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Internal Auditing and Performance of Government Enterprises: A Nigerian Study

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INTERNAL AUDITING AND PERFORMANCE OF GOVERNMENT ENTERPRISES A NIGERIAN STUDY

Strictly as per the compliance and regulations of:

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Design/ Methodology/Approach : The study adopted a nomothetic methodology (quantitative approach). Data were collected from key informants using a research instrument. Employing the Statistical Package for Social Sciences (SPSS) Version 13.0, returned instruments were analyzed using frequency tables, Pearson's and Stepwise Regression Method.

Finding : The study found no strong association between internal auditing practices and financial performance of GOCs and thattt political influences do not significantly impact this relationship. The weak association between internal auditing practicesand financial performance is attributed to these enterprises' inadequacy and poor implementation of internal auditing practices. Where internal auditing is de-emphasized it cannot impact positively on performance.

Practical Implications : The paper recommends the need for the establishment of an Audit Department where it is non-existent, taking into consideration the size of the Enterprise as well as the strenghtening of the Department by according it the necessary Professional independence and employing adequate number of experienced and qualified staff.

Originality/Value : This pape has provided useful insights and fresh emperical evidence of the relationship between internal auditing practices and financial performance of government enterprises in the Nigerian context.

Keywords : Internal Auditing ; Government –owned Companies ; Political Influence ; Financial Performance ; Nigeria.

I. Introduction

State participation in economic activity is a world-wide phenomenon. In Nigeria, the government at all levels is active participants in economic activity such as being involved in business activities through the floating of Government-Owned Companies (GOCs). GOCs in Nigeria are expected to operate like their private counterparts; obeying the rule of incorporation according to the company laws of Nigeria and making enough business profits to survive business competitions (Fubara 1982). However, quite a number of these companies are "sick" and some are in the process of becoming so. Concerned about the negative financial performance of majority of GOCs in Nigeria, Fubara (1982) examined the reasons for the prolonged abysmal GOCs' financial performance and established that GOCs perform very poorly in terms of profitability criteria set for them. He attributed the poor performance to inept management, insufficient funds, paucity of technology and incongruent management – organization-government objectives.

The unsatisfactory performance of GOCs in Nigeria had been blamed on diverse reasons. Makoju (1991) had blamed the poor performance state to the bureaucratic red-tapism and lethargy of the civil service which is still intact in the management and operations of such companies. The Federal Ministry of Finance Incorporated (2006) had identified high incidence of fraud, government's employment of staff based on political connections rather than on ability to perform, parliamentary control and financial indiscipline as causes of poor performance. Dogo (1990) has alleged that the accounting systems of GOCs in Nigeria do not seem to guarantee proper and up to-date financial records thus making auditing difficult, if not impossible. A BPE report (2003) states that only 160 of the 590 federal government-owned public enterprises were involved in economic activities and that their rate of return was less than 0.5 percent.

A company's accounting control practices (such as internal auditing) is widely believed to be crucial to the success of an enterprise as it acts as a powerful brake on the possible deviations from the pre-determined objectives and policies. This means that an organization that put in place an appropriate and adequate system of accounting controls is likely to perform better (in financial terms) than those that do not. As Okezie (2004) puts it, "an enterprise's internal audit function can significantly affect the operations of the enterprise and may have an impact on the ability of the entity to remain a going-concern. Conrad (2003) had portrayed Enron's demise as the consequence of a "few unethical 'rogues' or 'bad eggs' acting in the absence of any control". Thus inadequate control systems may

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negatively affect an organization's success. According to Hermanson and Rittenberg (2003) the existence of an effective internal audit function is associated with superior organizational performance.

Although prior research (for example, Mak, 1989 and Simons, 1987) suggest a link between accounting control practices and financial performance, majority of prior studies had concentrated mostly on the budgeting aspect of accounting controls. This aside, the available studies so far had dealt exclusively with large privately-owned companies especially in the advanced countries. Little is known, at present, about the influences of internal auditing practices on the financial performance of GOCs in Nigeria. It was in an attempt to fill this gap that we set out to assess empirically the impact of internal auditing practices on the financial performance of GOCs in Nigeria and to consider the effect of political interferences on this relationship.

II. Literature Review

a) *Internal Auditing*

Internal audit is a long-standing function and an effective tool of management in many organizations. It has been a recognized component of organizations in both the public and private sectors and in most industries for many years. Internal auditing is often seen as an overall monitoring activity with responsibility to management for assessing the effectiveness of control procedures which arc the responsibility of other functional managers. The internal audit function is not limited to the operation of any particular function within an organization. Rather, it is all-embracing and accordingly is structured in the organization as a separate entity responsible only to a high level of management. As Okezie(2004) puts it, the main objective of internal auditing is "to assist management in the effective discharge of their responsibilities by furnishing them with analysis, appraisal, recommendations and pertinent comments concerning the activities reviewed".

Internal auditing which is often seen as constituting a large and significant aspect of an organization's financial control system is a vehicle to success and survival. According to Rittenberg and Schwieger (1997) "internal auditing is taking on increased importance in many of today's global organizations by assisting management in evaluating controls and operations and thereby providing an Important element of global control". Venables and Impey (1991) also recognized the control role of internal auditing when they stated:

It is generally recognized that the proper organization, staffing and methodology of internal audit presents the board with the best means of focusing on its obligation to ensure proper controls in the business

However, the need for an internal audit function will vary depending on company specific factors including the scale, diversity and complexity of the company's activities and the number of employees as well as cost/benefit considerations (ICAEW, 1999). Moreover, Venables and Impey (1991) had argued that for an internal audit function to be effective to enable an organization realize its full benefits, the function must have clearly defined objectives, authority, independence and appropriate resources.

b) *Corporate Performance*

Performance is a term that is often discussed but rarely defined. Indeed, some writers see the term as highly ambiguous capable of no simple definition (Emmanuel *et al* 1990; Otley, I999). Earlier, Emmanuel *et al* (1990) had observed that the frequent use of the term suggests that it may more often be used to avoid precise definition of what is meant. According to Euske (1984), the most common definition of the term can be "accomplishments of the organization". Thus, an organization that is performing well is one that is successfully achieving its goals and is effectively executing suitable strategies.

GOCs are the creations of the government with government as shareholders holding these shares in trust for the general taxpaying public. Although, it is true that GOCs may be evaluated in the same way like their private counterparts (Mazzolini, 1979), it is equally important to remember that these companies were established also to promote government's socio-economic policies. Viewing it from this dimension, some scholars (for example, Lal, 1980) have argued that the evaluation of government investment should employ social/cost benefit analysis. In this circumstance, the performance of GOCs would be measured in terms such as employment which has been provided, assistance given in training manpower, standards of living improved and other welfare matters. These, no doubt, are important matters. But there is another side to this argument.

Fubara (1982) had established that the major objective of GOCs in Nigeria was "to make profit in order to remain in business". That means all other objectives such as providing employment and giving assistance to the community are regarded as secondary. If profit-making is the major objective of GOCs in Nigeria it follows that these companies should be evaluated using profitability criteria employed by privately-owned companies. Moreover, prior studies of GOCs' performance, for example, Prasad and Rao (1989), Fubara (1982), Hope (1982) and Rosete (1981) all employed profitability criteria in evaluating performance. Mazzolini (1979) had noted that economic results or performance of GOCs may be measured using their profitability: return on investment; sales growth and the balance sheet situation (say, liquidity situation). On the basis of these clarifications, the present study evaluates GOCs on the basis of their financial performance. Financial measures are typically derived from or directly related to chart of accounts and found in a company's profit and loss statement or balance sheet. According to Emmanuel *et al* (1990), financial performance measures serve two purposes: they measure the return given to the providers of finance (such as shareholders) and they present an assessment of the overall capabilities of the organization as a whole. The performance indices - profits, return on investment and return on equity - were, thus, adopted in this study.

c) Political Influence

Political influence or ministerial interference has been identified as the major curse on GOCs (Prasad and Rao, 1989, Akinsanya, 1992, Babu and Rao, 1998). These authors contended that the Supervisory ministry(ies) wants (want) to retain tight control over these enterprises and no enterprise was ever permitted to function as an autonomous body. Bjorkrnan (1998) had argued that an influence relationship may develop in any context whenever one party can persuade others of his ascendancy through his own resources. Political influence is generally seen in the matter of appointment of board members and of high officials to these enterprises and in policy formulation. As argued by Prasad and Rao (1989), the men on the board of an undertaking is of vital importance since the success or failure of an undertaking largely depends upon the constitution and composition of its higher levels of management. Further, Akinsanya (1992) had observed that political interference through the appointment of board members is not a bad idea in itself so long as it is done on merit. However, in Nigeria the main problem is appointing as board members not only those who failed woefully at the polls but also party faithful who tend to place their interests and those of their parties before those of the enterprises they serve. What this means is that if board members have no other means of livelihood they are likely to play politics before the interests of the enterprises. Thus, they will interfere with corporate management rather than lay down broad policies for management.

d) Internal Auditing and Corporate Performance

Most internal audit professionals argue that an effective internal audit function correlates with improved financial performance. According to Bejide (2006), an effective internal audit service can, in particular, help reduce overhead, identify ways to improve efficiency and maximize exposure to possible losses from inadequately safeguarded company assets all of which can have a significant effect on the bottom line. Similarly, Venables and Impey (1991) had stated that internal audit is an "invaluable tool of management for improving performance". Fadzil *et al* (2005) had also noted that internal auditors help run a company more efficiently and effectively to increase shareholders' value". And Hermanson and Rittenberg (2003) had argued that the existence of an effective internal audit function is associated with superior organizational performance.

At the empirical level, a survey conducted by KPMG (1999) found that the internal audit function in organizations where it exists, contributes substantially to performance improvement and assist in identifying profit improvement opportunities. Moreover, research evidence in corporate disasters, particularly financial fraud consistently documents an association between weak governance (e.g. less independent boards or the absence of an internal audit function) and the incidence of problems (e.g Dechow, *et al* 1996; Beasley , 1996, Beasley *et al* 2000; Abott *et al* 2000). Thus, internal audit by acting as a watchdog could save the organization from malpractices and irregularities thus enabling the organization to achieve its objectives of ensuring high level of productivity and profit.

Greenlay and Foxall (1997) note that although studies have found an association between accounting control systems and performance theory also predicts that these associations will be influenced by external environmental influences. Thus eventhough GOCs are intended to be insulated from politics they are however linked with politics through the powers vested in the respective Ministers, Commissioners or Deputy Governors. These powers, according to Akinsanya (1992), include power to appoint the Chairmen, Chief Executive Officers and members of the boards as well as power to offer advice or suggestions or make requests. Akinsanya (1992) contends that board members of GOCs in Nigeria are appointed not because of any requisite experience but largely because of political reliability. Hence, board members not only interfere with corporate management but also use their positions to promote the interests of their favourites with dire consequences for the enterprise's performance.

These considerations lead us to the following hypotheses:

H_{o1}: There is no significant relationship between the existence of an internal audit function and profit level in GOCs.

H_{o2}: There is no significant relationship between the existence of an internal audit function and returns on investment in GOCs.

H_{o3}: There is no significant relationship between the existence of an internal audit function and levels of return on equity in GOCs

H_{o4}: Political influences on the management of a GOC do not significantly influence the internal auditing practices/ performance relationship.

III. Data and Methodology

a) Research Design

The study adopted the survey research design. We considered this method appropriate as it is useful for the study of non-observable events such as opinions, attitudes preferences or dispositions (Soyombo, 2002, Fubara and Mguni, 1995). Specifically, the study was a correlation, non-contrived and cross-sectional survey having individuals (officials of GOCs) as unit of analysis. The design was such as to discover vital predictive relationship and degrees of association among variables.

b) Population, Sample Size and Questionnaire Administration

The study population consisted of all companies established and operated by the various state governments in the South-South region of Nigeria. Thus the study population was made up of the 65 state-owned companies listed in the 2008 updated company directory sourced from the Port Harcourt office of the Federal Ministry of Finance Incorporated (FMOFI). Our choice of GOCs in the South-South states alone was premised on the fact that GOCs in Nigeria have much similarity with respect to size, structure, operation and management (Akinsanya, 1992). It is expected therefore that the findings of the study will have equal applicability to these enterprises in other states in Nigeria. The FMOFI list shows the total and percentage shareholding in each company by the various state governments. Of the 65 companies listed, 50 are fully-owned (100 percent) by government while the rest 15 had "mixed ownership". Since we were interested in the government fully-owned companies, the 50 companies fully- owned by government were taken to constitute the sample size for the study. The survey questionnaire was, accordingly, mailed to the key financially knowledgeable persons in each of the 50 companies making up the sample size. These individuals comprising accountants, Chief Accountants, Chief internal auditors, internal auditors and finance managers constituted the respondents of this study. One copy of the closed-ended questionnaire each were administered on the 50 GOCs thus making 50 copies of questionnaire distributed. Respondents were allowed two months to respond with an additional two weeks for late responses. Of the 50 copies of questionnaire distributed, 47 were returned while 2 were discarded as these were not properly completed by the respondents. Thus, 45 copies of the questionnaire constituting 90 percent of the total number administered were admissible and used for the study.

c) Measurement of Variables

The predictor variable (internal auditing practices) was measured on a 5-point scale from the end points of Strongly Agree to Strongly Disagree. The criterion variable (corporate financial performance) was measured adopting the subjective approach whereby respondents were required to indicate on a 5-point scale ranging from 5 = definitely better to I = definitely worse, how their company had performed over the last five years relative to their major competitors on each of the following performance criteria: profit level, returns on investment and return on equity. As Falshaw *et al* (2006) had noted, these financial performance measures (as adopted in this study) are typically employed to measure performance as they are of interest to and accessible to powerful external stakeholders of an organization such as shareholders (in our study, the government). The construct, political influence, was measured in terms of government appointment of Board members. Respondents were asked to indicate on a 5-point scale the extent to which they agree that this variable affect the company's financial performance.

Although "size" was not one of the variables tested in this study, respondents were required in the research questionnaire to indicate the size of their organization. Adopting the classification criteria offered by the National Council of Industries in July 2001, enterprises with a labour force of not more than 300 employees were classified as "small" while those with a labour force of over 300 employees were classified as large. Respondents were asked to indicate the category to which their enterprise belonged. It was considered necessary to evaluate the size of the enterprises under survey since previous studies (Carcello *et al* 2005; Stewart and Kent 2006) had found internal auditing to be associated more with large than with small companies.

d) Validity and Reliability of Research Instrument

Attention was accorded the validity of the research instrument. Validity, according to Cooper and Schindler (2001), is the ability of research instrument to measure what it is expected to measure. It is a measure of degree of accuracy. The validity of the scales used in this study was assessed for content and construct validity. The content validity measured the extent to which it provides adequate coverage of the investigative questions guiding the study. In this study, this was enhanced through the combined processes of logical validation and expert opinion in the accountancy field. Scales of the study variables were tested for construct validity to ensure that they measure the intended theoretical construct or trait that it was designed to measure. Thus, when there is a relationship between a property being examined and other specified variables, a construct validity is said to exist (Black and Champion, 1976). The correlation among the components of the study variables provided sufficient evidence of the construct validity.

The reliability question was also addressed in the study. The reliability of a questionnaire refers to the consistency of responses that it elicits as perfectly reliable measure gives the same result every time it is applied. The reliability of the measures used in this study was assessed by computing the Cronbach alpha which is a function of the mean correlation of all the study items with one another and is synonymous with correlation coefficient. It actually assesses the degree to which responses to the items on a measure are similar thus serving as an indicator of internal consistency of a measure. An eighteen (18)-item questionnaire was constructed. Of this number, thirteen (13) items were found to have Cronbach alpha exceeding 0.7(as suggested by Nunally (1978). Five (5) items could not meet this cut-off criteria and were accordingly expunged (see Copy of questionnaire in the appendix). The actual Cronbach alpha deemed significant relating to the reliability estimates for each of the constituent elements of the study are highlighted in table 1 below:

Table 1 : Scale Reliability Perspectives

S/No	Scale Particulars	Correlation	Alpha
A	Internal Auditing Coefficient alpha for scale 0.7762		
1	The objective and scope of the internal audit function are clearly defined by company management	-0.2828	0.7544
2	In my company the internal auditor enjoys some degree of independence as manifested in his freedom to plan and carry out the work.	0.1182	0.7386
3	In my company, the internal auditor enjoys some degree of independence as manifested in his freedom to access the highest level of management	0.2444	0.7325
4	In my company, the internal auditor enjoys some degree of independence as manifested in his freedom to determine the appointment or removal, promotion and remuneration of all internal audit staff.	0.2924	0.7315
5	The internal auditor in my company has a clearly defined authority which empowers him to ask for any information which he considers necessary from any officer of the company.	0.3554	0.7281
6	The internal auditor in my company has a clearly defined authority which empowers him to the right of access to any part of the company property and to any document.	0.0525	0.7412
7	Our company management do take the necessary action on internal audit reports and recommendations.	0.6494	0.7126
8	The internal audit department of my company is adequately staffed in terms of number, qualification and experience.	0.6494	0.7133
9	In my company internal audit reports go to top management and this is considered better than taking such reports to the finance manager.	0.3491	0.7283
S/No	Scale particulars	Correlation	Alpha
B	Financial Performance		
	Coefficient Alpha = 0.7739		
10	Our company's profit levels are compared with those of major competitors	0.0527	0.7406
11	Our company's return on investment is compared with those of major competitors	0.1119	0.7482
12	Our company's return on equity is compared with major competitors	0.0959	0.7398
C	Contextual (Moderating) Factor		
13	Government's appointment of our company's Board members affect financial performance	0.0075	0.7427

Source: Survey Data, 2011

e) Methods of Data Analysis

Our statistical analysis of data using the SPSS involved the following: frequency tables, percentages, Pearson's Product Moment Correlation Coefficient, (r) and Stepwise regression analysis. Thus our interpretation of r and the level of statistical significance was strictly based on the SPSS output. Thus, the study used both descriptive and inferential analyses. Descriptive analysis was used to determine the extent of internal audit practices in the GOCs studied while the inferential analyses (Pearson's r and the Stepwise Regression Analysis) were used to test the hypotheses.

IV. DATA ANALYSES AND RESULTS

a) Describing Internal Auditing Practices in GOCs - Preliminary Analyses

Tables 2, 3, 4, and 5 summarised the questionnaire results of the internal auditing practices of GOCs using simple percentages and frequency tables. Table 2 shows the results on the issue of existence of internal audit departments, staffing and headship of the department.

Table 2 : Existence, Staffing and Headship of Internal Audit Departments

S/No	Item	Frequency	Percent
1	Existence of internal audit department:		
	Separate Internal Audit Dept	36	80
	No. Internal Audit Dept.	9	20
	Total	45	100
2	Number of Staff in Department:		
	Between 1 to 5	30	83.3
	Between 6 to 10	6	16.7
	More than 10	Nil	Nil
	Total	36*	100.0
3	Headship of Internal Audit Department:		
	▪ A Chief Internal Auditor with a Professional Accountancy Qualification	6	16.7
	▪ A Graduate Accountant		
	▪ A University Graduate without an Accountancy Background	13	36.1
	▪ A College Graduate with several years of experience	Nil	Nil
	Total	17	47.2
		36*	100.0

Source: Survey Data, 2011

**Frequency total is 36 and not 45 since 9 of tile companies that have no internal audit department did not complete this section of the questionnaire.*

The table shows that a majority of the surveyed companies, 36 (or 80 Percent) indicated the existence of an internal audit department while 9 (or 20 percent) said their company has no internal audit department. For the other companies having internal audit departments, the table shows that the departments are not adequately staffed in terms of numbers. None of the surveyed companies has more than 10 internal audit staff. Interestingly a majority of the GOCs (47 Percent) indicated that the department is headed by people with accountancy background that have several years of experience.

We also made an attempt to determine the degree of freedom of internal auditors to carry out their monitoring activities. Table 3 summarises the results on the extent of independence of internal auditors in GOCs.

Table 3 : Extent of Independence of Internal Audit Departments

Scale	Manifestation of Independence					
	Freedom to plan and carry out work		Free access to highest level of management		Freedom to control affairs of Department	
	Frequency	%	Frequency	%	Frequency	%
1	3	8.3	10	27.8	11	30.6
2	21	58.3	18	50.0	12	33.3
3	4	11.2	3	8.3	4	11.1
4	5	13.9	3	8.3	4	11.1
5	3	8.3	2	5.6	5	13.9
Total	36	100.00	36	100.00	36	100.00

Source: Survey Data, 2011

Scale: Ranging from 1 = Strongly Disagree 2 = Disagree
3 = Undecided; 4 = Agree to 5 = Strongly Agree

Table 3 shows that 66.6 percent of companies with internal audit departments disagree that their internal auditors have the freedom to plan and carry out the audit work. 11.2 percent were undecided while 22.2 percent agreed that internal auditors have that freedom. Also 77.8 percent disagree that the department enjoys free access by way of making reports to the highest level of management. On the issue of the freedom to control affairs of the department by way of determining the appointment, removal, promotion and remuneration of all internal audit staff, the majority view (63.9% percent) was that such freedom was absent. We also attempted to examine the question of whether internal auditors have clearly defined authority to carry out the work. That is, whether there existed any delegated authority to enter premises to interview staff, to examine documents and observe processes in order to collect audit evidence. As shown in table 4, the majority view was that internal auditors have restricted access to obtain information which they considered necessary for the audit (a 75 percent disagreement rating). 75 percent of the respondents also affirmed that internal auditors have limited right of access to examine documents. 19.4 percent and 16.7 percent respectively agreed on the aggregate that internal auditors have these rights.

Table 4 : Extent of Internal Auditors' Authority

Scale	Access to all Relevant Information		Right to enter Premises and access to any Document	
	Frequency	%	Frequency	%
1	12	33.3	8	22.2
2	15	41.7	19	52.8
3	2	5.6	3	8.3
4	4	11.1	4	11.1
5	3	8.3	2	5.6
Total	36	100.00	36	100.00

Source: Survey Data, 2011

Scale: Ranging from 1 = Strongly Disagree; 2 = Disagree
3 = Undecided; 4 = Agree to 5 = Strongly Agree

Matters relating to scope and objectives of internal audits, management action on audit reports and staffing in terms of number, qualification and experience also engaged our attention. The result is presented in table 5.

Table 5 : Internal Audit staffing, Management Action on Reports and Scope

Scale	Definition of Function					
	A well-defined scope/objective of I.A. function		Management Action on I.A. Reports		Staffing of I.A. Depts.	
	Frequency	%	Frequency	%	Frequency	%
1	2	5.6	10	27.7	8	22.3
2	9	25.0	18	50.0	15	41.7
3	2	5.6	2	5.6	3	8.3
4	18	50.0	4	11.1	7	19.4
5	5	13.8	2	5.6	3	8.3
Total	36	100.00	36	100.00	36.	100.00

Source: Survey Data, 2011
Scale: Ranging from 1 = Strongly Disagree; 2 = Disagree;
3 = Undecided; 4 = Agree to 5 = Strongly Agree

As revealed in table 5, the majority view (63.8 percent) was that there exist a well-defined scope and objectives of the internal audit function while 30.6 percent have a contrary view. As to whether company management do take the necessary action on internal audit reports and recommendations, the majority view (77.7 percent) was that this was not the case. On the issue of staffing of the department in terms of number, qualification and experience, 64 percent of the respondents disagreed that the function is well- staffed. 27.7 percent however, maintained that the department is adequately staffed while 8.3 percent were undecided. Having established the nature of audit practices in the surveyed GOCs, we now proceed to test the hypotheses of the study.

b) *Hypotheses Testing*

The system of hypotheses previously presented postulates relationships between corporate financial performance and internal audit practices and between the internal audit practice/performance relationship and the moderating variable-political influence. While the 2-variable hypotheses (H_{o1}-H_{o3}) are tested using the parametric Pearson Product Moment Correlation, r, the hypothesis involving moderator variable (H_{o4}) is tested using Stepwise Regression Analysis. The acceptance or rejection of each hypothesis is then determined by the significance of the regression coefficients.

H_{o1}: There is no significant relationship between the existence of an internal audit function and profit level in GOCs.

The test result is as shown in table 6. From the results there is a weak positive relationship between internal auditing practices and profit level in GOCs. The r value is 0.208 which is not significant (0.170) at the 0.05 level. The results support H_{o1} that there is no significant relationship between the existence of an internal audit function and profit level in GOCs.

Table 6 : Pearson's r (Internal Audit (I.A) and Profit Level (PL)

	IA	PL
Pearson's r: IA Correlation Coefficient	1.000	0.208
Significance (2-tailed)		0.170
N	45	45

Source: SPSS Window Output Version 13.0

H_{o2}: There is no significant relationship between the existence of an internal audit function and returns on Investment in GOCS.

Table 7 contains the test results. The table shows an r value of 0.091 which is not significant (0.208) at the 0.05 level. There is a negligible positive association between internal audit practices and Return on Investment. The result support H_{o2} that there is no significant relationship between the existence of an internal audit function and Return on Investment in GOCs. Thus, internal audit practices of GOCs do not significantly influence companies' return on investment.

Table 7 : Pearson's r (internal Audit and Return On Investment)

	IA	PL
Pearson's r: IA Correlation Coefficient Significance (2-tailed) N	1.000 45	0.091 0.208 45

Source: SPSS Window Output Version 13.0

H_{o3}: There is no significant relationship between the existence of an internal audit function and levels of Return on equity in GOCs.

The test result is presented in table 8. From the table, the r value shows a negligible negative association (-0.081) which is not significant (0.598) at the 0.05 level. This offers support to Ho3 that there is no significant relationship between the existence of an internal audit function and levels of return on equity in GOCs. Thus, internal audit practices of GOCs do not significantly influence companies' return on equity.

Table 8 : Pearson's r (Internal Audit and Return on Equity)

	IA	PL
Pearson's r: IA Correlation Coefficient Significance (2-tailed) N	1.000 45	-0.081 0.598 45

Source: SPSS Window Output Version 13.0

Test of mediator variable (political influence) on the internal audit practices/performance relationship.

H_{o4}: Political influence on the management of a GOC does not significantly influence the internal audit practices/performance relationship.

The Stepwise Regression Method was used for testing hypothesis 4. Using the method, data relating to the surveyed companies' internal audit practices were entered into the SPSS programme that ran the test. On the choice of "entry" and "stay" values of the Stepwise selection criteria we adopted the value of .05 and .10 for "entry" and "stay" respectively. Thus only variables that met the set criteria are entered into the model while those that failed to meet the criteria are eliminated. Variables are, thus, entered according to the magnitude of their contribution to R^2.

We tested for the effect of political influence (measured by government's appointment of board members) on the internal audit practices/ performance relationship. For this purpose, respondents were put into two categories. In the first category were respondents who 'disagreed" (through their rating) that Board appointment by government had an effect on the relationship. The second group were those who, also by their ratings, "agreed" that government's appointment of Board members had an effect on the relationship. Table 9 summarized the SPSS output.

Using the Stepwise Regression Method, we tested the rating of respondents regarding whether appointment by government of GOCs' board members had an effect on the predictor variable's relationship with profits. With respect to those who agreed that Board members appointment by government influenced the relationship, table 9 reveals that internal audit having an r value of 0.176 with a p-value of 0.164 does not significantly correlate with profit at the 0.05 level. Thus respondents are agreed that political influences measured by government appointment of Board members does not mediate on the influences of internal audit practices on profit levels of GOCs. Similarly, for respondents that disagreed with government appointment of board members as having an effect on the internal audit practices/performance relationship the Stepwise procedure revealed that there was no effect as the predictor variable failed to meet the method's criteria at the 95 percent level of confidence. Table 9 also show that government appointment of board members as suggested by the respondents' ratings has no moderating effect on the influences of internal audit practices on return on investment and return on equity of GOCs - the predictor variable was not entered and retained at the entry and stay values of .05 and .10 respectively. Thus, the test results offer support to Ho4 that political influence on the management of a GOC does not significantly influence the relationship between internal auditing practices and financial performance.

Table 9 : Summary of Results on the Effect of Political Influence

Moderating variable	IA/CFP Relationship	R^2	Pcc(r)	Sig	t	Sig.for t	F-value	Sig.for F
Political Influence:	IA&PL:							
Disagree with Board Appt.	IA		.241	.225				
Agree with Board Appt	IA		.176	.164	0.356	.724		
Disagree with Board Appt	IA&ROI: IA		.486	.055				
Agree with Board Appt	IA		.129	.236				
Disagree with Board Appt	IA & ROE: IA		.343	.137				
Agree with Board Appt	IA		.045	.401				

Source: SPSS Output of Survey Data, 2011
Correlation Significant at 0.05
APPT = Appointment; Pcc = Pearson Correlation Coefficient, r, IA = Internal Audit, PL = Profit Level; ROI = Return on Investment; ROE = Return on Equity
CFP = Corporate Financial Performance

V. Discussion of Findings

a) *Internal Auditing and Financial Performance of GOCs*

It is widely believed that internal auditing, where it exists, contributes to improved financial performance of the organization. According to Bejide (2006) "an effective internal audit service can, in particular, help reduce overhead, identify ways to improve efficiency and maximize exposure to possible losses from inadequately safeguarded company assets all of which can have a significant effect on the bottom-line". Venables and Impey (1991) opined that internal audit is an "invaluable tool of management for improving performance".

To Hermanson and Rittenberg (2003) the existence of an effective internal audit function is associated with superior organizational performance. Prasad and Rao (1989) expressed similar sentiments when they observed that the internal auditor by acting as a watchdog saves the organization from malpractices and irregularities thus enabling the organization to achieve its objectives of ensuring high level of productivity and profit.

Our findings in this study, however, contradicts the above positions. We found that there was no significant relationship between the existence of an internal audit function and financial performance of GOCs. That is, internal auditing, where it exists, does not influence the profit levels, return on investment and return on equity of GOCs. This findings is at odds with that of KPMG (1999) which identified a positive association between an internal audit function and financial performance. In a survey of some 201 senior company executives in the United States, the KPMG study found that the internal audit function in organizations, where it exists, contributes substantially to performance improvement and assist in identifying profit improvement opportunities. Our findings in this study also contradicts that of Fadzil, *et al* (2005) which found that internal auditors assist in running a company more efficiently and effectively to increase shareholders' value. On the other hand, the findings is similar to that of Griffiths (1999) which found no relationship between internal audits and performance. That study found widespread "lukewarm" or negative attitudes to internal audit (in the privately.-owned organizations studied) and that the function was lacking in skills and appropriately trained staff.

The absence of a significant relationship found between internal auditing practices and financial performance may be attributed to the size of GOCs involved in this survey. Internal auditing is believed to be associated more with large than with small companies. Prior studies (for example, Carcello *et al* 2005; Stewart and Kent, 2006) found a strong association between internal audit and the size of the firm. These findings suggest that smaller firms do not regard internal audit as cost effective. In the present study, a majority of the GOCs fall within the "small" category, (using the classification criteria adopted earlier stated in the methodology section). Even among some of the large ones having internal audit departments, the actual practices suggests a possible underemphasis on internal auditing. Therefore, the seemingly de-emphasis on internal auditing by the majority small GOCS may have contributed to the absence of a significant relationship between internal auditing practices and financial performance. Where internal auditing is deemphasized, clearly it cannot impact positively on performance.

It is a matter of concern that some of the GOCS do not have internal audit Departments. Interestingly, however, some of the companies (qualifying as large going by this study's criteria) had been making substantial profits for so many years now. This goes to affirm the fact that superior financial performance may not come about just from an internal audit function. Even in those cases where an internal audit department (or unit) exists, the departments were functioning with skeleton staff not adequate in relation to the size of the company. Majority of the companies have internal audit staff numbering between one and five. None has more than ten irrespective of the size (see Table 2). A majority of the internal audit Departments are headed by college graduates with years of experience or by graduate accountants. A negligible few are under the headship of a chief internal auditor with professional accountancy qualification.

The internal audit Departments of the surveyed enterprises could not have been effective as internal auditors in these companies lacked professional independence in the discharge of their duties. In order to serve a constructive purpose internal audit judgments have to be unbiased and therefore can only be made by taking an objective view from an impartial viewpoint. As we saw in Table 3, the internal audit Departments of these companies, where they exist, lacked the freedom to plan and carry out the work thus limiting the scope of the audit conducted by the Department. They also lacked the freedom of access to the highest level of management and to determine the appointment or removal, promotion and remuneration of internal audit staff all of which make for internal auditor's independence. In these situations, the watch dog's job of saving the undertaking from malpractices and irregularities which in turn leads to improved performance is greatly undermined. Moreover, where company management fails or it is reluctant to take actions on internal audit reports and recommendations, internal auditing suffers. This is the case of our surveyed companies as we saw in Table 5. The above discussion leads to a very significant conclusion: the internal audit function, where it exists, does not significantly influence financial performance of a GOC. The absence of a relationship may be attributed to a possible under-emphasis on internal auditing by GOCs. Where internal auditing is not accorded any serious attention, clearly it cannot impact positively on financial performance. Financial performance of a GOC may improve not as a result of just an internal audit function (especially when proper attention is not accorded it) but also from some other variables. The foregoing clearly shows that the functioning of the internal audit system in the surveyed GOCs had not been effective. Had it been effective, it would have benefited the enterprises in several ways by plugging out loopholes present in their various activities thereby improving financial performance.

b) Effect of Political Influence on the Internal Auditing Practice/Performance Relationship

Political influence (which we used in this study as synonymous with the external environment) was hypothesized to have a moderating effect on the internal audit practices/performance relationship. Political influence was measured by government's appointment of Board members. Prasad and Rao (1989) had alleged that political influence is generally seen in the matter of appointment of Board members and other executives to GOCs. The variable - political influence - was found to have no moderating effect on the relationship between internal auditing practices and financial performance of GOCs. This finding is consistent with William's (2005) study of small and medium sized Singaporean firms which found no direct relationship between accounting control practices and the overall firm performance when the environmental influences of uncertainty was added. Government's appointment of Board members which may include politicians may not afterall be bad *per se* so long as it is done on merit and not on political grounds. Akinsanya (1992) had observed that in the United Kingdom, the Minister is required to make appointments from among persons "appearing to him to be qualified as having had experience of and having shown capacity in industrial, commercial or financial matters, applied science and administration or the organization of workers".

In concluding our discussion, it may be necessary to point out that the absence of a significant relationship between internal auditing practices and the measure of financial performance adopted could mean that internal auditing practices have become a necessary but not sufficient condition for financial performance in GOCs in Nigeria.

VI. Implications of The Study

The present study has made some contributions to theory building and provide guidance to operators of GOCs in Nigeria in the following ways:

a) Theoretical Implications

An unexpected result and indeed a more interesting contribution to the literature, is the findings in this study of the absence of a significant relationship between internal auditing practices and financial performance. The auditing literature widely concede that internal auditing, where it is practiced, should result in superior organizational financial performance (see for example, Vanasco, *et al*, 1995; Hermanson and Rittenberg, 2003; Fadzil, *et al,* 2005, Bejide, 2006). The findings of this study suggests that GOCs lacked an effective monitoring system provided by internal auditing which ultimately resulted in the absence of a significant relationship between this control practices and financial performance. This is an important contribution to the literature since as this finding imply, the mere creation of an internal audit department in an organization does not automatically result in superior financial performance.

The department must receive the necessary adequate management support for it to function effectively.

Moreover, the present study extends previous research by providing useful insights into the internal auditing practices of GOCs in Nigeria. Prior accounting control practices research involving, particularly the budgeting aspect have largely been confined to privately-owned companies in the developed countries such as the U.S.A, the U.K. and New Zealand. Thus, the present study made a contribution given that there had been no prior research (to the best of our knowledge) dealing with the performance consequences of internal auditing practices in GOCs in Nigeria. The present study had filled this gap. Thus, the present study, has provided fresh empirical evidence relevant to theory-testing of the relationship between internal auditing practices and financial performance of GOCs. Thus, to researchers interested in this area, the present study had provided fresh empirical evidence relevant to theory-testing of the relationship between internal auditing practices and financial performance of GOCs. This study, hopefully, should rekindle their interest in this seemingly under-researched area in Nigeria especially when the bulk of the auditing literature suggests that internal auditing as a control mechanism should lead to improved financial performance of organizations. Evidence provided by the present study will provide a ready source of materials for such future studies.

b) Practical Implications

An important finding of this research pertains to the extent of the internal auditing practices in GOCs. The study had brought to the fore, the need for adequate staffing in terms of numbers, qualification and experience in the Internal Audit Departments of these companies as, well as the establishment of the Department where it is non-existent. There is no doubt that Internal auditing benefits managers in providing bases for judgment and action, helping managers by reporting weaknesses in control and performance, providing counsel to managers and board of directors on the solutions of business problems and supplying information that is timely, reliable and useful to all levels of management. If properly implemented, internal auditing, should contribute meaningfully to financial performance of GOCs.

To policy makers in GOCs in Nigeria, this study had also brought to the fore the significance of internal auditing and how it could assist the organization to achieve its profitability goals. It is noteworthy that at the time of this study some of the GOCs (falling within the scope of the study) have remained closed for many years with some "only merely alive" as they were owing arrears of workers' salaries. The present study is, thus, significant as it provides fresh evidence as to whether or not the "poor" performance state of these enterprises was due to the non-existence and/or inadequacy of the control structure such as that provided by internal auditing. Consequently, policy makers will be assisted to know the state of these enterprises for appropriate measures to be taken so that the scarce resources of the government are not misutilized and does not lead to demoralization of the concept of public enterprise system in Nigeria.

VII. Conclusion and Recommendations

From our discussion of findings, we can conclude that the present study provides some evidence on the performance consequences of internal auditing practices in GOCs in Nigeria. Specifically, the internal audit function, where it exists, in a GOC does not significantly influence financial performance and that political interferences by way of government's appointment of board members does not significantly impact these enterprises' financial performance. The absence of a relationship arose from possible under-emphasis on internal auditing by these enterprises. Where the internal audit function is de-emphasised (as the present study shows), clearly, it cannot impact positively on financial performance. Consequently, we strongly recommend the creation of an Internal Audit Department in those enterprises where there is none. Existing Departments then should be strengthened by according them the necessary professional independence and employing adequate number of experienced and qualified staff to enable the Department extend coverage of the audit to all significant activities of these enterprises. Had that function been effective, it would have benefited the enterprises in plugging out loopholes that may be present in the enterprises' activities with resultant positive effects on financial performance.

Although, the present study offered some contributions to our understanding of the relationship between internal auditing practices and corporate financial performance, future research should incorporate non-financial measures such as quality, employee satisfaction in addition to financial measures in order to further enrich our understanding of the internal auditing/performance relationship. It is also suggested that future research should examine companies with "mixed ownership", that is, those partly owned by government and partly by private investors so as to see what impact the elements of private and government ownership together would have in an internal auditing practices/performance study.

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Appendix

a) Survey Questionnaire

i. *Identification of Respondent*

1. Name of company (optional)

2. What percentage of the equity share is government-owned?

☐ 100% ☐ 50% and above ☐ less than 50%

3. Your functional position in the company? Please tick

☐ Internal auditor ☐ Chief Internal Auditor
☐ Accountant ☐ Chief Accountant
☐ Finance Manager

4. Your level of schooling/professional qualification? Please tick

☐ Bachelors degree ☐ Masters Degree ☐ Diploma
☐ Post Graduate Diploma ☐ College Certificate
☐ ACA ☐ Other (please specify)

5. The number of workers in my company is:

☐ Below 300 ☐ Over 300

ii. *Internal Auditing Practices*

A) Please tick (√) as appropriate in the spaces provided:

i) In my company:

- there is a separate internal audit unit/department

- there is no internal audit unit/department

(ii) The number of staff in the internal audit department is

Between 1 to 5 ☐ Between 6 to 1 ☐

More than 10 ☐

(iii) The internal audit department is functioning under the control of:

☐ A chief internal auditor with professional accountancy qualification

☐ A graduate accountant

☐ A college graduate with several years of experience

☐ A university graduate without an accountancy background

(B) Please indicate your agreement with the following statements relating to the internal audit function of your company. Use the response key: SA Strongly Agree: A = Agree; U = Undecided; D = Disagree; SD = Strongly Disagree

1	The objectives and scope of the internal audit function are clearly defined by company management	SA	A	U	D	SD
2	Freedom to plan and carry out the work					
3	Free access to the highest level of management					
4	Freedom to determine the appointment or removal, promotion and remuneration of all internal audit staff.					
	The internal auditor has a clearly defined authority which empowers him to:					
5	Ask for any information which he considers necessary from any officer of the company.					
6	The right of access to any part of the company and to any document.					
7	Company management do take the necessary action on internal audit reports and recommendations					
8	The internal audit department of my company is adequately staffed in terms of number, qualification and experience.					
9	The internal audit reports go to top management and this is considered better than taking such reports to the finance manager.					

iii. *Financial Performance*

10. Please rate by a tick (√), company's profit levels over the past five years relative to your major competitors using the following scale:

Definitely better	Better	Don't know	About the same	Definitely worse

11. My company had a

12. lways met its annual profit target. Please tick (√)

Strongly Agree	Agree	Undecided	Disagree	Strongly disagree

13. Kindly rate your company's return on investment over the past five years relative to your competitors. Please tick (√)

Definitely better	Better	Don't know	About the same	Definitely worse

14. My company's Return on investment had been satisfactory over the past five years. Please tick (√)

Strongly Agree	Agree	Undecided	Disagree	Strongly disagree

15. Kindly rate by a tick (√) your company's return on equity over the past five years relative to your major competitors on the following scale:

Definitely better	Better	Don't know	About the same	Definitely worse

16. My company had been paying dividends to government over the past five years. Please tick (√) the appropriate scale

Strongly Agree	Agree	Undecided	Disagree	Strongly disagree

17. How would you rate the financial performance of your company? Please tick (√)

Very high	High	Moderate	Low	Very low

iv. *Political Influences*

Please indicate your agreement with the following statement using the response scale: SA = Strong Agree; A = Agree; U = Undecided; D = Disagree; SD = Strongly Disagree

18. Government's appointment of my company's board members affect company's financial performance.

SA	A	U	D	SD

19. Political influence on my company's management generally affect financial performance

SA	A	U	D	SD