Syntax Literate: Jurnal Ilmiah Indonesia p–ISSN: 2541-0849
e-ISSN: 2548-1398
Vol. 9, No. 10, Oktober 2024

THE ROLE OF INTERNAL AUDIT PRACTICE IN PROMOTING OPERATIONAL COMPLIANCE: EVIDENCE FROM ADDIS ABABA HOUSING DEVELOPMENT CORPORATION

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Abstract

This research investigates the role of internal audit practices in promoting operational compliance within public sector organizations, with a focus on Addis Ababa Housing Development Corporation. Internal audit is essential in ensuring compliance with policies, laws, and regulations, contributing to the overall effectiveness and governance of organizations. The study examines key internal audit practices such as audit frequency, auditor independence, auditor competency, and audit reporting. A quantitative approach was employed, utilizing structured questionnaires distributed to finance managers, internal auditors, and senior accountants. Data were analyzed using descriptive and inferential statistics to determine the impact of internal audit practices on operational compliance. he results show that all the studied audit factors positively contribute to enhancing compliance. Auditor independence had the most significant influence, followed by auditor competency, audit frequency, and audit reporting. This highlights the necessity of frequent audits, unbiased auditor reporting, and specialized skills to ensure adherence to operational regulations. These findings emphasize the importance of strengthening internal audit practices in Ethiopia's public sector to improve governance and mitigate organizational risks. The study provides insights into improving audit practices, especially in resource-constrained environments like Ethiopia, and underscores the need for continued investment in auditor training and independent reporting mechanisms to safeguard organizational integrity

Keywords: Internal audit, operational compliance, audit frequency, auditor independence, public sector

Introduction

Internal audit is a core element for assuring operational compliance of regulated organizations to the set rules (Agoglia, Hatfield, and Lambert 2015a), regulation (Bugaje, Okpe, and Odunko 2023), policy and procedure (Dimitra and Ioannis 2015a). The main purpose of an internal audit is to offer reasonable assurance on the management and operations, risk management and internal control system of an organization (Alm 2019; Kalita and Tiwari 2023; Mengist and Kumar 2019). Internationally, the internal audit function has grown in appeal as corporations come under more scrutiny from the regulatory authorities, most especially in the financial, health and manufacturing industries (Alm 2019; Ussahawanitchakit and Intakhan 2011). Globally, organizations have accepted internal audits as a key component when it comes to compliance with their operations. As defined by the Institute of Internal Auditors (IIA), internal audit promotes corporate governance by assessing risks and confirming compliance with internal controls

How to cite: Melisew, C. G. (2024). The Role of Internal Audit Practice in Promoting Operational Compliance: Evidence from Addis Ababa Housing Development Corporation. *Syntax Literate. (9)10.* http://dx.doi.org/10.36418/syntax-literate.v9i10
E-ISSN: 2548-1398

and external rules (IIA, 2022). As observed, the growth of high-powered regulatory frameworks, including the complex Sarbanes Oxley Act in the United States and the GDPR in the European Union, have increased the need for experienced internal audit practices so as to escape costly compliance disasters (PWC, 2021). Frequency has been defined as the rate at which internal audits are completed, which is a significant factor in determining an organization's compliance with regulatory measures (Earnhart and Harrington, 2021; Joshi, 2020). As everyone else has testified, auditor independence helps to maintain the impartiality of audits, whereas audit competency, which involves the sheer experience and the knowledge that the audit team possesses, is central to conducting effective internal audits (Ardillah and Chandra 2022; Bappa and Yahaya 2024). Other elements of audit reporting practices that are also important include the ability of the report to allow management to act on audit findings, especially in cases of troubles with the clarity and transparency of the report (Hakim and Omri 2015; Kalita and Tiwari 2023; Krishnamoorthy, Wright, and Cohen 2002).

Public awareness in Africa still demands organizational internal audit functions to foster good practices and compliance within the operating environment. Research shows that internal audit helps introduce transparency and mitigate cases of fraud and corruption in the organization of the African public sector (Chan and Song 2021; Chekole Tekle, Abera Lemma, and Amassgaha 2024; Hakim and Omri 2015). There is growing attention by African governments and firms to develop and strengthen internal audit functions to increase compliance with financial laws and environmental and organizational requirements. However, issues to do with inadequate resources (Bappa and Yahaya 2024), inadequate training (Chekole Tekle et al. 2024), and political interferences often compromise the independence and efficiency of internal audit activities in those organizations in the continent (Joshi 2020). Audit competency is another area of concern since the majority of African countries need more qualified internal auditors. However, audit frequency is commonly less frequent, thus limiting the effectiveness of audit recommendations in compliance. In Ethiopia, internal audits have emerged as more important as organizations are keen to position themselves in relation to international standards of governance and compliance (Chekole Tekle et al., 2024). In particular, regulatory authorities, including banking and manufacturing industries, pay increased focus to the organization's internal audit procedures. Champions of internal audit profession development in Ethiopia are the Office of the Federal Auditor General (OFAG) and the Ethiopian Institute of Certified Public Accountants (EICPA). Despite this, internal audit effectiveness is a problem due to resource constraints, compromised independence, and the overall poor competencies of the internal auditors (Abebaw, 2019). Ethiopian audit reporting practices, however, still need to be stronger since audit findings are only sometimes effectively communicated to senior management. In addition, although auditor independence is an essential component in internal audits, auditor independence is challenged by undue influence from outside and internal management. Nevertheless, the future of internal audits in the organizations of Ethiopia has now been

realized to be more important for reinforcement, good governance, and operations risk management through frequent internal audits (Tesfaye, 2021).

In the area of tax compliance (Chekole Tekle et al. 2024) did a study in 2024 on the factors influencing the success of tax audits at Addis Ababa's Number One Medium Tax Payer Branch Office. From their research, they found that auditor competency, audit frequency, and audit independence were some of the core elements that influenced the efficiency of the tax audit and thus affected tax compliance (Chekole Tekle, Lemma and Amassgaha, 2024). These research findings could be useful in contributing to extensions of internal audit practice for purposes of enhancing compliance in the management of entities in other sectors in Ethiopia. Overall, therefore, an appreciation of how internal audits ensure compliance in operations is critical locally as well as internationally since internal audits are gradually being practised in the African region and Ethiopia. Audit frequency, independence, competency, and reporting practices are some of the critical issues that have a direct impact on establishing operational compliance as a crucial success factor for organizations globally.

One of the papers' areas of focus is operational compliance, the management of compliance, and its relationship to the successes and failures of organizations in business. Nonetheless, getting and sustaining operational compliance remains a problem for many of these organizations, specifically in the public sector. In Ethiopia, bureaucratic public enterprises like Addis Ababa Housing Development Corporation still experience increasing pressures in terms of regulatory changes and in discharging effective governance responsibilities. Unfortunately, these endeavours are often undermined and hampered by several organizational vices, including poor internal control systems, poor governance and management, and sub-optimal business processes. The internal audit function is understood and accepted by many as one of the most effective organizational controls for enhancing operational compliance (Hakim and Omri 2015; Mengist and Kumar 2019; Zhang and Wei 2022). Internal auditing plays an important role in helping organizations establish risks (Slemrod and Weber 2012; Ussahawanitchakit and Intakhan 2011), compliance with the law and rectifying any wrong docket as may be required (Francis 2004; Serikova et al. 2020).

However, as mentioned in previous sections, internal audits in many Ethiopian public institutions often need more freedom and influence to impact operational compliance effectively. In the Addis Ababa Housing Development Corporation, there have been some previous studies done on internal audits over a number of years amid reports of operational inefficiencies, policy violations, and financial corruption. Some of the potential problems responsible for these challenges include infrequent audits, lack of independence of auditors, restricted audit skills, and inadequate audit reporting. Notwithstanding the existence of internal audit units, these functions are perceived as after-the-event undertakings rather than as preventive mechanisms against compliance problems. Since the above objectives are crucial in establishing the extent to which internal audit practices enhance operational compliance within the organization, this particular study aims at finding out It seeks to evaluate the current practices in audit, for

example, audit frequency, auditor's independence, auditor's Competency, and reporting practices to ascertain whether the corporation has adequate compliance policies. Through the highlighted areas of concern and suggestions for improvement, the study will make a significant contribution to the understanding of how internal auditing can be utilized to strengthen operational compliance in the public sector of Ethiopia. The study examines key internal audit practices such as audit frequency, auditor independence, auditor competency, and audit reporting.

Research Method

The study employed an explanatory research design, which was considered most appropriate for explaining the research problem and determining the extent of compliance with the Addis Ababa Housing Development Corporation (AAHDC). This design enabled the means to gather data, which explained the current audit processes, the level of compliance at the organization, and other factors that showed the internal audit's potential to enhance compliance. Only the quantitative method was used, which means that the research gathered mainly numbers and then looked into their analysis (Bell, Bryman, and Harley 2022; Pandey and Pandey 2021). This approach was chosen to obtain variables like audit frequency, independence, Competency, and reporting practices and their relation to operational compliance. It was given a chance to test hypotheses with quantifiable human data. The target population was 18 finance managers, 14 internal auditors, and 18 senior accountants at the case organization AAHDC. These participants were recruited purposively, as the corporation only hired qualified staff for those positions. Due to the relatively small population size, the census was taken, and all the members of the internal audit team and the management staff were involved in the data collection process. It helped gather data from everyone who could have some input to contribute to the topic, thereby making the study very inclusive. The data was gathered from completed questionnaires developed for the purpose of capturing information in relation to internal audits, operations compliance, and organizational difficulties. The questionnaires included close-ended questions employing a Likert scale to measure perceived audit practices and their effect on compliance. Furthermore, the document analysis of audit reports and compliance records inputs additional quantitative data to give context to the numbers.

All collected data were subjected to descriptive and inferential analyses. Tabular analysis was used to analyze the data descriptively. In contrast, inferential statistics and regressions were used to test the hypotheses and to analyze the relationship between the variables relating to Internal Audit frequency and independence, auditor competency, and audit reporting practices to the level of operational compliance. This analysis was done using statistical software such as Statistical Package for Social Sciences (SPSS), which helps in retrieving precise results. In order to increase validity, the questionnaire was designed following scales that had already been used, and content validation was administered by auditing and compliance specialists. Since the items were developed from the study theories, pre-testing the items with a smaller sample from the target population enhanced item construct clarity. Internal consistency was also established to evaluate the reliability of measures, and a Cronbach's coefficient of more than 0.7 was used for the current study (Bruton, Conway, and Holgate, 2000; Tabachnick and Fidell, 2007). In light of the preceding, ethical practice was upheld to the letter throughout the study. Participants' consent was sought and documented, and an explanation of the study, the role of the participant, and information regarding rights, particularly the right to withdraw from the study at any one time,

was provided. Respondent anonymity and the confidentiality of the responses provided were preserved to minimize respondent bias. Data collected were analyzed securely, and results were processed without distortion in order to provide genuine information about the study. As a result, before beginning data collection, approval from the relevant institutional review boards was duly sought. Altogether, this research methodology allowed a systematic identification of the impact of internal audit practices upon operational compliance with the use of sound data collection and analysis tools, as well as compliance with ethical norms.

Result and Discussion

A demographic description of the respondents from Addis Ababa Housing Development Corporation shows that the organization's workforce is somewhat male-dominated across different departments, has different educational levels, and varies in experience. Of the total 128 employees, 51 (58.82%) are males, while 77 (41.18%) are females, and thus, gender diversity is very evident in such organizational finance, audit and accounting positions. In the area of education, the largest proportion possesses a bachelor's degree (54.90%). In comparison, almost as many (45.10 %) have obtained masters level education, showing highly educated employees equipped with the highest level of academic achievement. There is a fair distribution of the respondents as per their department; 35.29% of finance managers, 35.29% of senior accountants, and 27.45% of internal auditors are taken to study internal audit practices. With regard to experience, the majority (43.14%) of the participants claimed to have 6-10 years of experience, and a further 29.41% have 11-15 years of experience, which implies a strong mid-career group able to influence internal audit functions. In comparison, the remaining 9.80% have more than 16 years of experience. Given that its workforce comprises educated and experienced staff with cross-departmental exposure, AAHDC appears well positioned adequately to incorporate internal audit best practices that promote operational compliance, as well as encourage innovative practices into its internal audit function.

Table 1. Demographic Profile of Respondents

Demographic Variable	Frequency (N)	Percentage (%)
Gender		
Male	30	58.82%
Female	21	41.18%
Educational Qualification		
Bachelor’s Degree	28	54.90%
Master’s Degree	23	45.10%
Department		
Finance Managers	18	35.29%
Internal Auditors	14	27.45%
Senior Accountants	18	35.29%
Years of Experience		
0-5 years	9	17.65%
6-10 years	22	43.14%
11-15 years	15	29.41%
16+ years	5	9.80%

Source: Researcher survey, (2024)

Table 2. Analysis of Variance (ANOVA) and Coefficients for Operational Compliance

Model	Sum of square	df	Mean square	F	Sig
Regression	107.124	4	11.43	111.202	000
Residual	14.087	47	23		
Total	101.06	50			

Table 3. Operational Compliance (OC)

Coefficients	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta	111.202	000
(Constant)	.132	.132		.322	.000
FIA	.314	.096	.209	3.044	.002
AI	.320	.024	.467	4.927	.000
AC	.213	.063	.410	5.181	.000
AR	.274	.044	.183	3.030	.001
R^2					0.672

Predictors: Auditor Independence (AI), Audit Competency (AC), Audit Reporting (AR), Frequency of Internal Audits (FIA)
Source: Researcher Survey (2024)

Employing the findings from the analysis of variance (ANOVA) as well as the coefficients for operational compliance, the study comprehensively captures the determinants of compliance in the organization. The ANOVA reveals that the total regression model is significant, F (7,315) = 111.202, p = 0.000. This implies that the interaction between the predictor variables, AI, AC, AR, and FIA, can explain operational compliance.

The coefficient table shows that auditor independence (AI) has made the highest positive contribution to operational compliance with a Beta value of 467 and a t-value of 4.927 (p =.000), reaffirming the hypothesis was significant. Audit competency (AC) stands right next on the heels of it with a Beta of .410 and a t-value of 5.181 (p = .000), which confirms the role of skilled auditors in improving work compliance. The internal audit frequency (FIA) has a positive impact, reaching a Beta of.209 with a t-value of 3.044 (p = 0.002), proving that the higher the frequency of internal audits, the higher the companies' level of compliance. Moreover, audit reporting practices (AR) are also significant, having a positive beta of.183, t-value of 3.030 (p = 0.001); this clearly illustrates that for operational compliance, it is very important to have good reporting practices. The model accounts for 67.2% of the variation in operational compliance, as shown by the R^2 statistic of 0.672. This implies that the selected predictor variables are adequate to offer the right framework for analyzing the compliance issues in the organization. In particular, the results underscore the importance of auditor independence, Competency and reporting, as well as a frequent internal audit to ensure adequate operational compliance.

The findings of the study reveal that internal audit practices have an important function of enhancing operational compliance in the Addis Ababa Housing Development Corporation. The findings of the study are in line with (Agoglia et al. 2015a; Hakim and Omri 2015; Wibowo and Setyowati 2023). First, empirical evidence shows that audit

frequency has a significant positive relationship with the level of operational compliance. Frequent internal audits help in increasing compliance because the regular check always keeps a check and balance on non-compliance matters. To the same extent, this observation is in agreement with others, such as Bappa and Yahaya (2024(; Joshi (2020), who show that more frequent audits mean better monitoring and accountability. It is this consistency that serves to support the perception that continued monitoring is central to compliance management. Second, the study established that auditor independence is central to audit efficiency. It is more effective to have auditors with no recipe from management to enable them to deliver unbiased results. This results in a better internal audit, as the results of Zhang and Wei (2022) noted that auditor independence plays a key role in developing trust and providing objective compliance reports. This reduces the likelihood of any bias in the result since independent auditors' independence increases the audit process's credibility.

Third, this work establishes that audit competency leads to higher levels of operational compliance. Understanding compliance issues and recommendations is a combination of expert knowledge possessed by auditors. This finding is grounded in the theory of Competency, which proclaims that auditor specialization is connected with audit quality, according to Kalita and Tiwari (2023). Effective auditors do not only identify problems but also supply the necessary information that would enable the management to deal with compliance problems, hence boosting operational efficiency. Last, the study confirms that clear and transparent audit reporting is key to the improvement of operational levels of compliance. Financial reporting is supported by a detailed audit report that can readily facilitate corrective actions by management to sustain compliance. This is in tune with the research done by Wahyudin et al. (2022) on communication management to enhance decision-making in audit reports with a focus on compliance. Specifically, the clarity and transparency of audit communications are central to a management's ability to respond to matters identified by auditors. The reports also endorse the findings of this study by other authors, which establish essential internal audit practices as areas of accountability and operational compliance in both private and public sector organizations. Due to the elements of this study that link the audit frequency, independence, Competency, and reporting practices, this study shows the holistic view and perspective needed to improve the operational compliance in Addis Ababa Housing Development Corporation.

Conclusion

As such, the following recommendations can be made with respect to the findings with the aim of improving operation compliance within the Addis Ababa Housing Development Corporation. First, audit frequency needs to be improved so that more frequent audits can be performed in order to notice the violation immediately. Increasing the internal audit frequency will enhance proactive compliance, which will minimize small compliance breaches and turn them into substantial violations. For instance, organizing the audit in accordance with a strict plan – for instance, conducting audits quarterly – could greatly increase oversight and ensure that certain parameters are adhered to throughout the company on a stable basis. Second, establishing auditor independence is necessary to increase the objectivity of internal audits. It is important that the organization shields auditors and ensures that auditors do their tasks without any form of

influence from the managerial team. Mandating best practices that exclude the ways that auditors might have a conflict of interest, including the elimination of reporting lines between internal auditors and management, will enhance auditor independence and provide for a more accurate report. Third, the corporation should consider the training and the Competency of external auditors as its key concern. The training is important to update the auditors frequently with the policy changes and advancements in auditing practice and compliance. Any such course should be conducted on a regular basis to guarantee that the persons performing the auditing tasks are always competent in recognizing and dealing with compliance risks. Furthermore, the corporation should pursue other accreditation courses that will improve the competence and qualification of its internal auditors.

Last but not least, supplemental recommendations focus on the improvement of audit reporting to strengthen operational compliance. Rizqia and Lastiati's (2021) recommendations are that internal audit reports should be clear, brief, and constructive to enhance the flow of communication between auditors and management. Standardizing the formats used in reporting will make it easier for the management to see where the organization lacks in compliance so that necessary corrections can be addressed accurately. It is also essential to put in place arrangements for follow-up in order to achieve compliance by management with the recommendations given in audit reports. On this basis, the suggested recommendations will create a positive impact on the operational compliance of Addis Ababa Housing Development Corporation and organizational performance.

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