

**INTERNAL AUDITING PRACTICES AND FINANANCIAL PERFORMANCE
IN SELECTED PRIVATE BANKS IN MOGADISHU, SOMALIA.**

BY:

AHMED OMAR ABSHIR

MASTER OF BUSINESS ADMINISTRATION (KIU), BBA-ACCOUNTING (MU)

REG NO: MBA/38546/123/DF

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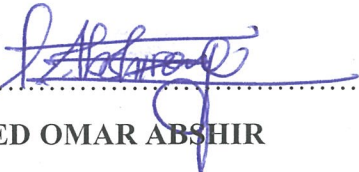
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DECLARATION A

I, AHMED ABSHIROW, declare that this dissertation is my own original work and has never been submitted for the award of a Degree in any University / Institution in and outside Somalia.

Signed


.....
AHMED OMAR ABSHIR

MASTER OF BUSINESS ADMINISTRATION (KIU), BBA-ACCOUNTING (MU)

Date


.....

DECLARATION B

This dissertation entitled: Internal audit practices and financial performance in selected private banks in Mogadishu Somalia, has been duly reviewed at each stage of its development by the undersigned as the candidate's supervisors.

Signed

Dr. SSendaji Muhammad (Supervisor)

.....

Date

DEDICATION

In a special way, I wish to dedicate my work to three very special people in my life. First, to the memory of my late mother, Mrs. Fadumo Ibrahim Abdi, who made me the person I am today. She was a wonderful mother and I will always appreciate the effort she invested into nurturing me and my siblings to greater heights.

I also dedicate my work to my Father Mr. Omar Abshirow Omar (Awyare) who has been there for me throughout my course and has constantly encouraged me to complete my dissertation so that I achieve my dream, “A masters in Business administration specially finance and banking”. His love, support and ignition of strengths can never be appreciated enough.

I also dedicate my work to my beloved brother, honorable person Hon. Abdullahi Omar Abshirow who has been giving me his support to complete this work, he is the one paid me my study of Master of Business admin-finance and banking without Allah and my beloved brother Mr. Hon. Abdullahi Omar Abshriow nothing could be possible to me.

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Special thanks to my parents, my sisters and brothers. Their unconditional support allowed me to achieve this goal; I thank to them for their love, endurance, persistence, and prayers.

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ABSTRACT

The Purpose of the Study was to establish the relationship between internal audit practices and financial performance in selected private banks in Mogadishu Somalia, the study also aims at testing the hypothesis. Four the research objectives have been formulated to guide the study namely to determine the profile of respondents in terms of age, gender, status, education level, job position, work experience, to determine the level of internal audit practices in selected private banks, to determine the level of financial performance in selected private banks, to determine if there is relationship between the level of internal audit practices and the level of financial performance in selected private banks. The study was based primarily on descriptive and co-relational design as well as quantitative methodology. The population was 160 employees of selected private banks and a sample has been taken using Slovene's formula. The sample of 114 employees was drawn and purposive sampling has been used and questionnaires have been used as research instruments.

The findings indicated that the sample was dominated by male staff (65.8%) over female staff (34.2%). Majority were aged between 20-25 years (36.0%), most of them had a Bachelor's degree (44.7%) whereas majority of them had worked for 1-2 years (28.9%) worked as treasury (24.6%). Also data analysis showed that there is a significant correlation between level of internal audit practices and financial performance ($r\text{-value}=.609$ and $\text{sig}=.000$), meaning that improvement in the internal audit practices increases the financial performance among the selected private banks in Mogadishu, Somalia.

The researcher also recommended that private banks of Mogadishu Somalia to always carry out control activities, control environment and monitoring daily operations, automatically and this will help them improve on their profitability, the employees of private banks in Mogadishu Somalia should always consider monitoring daily operations as an important factor whenever the work is being done in a timely manner and this will make their financial performance successes.

CHAPTER ONE

INTRODUCTION

1.0 Introduction

The study aimed at investigating internal auditing practices used by private banks in Mogadishu, Somalia and how they affected on financial performance. This chapter provided insight into the background, problem statement, and, objectives of the study, research questions, hypotheses, scope and significance of the study.

1.1 Background of the Study

Auditing has a significant role in the management of most organizations, it has become increasingly varied, both in scope and objective to assist all levels of management in assuring internal and external constituencies that financial resources are being properly managed and accounted for (James 2001).

In view of the recent global recession of 2009-10, When investments made by banks and financial institutions proved unsafe and almost triggered a financial meltdown that required strong input and investment by most democratic governments, the need for internationally regulated and well-audited financial institutions are greater than ever. Therefore financial institutions have started to concentrate on rigorous internal audit processes to implement financial performance of the organization, it is undertaken by an internal audit team that conducts regular control self assessments.

1.1.1 Historical prospective

Historically some types of internal auditing practices date back thousands of years. As mentioned earlier, the Greeks, Romans, and Egyptians were conducting audits before the birth of Christ. Interestingly, the scope of these early audits was in many ways akin to that of modern internal audits; both included an examination of the correctness of accounting records and an evaluation of the propriety of activities reflected in the accounts. Emphasis was on improving management

control over the activities of the organization. Such broad emphasis was not to reappear on a wide scale until after World War II (Institute of Internal Auditors, 2005).

In Africa, The internal audit has been developed and increased the attention to it and standards, guidelines and moral constitutions had been issued and became one of the important units in most banks in the world. Banks forms the chief corner-stone of any financial system, and indeed of the economy of a nation (James, 2003).

The demand for both external and internal auditing is sourced in the need to have some means of independent verification to reduce record-keeping errors, asset misappropriation, and fraud within business and no business organizations. The roots of auditing, in general, are intuitively described by accounting historian Richard Brown (1905, quoted in Mautz & Sharaf, 1961).

1.1.2 Theoretical prospective

Agency theory was also based on this study. This theory was developed by Dalton and Canella (2003), cited from journal of Business Strategy (2001). Agency Theory In its simplest form, agency theory explains the agency problems arising from the separation of ownership and control. The agency theory has its roots in economic theory and it dominates the corporate governance literature. Daily, Dalton and Canella (2003), point to two factors that influence the prominence of agency theory. Firstly, the theory is a conceptually simple one that reduces the corporation to two participants, managers and shareholders. Secondly, the notion of human beings as self interested is a generally accepted idea. Agency Theory In its simplest form, agency theory explains the agency problems arising from the separation of ownership and control.

1.1.3 Conceptual prospective

According (Kurt, 2000). Internal auditing practices are an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It 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. Internal auditing is a catalyst for improving an organization's effectiveness and efficiency by providing insight and recommendations based on analyses and assessments of data and business processes. With commitment to integrity and accountability, internal auditing provides value to governing bodies and senior management as an objective source of independent advice.

The aim of internal auditing is to improve organizational efficiency and effectiveness through constructive criticism. Internal audit has four main components: (1) internal audit function; (2) internal control system; (3) control environment; control activities and monitoring, (Eden and Mariah 1996).

Differences of opinion have long existed about the meaning and objective of internal control. Many people interpreted the term internal control as the steps taken by business to prevent fraud both misappropriation of assets and fraudulent financial reporting. Others, while acknowledging the importance of internal control for fraud prevention, believed the internal control has an equal role in assuring control over manufacturing and other processes (Whittington and Pany, 2001).

By internal auditing, therefore the researcher's operational definition implied that the internal audit is one of the important means for management to confirm and verify the compliance of administrative units in the financial and administrative policies, legislations, financial and Administrative systems and the adopted public policies.

Performance implies a combination of doing a job effectively and efficiently, with a minimum degree of employee created disruptions (Decenzo & Robbins, 1998).

By performance therefore the researcher's operational definition implied: is the end result of an activity.

According (Mullins,2002) refers financial performance how the organization scores on the different dimensions such performance as referring to output or results of an organization as measured against its intended outputs (as financial performance indicators, Profitability, Credit risk, Liquidity risk, financial institution and Compliance with laws and regulation

The financial institutions accountant has the responsibility of financial performance arrangements to assist management in the performance of the services of the institution while the financial institution auditor has among other duties the complementary role to examine whether management actually performs that efficiently. Every firm is most concerned with its profitability. One of the most frequently used tools is financial ratio analysis, which is used to determine the company's bottom line. Profitability measures are important to company managers and owners alike. If a small business has outside investors who have put their own money into

the company, the primary owner certainly has to show profitability to those equity investors. Profitability ratios show a company's overall efficiency and performance. We can divide profitability ratios into two types: margins and returns. Ratios that show margins represent the firm's ability to translate sales dollars into profits at various stages of measurement. Ratios that show returns represent the firm's ability to measure the overall efficiency of the firm in generating returns for its shareholders (Rosemary, 2011).

Some key financial ratios that are particularly useful as criteria for strategy evaluation are as follows: Return on investment, Return on equity, Profit margin, Market, Debt to equity, Earnings per share, Sales growth and Asset growth (zainbooks, 2009).

There gaps to the business manufacturing and services providers in Somali, especially the capital in the town of Mogadishu, those private banks effected by lack of ability to hire auditors, and lack of strong financial updated system.

1.1.4 Contextual prospective

Since the former central government of Somalia collapsed in 1991, there was a problem of failure in financial performance and managing the finance probably has become poor, there is a widely problem that Salam Somali Bank and Dahabshil Bank in Mogadishu failed to use their financial successfully. They pointed out that there is a signs which show that they had a problem such as in adequacy resource, poor customers service that caused many customers has left from the private banks in Mogadishu, and also it has reduced investments of the new organizations because of the reputations of these private banks has been negatively affected by poor financial performance, lack of government policies and regulation of financial institution. Therefore, internal auditing practices ensure compliance to set management policies. It also ensures that top management meet its overriding responsibility of establishing and maintaining a system regarding quality management, goals, resources, processes and effective performance which include monitoring and measuring the system's effectiveness and efficiency. Dahabshil and Salam Somali Bank, Somalia, are part of the private banks that operate in many other parts of the developing world. Salam Somali Bank and Dahabshil Bank under the guidance of their Highness, these two private banks, currently operate inside Somalia, they offer quality financial services; these banks are being developed the last five years. Dahabshil and Salam Somali Bank

employ many people who facilitate the need for the stakeholders and customers; they are the ones trying to fulfill services that are provided by the banks existing in the world.

1.2 Statement of the Problem

After collapsed the central bank of Somalia, there was a problem for poor financial performance in private banks in Mogadishu, Somalia. This problem caused poor financial performance entire business's manufacturing companies especially profit margin, return on assets, and return on equity.

In Somalia, the audit function in the banking sub-sector has not been fully taped since 1991; this could be seen in the numerous cases of errors, intent to defraud and other fraudulent acts that exist in the banking industry. It is therefore, no wonder that the distress in the banking sub-sector in the nineties reflected lack of effective control mechanism of the audit function in the banking industry.

The experience of failed banks in Somalia and other nations have called for reinforcement of audit and the strengthening of the control system in the Somalia banks. Despite all the efforts to put in place internal audit, there are continued reports of a wide range of financial fraud practices inside the organization, mismanagement, error of the transactions, thefts, waste of organization's assets and by passing laid down policies and procedures.

According to Roko, (1994), Internal audit is an integral part of the internal control system of financial institutions, at the heart of banking is the audit function: This is evidenced by the fact that all other departments are linked with internal audit department. The importance of internal audit system cannot be overemphasized, since organizations have recognized internal audit function as a tool for ensuring effective workings of the internal control system.

Okolo, (2001) describes internal audit functions as an aspect of control mechanism, within a business, manned by specially assigned staff. However, in Somalia, the audit function in the banking sub-sector has not been fully taped.

It is against this background that, any economic difficult existing these private banks in Mogadishu, could be made survival by using control mechanism, daily monitoring in business activities, to insure that the financial information in the banks are reliable, to comply with the laws and regulations and doing constantly further research on the environment which

surrounding them. Therefore, this study attempts to find out the role of internal auditing practices on financial performance in Private Banks in Mogadishu, Somalia.

1.2 General objectives

To investigate how the internal auditing practices can contribute to an improvement in financial performance in selected private banks in Mogadishu Somalia.

1.4 Specific Objectives

The study was guided by the following research objectives:

- (i) To determine the level of internal auditing practices in selected private banks in Mogadishu Somalia.
- (ii) To determine the level of the financial performance in selected private banks in Mogadishu Somalia.
- (iii). To determine if there is significance relationship between internal auditing practices and financial performance in selected private banks in Mogadishu Somalia.

1.5 Research questions

The study was guided by the following research questions:

- (i) What is the level of internal auditing practices in selected private banks in Mogadishu Somalia?
- (ii) What is the level of financial performance in selected private banks in Mogadishu Somalia?
- (iii) Is there a significance relationship between internal auditing practices and financial performance in selected private banks in Mogadishu Somalia?

1.5 Hypothesis.

H0: There is no significant relationship between the level of internal auditing practices and financial performance of selected private banks in Mogadishu, Somalia.

1.6 Scope of the study

1.6.1 Geographical scope+

2The study was conducted within the capital city of Somalia, Mogadishu. Mogadishu provided an optimal focus on for this study because it is where most of the private banks are developed.

1.6.2 Time Scope

The study was covered the period 2013-2014 the period when most local banks were faced with challenges of internal auditing practices and financial performance in selected private banks in Mogadishu Somalia.

1.6.3 Content scope

The study consists of a literature review, combined with an empirical investigation on: The current role of internal auditing practices and Improving on the financial performance of these private banks in Mogadishu Somalia.

1.6.4 Theoretical scope

The theory was based on this study is agency theory. This theory was developed by Dalton and Canella (2003), cited from journal of Business Strategy (2001).

1.7 Significance of the Study

The study shall be importance to the banks, how to present financial statement accurate and information inside the banks and, also the study will be important to the stake holders who rely on the work of internal auditing practices. This study will be important for the banks when they went to make investment or not, if the bank presents more profit and good governance, then the investors start to invest the companies. Findings of the study were revealing the position of the internal audit function in the organization as to whether it adds value or not to the financial performance of the organization. Recommendations like re-engineering audit roles requiring auditors to “think out of their boxes” and advocate innovative audit approaches like proactive auditing process review audits would go a long way to improve on financial performance.

All the above may be achieved by establishing the effect of internal audit function on the financial performance and suggesting possible solution.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter discussed in detail the variables under study (internal auditing practices and financial performance), the theories to which the study was based on and related studies.

2.1 Theoretical review

Agency theory was also based on this study. The agency theory has its roots in economic theory and it dominates the corporate governance literature. Daily, Dalton and Canella (2003), point to two factors that influence the prominence of agency theory. Firstly, the theory is a conceptually simple one that reduces the corporation to two participants, managers and shareholders. Secondly, the notion of human beings as self interested is a generally accepted idea.

Agency theory explains the agency problems arising from the separation of ownership and control. It “provides a useful way of explaining relationships where the parties’ interests are at odds and can be brought more into alignment through proper monitoring and a well planned compensation system (Davis, Schoorman and Donaldson, 1997:24). In their assessment and review of agency theory, Eisenhardt (1989) outlines two streams of agency theory that have developed over time: Principal agent and positivist. Principal agent relationship: Principal agent research is concerned with a general theory of the principal agent relationship, a theory that can be applied to any agency relationship e.g. employer employee or lawyer client. Eisenhardt describes such research as abstract and mathematical and therefore less accessible to organizational scholars. This stream has greater interest in general theoretical implications than the positivist stream.

Agency theory and the firm: a positivist perspective: Positivist researchers have tended to focus on identifying circumstances in which the principal and agent are likely to have conflicting goals and then describe the governance mechanisms that limit the agent’s self serving behaviour (Eisenhardt, 1989). This stream has focused almost

Exclusively on the principal agent relationship existing at the level of the firm between shareholders and managers. For example, Jensen and Meckling (1976), who fall under the positivist stream, propose agency theory to explain, inter alia, how a public corporation can exist

given the assumption that managers are self seeking individuals and a setting where those managers do not bear the full wealth effects of their actions and decisions.

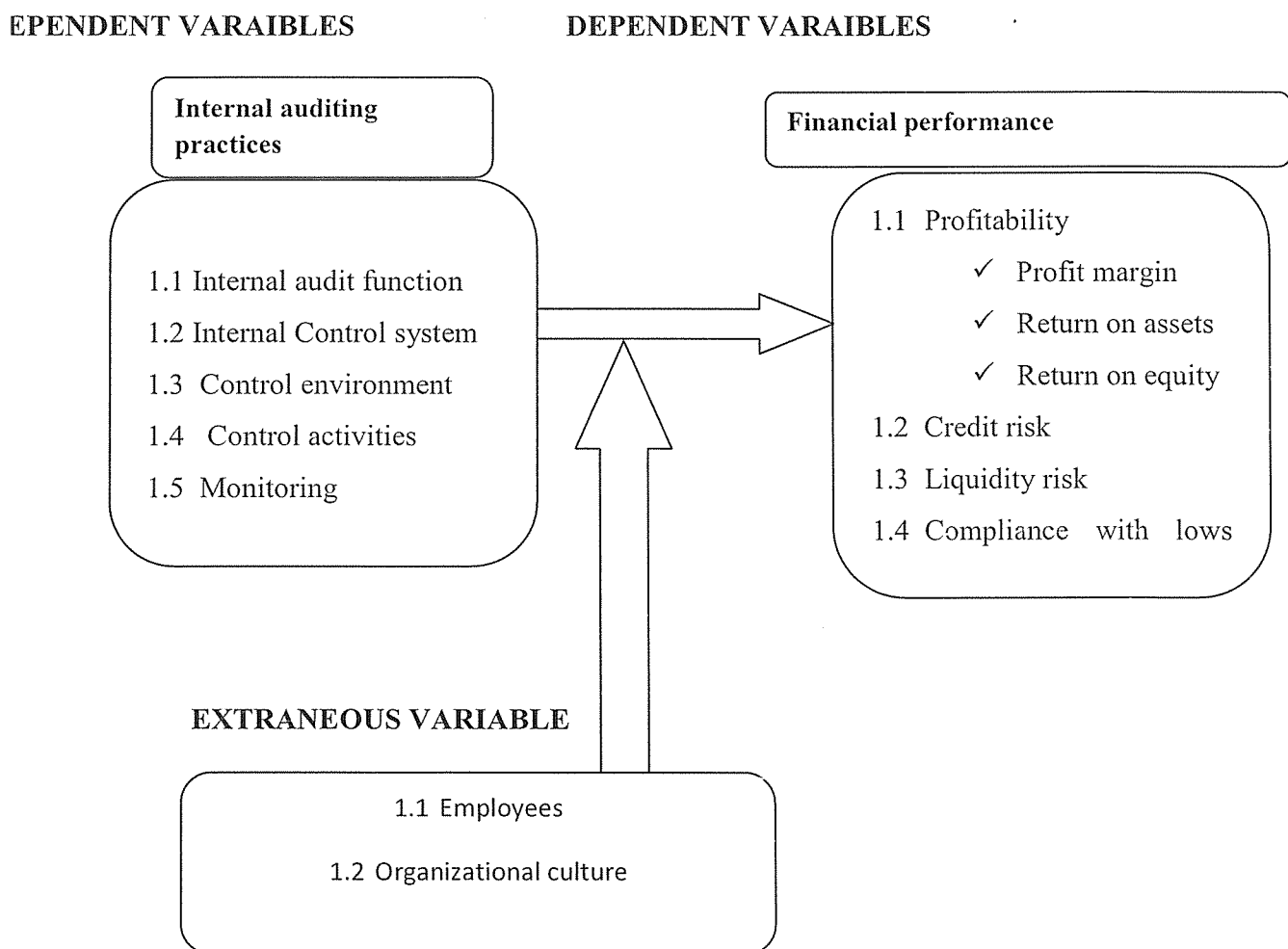
Therefore the dependent and independent variable of this research were based on the theory of agency.

Agency theory was based on this study; therefore this theory is so important in this study because they would contribute to develop internal audit function in private banks in Mogadishu, Somalia.

2.2. CONCEPTUAL FRAMEWORK

The conceptual framework below shows a diagrammatic representation of the inter- relationship between independent, intervening and dependent variables of the study.

Figure 2.2: Internal auditing practices and financial performance.



Source: Adapted from Robin and Jadan (1994).

The conceptual framework above is derived from the views of Robin and Jadan (1994) and tries to explain the relationship that exists between the dependent, independent and intervening variables that all put together, create an impact on financial performance in any given organization. Considering all the variables mentioned, it is the dependent variable (financial performance) that was of the primary interest for this study.

The framework shows that three sub themes of independent variables (control environment, control activities and monitoring) are used in an attempt to elaborate deeply the extent to which they can create an effect on financial performance. In addition, these three sub themes are used as a basis for the questionnaire. From the framework, the researcher believes that financial performance can partly be affected by the independent variables, which can lead to either poor financial performance or good performance. It is important to note that when a financial experiences a state of dissatisfaction, he/she may respond to the imbalance by opting for a number of actions that may lead to low performance and hence failure to achieve personal and organizational goals and objectives.

It is also indicated in the framework, that the intervening variable had the potential to influence financial performance. For instance, an employee might be paid a satisfactory reward, experience job satisfaction or be happy with the available welfare facilities provided to him or her and hence a hope for better performance. However, whenever one of the extraneous variables intercept in between the independent and dependent variables (as shown in the frame work), the financial performance is likely to be affected positively or negatively.

2.3 Review of Related literature

Related literature presented an analysis of previous research studies carried out on aspects of internal auditing practices and financial performance with an aim to draw meaningful relation to the prevailing situations in Salam Somalia Bank and Dahabshil Bank and further identify gaps for future research.

2.3.1 Internal auditing practices.

According (Kurt, 2000). Internal auditing practices are an independent, objective assurance and consulting activity designed to add value and improve a bank's operations. It 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. Internal

auditing is a catalyst for improving an organization's effectiveness and efficiency by providing insight and recommendations based on analyses and assessments of data and business processes. With commitment to integrity and accountability, internal auditing provides value to governing bodies and senior management as an objective source of independent advice. Professionals called internal auditors are employed by organizations to perform the internal auditing activity.

The objectives of Internal Audit are to:

- Independently review and appraise systems of control throughout the authority and its activities
- Ascertain the extent of compliance with procedures, policies, regulations and legislation
- Provide reassurance to management that their agreed policies are being carried out effectively
- Facilitate good practice in managing risks.
- Recommend improvements in control, performance and productivity in achieving corporate objectives.
- Identify fraud as a consequence of its reviews and to deter crime.

2.3.2 Internal Audit Function

Ellis, (2000) argues that internal auditing practices can be regarded a managerial control, which functions by measuring and evaluating the effectiveness of other controls. Williams, (2002) on the other hand asserts that, the primary objective of modern internal auditing is that it functions as a service to management by providing independent management oriented advice on an organization's operations and performance.

In recent years stakeholders expectations from internal audit functions have changed significantly observes (Thornton, 2004). The focus has now moved from a compliance and financial control function, to facilitating organizations to proactively identify assess and control risks. This demands that the Internal Audit function be very close to the business while maintaining independence, demonstrating a pro-active attitude in anticipating risks, controlling inefficiencies and acting as an agent of change adds (Roth, 2004).

2.3.3 Internal Control System

According to the Standards for Professional Practice of Internal Auditors (Pickett,2005), internal controls comprise, the plan and methods of the organization adopted to safeguard assets, comply with laws and regulations, ensure the completeness and correctness of accounting data, promote efficiency and encourage adherence to management policies. Kazt, (2004) argues that, to ensure the goals and objectives of a financial institution are properly met, that the company will achieve long-term profitability targets, and maintain reliable financial and managerial reporting, a system of strong internal controls must be in place.

COSO, (1992) states that company management should continuously and periodically evaluate the effectiveness of its internal controls. Roth (2004) confirms further that frauds that caused the collapse of Enron and World Com could not have arisen from the non-compliance with low-level accounting procedures. The root cause is always a break down in the control environment usually the ethical climate and \the behaviour of executives.

2.3.4. Control Environment

According to Cascarino and Van Esch. (2005). control environment is the tone set by top management and the overall attitude, awareness and actions of the board of directors, Management, owners, and others concerning the importance of internal control and the emphasis placed on control in the company's policies, procedures, methods, and financial performance, COSO, (1992) makes it clear that the control environment is the most important component of internal control and it can improve financial performance of the organizations. (Bertalanffy,1997), identifies attributes of control environment as; integrity and ethics of management, competence of employees, operating style of management, structure of the organization, involvement of board of directors and audit committee and evaluation of the environment.

2.3.5 Control Activities

According to the Statement on Auditing Standards (Maniak, 1990). Control activities are the policies and procedures that help ensure to improve financial performance of the organization. Crawford (2000) states that until recently, this has been the historical component of internal control. Jago, (2005) asserts that control activities can be categorized as authorization;

segregation of duties, record keeping, safeguarding and reconciliations and these controls depend greatly on the activity under consideration.

(Hald, 2003). argues that a great deal of activity specific knowledge is required to determine what the controls should be. COSO'S control framework presents a risk control matrix that analyzes activity-level objectives, risks, and controls. COSO lists some complete frameworks, or models, that can be used to model control activities such as, Control Objectives for Information Technology (COBIT), Systems Assurance and Control (SAC), Total Quality Management (TQM), and System Development Life Cycle (SDLC) depending on the activities involved. Warren, (2003) argues that control activities usually involve two elements: a policy establishing what should be done and procedures to affect the policy.

2.3.6 Monitoring

Monitoring is a process that assesses the quality of internal control performance over time (Willis & Lightle, 2000). Chioccola & Muhlstein, (2005) argue that financial structure should include an independent monitoring function over derivatives, providing senior management with an understanding of the risks of derivative activities, validating results, and assessing compliance with established policies.

According to Thornton, (2005) the process of monitoring can be accomplished through ongoing monitoring activities, separate evaluations or a combination of the two. Ongoing monitoring occurs in the course of operations and includes regular management and supervisory activities, and other actions personnel take in performing their duties.

In line with Thornton, (Warren, 2003) asserts that the scope and frequency of separate evaluations will depend primarily on an assessment of risks and the effectiveness of ongoing monitoring procedures and warren, 2003 says to minimize cost and maximize the profits of the organization, monitoring should be considered first and implemented any transaction happens in the organization . Thus internal audit should promptly identify internal control deficiencies and report them upstream, with serious matters reported to top management and the board.

2.4 Financial Performance

2.4.1 Relevance of Financial Report

Relevance and organizing (now referred to as "representational faithfulness") are important qualities of financial reporting that both the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) use in setting standards (FASB 2010; IASB 2010). Relevance addresses the pertinence of an economic construct (e.g., fair value, historical cost) to a user's decision. Reliability addresses how well that economic construct, or phenomenon, is depicted or measured (e.g., fair value based on a market transaction or model inputs). Standard setters state that although the decision usefulness of accounting information is a joint function of its relevance and reliability, these two qualities are distinct and independent (FASB 2010).

What we mean by reliability of financial reporting is the preparation of reliable published financial statements. The report includes interim and condensed financial statements and selected financial data derived from such statements. Reliability refers to the quality of information, to what extent the information is free from error in reasonable terms. Reliability of financial reporting means the preparation of timely, reliable and relevant reports needed for decision-making within the organization. It also addresses the need for financial statements, reliable annual accounts and other financial information for shareholders, board of directors, supervisors and other external parties, whose quality and integrity are absolutely necessary in making decisions (Bushman, 2007).

Financial statements cannot be useful if they are based on unreliable and inaccurate recordings of transactions. There is no greater example of the garbage in, garbage out principle than financial statement preparation. The problem is that financial statement users cannot usually assess the presence of garbage simply by reading the statements. The statements may look fine, but in reality be riddled with inaccuracies (Aldridge and Colbert, 1994).

2.4.2 Compliance with Laws and Regulations

A standard dictionary definition of compliance conjures notions of conformity – “the act or an instance of complying; obedience to a request or command” (Concise OED, 1990 quoted by Hutter, 1997).

Compliance with laws and regulations deals with those laws and regulations which the organization is subject to. First and foremost, the organization must be aware of all laws and regulations to which it is subject such as generally accepted accounting principles (GAAP), EU rules and regulations, corporate governance rules, and other specific ones (Bushman, 2007).

In general, compliance means conforming to a rule, such as a specification, policy, standard or law. Regulatory compliance describes the goal that corporations or organizations aspire to in their efforts to ensure that personnel are aware of and take steps to comply with relevant laws and regulations (john 2003).

Due to the increasing number of regulations and need for operational transparency, organizations are increasingly adopting the use of consolidated and harmonized sets of compliance controls. This approach is used to ensure that all necessary governance requirements can be met without the unnecessary duplication of effort and activity from resources (Aldridge and Colbert, 1994).

Compliance objectives needed to be reaching in order to protect the organization's franchise and reputation, by respecting the laws and regulations, the supervisory requirements and the organization's policies and procedures (Applegate and Wills, 1999).

2.4.3 Efficiency and Effectiveness of Operations

Efficient refers to the relationship between the resources used and the outputs produced to achieve the objectives. It means the minimum resource inputs to achieve a given quantity and quality of output, or a maximum output with a given quantity and quality of resource inputs. Effective refers to the accomplishment of objectives or to the extent to which the outcomes of an activity match the objective or the intended effects of that activity. "Performance and profitability goals as well as safeguarding of resources are the major objectives to be attained by effective and efficient operations. This implies that operations are performed so as to attain their intended effect (COSO, 1992).

Operational objectives are designed to maintain efficiency and effectiveness in the operations of a company. Included in operational objectives are procedures that promote companies' use of assets and resources properly. There are two types of internal controls. Preventative controls are procedures used to avoid potential problems before they happen. Operational objectives are designed to serve this purpose. Procedures developed to meet operational objectives include

things such as the separation of duties and the requirement of proper authorization and password usage to control access to important company information (Bushman, 2007).

2.4.4 Profitability

Corporate earnings are important to investors. By comparing corporate earnings of prospective investments, one makes wiser investment decisions. Profitability ratios are some of the measures that provide tools to make these comparisons. Inman, (2001) defines profitability ratios as measures of performance showing how much the firm is earning compared to its sales, assets or equity. Madonna, (2001), identifies three important profitability ratios to include: net profit margin, return on assets and return on equity.

2.4.4.1 Profit Margin

Profit Margin measures how much a company earns relative to its sales. According to Lesonsky, (2000), there are two profit margin ratios; operating profit margin and net profit margin. A company with a higher profit margin than its competitor is more efficient. (Gleim, 2004) However argues that profit margin is a key indicator that describes the profit generating capacity of the flow of revenue, but does not tell much about the actual efficiency of its employees.

2.4.4.2 Return on Assets

According to Gillooly, (2004), Return on Assets shows how well management is performing on all the firm's resources. Allis, (2004) Says ROA measures how efficiently profits are being generated from the assets employed in the business when compared with the ratios of firms in a similar business. A low ratio in comparison with industry averages indicates an inefficient use of business assets. The Return on Assets Ratio is calculated as $\text{Net Profit before Tax} / \text{Total Assets}$. From the assertions of Kennon, (2004) the general rule is that anything below 5% is very asset heavy.

2.4.4.3 Return on Equity (ROE)

Sabatini, (2000) explains ROE as a measure of the return an investor receives on the capital that has been invested in the business. DiNunno (2002) argues that ROE estimates are often based on current performance assumptions without an understanding of the impact of these changes. The real value of ROE estimation and measurement is in examining all the costs and benefits to

determine business impact (operations, staffing and opportunities, for example) and shape company strategy.

Kennon (2004) argues that organizations that generate high returns relative to their shareholder's equity are organizations that pay their shareholders off handsomely, creating substantial assets for each dollar invested. Such organizations are more than likely self-funding companies that require no additional debt or equity investments. By relating the earnings generated to the shareholder's equity, an investor can quickly see how much cash is created from the existing assets.

2.4.5 Credit risk

Kennon (2004), Credit risk is the risk that the borrower will be unable to repay loans as they fall due, and the borrower's failure to comply with agreed credit terms. Ranson, (2005) asserts that credit risk relates to the possible loss in asset value due to the default of counterparty banks, issuers of securities or other counterparties, as an example, According to HFCU Risk Management Policy (2002) and Bank Uganda Regulatory Guidelines, credit risk refers to loans whose principal and interest is due and unpaid for 90 days or more; or interest payments equal to 90 days interest or more have been capitalized. According to Sooran, (2005), banks and other lending institutions must constantly balance risks and rewards because too high a price on loan products will cause loss of customers while too low a price, will starve the profit margin of the institution.

2.4.6 Liquidity risk

According to Matz, (2005) liquidity risk is the current and prospective risk to earnings or capital arising from a bank's inability to meet its obligations when they come due without incurring unacceptable losses. Liquidity risk includes the inability to manage unplanned decreases or changes in funding sources. To support Matz's view, (Sooran, 2005) adds that liquidity risk arises from the failure to recognize or address changes in market conditions that affect the ability to liquidate assets quickly and with minimal loss in value.

2.5 Related Studies.

Using data from 250 auditing practitioners from Kuala Lumpur Stock Exchange (currently known as Bursa Malaysia) - listed companies, this study suggests that independence, scope of audit work, audit reporting, audit programs, management of internal audit department, performance of audit work, audit reviews, objectivity and professional proficiency are important internal auditing practices from the perception of internal auditors. This study also suggests that risk assessment, control activities, control environment, information and communication and monitoring are important quality of internal control system from the perception of audit committee. This study also set out to examine the influence of internal auditing practices on the quality of financial performance. Management of internal audit department, professional proficiency, objectivity, return on assets, return on equity and audit review of the internal auditing practices were shown to be statistically influence the monitoring aspect of internal control system. Scope of audit work and performance of audit work influence the information and communication aspect of internal control system. Performance of audit work, professional proficiency and objectivity statistically influence the control environment. Management of internal audit department, performance of audit work, audit program and audit reporting statistically influence the risk assessment of the internal control system while performance of audit work and audit reporting statistically influence the control activities Prof Dr. Hasnah Haron, Prof Dr. Muhamad Bin Jantan Octoper, (2005).

A study was conducted in (2005) by Mohamed and Jama in Yemen. They declared that the financial performance with a sample of 104 Staffs' these two researchers indicated that there is a main factor involved: to encourage the firms by using financial ration analysis.

Furthermore, another study was conducted by Jadan (1993) a study on Malaysia revealed that providers of internal auditing practices have not done enough in educating stuffs on their products; that study indicated the 75% of the respondents had limited knowledge in internal audit in the banking systems.

A study was conducted (2003) by faudziah hanim bt hj. Fadzil she declared that The performance of an internal audit department must function in a manner that is in accordance with applicable professional standards such as Standards for the Professional Practice of Internal Auditing (SPPIA, 2000) and the quality of the internal control systems. Given the current business scenario, this study looked at the internal auditing practices and performance of internal

audit departments. Using data from 250 auditing practitioners in KLSE-listed companies, this study suggests that independence, scope of audit work, audit reporting, audit programs, management of internal audit department, performance of audit work, audit reviews, objectivity and professional proficiency are important internal auditing practices from the perception of internal auditors. This study also suggests that risk assessment, control activities, control environment, information and communication and monitoring are important quality of internal control system from the perception of audit committee. This study also examines the influence of internal auditing practices on the quality of internal control system. Management of internal audit Department, professional proficiency, objectivity and audit review significantly influence the monitoring of the quality of the internal control system. Scope of work and performance of audit work significantly influences the information and communication of the quality of the internal control system while performance of audit work, professional proficiency and objectivity significantly influence the control environment of the quality of the internal control systems. The study also shows that the management of internal audit department, performance of audit work, audit program and audit reporting significantly influences the risk assessment of the quality of the internal control system. On the other hand, performance of audit work and audit reporting significantly influences the control activities of the quality of the internal control system. Information and communication and risk assessment of the quality of the internal control systems do significantly influence the performance of the internal audit department. This study Further shows that scope of audit work, professional proficiency, independence and audit reporting of the internal auditing practices significantly influence the performance of the internal audit department. Finally, the study shows that risk assessment of the quality of the internal control system partially mediates the audit reporting of the internal auditing practices and the performance of the internal audit department.

However, based on the previous studies and arguments in many different countries, they agreed mostly that an internal auditing practice is very important issue in the banking system and any manufacturing companies.

Though in Somalia, the previous studies were not carried out more about addressing the internal auditing practices and financial performance, so it is needed to do further research on this topic. Thus, this study will attempt to investigate internal auditing practices and financial performance.

CHAPTER THREE

METHODOLOGY

3.0 Introduction

This chapter consisted of design, population, sampling strategies, data collection methods, data collection instruments, Validity and Reliability of the Instrument, procedure and data analysis.

3.1 Research Design

This study was undertaken using a descriptive design and descriptive co relational research design to determine significance relationship between the level of internal auditing practices and the level of financial performance in selected private banks in Mogadishu Somalia and it was mainly descriptive in nature. Due to limited time and resources, the researcher chose this method because it would reduce time wasting and ensure that representation of respondents was done according to those found at the private banks. Both qualitative and quantitative data were collected by use of this design and further subjected to scientific and descriptive analyses.

3.2 Research Populations

The study focused on two private banks which were Dahabshil bank and Salama Somali bank. All those private banks locate in Mogadishu, Somalia. The target populations of this study were 160 from the staff of those private banks. This population is seeking because it possessing an adequate understanding of internal audit and also they are aware of the weaknesses or malfunctions of the financial performance. The total population of the study will be 160 employees, Computed (Using Slovens' Formula) sample size are 114.

3.3 Sample Size

In view of the nature of the target population was the staff of those private banks; a sample was taken from each category. Table 3.1 shows the respondents of the study. The Sloven's formula was used to determine the minimum sample size.

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

Where **n** is the required sample size, **N** is the target population size and **e** is the standard error or level of significant, which is popular known to be equal **0.05** or **5%**.

$$n = \frac{160}{1 + 160 (0.05)^2}$$

$$n = \frac{160}{1 + 160 (0.0025)} = \frac{160}{1.4} = 114$$

Therefore, 84 employees was selected from Dahabshil Bank while 76 employees from Salam Somali Bank. From there, each sample size of these banks was as follows:

1. Dahabshil Bank:

$$n = \frac{N_{\text{servie}}}{N_{\text{overall population}}} \times \text{Sample size} = \frac{84}{160} \times 114$$

$$n = 59.85 = 60$$

Salam Somali Bank:

$$n = \frac{N_{\text{servie}}}{N_{\text{overall population}}} \times \text{X sample size} = \frac{76}{160} \times 114$$

$$n = 54.15 = 54$$

Table 3.3: Showing the target respondents to be used in the study

Population Category	Population Name	Population Sample	Sample Size
Dahabshil bank	Employees	84	60
Salama Somali bank	Employees	76	54
Total		160	114

Source: respondent categorization by the researcher (2014)

3.4 Sampling procedures

The study was used purposive sampling technique to select those two private banks to participate in the study. Dahabshil bank and Salam Somali bank were selected because they are the major private banks in Mogadishu, Somalia.

Mean	Description
-------------	--------------------

4.21-5.00	very high
-----------	-----------

3.41-4.20	high
-----------	------

2.41-3.40	medium
-----------	--------

1.81-2.40	low
-----------	-----

1.00-1.80	very low
-----------	----------

3.5 Research Instrument

In a bid to enhance the reliability of the findings, Different instruments were used for the data collection. Thus, the major data collections of instruments were used in this study are namely, questionnaire and interview guide. The choices of these instruments were guided by the data required and the objectives of the study.

3.6 Validity and Reliability of the Instrument

Validity is the quality of the test doing what is designed to do (Salkind, 2000). In this research validity of the respondent's instruments, questionnaire and interviews are establishing through a

content validity index CVI by consulting finance and accountant experts. In validity content concerned with a test's ability to include or represent all of the content of a particular construct, is assessed by overview of the items by trained individuals taking CVI above 0.70 as accepted for social sciences (Amin, 2005).

The individuals made their judgments about the relevance of the items. The CVI was established using the formula: $CVI = \text{Number of items declared valid} / \text{Total number of items}$

The results of the CVI are shown in table 3.2 below

Variable	Number of items	CVI
Internal auditing practices	10/10	1
Financial performance	18/18	1

Source: Primary data

Table 3.2 shows that internal audit will be measured using 10 items and yielded CVI of 1 while financial performance was measured 18 items and yielded a CVI of 1 Since two variables yielded a CVI above 0.70 accepted for social sciences, it was concluded that the instrument had a good validity hence relevant.

To achieve accuracy or reliability, pre-testing of the instruments was done. This was done with similar private banks in Mogadishu, somalia. Questionnaires were distributed to those categories of staffs as pilot test. The results from this pre-testing helped in rephrasing and adjustment of questions that were unclear so as to bring about clarity and reliability.

Table 3.4: Reliability Test Results

Variables	No of Items in the Questionnaire	Cronbach's Alpha
Internal audit practices	10	0.8
Financial performance	18	0.94

The findings in Table 3.4 shows that computed Cronach Alpha obtained from the reliability test was 0.8 from the variable of internal audit practices, 0.94 from the variable of financial performance and those were greater than the estimated alpha of 0.70 thus, the instruments were considered reliable.

3.7 Data Gathering Procedures

The following data collection procedures were implemented:

3.7.1 before the administration of the questionnaires

1. An introduction letter obtained from the College of Higher Degree and Research for the researcher to ask for approval to conduct the study from respective managers of private banks in Mogadishu, Somalia.
2. When approved, the researcher secured a list of the qualified respondents from the private banks directors and select through systematic random sampling from this list to arrive at the minimum sample size.
3. The respondents explained about the study and requested to sign the Informed Consent Form (Appendix 3).
4. Selected research assistants who would assist in the data collection; briefed and oriented them in order to be consistent in administering the questionnaires and interviews.

3.7.2 During the administration of the questionnaires

Specifically, the researcher and his assistants was a seriously particular in requesting the respondents the following: (1) to sign the informed consent; (2) to answer all questions hence should not leave any item unanswered; (3) to avoid biases and to be objective in answering the questionnaires. The researcher and his assistants were tried retrieving the questionnaires and interview within two weeks from the date of distribution. All questionnaires and interviews retrieved were checked if completely filled out.

After the administration of the questionnaires, the data collected was organized, collated, summarized, statistically treated and drafted in tables using the Statistical Package for Social Sciences (SPSS).

3.8 Data analysis

After received the questionnaire back, the researcher encoded the data into the computer and statistically treated using the Statistical Package for Social Sciences (SPSS)

3.9 Ethical Considerations

Bearing in mind the ethical issues, the researcher provided the respondents with the necessary information as regards the main purpose of the research, expecting duration and procedures to be following, and be in position to keep privacy and not disclose the confidentiality of respondents and researchers responsibility.

CHAPTER FOUR

PRESENTATION, ANALYSIS AND INTERPRETATION OF RESULTS

4.0 Introduction

This chapter shows the background information of the respondents, the level of internal auditing practices and financial performance and it also shows the significant relationship between the level of internal auditing practices and financial performance in private banks in Mogadishu Somalia, their responses were analyzed using frequencies and percentage distributions as indicated in table 4.1

4.1 Demographic Characteristics of the Respondents

Table: 4.1 Profile of Respondents

Category	Frequency	Percentage %
Age for the respondents		
20-25 years	41	36.0
26-35 years	33	28.9
36-45 years	26	22.8
above 45 years	14	12.3
Total	114	100.0
Gender for the respondents		
Male	75	65.8
Female	39	34.2
Total	114	100.0
marital status for the respondents		
Single	48	42.1
Married	66	57.9
Total	114	100.0
Qualification for the respondents		
Secondary school	10	8.8
Diploma	25	21.9
Bachelor degree	51	44.7
Postgraduate	28	24.6

Total	114	100.0
Position for the respondents		
Member of board of directors	19	16.7
senior management	22	19.3
internal auditor	12	10.5
Accountant	16	14.0
Treasury	28	24.6
Cashier	17	14.9
Total	114	100.0
Experience for the respondents		
Below one year	24	21.1
1-2 years	33	28.9
3-4 years	32	28.1
above 5 years	25	21.9
Total	114	100.0

Source: primary data, SPSS output version 14.0

In this table 4.1, the majority 41(36.0%) of the respondents were aged between 20-25 years while 33 (28.9%) of the respondents were aged between 26-35 years and this table indicated that 26 (20.8%) of the respondents were aged between 36-45 years likewise 14 (12.3%) of the respondents were aged between 45 and above.

The data from table 4.1 indicates the distribution of respondents according to the gender. The results show that the majority of the respondents 75(65.8%) were male while 39 (34.2%) were female, this results shows that males work for the commercial banks in Mogadishu more than females.

In this table 4.1, the majority 48 (42.1%) of the respondents were single while 66 (57.9%) of the respondents were marriage, this result show that marriage persons more than the singles.

In this table 1, the majority 51 (44.7%) of the respondents are Bachelor degree holders. While 28 (24.6%) of the respondents are postgraduate degree holders, this results also shows that 25 (21.9%) o the respondents are diploma holders while 10 (8.8%) of the respondents only are secondary school The results show that managers and banking officers in the selected banks are qualified, hence resourceful. However the level of qualification has to be improved in order to reinforce the staff knowledge and skills. This is because in the future the lack of advanced degree holders shall challenge the financial performance with regard of human resource especially as they are operating in a competitive financial market.

The data from table 4.1 indicates the distribution of respondents according to their position. The results show that majority 28 (24.6%) of the respondents are treasure; 22 (19.3%) of the respondents are senior management while 19 (16.7%) of the respondents are member of the board directors; 12 (10.5%) of the respondents are internal auditors while 16 (14.0%) of the respondents are accountants. The above mentioned results show that the position of the bank officers matches with nature of operations they are performing and especially those related to internal auditors and accounting. This is supported by the view of Weetman where he stated that the participants in communication process cover a range of expertise and educational background, so far as accounting is concerned. In our case the participation of accountants in financial reporting which is a part of financial communication is an asset to the selected banks.

The data from table 4.1 show the distribution of respondents according to their professional experience. 33 (28.9%) which represent the majority of the respondents have a professional experience of 1 to 2 years. The results also indicate that (28.1%) of the respondents have a professional experience of 3 to 4 years and The results indicates that It is deduced from the table 4.1 indicates that the majority of the respondents 33 (28.9%) were experienced between 1-2 years; 32 (28.1%) of the respondents were experienced 3-4 years while 25 (21.9%) of the respondents were experienced between above 5 years also 24 (21.1%) of the respondents were experienced below one year.

Findings

The findings indicated that the sample was dominated by male staff (65.8%) over female staff (34.2%). Majority were aged between 20-25 years (36.0%), most of them had a Bachelor's degree (44.7%) whereas majority of them had worked for 1-2 years (28.9%) worked as treasury (24.6%).

4.2 Research question one: level of internal auditing practices

Research question one is derived from the first objective of the study. The first objective of this study was to determine the level of internal auditing practices in Mogadishu, Somalia.

To achieve this objective, respondents were given a number of questions to provide answers to research question, Each of these questions were based on the five point likert scale; where the respondents were asked to rate the extent to which internal auditing practices is high or low by indicating the extent to which they agree or disagree with each question and their responses were analyzed by using SPSS and summarized by using means, interpretation and rank as indicated in table 4.2

Table 4.2 Level of internal auditing practices

Indicators	Mean	Standard deviation	Interpretation	Rank
Control environment				
1. Internal audit is a adequate staffed	4.14	1.166	High	1
2. internal audit operates with a formal charter approved by the board of this bank	4.87	.489	Very high	2
3. The internal audit staff possesses the skill and knowledge to undertake the work program	4.96	.295	Very high	3
4. Internal auditing practices in this bank is independent	4.99	.094	Very high	4
Average mean	4.74		Very high	
Control activities	Mean	Standard deviation	Interpretation	Rank

1. internal audit identifies and profiles its stakeholders and audits clients, their needs and expectations	2.26	.852	Low	1
2. Refocusing internal audit function and extracting more value from it are imperative if the business into build comparative advantage	4.63	.707	Very high	2
3. Internal audit has moved away from being reactive to being proactive and risk focused	4.84	.390	Very high	3
Average mean	3.91		High	
Monitoring	Mean	Standard deviation	Interpretation	Rank
1. Any operation being held in this bank is audited daily by the auditors	4.28	.973	Very High	1
2. Internal audit has a comprehensive internal monitoring program	4.44	.969	Very High	2
3. The organization have assessed the need for the use of internal capability for monitoring and review of internal controls	4.77	.580	Very high	3
Average mean	4.4		Very High	
Grand mean	4.3		Very High	

Source: primary data, SPSS output version 14.0

Control environment- four items were used to measure this construct and all the items were rated very high, therefore on average control activity was rated very high and this was indicated by the average mean (mean=4.74), implying that control activity is frequently practiced by private banks in Mogadishu Somalia.

Control activities- this variable was measured by three items and respondents were asked whether they agreed or disagreed with the statements under investigation. Responses reveal that control activities as a construct on the independent variable was rated high (mean= 3.91), this implying that having control activities always helps the employers in predicting future performance of their private banks.

Monitoring- Three items were used to measure this construct so the respondents were asked whether they agreed with the statements there in, their responses indicated that monitoring any operation as a construct on the independent variable was rated very high with overall mean (mean=4.4), this implying that banks in Mogadishu have the ability to monitor and review the internal controls.

Findings

This findings indicate that the level of internal auditing practices is generally rated very high level and this is indicated by the overall mean (overall mean=4.3), this implies that the workers in the selected private banks in Mogadishu Somalia have the required internal auditing practices, internal auditing practices was broken into three major constructs and these included the following; control environment, control activities, monitoring.

4.3 Research question two: level of financial performance

The dependent variable in this study was financial performance and the researcher wanted to determine its level, financial performance was broken into six constructs with their questions and these include the following; Reliability of financial report and compliance with laws and regulations, profitability, credit risk and liquidity, efficiency and effectiveness of operations. Each of these questions were based on the five point likert scale; where the respondents were asked to rate the extent to which financial performance is high or low by indicating the extent to which they agree or disagree with each question and their responses were analyzed by using SPSS and summarized by using means, interpretation and rank as indicated in table 4.3.

Table 4.3: Level of financial performance

Indicators	Mean	Standard deviation	Interpretation	Rank
Reliability of Financial Report				
1. The bank records daily transactions with their source documents	4.53	1.191	Very high	1
2. Financial reports published as soon as possible after the end of the reporting period to inform decision making	4.91	.432	Very high	2
3. The financial report of this bank is presenting accurate description of the financial facts and events during the past period.	5.00	.000	Very high	3

Average mean	4.81		Very high	
Compliance with laws and regulations	Mean	Standard deviation	Interpretation	Rank
1. The bank's rules and regulations are understandable and provisions in detail	4.05	1.475	High	1
2. The bank is taking steps to comply with relevant laws and regulations	3.0	1.166	Medium	2
3. The bank practices the low and regulations in regular contexts	2.4	1.191	Low	3
Average mean	3.15		Medium	
Profitability	Mean	Standard deviation	Interpretation	Rank
1. The management establishes the minimum return required to meet the company's return	4.31	1.106	Very high	1
2. Comparisons are made of the current profits with the profits made in the previous years to assess profitability trends	4.44	.969	Very high	2
3. Your bank determines the profitability of each product by identifying the components of revenue and expenses for each product	4.90	.595	Very high	3
Average mean	4.55		Very high	
Credit risk	Mean	Standard deviation	Interpretation	Rank
1. The bank has appropriate policy and procedures for the collection of its loans in default	4.26	.941	Very high	1
2. The bank has in place appropriate internal procedures for the identification and measurement of credit risk	4.39	.974	Very high	2
3. The bank assesses the borrower's capacity to meet the obligations and the quality of collateral pledged for the claim	4.44	.969	Very high	3
Average mean	4.36		Very high	
Liquidity	Mean	Standard deviation	Interpretation	Rank
1. The bank maintains adequate liquidity ratios for its assets	4.04	1.000	High	1
2. There is existing appropriate internal procedure for the calculation and measurement of liquidity risk	4.10	1.085	High	2
3. The bank adequately plans and adjusts inflows and outflows of liquid assets so as to prevent maturity mismatch	4.32	.970	Very high	3
Average mean	4.15		High	
Efficiency and effectiveness of operations	Mean	Standard deviation	Interpretation	Rank

1. The bank uses its assets and resources properly	2.21	1.046	Low	3
2. The bank performs reviews on their operations	4.35	1.047	Very high	
3. Organization's resource are safeguarding in safe places	3.1	.789	Medium	
Average mean	3.22		Medium	
Grand mean	4.02		High	

Source: primary data, SPSS output version 14.0

Reliability of financial report- three items were used to measure this construct so the respondents were asked whether they agreed or disagreed with the statements, their responses were rated very high with the overall mean (mean=4.81), this variable implying that financial report of the banks in Mogadishu prepared and presented well and financial information is always printed to the financial institutions.

Compliance with laws and regulations, three items were used to measure the construct so the respondents were asked whether they agreed with statements, the responses of these items were rated neutral with overall mean (mean=3.15), this implying that the respondents were silent to answer this construct means that they don't have more information about how these private banks comply with their rules and regulations.

Profitability- this variable was operationalized by using three items and the respondents were asked if they agreed with the statements under investigation, their responses revealed that on average profitability was rated very high with overall mean (mean= 4.55), implying that the financial performance reported by the selected private banks in this sample is simply identified the components of revenue and expenses by the owners.

Credit risk- three items were used to measure this construct and respondents were asked whether they agreed with the statements. Responses indicated that credit risk was rated very high level on average (mean =4.36), implying that majority of private banks in Mogadishu, Somalia highly recognized credit risk items while reporting the financial information to the users.

Liquidity- three items were used to measure this construct and results indicated that on average liquidity of financial performance was rated high level and this was indicated by the average

mean (mean=4.15), implying that the private banks in Mogadishu plans and adjusts inflows and outflows of liquid assets so as to prevent maturity mismatch.

Efficiency and effectiveness of operations-Three items were used to measure this construct so that the respondents were asked whether they agreed with the statements there in, their responses indicated that efficiency and effectiveness of operations were rated medium level with overall mean (mean=3.22), implying that the employees of the private banks in Mogadishu, they don't have enough information about the efficiency and effectiveness of operations therefore, they said "medium".

Findings

Results in table 4.3 denoted that financial performance was generally rated high level and this was indicated by the grand mean (mean=4.02), implying that the selected private banks in this sample always produce high quality of financial performance to the users such as stake holders and government, customers, owners, staffs and so on.

4.4 Research question three: Hypothesis

The last objective in this study was to establish whether there is a significant relationship between the level of internal auditing practices and financial performance in selected private banks in Mogadishu Somalia, the researcher stated a null hypothesis that there is no significant relationship between internal auditing practices and financial performance; therefore to achieve this third objective and to test this null hypothesis, the researcher had to correlate the means on internal auditing practices and means on financial performance by using the Pearson's Linear Correlation Coefficient as indicated in Table 4.4

Table 4.4 relationship between the levels of internal auditing practices and financial performance

Variables correlated	r-value	Sig	Interpretation	Decision on Ho
Internal auditing practices Vs Financial performance	.609	.000	Significant correlation	Rejected
Correlated Vs analysis				

**** Correlation is significant at the 0.01 level (2-tailed), Source: SPSS output, version 14.0, 2014.**

Pearson's product moment correlation in table 4.4 yielded $r = 0.609$ and the sig value = 0.000 which is less than $\alpha = 0.05$. Hence, the research hypothesis was rejected that there is no significance relationship between the level of internal auditing practices and financial performance.

Findings

Results in table 4.1 indicated a positive and significant relationship between the level of internal auditing practices and financial performance ($r\text{-value} = .609$ and $\text{sig} = .000$), implying that improvement of in the internal auditing practices increases the financial performance among the selected private banks in Mogadishu, Somalia.

4.5 Regression analysis

To establish the effect of internal auditing practices on financial performance in Mogadishu, a multiple regression analysis was conducted to establish the relative effect of internal auditing practices to financial performance in Mogadishu, Somalia.

Table 4.5: Regression between level of internal auditing practices and financial performance

Variables regressed	Adjusted r ²	F-value	Sig.	Interpretation	Decision on Ho
Internal auditing practices Vs Financial performance	.484	36.275	.000	Significant effect	Rejected
Coefficients	Beta	t-value	Sig.		
(Constant)		1.331	.186	Significant effect	Rejected
Control environment	.382	5.266	.000	Significant effect	Rejected
Control activities	.232	3.131	.002	Significant effect	Rejected
Monitoring	.606	7.653	.000	Significant effect	Rejected

From the table 4.5 it is clear that this model has good correlation as the r is significant relationship ($R^2 = .484$). The model is significant ($F = 36.275$, $P\text{-value} = 0.000$). It implies that 48.4% of Internal auditing practices influenced by financial performance

Findings

Regression analysis results in table 4.5 above indicated that internal auditing practices accounted for 48% on the quality of financial performance indicated by adjusted r squared of 0.484 leading to a conclusion that internal auditing practices significantly influences the financial performance among the private banks in Mogadishu Somalia.

The coefficients table further showed that of all the aspects of internal auditing practices; monitoring accounted for the biggest improvement on the level of financial performance ($\beta = 0.606$, $\text{Sig} = 0.002$). Hence the research hypothesis was rejected that there is no significant positive relationship between the level of internal auditing practices and financial performance.

This meant that staff of private banks in Mogadishu believed that internal auditing practices were able to lead to financial performance. Surely, during interviews, staffs expressed a wide belief that the only component of the internal auditing practices that was related on financial performance. Consequently the researcher had a right to believe that the financial performance was lacking liquidity.

CHAPTER FIVE

DISCUSSIONS, CONCLUSIONS AND RECOMMENDATIONS

5.0 Introduction

This chapter has been designed to give a detailed account to the findings emanated from the study results in chapter four. This chapter focused on the subsequent sections that emerged from the research hypotheses as witnessed below:

5.1 Discussion of results on variables of internal auditing practices

This study was set to find out the relationship between internal auditing practices and financial performance in the selected private banks in Mogadishu Somalia. It was guided by three specific objectives, that included determining i) the level of internal auditing practices ; ii) determining financial performance in the selected private banks in Mogadishu Somalia; iii) the relationship between internal auditing practices and financial performance in the selected private banks in Mogadishu Somalia.

The study findings indicated that majority of respondents of these workers in the selected private banks of Mogadishu Somalia were aged (36.0%) ranging between 20-25 years of age, (65.8%) of the respondents were males, (65.8%) of the respondents were married persons, (44.7%) of the respondents were having bachelor holders and worked as treasury (24.6%), (28.9%) of the respondents were professional experience between 1-2 years.

Data analysis using means denoted that the level of internal auditing practices was generally rated very high level and this is indicated by the overall mean (mean=4.3), implying that that the workers in the selected private banks in Mogadishu, Somalia have enough knowledge for auditing practices.

Control environment- four items were used to measure this construct and all the items were rated very high, therefore on average control activity was rated very high and this was indicated by the average mean (mean=4.74), implying that control environment is frequently practiced private banks in Mogadishu Somalia as stated According to Cascarino and Van Esch. (2005).

control environment is the tone set by top management and the overall attitude, awareness and actions of the board of directors, Management, owners, and others concerning the importance of internal control and the emphasis placed on control in the company's policies, procedures, methods, and organizational structure.

Control activities- this variable was measured by three items and respondents were asked whether they agreed or disagreed with the statements under investigation. Responses reveal that control activities as a construct on the independent variable was rated high (mean= 3.91), this implying that having control activities always helps the employers in predicting future performance of their private banks, according to the Statement on Auditing Standards (Maniak, 1990). Control activities are the policies and procedures that help ensure that management's directives are carried out.

Monitoring- Three items were used to measure this variable so the respondents were asked whether they agreed with the statements there in, their responses indicated that monitoring any operation as a construct on the independent variable was rated very high level with overall mean (mean=4.4), this implying that banks in Mogadishu have the ability to monitor and review the internal controls. This also is argued by Chioccola & Muhlstein, (2005) that organizational structure should include an independent monitoring function over derivatives, providing senior management with an understanding of the risks of derivative activities, validating results, and assessing compliance with established policies.

Findings

The findings indicated that The level of internal auditing practices is generally rated very high level and this is indicated by the overall mean (overall mean=4.3), this implies that the workers in the selected private banks in Mogadishu Somalia have the required internal auditing practices , internal auditing practices was broken into five constructs and these included the following; control environment, control activities, monitoring, reliability of financial report and compliance with laws and regulations.

5.2 Discussion of results on variables of financial performance

Reliability of financial report- three items were used to measure this variable so the respondents were asked whether they agreed or disagreed with the statements, their responses were rated very high level with the overall mean (mean=4.81), this implying that financial report of the banks in Mogadishu prepared and presented well and financial information is always printed to the financial institutions. Relevance and reliability (now referred to as "representational faithfulness") are important qualities of financial reporting that both the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) use in setting standards (FASB 2010;

Compliance with laws and regulations, three items were used to measure the construct so the respondents were asked whether they agreed with statements, the responses of these items were rated medium with overall mean (mean=3.15), this implying that the respondents were silent to answer this construct means that they don't have more information about how these private banks comply with their rules and regulations. This also stated by (Bushman, 2007) "Compliance with laws and regulations deals with those laws and regulations which the organization is subject to. First and foremost, the organization must be aware of all laws and regulations to which it is subject such as generally accepted accounting principles (GAAP), EU rules and regulations, corporate governance rules, and other specific ones".

Profitability- The first variable was operationalized by using three items and the respondents were asked if they agreed with the statements under investigation, their responses revealed that on average profitability was rated very high level with overall mean (mean= 4.55), implying that the financial performance reported by the selected private banks in this sample is simply identified the components of revenue and expenses by the owners, this is stated by Lesonsky, (2000), there are two profit margin ratios; operating profit margin and net profit margin. A company with a higher profit margin than its competitor is more efficient. (Gleim, 2004).

Credit risk- as second variable was used three items to measure this construct and respondents were asked whether they agreed with the statements. Responses indicated that credit risk was rated very high level on average (mean =4.36), implying that majority of private banks in

Mogadishu, Somalia highly recognized credit risk items while reporting the financial information to the users. this variable was noted by Ranson, (2005) asserts that credit risk relates to the possible loss in asset value due to the default of counterparty banks, issuers of securities or other counterparties, as an example, According to HFCU Risk Management Policy (2002) and Bank Uganda stated that “credit risk refers to loans whose principal and interest is due and unpaid for 90 days or more; or interest payments equal to 90 days interest or more have been capitalized”.

Liquidity- the third variable was used three items to measure this construct and results indicate that on average liquidity of financial performance was rated high level and this was indicated by the average mean (mean=4.15), implying that the private banks in Mogadishu plans and adjusts inflows and outflows of liquid assets so as to prevent maturity mismatch. According to Matz, (2005) liquidity risk is the current and prospective risk to earnings or capital arising from a bank's inability to meet its obligations when they come due without incurring unacceptable losses.

Efficiency and effectiveness of operations-Three items were used to measure this construct so that the respondents were asked whether they agreed with the statements there in, their responses indicated that efficiency and effectiveness of operations was rated medium level with overall mean (mean=3.22), implying that the employees of the private the banks in Mogadishu, they don't have enough information about the efficiency and effectiveness of operations therefore, they said “medium”.. Effective refers to the accomplishment of objectives or to the extent to which the outcomes of an activity match the objective or the intended effects of that activity. “Performance and profitability goals as well as safeguarding of resources are the major objectives to be attained by effective and efficient operations. This implies that operations are performed so as to attain their intended effect (COSO, 1992). Such objectives can be accessed through biannual or quarterly performance audits.

Findings

The findings of the study indicated that the level of financial performance of these private banks in Mogadishu were generally rated high level and this was indicated by the grand mean the (mean=4.02), implying that the selected private banks in this sample always produce high quality

of financial performance to the users such as stake holders and government, still financial performance was broken into four variables which included the following; profitability, credit risk, liquidity and efficiency and effectiveness of operations.

5.3 Discussion of results on the hypothesis

The findings also indicated a positive and significant relationship between the level of internal auditing practices and financial performance ($r\text{-value}=0.609$ and $\text{sig}=.000$), meaning that improvement in internal auditing practices increases the financial performance among the selected private banks in Mogadishu, Somalia.

5.4 Conclusion

From the findings of the study, the researcher concluded that majority of the respondents in this sample (65.8%) were males ranging between 20-25 years of age (36.0%), these were bachelor holders (44.7%) and married persons were (57.9%) worked as a treasury (24.6%), (28.9%) were experienced between 1-2 years.

The findings indicated that The level of internal auditing practices is generally rated very high level and this is indicated by the overall mean (overall mean=4.3), this implies that the workers in the selected private banks in Mogadishu Somalia have the required internal auditing practices , internal auditing practices was broken into five constructs and these included the following; control environment, control activities, monitoring, reliability of financial report and compliance with laws and regulations.

The financial performance of the private banks in Mogadishu was generally rated high level and this was indicated by the grand mean (mean=4.02), implying that the selected commercial banks in this sample always produce high quality of financial performance to the users such as stake holders and government, still financial performance was broken into four variables which included the following; profitability, credit risk, liquidity and efficiency and effectiveness of operations.

There is a positive and significant relationship between the level of internal auditing practices and financial performance ($r\text{-value}=.609$ and $\text{sig}=.000$), meaning that improvement in the internal auditing practices increases the financial performance among the selected private banks in Mogadishu, Somalia.

5.5 Recommendation

1. The researcher recommends to the private banks of Mogadishu, Somalia to always carry out controlling the environment that they are operating and this will help them improve on their control environment.
2. The researcher recommends also to private banks of Mogadishu Somalia to always categorize as authorization; segregation of duties, record keeping, safeguarding and reconciliations and these controls depend greatly on the activity under consideration
3. The researcher recommends to private banks of Mogadishu Somalia always to monitor any operation being held in the organization. This will help managers to flow up the transactions happens in the organization.
4. The researcher recommends to private banks of Mogadishu Somalia always to adequately plans and adjusts inflows and outflows of liquid assets so as to prevent maturity mismatch.
5. The researcher recommends to private banks of Mogadishu Somalia always to Compare the current profits with the profits made in the previous years to asses profitability trends.

5.6 Areas for further research

Prospective researchers and even students are encouraged to research on the following areas;

1. Internal auditing practices and financial performance in private banks in Mogadishu Somalia.
2. Control environment, control activities, profitability and credit risk among private banks in Mogadishu, Somalia.
3. Financial performance reported daily by private banks in Mogadishu, Somalia.

5.7 Limitation of the Study

In view of the following threats to validity, the researcher allowed 0.05 level of significance. Measures are also indicated in order to minimize if not to eradicate the threats to the validity of the findings of this study.

1. Extraneous variables which beyond the researcher's control such as respondents' honesty, personal biases and uncontrolled settings of the study.
2. Testing: The use of research assistants can be about inconsistency in the administration of the questionnaire in terms of tie of administration, understanding of the items of in the questionnaire and explanations given to the respondents. To minimize this threat, the research assistants will be oriented and briefed on the procedures to be done in the data collection.
3. Attrition/ Morality: Not all questionnaires may be turned completely answered nor even retrieved back due to circumstances on the part of the respondents such as travels sickness, hospitalization and refusal/withdrawal to participate.

In anticipation to this, he the researcher reserved more respondents by exceeding the minimum sample size. The respondents also reminded not to leave any item in the questionnaires unanswered and will be closely followed up as to the date of retrieval.

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APPENDIXES A

QUESTIONNAIRE FOR INTERNAL AUDITING PRACTICES AND ITS EFFECT ON FINANCIAL PERFORMANCE IN SALAM SOMALI BANK AND DAHABSHIL BANK

4.0 Introduction

Dear respondent,

This research questionnaire has been prepared by the researcher to gather information regarding internal auditing practices in Salam Somali Bank and Dahabshil Bank and its effects on the financial performance. The study is for purely academic purposes. You are hereby assured that your identity and the information you provide will be kept confidential.

4.1 Demographic Information of the respondents

Instructions: Please tick against the category that best describes you.

1. Age

Age	Code	
20-25	1	
26-35	2	
36 -45	3	
Above 46 years	4	

2. Gender

Gender	Code	
Male	1	
Female	2	

3. Martial Status

Martial Status	Code	
Single	1	
Married	2	

4. Highest Qualification

Qualification	Code	
Secondary School	1	
Diploma	2	
Bachelor	3	
Postgraduate	4	

5. What position do you hold in the organization?

Position	Code	
Member of Board of Directors	1	
Senior management	2	
Internal auditor	3	
Accountant	4	
Treasury	5	
Cashier	6	

6. How many years have you worked in this organization?

No of Years	Code	
Below one year	1	
1 - 2 years	2	
3 – 4 years	3	
5+years	4	

APPENDIX B

INDIPENDENT VARIABLE, INTERNAL AUDITING PRACTICES

This questionnaire is designed with a view to gaining insight into your perception as to what forms of internal auditing practices would contribute the effectiveness of financial performance to your banks. There are no right and wrong answers and your anonymity is ensured.

Please indicate the extent to which you strongly Agree - SA, Agree – A, Disagree – D, or Strongly Disagree – SD to the following statements by way of ticking appropriate.

4.26----5 strongly agree ———>very high ———>you agree with no doubt
 3.5-----4.25- Agree ———> high ———> you agree with some doubt
 2.76----3.5 –Neutral ———> medium ———>no agree, no disagree
 1.76-----2.75 Disagree ———> low ———> you disagree with some doubt
 1----1.75 strongly disagree —>Very low ———>you disagree with no doubt

No.	Internal auditing practices	Scale				
	Control environment					
1	Internal audit is a adequate staffed	1	2	3	4	5
2	internal audit operates with a formal charter approved by the board of this bank	1	2	3	4	5
3	The internal audit staff possesses the skill and knowledge to undertake the work program	1	2	3	4	5
4	Internal auditing practicesin this bank is independent	1	2	3	4	5
	Control activities					
1	Internal audit identifies and profiles its stakeholders and audits clients, their needs and expectations	1	2	3	4	5
2	Refocusing internal audit function and extracting more value from it are imperative if the business into build comparative advantage.	1	2	3	4	5

3	Internal audit has moved away from being reactive to being proactive and risk focused	1	2	3	4	5
	Monitoring					
1	Any operation being held in this bank is audited daily by the auditors	1	2	3	4	5
2	Internal audit has a comprehensive internal monitoring program	1	2	3	4	5
3	The organization have assessed the need for the use of internal capability for monitoring and review of internal controls	1	2	3	4	5

APPENDIX C

QUESTIONNAIRE DETERMINES FINANCIAL PERFORMANCE

This questionnaire is designed with a view to gaining insight into your perception as to what forms of internal auditing practices would contribute the effectiveness of financial performance to your banks. There are no right and wrong answers and your anonymity is ensured.

Please write your answer to the statements below. Kindly use the rating guided as follows:

- 4.26----5 strongly agree → very high → you agree with no doubt
 3.5-----4.25- Agree → high → you agree with some doubt
 2.76----3.5 –Neutral → medium → no agree, no disagree
 1.76-----2.75 Disagree → low → you disagree with some doubt
 1----1.75 strongly disagree → Very low → you disagree with no doubt

No.	Internal auditing practices	Scale				
	Reliability of Financial Report					
1	1. The bank records daily transactions with their source documents	1	2	3	4	5
2	2. Financial reports published as soon as possible after the end of the reporting period to inform decision making	1	2	3	4	5
3	3. The financial report of this bank is presenting accurate description of the financial facts and events during the past period.	1	2	3	4	5
	Compliance with laws and regulations					
1	The bank's rules and regulations are understandable and provisions in detail	1	2	3	4	5
2	The bank is taking steps to comply with relevant laws and regulations	1	2	3	4	5
3	The bank practices the law and regulations in regular contexts	1	2	3	4	5
1	Profitability					

2	The management establishes the minimum return required to meet the company's return	1	2	3	4	5
3	Comparisons are made of the current profits with the profits made in the previous years to assess profitability trends	1	2	3	4	5
	Your bank determines the profitability of each product by identifying the components of revenue and expenses for each product	1	2	3	4	5
	Credit risk					
1	The bank has appropriate policy and procedures for the collection of its loans in default	1	2	3	4	5
2	The bank has in place appropriate internal procedures for the identification and measurement of credit risk	1	2	3	4	5
3	The bank assesses the borrower's capacity to meet the obligations and the quality of collateral pledged for the claim	1	2	3	4	5
	Liquidity					
1	The bank maintains adequate liquidity ratios for its assets	1	2	3	4	5
2	There is existing appropriate internal procedure for the calculation and measurement of liquidity risk	1	2	3	4	5
3	The bank adequately plans and adjusts inflows and outflows of liquid assets so as to prevent maturity mismatch	1	2	3	4	5
	Efficiency and effectiveness of operations					
1	The bank uses its assets and resources properly	1	2	3	4	5
2	The bank performs reviews on their operations	1	2	3	4	5
3	Organization's resource are safeguarding in safe places	1	2	3	4	5

APPENDIX D

INTERVIEWS DETERMINE INTERNAL AUDITING PRACTICES ON FINANCIAL PERFORMANCE IN SALAM SOMALI BANK AND DAHABSHIL BANK

1. In your own understanding, what is the importance of control environment in your organization?
.....
.....
.....
.....
2. Does the internal audit staff possess the skill and knowledge to undertake the work program in your bank? If yes or no why?
.....
.....
.....
3. What do you think are the advantage of control activities in your bank?
.....
.....
.....
4. What do you think should be the basis of monitoring in your bank? Why?
.....
.....
.....
5. How can financial report reliable in your bank?
.....
.....
.....
.....
6. In your understanding, how do you comply with the lows and regulations in your bank?
Is it important factor to comply with the lows and regulations in any organization? Why?

.....
.....
.....

7. What are the factors that make your financial profitable?

.....
.....
.....

8. What do you think are the limitations to success of the credit risk?

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.....
.....

9. What do you consider the successes of liquidity in your bank?

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.....

10. How can your operations of your bank can be efficiency and effectiveness at any stage you are doing?

.....
.....
.....

Thank you very much

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