to be affected by organizational change. He concludes that agency theory provides a basis for rich research, which can benefit both the academic community and internal auditing profession.

According to Anderson, Francis & Stokes (1993), Agency theory describes firms as necessary structures to maintain contracts, and through firms, it is possible to exercise control which minimizes opportunistic behavior of agents. In order to harmonize the interest of the agent and the principal, a comprehensive contract is written to address the interest of both the agent and the principal; they further explain that the relationship is further strengthened by the principal employing an expert to monitor the agent. An agency relationship exists when managers and those employed perform a service on behalf of owners or shareholders with the delegation of some decision-making authority (ICAEW, 2005; Subramaniam, 2006). 'The qualitative state of excellence in decision-making' is good governance (Bridgman, 2007).

However, the momentum of companies being publicly listed made the separation of owners from actively managing their companies more prominent, casting doubts on sound managerial capacities of directors and senior management. Conflicting self-interest of owners and agents, first highlighted by Adam Smith in 1776, in The Wealth of Nations and reiterated by Jensen and Meckling (1976), together with information asymmetries, caused agency problems (ICAEW, 2005; Subramaniam, 2006). In the case of listed companies, the distance between the owners and the agents – the management team – is great; owners who are shareholders are not involved in the management of their organizations.

Jensen and Meckling (1976) argued that agents are inclined not to maximize the wealth of the owners and in mitigation, monitoring activities such as external audits, are imposed by the owners. In Malaysia, three recently reported cases dealt with managerial problems. First, in Southern Bank Bhd., revenue and profits were falsified and creatively accounted for with overstatement of net assets by RM160 million in 2005 (Shah, 2007). Secondly, the revenues of Transmile Group Bhd. from years 2004 to 2006 were overstated by RM622 million (Associated Press, 2007).

Finally, Megan Media Holdings Bhd. suffered losses of RM1, 14 billion in 2007 due to accounting fraud at its subsidiary (Lee *et al.,* 2008). These cases highlight the incongruence in expectations of good governance and, due professional care and diligence, of directors, managers, as well as auditors. Jensen and Meckling (1976) specified two agency costs in the management of companies: monitoring costs and bonding costs. According to Godfrey, Hodgson, & Holmes (2003) monitoring costs include costs of auditing, management compensation plans, budgets and operating rules.

Fees to external auditors are considered as monitoring costs (Godfrey et al., 2003). Notwithstanding the weaknesses in the monitoring activities as indicated in the corporate scandals above, reliance by external auditors on the internal audit function generates cost savings in audit fees to the organization (Brown, 1983; Haron et al., 2004). Internal audit has been identified as a bonding cost because the agents undertake to guarantee against any malfeasance by conducting the checks on their operational activities by appointing specified persons in their companies (Jensen & Meckling, 1976).

Within the organizational structure, internal audit is charged with the oversight of good governance. Internal auditors look at the future by reviewing controls and processes in contrast with external auditors who attest on representations made by management on historical events namely, financial statements for statutory purposes (similarly Dittenhofer, 1997). By evaluating and relying on competent internal audit, the extent of work by external auditors is expected to be reduced.

The simplistic view in agency theory of untrustworthiness of agents negates inherent human nature and motivation. Central to human psychology are the self-actualization needs, first coined by Kurt Goldstein and later used by Maslow: the tendency to achieve one's potential and having the sense of truthfulness (Maslow, 1943). Dittenhofer (1997) clarified that "the need to be accepted and recognized" and the "desire to be a part of the organization" changed the ways internal auditors operate. Agency theory has been an influential and dominant perspective in the study of management for decades (Cruz, Gómez-Mejía, and Becerra, 2010; Davis, Schoorman, and Donaldson, 1997; Nyberg, Fulmer, Gerhart, and Carpenter, 2010).

The view of internal auditors as watchdogs only, is changing. Audit, as it is currently practiced, goes beyond the requirement under existing legislations. It also may provide answers to questions on bias in decision making, particularly in owner controlled companies (ICAEW, 2005). In stating their opinions on the financial statements of a company, the external auditors also form an opinion on the trustworthiness of the internal auditors' work and the system of internal control; reducing external audit work.

The requirement to give value added service to the organization when performing internal audit acknowledges the role of internal auditors working in consultation with management (Bou-Raad, 2000; IIA, 2010b). Instead of auditing, 'assurance services' has been used for reviews made by internal auditors and to provide advice or recommendations to management to assist in business strategies. Through their professional background and competency, internal auditors are involved in the development of internal control structures or management control processes and risk management.

The involvement of internal auditors beyond the role of controllers or monitoring agents contributes to better internal control structure and quality of information for decision-making. Bou-Raad (2000) concluded that internal auditors are able to determine their independence and would not undermine their competency and integrity, and those organizations recognize internal auditors' services in business practices. The emerging recognition of the expanded role of internal auditors and the benefits of internal auditors' services in aiding organizations to meet their business objectives require more than agency theory can explain.

Meckling and Jensen (1976) in their paper on the theory of the firm defined the agency relationship as a contract under which one or more persons (the principal(s) engage another person (the agent) to perform some services on their behalf which involves delegating some decision making authority to the agent. Thus, for the internal audit to be effective there is need for not only their independence but also the top management support. The first scholars to propose, explicitly, that a theory of agency be created, and to actually begin its creation, were Stephen Ross and Barry Mitnick, independently and roughly concurrently.

Ross is responsible for the origin of the economic theory of agency, and Mitnick for the institutional theory of agency. Ross introduced the study of agency in terms of problems of compensation contracting; agency was seen, in essence, as an incentives problem. Mitnick introduced the now common insight that institutions form around agency, and evolve to deal with agency, in response to the essential imperfection of agency relationships. This behavior never occurs as it is preferred by the principal because it does not pay to make it perfect. But society creates institutions that attend to these imperfections, managing or buffering them, adapting to them, or becoming chronically distorted by them. Thus, to fully understand agency, we need both streams to see the incentives as well as the institutional structures (Mitnick, 2006).

From an agency perspective, the importance of strong governance stems from the need to align the interests of management with other stakeholders in the firm in order to reduce agency costs and increase the internal audit department effectiveness. Hastori et al. (2015) and Fauzi and Locke (2012) have found that larger board size reduces the agency cost.

The Gul et al., (2012) and Singh and Davidson (2003) have discovered that smaller board size helps in curtailing the agency cost. Rashid (2015), Gul et al. (2012) and Miller (2009). Various corporate governance mechanisms can be used to monitor the management's behavior and these include independent directors on the board, an independent board chair, an effective audit committee and both external and internal audit. Davidson et al., (2005) describe the complex interactions between these governance mechanisms as the corporate governance mosaic.

Agency theory views audit as one of the monitoring mechanism to curb management aberrant activities. It is assumed that an audit provides an independent check on the work of agents and of the information provided by an agent, which helps to maintain confidence and trust. The auditor’s role is to assess whether the financial statements, prepared by the agent, are faithfully represented and are prepared in accordance with generally accepted accounting principles. The financial statement audit makes management accountable to shareholders for its stewardship of the organization (Akinbuli, 2010 and Hayes, et al 1999 and 2005).

This theory is applicable since not all citizens can participate in the management of nations' resources thus the appointments of officials into public offices by the citizens to manage the public resources on their behalf. But due to information asymmetries between principals (citizens) and agents (public officials) and differing motives, principals may lack trust in their agents and may consequently need to put in place mechanisms to reinforce this trust. Agency theory is extensively employed in the accounting literature to explain and predict the appointment and performance of external auditors and financial consultants.

This theory no doubt relates to this study as it helps to explain the role and responsibilities of internal auditors which if methodically applied would help to improve corporate governance in health sector.

2.5.2 Stewardship Theory

The roots of the stewardship theory are psychology and sociology. Davis, Schoorman and Donaldson (1997) states that theory protects steward and maximize the wealth of shareholders through firm performance, in light of the fact that by so doing, the steward's utility cutoff points are expanded. Based on their definition, stewards are executives and managers of the firm working, protecting and making profits for the shareholders. Contrary to the agency theory that focuses on the perspective of individualism (Donaldson and Davis, 1991), the stewardship theory weights on the top administration's part as stewards who coordinate their objectives as a major aspect of the organization. The hypothesis recommends that stewards are persuaded and fulfilled when hierarchical achievement is accomplished

While Agyris (1973) argues that the theory of agency identifies employees or people as material beings, Donaldson and Davis (1991) observe that the theory of stewardship recognizes the value of structures that empower the steward and offers full autonomy built on trust. Additionally, the approach focuses on the rank of staff or the management to be more independent to maximize the investors‟ returns. In addition, Fama (1980) contends that the directors and administrators also manage their careers so as to portray themselves as active stewards of the organization.

Besides, Shleifer and Vishny (1997) state that managers return finance to shareholders so as to establish a good reputation which will enhance their re-entry in the market for future finance. Davis (1997) and Tosi (2003) contend that the participative management and involvement-oriented philosophy adopted by the theory of stewardship is beneficial to the firm. The Philosophy reduces the need for austere internal control methods to curb agency costs and governance challenges, part of which involves the work of internal audit in a company.

According to Meckling and Jensen (1994), when owners directly manage their firm's costs incurred in controlling agency problems such as reducing moral hazards, and information asymmetries are reduced. Besides, when owners manage their companies, they are more likely to align their interests with growth opportunities and risk. Therefore, stewardship theory differs from agency theory in that it does not emphasize the need to incur agency or monitoring cost which incorporates setting up internal audit function. However, Donaldson and Davis (1991) argue that amalgamation, rather than separation, of the two theories, enhances the proceeds of a company.

In working towards organizational ends the personal needs of directors are fulfilled (Sundaramuthy and Lewis 2003; Kluvers and Tippett 2011). Therefore, managers must seek ways to strike a balance between agency theory and stewardship theory. In this study, stewardship theory assumes that managers keep their best interests in mind to the detriment of shareholders. It determines certain components whose risks are associated with auditing practices in the organization. The theory aims to motivate managers and auditing committee to be keen on identifying any risk that may arise on failure by the accountants and auditors to give clear position of an organization. The key presumption underlying the solutions of Stewardship Theory is that the practices of the chief are adjusted to the interests of the principals.

2.6 Conceptual Framework

The independent variables in this research are the risk management, internal environment audit practices, control activities and audit monitoring controls, while the dependent variable is corporate governance.

Independent Variables **Dependent Variable**

Internal Audit **Corporate Governance**

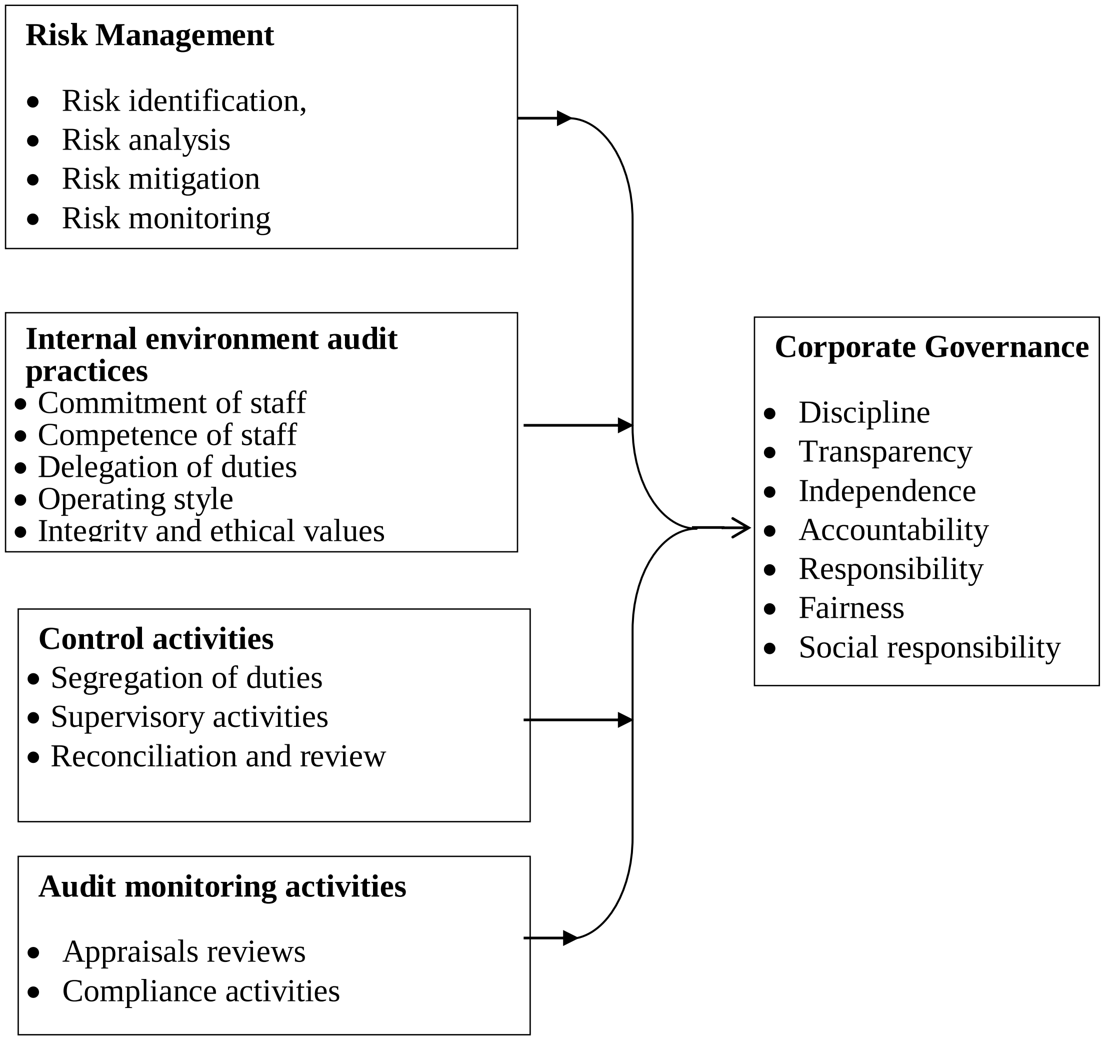

Figure 2.1: Conceptual framework

CHAPTER THREE

RESEARCH METHODOLOGY

3.0 Introduction

This chapter presents the research design, study areas, target population, description of the sample and sampling procedures, description of the data collection instruments, validity and reliability of the research instruments, data collection procedures, data analysis procedures and ethical considerations.

3.1 Research Design

An explanatory research design was employed. According to Trochim (2004), this design is used to structure the research to show how all of the major parts of the research samples or groups measure treatments and methods of assignment work together to address the central research questions. Explanatory research design was used to determine the effect of internal audit practices on corporate governance of the health sector in Kenya. This is consistent with the findings by Cooper & Schindler (2008) that often when the universe of study is unknown, explanatory design forms the first step of the research.

The study adopted explanatory research design that is quantitative in nature and hypotheses tested by measuring the relationships between variables while data was analyzed using statistical techniques. It also included other types of quantitative research which attempted to identify causal relationships through the analysis of correlations between variables (Maxwell & Mittapalli, 2008). The study used terms such as influence, impact and effect which contribute to common qualitative research and such terms imply causal relationship.

The explanatory research design is suitable because the study is mainly concerned with quantifying a relationship or comparing groups purposely to identify a cause-effect relationship. The design was adopted as it supports the use of quantitative data and promotes comparison and statistical analysis. The design is intended to provide statistical information about aspects of internal audit practices on corporate governance of the health sector in Kenya that is of interest to policy makers. This enabled the researcher to collect data from the health sector in Kenya.

3.2 Study Area

This study area was selected to determine the effect of internal audit practices on corporate governance of the health sector in Kenya since there is no similar study having been done in the study area. It is therefore believed that the study area gives a wide and varied view of the problem under study and become a representative sample.

3.3 Target Population

The study sought the views from internal auditors and risk managers of the referral hospitals in the health sector. The target population of this study was 110 auditors of Referral hospitals in the health sector of Kenya.

3.4 Sampling Procedures and Sample Size

The purpose of sampling is to gain an understanding about some features or attributes of the whole population based on the characteristics of the sample. The sampling frame for this study was internal auditors and risk managers of the Referral Hospitals in the health sector of Kenya. The researcher used simple random sampling technique to select the internal auditors of Referral Hospitals in the health sector. Simple random sampling was used as a major sampling technique because each respondent had an equal chance of inclusion in the sample. It was appropriate because the entire population was relatively large, diverse and sparsely distributed, hence random sampling technique helped to achieve the desired objective. This technique was appropriate for the study as it is cost effective and efficient in administration.

The sampling technique gave each respondent in the population an equal probability of being the sample. This allowed equal representation of all individuals in the defined population to be selected as part of the sample (Kombo & Tromp, 2006). This is important as it helps reduce biases that may arise. This technique is appropriate for the study since it is a representative sample and that all the members of the target population were represented. The sampling technique gave each element in the population an equal probability of getting into the sample. Using Yamane's (1972) sample size formula at 95% confidence level, P = 0.5, the sample size will be computed:

$$n = \frac{N}{1 + N(e)^2}$$

Where;

n = the sample size,

N = the population size,

e = the acceptance sampling error

= $110/1+110(.05)^2$ = 110/1.275 = 110/1.275

= 86 respondents.

From the target population of 110 and a sample size of 86 respondents was selected.

3.5 Research Instruments

The research instruments that were used in this study are questionnaires and interview schedules.

3.5.1 Questionnaire

Primary data was collected by use of structured questionnaires that captured the various variables of the study. Questionnaires are set of questions which gave answers of the research participants in a set of ways. Most questionnaires were designed to gather already structured data and so include a set of answers which the respondent chose from, although some may include more open-ended questions. This gave a provision where all the participants are asked the same questions in the same order and using the same wording and have the same set of answers to choose from (Matthews & Ross 2010).

According to Kothari (2008), questionnaires are usually free from the interview bias as the answers are in respondent's own words. Respondents had an adequate time to give well thought out answers. It will have an advantage of obtaining standard responses to items, making it possible to compare between sets of data (Matthews & Ross 2010). It also allowed the participants to give their own opinion on the issue at stake. The questionnaires were designed to address specific objectives. It had both closed-ended and open-ended questions that were administered to internal auditors of the health sector who participated in the study. The closed ended items gave precise information which minimized information bias and facilitated data analysis by generating quantitative data.

3.5.2 Interview Schedule

Orodho (2008) postulate that many people are willing to communicate orally than in writing and they would provide data more readily and fully than on a questionnaire. According to Kumar (2006), the advantages of using a structured interview is that the level of incomplete questionnaires is reduced. The researcher was able to clarify any queries concerning the questions. This ensured that answers reliably aggregated and that comparisons could be made. A structured interview schedule was used to gather information from risk managers. The interview schedule designed was structured according to research objectives.

3.6 Piloting

To test the validity and reliability of the research instruments, pilot-tested questionnaire was used. Orodho (2003) posits that a pilot study is necessary for testing the reliability of data collection instruments. The pilot study was conducted to refine the questionnaire, identify loopholes in the instrument before the actual survey. The researcher conducted a pilot study among risk managers and internal auditors of the Referral Hospitals in the health sector from Kakameka County and others which have similar characteristics within North Rift region. The pilot study enabled the researcher to ascertain the reliability and validity of the research instruments.

3.6.1 Validity

According to (Paton, 2002) validity is quality attributed to proposition or measures of the degree to which they conform to establish knowledge or truth. During questionnaire development, various validity checks were conducted to ensure the instrument measure what it was supposed to measure. Validity is the extent to which a construct measures what it is supposed to measure (Hair *et al.*, 2007). There are three important approaches to assessing measurement validity: content validity (also referred to as face validity), construct validity and criterion validity. The study utilized content and construct validities. Content validity is the most important validity test (Hair *et al.*, 2007). It was based on the extent to which a measurement reflects the specific intend domain of content. To ensure content validity, discussions were held with experts during the instrument formulation stage to ensure that the measure included an adequate and representative set of items given in the content.

Face validity simply means that the validity is taken at face value. As a check on face validity, research instruments were given to experts to obtain suggestions for modification. Face validity indicates that the items that are intended to measure a concept on the face will look like they measure the concept. Face Validity will be established by ascertaining whether at face value, the questions appear to be measuring the construct as per the research objectives. The researcher observed this to ensure that the instruments provide adequate coverage of the study concepts.

Construct validity assesses what the construct or scale is in fact measuring. Construct validity was maintained through anchoring of the constructs to the theory from which they derived. The validity of the instrument was determined by the researcher using expert judgment. This was done by discussing the items in the instrument with the supervisors, lecturers from the department of Finance and made necessary modifications. Advice given by these people helped the researcher improve the validity of the research instruments.

3.6.2 Reliability

Regardless of the research procedure used and the method employed, researchers need to consistently measure what it ought to accurately. In order to test the reliability of the research instrument, the test- retest method was used. The questionnaire was administered during the pilot study and Cronbach's Coefficient Alpha was used to determine the reliability of the research instrument. A reliability coefficient of 0.7 and above was assumed to reflect the internal reliability of the instruments (Fraenkel & Wallen, 2000). The entire questionnaire was deemed as reliable after several typographical errors and omissions detected were corrected in the instrument confirming that it is sufficient to be used in the main study.

3.7 Data Analysis

After all data had been collected, the researcher conducted data cleaning, which involved identification of incomplete or inaccurate responses and corrected to improve the quality of the responses. The data was coded and entered in the computer for analysis using the Statistical Package for Social Sciences (SPSS). The research yielded both qualitative and quantitative data. Qualitative data was analyzed qualitatively using content analysis based on analysis of meanings and implications emanating from respondent's information and documented data.

Quantitative techniques such as inferential statistics were used to understand relationships between different variables. The descriptive analyses that were used include mean, percentages, standard deviation and frequencies. Inferential statistics was used to analyze relationship between variables. This was done using correlation and multiple regression analysis. Pearson product moment of correlation was used to determine the effect of internal audit on corporate governance of the health sector in Kenya. It was appropriate to use the technique since the data used was of interval scaled variables. The multiple regression analysis was used to explain the extent to which internal audit (independent variable) explains the corporate governance of the health sector in Kenya (dependent variable).

The multiple regression is a parametric statistic used since the data adhere to the following assumptions or parameters (Field, 2009): data must be on interval level, a linear relationship must exist (will be indicated by means of a scatter plot), the distributions must be similar (thus, if they are skewed, they must be skewed in the same direction), but preferably normal, outliers must be identified and omitted from the computation. Through Multiple regression analysis, scatter plot was used to determine whether there were linear relationships between independent and dependent variables. Multiple regression analysis was used to test Hypotheses. The multiple regression equation model will be as follows:

$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon$………………………………...…………Equation 1

Where:

Y= Corporate governance

β0=Regression Constant

$\beta_1 X_1$=risk management

$\beta_2 X_2$=internal environment audit practices

$\beta_3 X_3$= control activities

$\beta_4 X_4$= audit monitoring activities

ε=Error term

CHAPTER FOUR

DATA PRESENTATION, ANALYSIS AND INTERPRETATION

4.0. Introduction

This chapter presents the data, analyses the data and interprets the information from the findings which were collected through the questionnaires and interview schedules in order to provide a real picture about the effect of internal audit practices on corporate governance of the health sector in Kenya. The chapter is organized as follows: back ground information, descriptive analysis, correlation and multiple regression analysis. The data contain responses from the respondents' questionnaire for the employees. A total of 83 questionnaires were returned out of the 101 that were given out. This have a response rate 96.5%.

4.1 Background Information of the Respondents

The background information was sought during the study and comprised of gender, age and length of service.

4.1.1 Gender of the respondents

The study aimed to establish the distribution of respondent's gender. According to the study findings most (51.8%) of the respondents were male while the rest 48.2% were female. It can therefore be concluded that majority or most of the employees in the audit department were male while their counterparts occupy the other portion.

Table 4.1: Gender of Respondents

	Frequency	Percent	Cumulative Percent
Male	43	51.8	51.8
Female	40	48.2	100.0
Total	**83**	**100.0**	

Source: Survey data, 2018.

4.1.2 Age of the respondents.

From the study 28, (33.7%) of the respondents aged between 40 and 49 years and 25(30.1%) were aged between 30 and 39 years whereas, 30(36.1%) aged 21 and 29 years. This depicts that majority of the auditors involved in the study aged more than 30 years.

Table 4.2: Age of Respondents

	Frequency	Percent	Cumulative Percent
40-49 Years	28	33.7	33.7
30-39 Years	25	30.1	63.8
21 -29 years	30	36.1	99.9
Total	**83**	**100.0**	

Source: Survey data, 2018.

4.1.3 Length of Service of Respondents

From the study findings most 44(53%) of the respondents had worked in the organizations for a period of 11-15 years, whereas 19(22.9%) had worked for a period of between 16 and 20 years, while 13 (15.7%) had worked for a period of 6 and 10 years and the rest 7(8.4%) had served in the organization for more than 21 years. This suggests that most of the respondents of this study had worked for an abundant time therefore they were familiar with the data that the study looked for relating to the health sector.

Table 4.3: Length of Service of Respondents

	Frequency	Percent	Cumulative Percent
6-10years	13	15.7	15.7
11-15 years	44	53.0	68.7
16-20 years	19	22.9	91.6
21 and above	7	8.4	100.0
Total	**83**	**100.0**	

Source: Survey data, 2018.

4.2 Descriptive Analysis

Descriptive analysis was used to describe the features of independent and dependent variables as per the provided summaries about the variable measures. The independent variables comprise of Risk management, internal environment audit practices, Control activities and audit monitoring activities. The findings were based on a 5-point Likert scale with 5 –Strongly Agree; 4 - Agree; 3 - Neutral; 2 –Disagree; 1 –Strongly Disagree. The descriptive analysis used included mean, standard deviation, skewness and kurtosis. The mean was used as a measure of central tendency, while standard deviation was used as a measure of dispersion to inform how the responses were dispersed from the mean.

4.2.1 Descriptive Statistics on Corporate Governance

The dependent variable during the study was corporate governance of the health sector in Kenya. Study respondents were asked to rate on a five-point Likert scale their level of agreement on several statements describing the corporate governance of the health sector in Kenya and their response are summarized in Table 4.4. Majority of the respondents agreed that the discipline in the healthy sector has improved as indicated by a mean of (3.88). Transparency in the health sector was also established to have improved as shown by a mean of (3.80).

The independence of health sector has improved as indicated by a mean of (3.82). The respondents agreed that accountability has improved as shown by a mean of 3.87. The responsibility of the health sector's audit has improved as shown by a mean of 4.04. The fairness of the health sector has improved as shown by a mean of 3.83 and finally the social responsibility in the health sector has improved as shown by a mean of 4.25.

Table 4.4: Descriptive Statistics of Corporate Governance

	Mean	Std. Deviation	Skewness	Kurtosis
Discipline	3.88	1.03	-1.27	1.42
Transparency	3.80	1.10	-0.87	0.00
Independence	3.82	1.19	-1.12	0.48
Accountability	3.87	1.08	-1.16	0.84
Responsibility	4.04	1.08	-1.34	1.41
Fairness	3.83	1.29	-1.09	0.12
Social responsibility	4.25	0.95	-1.59	2.61
Mean	**3.92**	**0.76**	**-1.16**	**1.27**

Source: Survey data, 2018.

The findings showed that all the statements representing corporate governance had a mean score of between 3.80 and 4.25. This indicated that the respondents rated the corporate governance variable to have improved as shown by a mean score of 3.92. Similarly, the standard deviation ranged between 0.95 and 1.29. For item scores, skewness values were smaller than -1.59 and kurtosis values were smaller than 2.61 (Table 4.4). With regard to the average scores, skewness value was -1.16 and kurtosis was 1.27 respectively. This falls below the cut-off values for severe non-normality (skewness values > 2 and kurtosis values > 7) proposed by Curran, West, & Finch (1996). It could then be deduced that the responses to the corporate governance items were not deviating much from the expected responses.

From the seven statements used in explaining corporate governance, it was noted that they had an overall mean score of 3.92 indicating that respondents rated the corporate governance in the health sector to have improved. The study finding on corporate governance indicated that the independence, fairness, responsibility, accountability, social responsibility, discipline and transparency have improved in the health sector.

4.2.2 Descriptive Statistics on Independent Variables

The respondents were asked to rate on a five-point Likert scale their level of agreement on several statements describing the independent variables. The independent variables comprise of risk management, internal environment audit practices, control activities and audit monitoring activities. The findings were based on a 5-point Likert scale with 5 –Strongly Agree; 4 - Agree; 3 - Neutral; 2 –Disagree; 1 –Strongly Disagree. The descriptive analysis used included mean, standard deviation, skewness and kurtosis as summarized in the following sections.

Table 4.5: Risk management

	Mean	Std. Deviation	Skewness	Kurtosis
Risk identification	3.7711	1.28144	-1.054	.069
Risk assessment	3.1205	1.38280	-.136	-1.382
Risk mitigation	3.7952	1.10165	-.871	.000
Risk monitoring	3.7952	1.18691	-1.116	.480
Suggest risk management strategies	3.8675	1.07942	-1.161	.840
Provide assurance that the risks are being appropriately managed	4.0361	1.07574	-1.338	1.409
Assess ethics and values within the organization	3.7952	1.28556	-1.088	.121
Assess performance management	3.8795	1.14122	-.868	.050
Assess communication of risk	3.3976	1.14700	-.736	-.278
Unplanned and informal reviews of other areas of concern, including unacceptable levels of risk	3.7952	1.10165	-.871	.000
Mean	**3.7253**	**.64710**	**-1.082**	**1.009**

Source: Survey data, 2018.

The findings showed that all the statements representing the risk management had a mean score of between 4.0361 and 3. 1205. This indicates that the respondents rated risk management variable to have improved as shown by a mean score of 3. 7253. Standard deviation ranged between1.07574 and 1. 38280. Skewneness values were smaller than -1.338 while Kurtosis was 1.409 (Table 4.5). With reference to the average scores, skewness value was -1.082 and kurtosis was 1.009 respectively. This falls below the cut-off values for severe non-normality (skewness values > 2 and kurtosis values > 7) proposed by Curran, West, & Finch (1996). It could then be seen that the statement used to explain the risk management were normal.

Table 4.6: Internal environment audit practices

	Mean	Std. Deviation	Skewness	Kurtosis
Reviews of individual systems and processes	3.7952	1.18691	-1.116	.480
Provide Financial controls	3.8675	1.07942	-1.161	.840
Managerial controls	4.0361	1.07574	-1.338	1.409
Operational policies controls	3.7952	1.28556	-1.088	.121
Control information within the organization	3.6145	1.31438	-.800	-.451
Accounting Information and communication	4.1446	1.06075	-1.427	1.542
Assessment of internal control framework	3.7470	1.31449	-.969	-.116
Methodical examination of business processes and connected controls	3.7952	1.10165	-.871	.000
Provision of independent verification of a sufficient sample of transactions to ensure integrity of the decision-making process	3.7952	1.18691	-1.116	.480
Ongoing and independent reconciliation of all balances	3.8675	1.07942	-1.161	.840
Mean	**3.8631**	**.63086**	**-.772**	**-.063**

Source: Survey data, 2018.

The findings showed that all the statements representing the internal environment audit practices had a mean score of between 4.1446 and 3. 6145. This indicates that the respondents rated Internal environment audit practices variable to have improved as shown by a mean score of 3. 8631. Standard deviation ranged between 1.31449 and 1. 06075. Skeweneness values were smaller than -1.338 while Kurtosis was 1.542 (Table 4.6). With reference to the average scores, skewness value was -1.772 and kurtosis was -.063, respectively. This falls below the cut-off values for severe non-normality (skewness values > 2 and kurtosis values > 7) proposed by Curran, West, & Finch (1996). It could then imply that the statement used to explain internal environment audit practices were good.

Table 4.7: Control activities

	Mean	Std. Deviation	Skewness	Kurtosis
Provides effective systems for managing and accounting for physical and financial assets	4.0361	1.07574	-1.338	1.409
Provide Financial controls	3.7952	1.28556	-1.088	.121
Reviews of operational and financial performance	3.3373	1.23246	-.596	-.655
Operational policies controls	3.5060	1.22348	-.649	-.592
Provides for the timely reconciliation of accounts	3.5904	1.37074	-.645	-.895
Accounting Information and communication	4.1205	1.04061	-1.311	1.131
Assessment of internal control framework	4.2048	.83752	-1.299	2.338
Methodical examination of business processes and connected controls	3.7952	1.10165	-.871	.000
Ensure reliability and integrity of financial and operational information	3.8313	1.20789	-1.114	.410
Ongoing and independent reconciliation of all balances	3.8916	1.03608	-1.126	.887
Mean	**3.8048**	**.61166**	**-.725**	**-.204**

Source: Survey data, 2018

The findings showed that all the statements representing the control activities in this study had a mean score of between 4.2048 and 3. 3373. This indicates that the respondents rated Control activities variables to have improved as shown by a mean score of 3.8048.Standard deviation ranged between 1.37074 and.83752.Skewness values were smaller than -.596 while Kurtosis -.895.(Table Table 4.7).With reference to the average scores, Skeweness value was -.725 and Kurtosis -.204, respectively. This falls below the cut-off values for severe non-normality (skewness values > 2 and kurtosis values > 7) proposed by Curran, West, & Finch (1996). It could then imply that the statement used to explain control activities were good.

Table 4.8: Audit monitoring activities

	Mean	Std. Deviation	Skewness	Kurtosis
Ensure disbursements comply with specified procedures	3.9036	1.12200	-1.133	.570
Provision of independent verification of a sufficient sample of transactions to ensure integrity of the decision-making process	3.7108	1.21505	-.885	-.200
Providing information about any fraudulent activities or irregularities	3.8916	1.04779	-1.017	.632
Assessment of risks	3.8193	1.11688	-1.140	.673
Appraisals of the achievement of corporate goals and objectives	3.7349	1.30743	-1.034	-.049
Compliance with laws, regulations, and contracts	3.7831	1.21020	-1.093	.285
Advice and comment on devotion to the values and code of conduct/code of ethics of the organization	4.2771	.85985	-1.517	2.747
Mean	**3.8744**	**.66574**	**-.700**	**.043**

Source: Survey data, 2018.

The findings showed that all the statements representing Audit monitoring activities had a mean score of between 4.2771 and 3.7108.This indicates that the respondents rated Audit monitoring activitie**s** variables to have improved as shown by a mean score of 3.8744.The Standard deviation ranged between 1.30743 and .85985. Skweness values were smaller than1.517 while Kurtosis was -.200. (Table 4.8), respectively. This falls below the cut-off values for severe non-normality (skewness values > 2 and kurtosis values > 7) proposed by Curran, West, & Finch (1996). It could then imply that the statement used to explain audit monitoring activities were good.

4.3 Correlation Analysis on study Variables

The researcher runs the correlation matrix in order to check whether there was association between variables. To achieve this, Pearson's correlation was carried out and was appropriate because all the variables were in interval scale. The findings of the correlation analysis (As shown in table 4.9) indicated that there is a positive correlation between risk management and corporate governance in the health sector (r=0.874, p=0.000). Therefore, an increase in risk management led to improvement in the corporate governance in the health sector.

Results of the study also showed that there is a significant positive correlation between internal environment audit practice and corporate governance in the health sector (r=0.904, p=0.000). Thus, an increase in internal environment audit practice led to improvement in the corporate governance in the health sector. The findings of the correlation analysis indicated that there is a positive correlation between control activities and corporate governance in the health sector (r=0.813, p=0.000). Therefore, an increase in control activities led to improvement in the corporate governance in the health sector. Results of the study also showed that there is a significant positive correlation between monitoring activities and corporate governance in the health sector (r=0.411, p=0.000). Thus, an increase in monitoring activities led to improvement in the corporate governance in the health sector.

Table 4.9: Correlation Analysis of the Variables

		Governance	Risk	Environment	Control	Monitoring
Governance	Pearson Correlation	1	.874**	.904**	.813**	.411**
	Sig. (2-tailed)		.000	.000	.000	.000
Risk	Pearson Correlation	.874**	1	.845**	.757**	.388**
	Sig. (2-tailed)	.000		.000	.000	.000
Environment	Pearson Correlation	.904**	.845**	1	.829**	.299**
	Sig. (2-tailed)	.000	.000		.000	.006
Control	Pearson Correlation	.813**	.757**	.829**	1	.322**
	Sig. (2-tailed)	.000	.000	.000		.003
Monitoring	Pearson Correlation	.411**	.388**	.299**	.322**	1
	Sig. (2-tailed)	.000	.000	.006	.003	

** Correlation is significant at the 0.01 level (2-tailed).
b Listwise N=83

4.4 Multiple Regression Analysis

A multiple regression model was used to explore the relationship between the effect of internal audit practices (risk management, internal environment audit practices, control activities and audit monitoring activities) on corporate governance of the health sector in Kenya. The R^2 represented the measure of variability in corporate governance in health sector that the predictors are accounting for.

From the model, (R^2 = .874) showing that factors account for 87.4% variation in corporate governance in health sector. The predictors used in the model captured the variation in the corporate governance in health sector. The change statistics were used to test whether the change in adjusted R^2 is significant using the F-ratio as shown in Table 4.10. The model caused adjusted R^2 to change from zero to .874 and this change gave rise to an F- ratio of 135.45, which is significant at a probability of .05.

Table 4.10: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df2	Sig. F Change
1	.935[a]	.874	.868	.27700	.874	135.452	4	78	.000

a. Predictors: (Constant), Monitoring, Environment, Control, Risk

The analysis of variance was used to test whether the model could significantly fit in predicting the outcome than using the mean as shown in (Table 4.11). The regression model with the predictor was significant (F=135.45, p value =0.001) shows that there is a significant relationship between internal audit practices and corporate governance in health sector. Additionally, the F-statistic is significantly greater than 1 thus indicating the appropriateness of the model in testing the relationship between independent and dependent variable. This means that the model is appropriate for use running a factor analysis. Thus, there is significant relationship between internal audit practices and corporate governance in health sector in Kenya.

Table 4.11: ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	41.571	4	10.393	135.452	.000[b]
	Residual	5.985	78	.077		
	Total	47.556	82			

a. Dependent Variable: Governance
b. Predictors: (Constant), Monitoring, Environment, Control, Risk

4.4.1 Regression Coefficients

In addition, the β coefficients for internal audit practices as independent variables were generated from the model in order to test the hypotheses of the study. The t-test was used as a measure to identify whether the internal audit practices as predictor is making a significant contribution to the model. Table 4.12 gave the estimates of β-value and the contribution of each predictor to the model. The β-value for risk management, internal environment audit practices, control activities and audit monitoring activities had a positive coefficient, depicting positive relationship with corporate governance in health sector as summarized in the model as:

$Y = -0.843+0.370X_1+0.613\ X_2+0.153X_3+0.112X_4 +\varepsilon$ ………..…...…… Equation 4.1

Where: Y = corporate governance, X_1 = risk management, X_2 = internal environment, X_3 = control activities, X_3 = monitoring activities, ε = error term

From the findings, the t-test associated with β-values was significant and the internal audit practices as the predictor was making a significant contribution to the model. The coefficients results showed that the predicted parameter in relation to the independent factors was significant. The study hypothesized that there was no significant relationship between risk management and corporate governance in health sector. The study findings depicted that there was a positive significant relationship between risk management and corporate governance in health sector (β_1=0.370 and p value<0.05). Since the *p* value was less than 0.05 the null hypothesis (**Ho_1)** was rejected. The proper risk management led to an increase in corporate governance in health sector in Kenya. A good risk management led to an improvement in corporate governance in health sector in Kenya. The findings of the study are consistent with Saunders and Cornett (2006) study that current organizations are in the hazard administration business as they embrace the elements of bearing and overseeing dangers in the interest of their clients through the pooling of dangers and the offer of their administrations as hazard authorities.

The study hypothesized that there was no significant relationship between internal environment audit practices and corporate governance in Kenya's health sector. The findings showed that there was a positive significant relationship between internal environment audit practices and corporate governance in health sector (β_2=0.613 and p value<0.05). Since the *p* value was less than 0.05 the null hypothesis (**Ho_2)** was rejected. A good internal environment audit practices led to an improvement in corporate governance in health sector in Kenya.

A rise in internal environment audit practices led to a rise in corporate governance in health sector in Kenya. This agrees with Cai (2007). Internal auditing shapes a key managerial control mechanical assembly that is clearly associated with the structure and general standards of an affiliation. An effective internal audit service help to reduce overhead, distinguish approaches to enhance proficiency and boost introduction to conceivable misfortunes from deficiently shielded organization resources all of which can significantly affect the main issue.

Table 4.12: Regression Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	-.843	.233		-3.613	.001		
	Risk	.370	.093	.314	3.981	.000	.259	3.861
	Environment	.613	.109	.508	5.650	.000	.200	5.010
	Control	.153	.091	.123	1.673	.098	.299	3.346
	Monitoring	.112	.050	.097	2.223	.029	.839	1.192

a. Dependent Variable: Governance

Internal audit practices helps an organization to achieve its goals by bringing an orderly, trained way to deal with, assess and enhance the adequacy of hazard administration, control, and administration forms. The internal audit action assesses chance exposures identifying with the association's administration, operations and data frameworks. The interior evaluators are relied upon to give proposals to change in those territories where openings or insufficiencies are distinguished. Cohen (2002) pointed that internal auditing practices is a crucial part of an organization performance in both private and public sectors. Internal audit helps an organization to complete its targets by bringing a composed, restrained approach that to build up the adequacy of hazard administration, control and administration forms (IIA, 2004). Internal audit practices in organization can fundamentally influence the operations of the business and may affect the capacity of the firm to remain competitive.

The study had further hypothesized that there was no significant relationship between organization control activities and corporate governance in health sector. The findings indicted that there was a positive insignificant relationship between control activities and corporate governance in health sector (β_3=0.153 and p value >0.05). Since the *p* value was more than 0.05 the null hypothesis (**Ho_3**) fails to be rejected. Hence the conclusion that the control activities do not improve corporate governance in health sector in Kenya. The findings of the study are consistent with the results of Anduuru (2005) that organizations that have control activities in place outdo the one without in their performance.

The study also hypothesized that there was no significant relationship between audit monitoring activities and corporate governance in health sector. The findings showed that there was a significant positive relationship between audit monitoring activities and corporate governance in health sector (β_4=0.112 and p value<0.05). Since the *p* value was less than 0.05 the null hypothesis (**Ho_4**) was rejected. A good audit monitoring activities led to an improvement in corporate governance in health sector in Kenya. A rise in audit monitoring activities led to a rise in corporate governance in health sector. This agrees with Hayes (2005) that internal controls provide sensible yet not outright confirmation to a firm management and board of directors that the organization targets will be accomplished. On internal control practices, the study concluded that a company's internal control practices is widely believed to be crucial to the success of an enterprise since it acts as a powerful brake on the possible deviations from the predetermined objectives and policies. This implies that an organization that set up a suitable and sufficient arrangement of internal controls is outdoing it is competitors and player that do not have such systems. Thus inadequate control systems may have negatively affected an organization's success and that successful internal control practices is connected with prudent organizational performance.

From the model, (R^2 = .874) showing that the factors account for 87.4% variation in corporate governance in health sector. The predictors used in the model captured the variation in the corporate governance in health sector. This finding support the findings of Hayes (2005) that internal control involves five parts; the internal environment audit practices, the risk assessment, advanced information communication systems, control activities and audit monitoring controls.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter depicts the summary of the findings, conclusions and recommendations. The chapter is therefore structured into summary of findings, conclusions, recommendations and areas for further research.

5.2 Summary of the Findings

The study findings indicated that the internal audit with respect to risk management in the health sector in Kenya were achieved through risk identification, mitigation and monitoring. The risk management strategies, provide assurance that the risks are being appropriately managed, assess ethics and values within the organization, assess performance management and had unplanned and informal reviews of other areas of concern, including unacceptable levels of risk. There was a significant positive relationship between risk management and corporate governance in health sector (β_1=0.370 and p value<0.05). The null hypothesis (Ho_1) was rejected. Proper risk management led to an increase in corporate governance in health sector. A good risk management led to an improvement in corporate governance in health sector.

The findings indicated that internal environment audit practices enabled the referral hospitals in Kenya to review individual systems and processes, perform managerial controls and control information within the organization. There was provision of independent verification of a sufficient sample of transactions to ensure integrity of the decision-making process and make provision for adequate communication. The internal audit makes sure employees, contractors and suppliers have skills needed and appropriate training; meet the requirements of formal Environmental management system (EMS) standard and meet legal requirements. There were effective emergency procedures and control systems that agree with policies, objectives and targets of Environmental management system

There was a positive significant relationship between internal environment audit practices and corporate governance in health sector ($\boldsymbol{\beta_2}$=0.613 and p value<0.05). The null hypothesis (Ho_2) was rejected. A good internal environment audit practice led to an improvement in corporate governance in health sector. A rise in internal environment audit practices led to a rise in corporate governance in health sector. Therefore, providing a proper control environment for any public sector entity is very essential to the effectiveness of its operations and transparency in reporting. Internal audit function plays a role of managing control environment of the entity.

The control activities in the internal audit comprise of provision of accounting information and communication, effective systems for managing and accounting for physical and financial assets. The methodical examination of business processes and connected controls, provide financial controls as well as ensuring reliability and integrity of financial and operational information together with ongoing and independent reconciliation of all balances.

There was a positive insignificant relationship between control activities and corporate governance in health sector ($\boldsymbol{\beta_3}$=0.153 and p value >0.05). The null hypothesis (Ho_3) fails to be rejected. Therefore, we can conclude that the more the control activities do not improve corporate governance in health sector. Organizations establish systems of internal control to help them achieve performance and organizational goals, prevent loss of resources, enable production of reliable reports and ensure compliance with laws and regulations.

This study finding indicated that the audit monitoring activities in the health sector consist of advice and comment on devotion to the values and code of conduct/code of ethics of the organization, ensure disbursements comply with specified procedures and providing information about any fraudulent activities or irregularities. There was assessment of risks, compliance with laws, regulations, and contracts and appraisals of the achievement of corporate goals and objectives.

The findings showed that there was a positive significant relationship between audit monitoring activities and corporate governance in health sector ($\boldsymbol{\beta_4}$=0.112 and p value<0.05). The null hypothesis (Ho_4) was rejected. A good audit monitoring activity led to an improvement in corporate governance in health sector. A rise in audit monitoring activities led to a rise in corporate governance in health sector. Internal auditors play a key role in monitoring a company's risk profile and identifying areas to improve risk management.

From the model, (R^2 = .874) showing that the factors account for 87.4% variation in corporate governance in health sector. The predictors used in the model captured the variation in the corporate governance in health sector. The β-value for risk management, internal environment audit practices, control activities and audit monitoring activities had a positive coefficient, depicting positive relationship with corporate governance in health sector in Kenya.

5.3 Conclusion of the Study

The risk management strategies provide structured and coherent approach to identifying, assessing and managing risk. Risk management influences the corporate governance in the health sector positively. Proper risk management always increased corporate governance in health sector. A good risk management also led to an improvement in corporate governance in health sector.

The internal environment audit practices enabled the hospitals in Kenya to review individual systems and processes, perform managerial controls and control information within the organization. It ensured integrity of the decision-making process and made provision for adequate communication. A good internal environment audit practices led to an improvement in corporate governance in health sector. Providing a proper control environment for any public sector entity is very essential to the effectiveness of its operations and transparency in reporting. Internal audit function plays a role of managing control environment of the entity.

The control activities in the internal audit enabled provision of accounting information and communication, effective systems for managing and accounting for physical and financial assets. The methodical examination of business processes and connected controls, provide financial controls as well as ensure reliability and integrity of financial and operational information as well independent reconciliation of all balances. There was a positive insignificant relationship between control activities and corporate governance in health sector. The control activities do not improve corporate governance in health sector.

The audit monitoring activities enabled the provision of advice and ensures disbursements compliance with specified procedures. There was assessment of risks, compliance with laws, regulations, and contracts and appraisals of the achievement of corporate goals and objectives. Audit monitoring activities significantly influence corporate governance in health sector. A good audit monitoring activity led to an improvement in corporate governance in health sector. Internal auditors play a key role in monitoring a company's risk profile and identifying areas in which to improve risk man

5.4 Recommendation of the Study

Based on the study findings, the following recommended were made:

The study recommended that risk assessment should be led at the level of individual organizations and over the wide range of exercises and auxiliaries of the solidified association. This includes evaluating the risks to determine which are controllable by the hospital and which are not. This can be accomplished through various methods. This addresses both measurable and non-measurable aspects of risks and weighs costs of controls against the benefits they provide. In order for risk assessment to remain effective, senior management needs continually to evaluate the risks affecting the achievement of its goals and react to changing circumstances and conditions. Internal controls should also be revised to appropriately address any new or previously uncontrolled risks.

On control environment, the study concludes that management attitude should be committed to ethical business practices and follows the established control procedures. This is the establishment for every other segment of inside control, giving order and structure. The study also concludes that where an enterprise has environmental considerations as some of their objectives, it is entirely necessary and appropriate that internal control should facilitate the assured achievement of those objectives. Hospitals should have separate environmental audits conducted by someone other than internal audit; but internal audit should be in a position to provide this service to the business, and to take account of work done by others that contribute to meeting this objective.

To the effect of control activities on organization performance, the study recommends that internal control ought to be viable when looking at outline. Can amazingly be gainful and is as a rule for association administration and broadly to monetary proclamations at present. A wide range of business firms have utilized interior controls through the development of strategies to guarantee shielding resources and beneficial business environment particularly bookkeeping arrangement, administration approach, and operational strategy.

Subsequently, inner control ought to be all the time survey in all parts of the organization and embed inward controls that will reinforce the organization and increment benefit. An effective internal control system requires that an appropriate control structure be set up, with control activities defined at every business level. These should include: top level reviews, appropriate activity controls for different departments or divisions, physical controls, checking for compliance with exposure limits and follow-up on non- compliance, a system of approvals and authorizations and a system of verification on reconciliation.

5.5 Area for Further Study

The study recommended that a study be done on the role of internal auditing in the corporate governance with focus to private hospitals in order to depict real situation across the sectors. The study also recommends that a study be done on challenges that affect internal auditing practices in both public and private sectors. Finally the study recommended that further research be done on the impact of the internal control activities

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APPENDICES

Appendix I: Introductory Letter

Dear Respondent,

My name is John Kipkirui Rotich. I am currently carrying out a study on Effect of Internal Audit Practices on corporate governance of the health sector in Kenya for the purpose of writing a project as a requirement for the award of Master of Business Management (Finance Option) Moi University. The topic of study is "**EFFECT OF INTERNAL AUDIT PRACTICES ON CORPORATE GOVERNANCE OF THE HEALTH SECTOR IN KENYA".**

You have been selected to participate in this study due to the importance of your information in the study. The information you provide will only be used for the purpose of this study and will be treated with confidentiality and that the management will not be liable for any information given.

Please feel free and answer all the questions truthfully.

Yours sincere

John Kipkirui Rotich

Appendix II: Questionnaire

Section A: Demographic Information

1. Gender of the respondent   Male [ ] Female [ ]

2. Age of the respondent

Below 20 years [ ] 21-29 years [ ] 30-39 years [ ] 40-49 years [ ]

50 years and above [ ]

3. Length of service in the organization

0-5 years [ ] 6-10 years [ ] 11-15 years [ ] 16-20 years [ ]

21 years and above [ ]

Section B: Risk Management

4. How effective are the following functions of internal audit through risk management in the health sector? Use a scale of 1-5 where 5= very effective, 4= effective, 3 = moderately effective, 2= slightly effective and 1= ineffective

Risk management	1	2	3	4	5
Risk identification					
Risk assessment					
Risk mitigation					
Risk monitoring					
Suggest risk management strategies					
Provide assurance that the risks are being appropriately managed					
Assess ethics and values within the organization					
Assess performance management					
Assess communication of risk					
Unplanned and informal reviews of other areas of concern, including unacceptable levels of risk					

Section C: Internal environment audit practices

5. How effective are the following functions of internal audit through internal environment audit practices in the health sector? Use a scale of 1-5 where 5= very effective, 4= effective, 3 = moderately effective, 2= slightly effective and 1= ineffective

Internal environment audit practices	**1**	**2**	**3**	**4**	**5**
Reviews of individual systems and processes					
Provide Financial controls					
Managerial controls					
Operational policies controls					
Control information within the organization					
Accounting Information and communication					
Assessment of internal control framework					
Methodical examination of business processes and connected controls					
Provision of independent verification of a sufficient sample of transactions to ensure integrity of the decision making process					
Ongoing and independent reconciliation of all balances					

Section D: Control activities

1. How effective are the following functions of internal control activities in promoting good governance in the health sector? Use a scale of 1-5 where 5= very effective, 4= effective, 3 = Moderately effective, 2= slightly effective and 1= ineffective

	1	**2**	**3**	**4**	**5**
Provides effective systems for managing and accounting for physical and financial assets					
Provide Financial controls					
Reviews of operational and financial performance					
Operational policies controls					
Ensure existence of segregation of duties.					
Accounting Information and communication					
Assessment of internal control framework					
Methodical examination of business processes and connected controls					
Ensure reliability and integrity of financial and operational information					
Ongoing and independent reconciliation of all balances					

Section E: Audit monitoring activities

How effective are the following functions of audit monitoring activities in the health sector? Use a scale of 1-5 where 5= very effective, 4= effective, 3 = moderately effective, 2= slightly effective and 1= ineffective

Monitoring	**1**	**2**	**3**	**4**	**5**
Ensure disbursements comply with specified procedures					
Provision of independent verification of a sufficient sample of transactions to ensure integrity of the decision making process					
Providing information about any fraudulent activities or irregularities					
Assessment of risks					
Appraisals of the achievement of corporate goals and objectives or Performance reviews – appraisals					
Compliance with laws, regulations, and contracts					
Advice and comment on devotion to the values and code of conduct/code of ethics of the organization or monitoring compliance of the above.					

Section F: Corporate governance

6. How would you rate the following attributes of corporate governance in the last Three years in the health sector? Use a scale of 1-5 where 1 is greatly decreased, 5 greatly improved.

	Greatly improved	**Improved**	**Constant**	**Decreasing**	**Greatly decreased**
Discipline					
Transparency					
Independence					
Accountability					
Responsibility					
Fairness					
Social responsibility					

Appendix III: Interview Schedule

1. Could you describe the influence of risk management on corporate governance of your firm?
2. Has there been any instance where internal audit is carried out to establish the effect of internal environment audit practices on corporate governance in your organization?
3. What are the types of audit conducted in the company to establish the influence of control activities on corporate governance?
4. Who do internal auditors report to?
5. Do you feel that internal audit has any impact in the corporate governance of this organization?
6. Is the audit committee involved in the activities of internal audit?
7. Is there any relationship between audit monitoring activities and corporate governance in your firm?