American International Journal of Business Management (AIJBM)
ISSN- 2379-106X, *www.aijbm.com Volume 5, Issue 10 (October-2022), PP 61-71*

Internal Audit and Financial Accountability in County Governments of Western Kenya: applications of internal audit independence

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Abstract: *Internal audit is a critical aspect in all organizations as it helps in the efficient and effective management of public resources. Auditor general report have established that many county governments are still facing challenges of resource allocation and misappropriation of funds.This has increased the need for internal audit in all county governments. The main objective of this study was to evaluate the influence of internal audit on financial. The specific objective was to evaluate the influence of internal audit independence on financial accountability in county governments in western Kenya. The study was guided by accountability theory and the assumption that county governments in Kenya incorporated internal audit. The target population of the study was 194 respondents drawn fromcabinet executive committee members for finance, director internal audit services, principal auditors,audit assistants and accountantsinfour county governments in western Kenya. Correlational research design was used. Proportionate stratified random sampling was used to select respondents. Primary data was collected through the use of questionnaires and secondary data through analysis of auditor general reports. A pilot study was done in Kisumu County government. Cronbach's Alpha was used to test reliability. Validity was tested by experts and factor analysis. Data was analyzed using SPSS version 27. Both descriptive and inferential statistics was obtained. The results from the regression analysis depicted that internal audit had a negative and significant influence on financial accountability by reducing unsupported expenditure. The study therefore concluded that improvement on internal audit improves financial accountability by reducing unsupported expenditure. The study recommended that management of county governments should not interfere with the duties of internal auditors.*

Keywords:Internal Audit: Financial Accountability: County Governments

I. Introduction:

Internal audit is the critical aspect of promoting financial accountability in organizations, whether public or private. Audits with organizations help in the minimization of wastage or misuse of resources. This is because management of the resources require high accountability within the organization, otherwise if not, there will be extreme embezzlement of resources by the people provided with the obligation to handle public funds on behalf of the citizens (Grubor, 2020).

Internal audit checks on county government function of managing public money in an effective and transparent way. Internal audit implementation has been a challenge due to weak internal controls. Due to this challenge, an internal audit arose to give an objective assurance that is purposed to add value to and improve an organization's operations and ensure all transactions are appropriately authorized, executed and recorded (Trotman & Andrew, 2018). Despite the existence of this internal audit, county governments are still facing challenges on misallocation of resources and misappropriation of funds. Busia county government was found with the un-vouched expenditure of goods and services figure of Kshs.242.5 million with no supporting documents (The Auditor General Report, 2019). Due to this situation, employee's payments in many county governments areusually delayed. Some employees have been retrenched, some county government projects have stalled and others have delayed to be completed and this has led to the need to evaluate the influence of internal audit on the financial accountability of county Governments in western Kenya.

II. Objectives of the study

General Objective

The main objective of this study was to evaluate the influence of internal audit on financial accountability in county governments in western Kenya.

Specific Objective

The specific objective of the study was to evaluate the influence of internal audit independence on financial accountability in county governments in western Kenya.

Conceptual Framework

Independent Variable **Dependent Variable**

Internal Audit

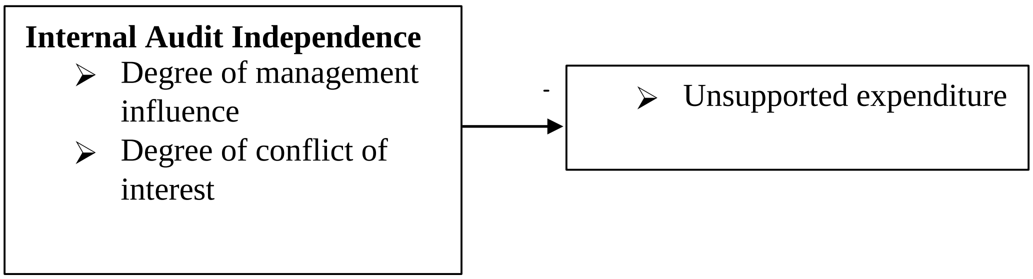

Figure 1: Conceptual Framework

III. Theoretical Review

The Agency Theory.

The agency theory was first proposed by(Ross & Mitnick, 1973). They stated the theory as a principle used to explain and resolve issues in the relationship between business principals and their agents. According to them, audit services are used in the interests of both third parties and management. There is an agency connection between the agent and the principals, in which the agent is given decision-making authority.

The agency theory describes how one party defines the tasks which the second party is supposed to undertake. This second party (agent) is supposed to achieve a commission on behalf of the first party known as the principal. The theory focuses on the cost and advantages of an agent-principal relationship. It also advocates that to limit the risk of a moral threat, principals and agents contract to maximize benefits, which involves establishing monitoring functions like auditing. The philosophy recommends that a firm's fundamental aim is to make the superlative use of the stockholders' funds (Jensen & Meckling, 1976).

Both the principal and the agent, according to the theory, strive to maximize utility. They all have interests and the principal usually wants the agent to operate in his best interests. However, the agent's best interests may not always be the same as that of the principal's, for example, auditors are expected to monitor the performance of management on behalf of the stakeholders. Auditors sometimes fail to work as per the interest of the stakeholders as they collude with the management in the performance of their tasks. The most challenging aspect of this principal-agent relationship is adverse selection, which occurs when the principal does not have access to all available information at the moment of decision-making (Adams & Michael, 2011).

Different risk preferences, information asymmetry, moral hazard, conflicts of interest, and agency costs result from the separation of ownership and control. The idea suggests a number of solutions, including strong management ownership, independent board members, and a number of committees, all of which can reduce agency conflict and expenses. (Brahmadev & Leepsa, 2017). Agency theory focuses on the nature of the principal-agent relationship, the rights and responsibilities of the parties involved, agency problems and their mitigation through regulations, various corporate governance practices and observations aimed at controlling the decisions and actions of the agents in the modern firm. The dilemma of conflicting interests among the parties in a relationship or contract is at the heart of the agency theory (Nwaubani, 2019).

This theory was relevant to the study since the agency problem relates to county government who incur agency cost by employing internal auditors to minimize the conflict between executors of county government services and county government stakeholders that may lead tomisappropriation of funds. However, the internal auditors may have conflict of interest and may collude with management and fail to reveal true and fair view of the county governments.

Literature review

Nyaga, Ndungu and Kamau (2018) carried a research on the influence of internal audit independence on effectiveness in Kirinyaga county government. A descriptive research design was used. The target population consisted of forty-six (46) staff members from the directorate of internal audit. Closed ended questionnaires were administered in primary data collection.Descriptive and regression analysis was used to analyze data and was done with the help of SPSS. The study revealed that internal audit independence had a positive and significant effect on the effectiveness of county government.

Jachi, Moses and Lucky (2019) examined the impact of internal audit independence on the transparency and accountability of Zimbabwe local authorities. The study targeted eight audit Practitioners (Chief Audit Executives and Audit Staff) and thirteen senior managements. Survey data was collected. Semi-structured questionnaires were used to collect primary data. Secondary data was also collected from various documentary sources with a guide of review checklist. The hypothesis was tested using correlation and regression analysis. The study findings revealed that an independent internal audit function is positively associated with transparency and accountability.

Thuranira, Waweru and Walubuka (2020) studied the effect of internal audit independence on the corporate governance of county governments in Kenya. The study applied descriptive and inferential designs. Census method was employed where all technical staff members of internal audit and accounting departments were used. The study adopted regression analysis. The study showed a positive and significant relationship between internal audit independence and the financial performance of county governments.

Summary of Literature Review

Most of the studies relating to internal audit aspect were reviewed. Most of them were on internal audit and financial performance and others on internal audit and financial sustainability. There was no study on how general internal audit relate with financial accountability especial on unsupported expenditure.

IV. Research methodology

Research design

The study adopted correlational research design. This design was appropriate in establishing the relationship that existed between internal audit and financial accountability of county government. The research design is also relevant as it assisted in obtaining true and accurate information on independent and dependent variable as they are (Kothari, 2014).

Target Population

The study targeted 194 respondents consisting of 67 cabinets' executive committee members for finance, 4 director internal audit services, 4 principal auditors**,** 36audit assistantsand 83 accountantsfrom the four-county governments in Western Kenya (Kakamega, Vihiga, Bungoma and Busia) as shown in table 1

Table 1: Target Population

Category	Number	Percentage
Cabinet executive committee members for finance	67	35
Director of internal audit services	4	2
Principal auditor	4	2
Audit assistants	36	19
Accountants	83	42
Total	**194**	**100**

Source:Human Resource Registry of all County Government (2022)

Sample and Sampling Technique

Sample

This study used fishers' equation as adopted by (Jung, 2014). The equationis most appropriate in determining the sample size where the targeted population is less than one thousand units.

The sample was calculated as follows;

The formula is given by $n_o = \frac{Z^2 P(1-P)}{I^2}$

Where;

n - Desired sample size

Z – The normal standard deviation at the confidence level of 95% equivalent to 1.96

P - Proportion of the population with the desired characteristics

This study will assume 50:50, a probability of 0.5

I^2 - Degree of precision which is 5%

Since the proportion of the population with the characteristics is not known, 50% will be used

Therefore, $n_o = \frac{1.96^2 * 0.5(1-0.5)}{(0.05)^2}$

$n_0 = 384$

However, since the target population was less than 1000, the sample size adjustment was done using the formula

$$n = \frac{no}{1 + \frac{(no-1)}{N}}$$

$$n = \frac{384}{1 + \frac{(384-1)}{194}}$$

$$n = \frac{384}{1+2.9237}$$

n=129

This sample size is 66% of the total population. Collins and Hussey (2014) argues that if well chosen, samples of above 10% of a population give good and reliable findings.

Sampling technique

Proportionate stratified random sampling was employed by the study to obtain sub-samples for each category of respondents.

Table 2: proportionate Distribution of Sample Size

Category	Total	Percentage
Cabinet executive committee members of the finance	43	33
Director of internal audit services	4	3
Principal auditor	4	3
Audit assistants	23	18
Accountants	55	43
Total	**129**	**100**

The members of the sub strata were randomly selected until saturation

Data Collection

The study used both primary and secondary data. Primary data was collected through use of questionnaires that were distributed by the research assistants to the respondents face to face in all the four selected county governments. A period of two weeks was allowed for the respondents to fill up the questionnaires. After the allowed period the research assistants collected back the questionnaires. Secondary data was collected by analyzing auditor general report on county governments for the period of 2020/2021. All the amount relating to expenditures that lacked supporting documents were identified and recorded.

Pilot Test

A pilot test was done in Kisumu county Government in the western region selected randomly. The scope was ideal since the county government of Kisumu was located in the same region as counties in western Kenya, thus exhibiting the same characteristics. Questionnaires were given to nine cabinet executive committee members for finance, one director internal audit services, one principal auditors**,** five audit assistants and eleven accountants. This gave a total of 27 respondents out of 129 sampled respondents. This amounted to 20.9% which is considered satisfactory since an aggregate of above 10% of the expected sample size is considered satisfactory (Cooper & Schndler, 2011). Reliability and validity of the research instrument was tested.

Reliability refers to the degree to which a research instrument yields consistent results or data after repeated trials and is the accurate representation of the total population under study. Reliability was measured using Cronbach's alpha, where its values range from 0 to 1. Values between 0.7 and 1.00 indicate a considerable reliability hence acceptable and values below 0.70 are considered less reliable thus not acceptable (Fraenkel & Wallen, 2000). All the study constructs had reliability measures above 0.7 indicating the research instruments were reliable. Table 3 shows the

Cronbach's Alpha of the various study constructs.

Table 3: Cronbach's Alpha Reliability

Construct	Number of Items	Cronbach alpha	Conclusion
Internal audit independence	11	0.877	Reliable

Validity is the judgement on how well a test measure purports to measure what is intended to measure (Kothari 2014). Validity was tested through an expert analysis and factor analysis. Experts including supervisors and other specialist in accounting were given questionnaire. They identified all the irrelevant, offensive, ambiguous and awkward questions restructured it appropriately.

Factor analysis tested validity by assessing the construct validity of the questionnaire so as to give an assertion that features being verified by a tool of data collection adequately and properly cover what is intended. Dimension reduction of observed variables was used to test validity. KMO and Bartlett's tests were carried in this study in order to explore the adequacy of data sampling and in determining its suitability for factor analysis.

The KMO statistics for all the variables were found to be above 0.5 implying the suitability of data for factor analysis. According to (Tabachnick & Fidell, 2007) considered a KMO value of above 0.5 to be suitable for factor analysis. The adequacy of the sampling was determined by Bartlett's tests that were based on the significance of the chi-square statistics. According to this pilot study, all Bartlett's statistics have p-values of 0.000 which are all less than 0.05 implying that the item correlation matrix is not an identity matrix thus the pilot study data is adequate and suitable for the factor analysis models carried out. Table 4 shows the KMO and Bartlett's tests which are measures of validity.

Table 4: KMO and Bartlett's Tests

	Items retained	AVE	KMO	Bartlett's test		
				χ^2	df	p-value
Internal audit independence	11	0.536	0.768	457.178	45	0.000

The data collected was cleaned, sorted, coded and run through the statistical package for social sciences (SPSS) version 27. Diagnostic tests used by the study included normality test measured using Shapiro Wilk, autocorrelation test using Durbin Watson, multicollinearity test using variance inflation factor and heteroscedasticity test using Breusch Pagan test. Both descriptive and inferential statistics was generated. Data was presented using tables and graphs. The following regression model was used to establish the strength of the relationship between internal audit and Financial Accountability.

$\hat{Y}=ß_0+ß_1IAI+\varepsilon$………………….3.1

Where:

Y-Financial Accountability

$ß_0$- Constant

$ß_1$ - Regression Coefficients

IAI-Internal Audit Independence

ε -The error term

Response Rate

The study targeted 194 respondents in four county governments in western Kenya. Only 129 respondents were selected and given questionnaires. Questionnaires from 110 respondents were received while the rest did not return their questionnaires representing 85.27% of the respondents that were targeted. This was deemed adequate for the study based on the suggestions given by (Edward & Roberts, 2002) who considered a response rate of below 60% to be poor and above 60% to be adequate.

Table 5: Response Rate

Targeted respondents	returned questionnaires	Response Rate
129	110	85.3%

Demographic information Number of Years Served in the County Government
Majority of the respondents at 57.3% had served at the county government for a period of more than three years as shown in table 6. This implied that majority of the employees had adequate knowledge and experience on county government meaning that the responses obtained from them were very objective and reliable.

Table 6: Number of Years Served in the County Government

	Frequency	Percent	Cumulative percent
Above 6 years	22	20.0	20.0
3-5 years	41	37.3	57.3
1-2 years	27	24.5	81.8
Below one year	20	18.2	100.0
Total	110	100.0	

Professional qualification in relation to accounting knowledge
A large number of the respondents at 81.0% had qualification in ATD and CPA as shown in table 7. This means that most of the employees in county government are competent as they have the required qualification to carry their respective duties effectively. In few county governments employees had no professional qualification hence were not competent enough to detect cases of corruption at the county government hence lowering the level of financial accountability.

Table 7: Professional Qualification in Relation to Accounting Knowledge

	Frequency	Percent	Cumulative percent
Others (specify)	8	7.3	7.3
Certificate in accounting and management skills (CAMS)	13	11.8	19.1
Accounting Technical Diploma(ATD)	39	35.5	54.5
Certified Public Accountants (CPA) Total	50	45.5	100.0
	110	100.0	

Descriptive statistics
The study sought to determine the influence of internal audit independence on financial accountability in county governments of western Kenya. The results were in table 8 show that management of most county governments interfere with duties of internal auditors with a mean of 3.05, the independence of internal auditors positively influences financial accountability with a mean of 3.77, Internal auditors had conflict of interests while carrying out their duties with a mean of 3.12, Conflict of interest by internal audit staff affects financial accountability with a mean of 3.55, Interference by top management on internal audit activities negatively impacts on financial accountability with a mean of 3.75, Internal auditors have family ties with top management with a mean of 3.07, Internal auditors have no integrity required to carry out their duties with a mean of 3.05, The integrity of internal audit staffs positively affects financial accountability with a mean of 3.75, Internal audit staff do not carry out their duties objectively without threat from management with a mean of 3.35 and threats from management to internal audit staff negatively affects financial accountability with a mean of 3.62.

Table 8: Internal Audit Independence and Financial Accountability

Statements	Minimum Statistic	Maximum Statistic	Mean Statistic	Std. Error	Std. Deviation Statistic
Management of county government does not interfere with duties of internal audit.	1	5	3.05	.124	1.302
The independence of internal auditors positively influences financial accountability.	1	5	3.77	.113	1.186
Internal auditors do not have a conflict of interest while carrying out their duties.	1	5	3.12	.133	1.393
Conflict of interest by internal audit staff affects financial accountability.	1	5	3.55	.102	1.072
Interference by top management on internal audit activities negatively impacts financial accountability.	1	5	3.75	.115	1.211
Internal auditors have no family ties with top management.	1	5	3.07	.126	1.325
Internal auditors have the integrity required to carry out their duties.	1	5	3.05	.136	1.430
The integrity of internal audit staff positively affects financial accountability.	1	5	3.75	.121	1.272
Internal audit staff carries out their duties objectively without threat from management.	1	5	3.35	.129	1.358
Threats from management to internal audit staff negatively affect financial accountability.	1	5	3.62	.120	1.256

Inferential Statistics

The main objective of the study was to evaluate the influence of internal audit on financial accountability in county governments in western Kenya. Data was analyzed with the help of multiple binary regression to assess for the relationship between the independent variable and dependent variable. It also helped in testing the hypothesis of the study and in determining whether internal audit independence had a significant influence on financial accountability in county governments of western Kenya.

Correlation Analysis

Pearson product moment correlation was used to assess the strength and direction of the relationship between internal audit competence and financial accountability in county governments of western Kenya. The values from the correlation coefficient ranges from -1 to +1.

The closer the values to -1 and +1 the closer the relationship between two variable and vice versa. A value of +1 indicates perfect positive relationship, a value of -1 indicates perfect negative relationship and a value of 0 indicates no relationship. The correlation coefficient was tested at 95% confidence level based on 2 tail test. Therefore, the rejection criteria were based on a p value of 0.05 where values above it was deemed as insignificant while values below it is significant.

The correlation coefficient of internal audit independence was -0.721 implying that there is a significant strong negative association with financial accountability since the p values of 0.017 was less than 0.05.

Table 9: Correlation Matrix

	IAI

Y0	-0.721* 0.017

a. Predictors: (Constant), IAI
b. Dependent Variable: Financial Accountability

Model Summary[b]

The model summary helps in reporting the strength of the relationship within the model variables and the dependent variable as shown in table 10. R is a multiple correlation coefficient that depicts the linear correlation between observed model predicted values of the dependent variable. R value of 0.625 suggests a strong direct correlation between independent and dependent variables. R square depicts the coefficient of determination which indicates the variability in the independent and dependent variables. The R square value of 0.426 shows that 42.6% variation in financial accountability are caused by the internal audit independence. The remaining 57.4% of the variations in financial accountability are caused by other factors not found in the model. R square adjusted indicates that the percentage estimate of this explainable dispersion for the total population under the investigation is 41.8%.

Table 10: Model Summary[b]

Model	R	R Square	Adjusted Square	R Std. Error of the Estimate
1	.625[a]	.426	.418	.413

a. Predictors: (Constant), IAI.
b. Dependent Variable: Financial Accountability

ANOVA[a]

The ANOVA table 11 depicts the relationship between internal audit components and financial accountability of county governments in western Kenya. The overall model indicates that internal audit has a significant influence on financial accountability at 95% confidence interval with a p value 0.001<0.05. This significance can also be supplemented with derived f statistics value of 2.83 which is greater than a critical f value of 2.46.

Table 11: ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	1.339	4	0.3348	2.83	.001[b]
	Residual	12.431	105	0.1184		
	Total	13.77	109			

a. Predictors: (Constant), IAI
b. Dependent Variable: Financial Accountability

V. Regression Coefficients Analysis

Table 12 shows the regression coefficient of the independent variables which aids in explaining how each influences the dependent variable. Therefore, on the basis of the results in table 12, the constant value of 9.154 is significant at 95% confidence interval indicated with a p-value of 0.011<0.05. The constant value depicted that when county government have not adopted internal audit, the average financial accountability which is measured by the amount of unsupported expenditure in the selected county governments of Western Kenya is approximately Sh. 1.425 billion per year (Antilog of 9.154). Internal audit independence (IAI) had a coefficient of -0.214.

Table 12: Regression Coefficients

Model	Unstandardized Coefficients		T	Sig.
	B	Std. Error		
(Constant)	9.154	2.32	3.944	.011
IAI	-.214	-.068	-3.163	.018

a. Predictors: (Constant), IAC
b. Dependent Variable: Financial Accountability

The results from the regression coefficient analysis was used to establish the following regression model.

$$\log\hat{Y} = 9.154 - 0.214\,\mathrm{IAI} \quad \text{…………………} \quad (4.1)$$

From the results of regression analysis in table 12, internal audit independence had a regression coefficient of -0.214 with a p value of 0.018. The p value was less than 0.05 implying that internal audit independence is statistically significant. The t statistics of -3.163 was less than the t critical value of -1.660 implying also that there is a significant relationship. The null hypothesis that internal audit independence had no significant influence on financial accountability was therefore rejected. This imply that when internal audit independence is adopted by county governments it will aid in reducing the log average of unsupported expenditure thus improving financial accountability in county governments of western Kenya by 0.214 from 9.154 to 8.94 resulting into unsupported expenditure of 0.87 billion (Antilog of 8.94).

The results from this study are in agreement with the findings from the descriptive statistics that elaborated that most respondents were in agreement that indicators of internal audit independence like independence of internal auditors, conflict of interest by internal audit staff, interference by top management on internal audit activities, integrity of internal audit staffs, threats from management improves financial accountability in county governments of western Kenya.

The results of the study were also in line with the results from a research done by (Nyanga, Ndungu, & Kamau, 2018), who carried out a study on the influence of internal audit independence on effectiveness in Kirinyaga county government and found that internal audit independence had a significant positive influence on effectiveness of county government. These findings also were similar to a study done by (Jachi, Moses, & Lucky, 2019) who researched on impact of internal audit independence on transparency and accountability of Zimbabwe local authorities and revealed that an independent audit function was positively associated with transparency and accountability.

The results also support the agency theory that explains the relationship between principal and its agent. Once the management of county governments have incurred the agency cost by employing auditors then misuse of public resources will be minimized. Once the management of county governments has also assigned duties to auditors then it should allow them to act without interference in order to give independent reports.

Summary of the Findings

The study was conducted in order to evaluate the influence of internal audit on financial accountability of county governments of western Kenya. The specific objectives were; to evaluate the influence of internal audit independence, internal audit competence, top management support, and compliance with auditing standards on financial accountability in county governments of western Kenya. The study adopted both descriptive and inferential statistics in the analysis.

The first specific objective of the study was to evaluate the influence of internal audit independence on financial accountability of county governments of western Kenya. The objective was based on the null hypothesis that internal audit independence had no influence on financial accountability. From the descriptive statistics it was found that in many county governments management interferes with duties of auditors, internal auditors had conflict of interest and family ties, lacked the required integrity in performing their duties. Correlation analysis show a strong correlation of -0.721 and a p value of 0.017 with financial accountability (unsupported expenditure). Regression analysis indicated a regression coefficient of -0.214 with a p value of 0.018 indicating that a negative significant relationship between internal audit independence and financial accountability through reduction of unsupported expenditure. Therefore, the null hypothesis was rejected implying that when internal audit independence is improved unsupported expenditure would reduce by 0.214.

Conclusions

From the descriptive statistics it was found that majority of the respondents agreed that internal audit independence improves financial accountability in many county governments of western Kenya. From the inferential statistics (regression coefficient=-0.214, p value=0.018) it can be concluded that there is a significant relationship between internal audit independence and financial accountability in county governments of western Kenya. The study established that independence of internal auditors, integrity of internal auditors, non-conflict among auditors helped county governments of western Kenya to improve financial accountability by reducing the amount of unsupported expenditure. It was therefore necessary for county governments of western Kenya to work towards improving internal audit independence through eliminating or minimizing conflict of interest, family ties, management threat in order to ensure financial reports released by auditors reflect the true and fair view of county governments of western Kenya.

Recommendations

From the descriptive statistics, majority of the respondent in many county governments of western Kenya agreed that there is interference of management on auditors' duties, there is conflict of interest among the auditors, internal auditors have family ties with management and internal auditors have no integrity. From the inferential statistics, it was found that internal audit independence had a negative and significant influence on financial accountability through reduction in unsupported expenditure.

The study therefore recommends that the management of county governments should not interfere with the duties of internal auditors and should give auditors freedom to exercise their duties. This will help in improving financial accountability because internal audit will independently perform their functions and be able to reveal all the loopholes that may encourage one to be involved in corruption.

It was also recommended that management should find ways of reducing conflict of interest among the auditors. This can be by eliminating factors that encourage conflict of interest or punishing does involved in conflict of interest. Auditors having conflict of interest perform their duties based on their interest as they will be priotizing their interest at the expense of the organization. Reduction or elimination in the conflict of interest will improve financial accountability and help in reducing the amount of unsupported expenditure in county governments of western Kenya.

It was further recommended that management should encouraged auditors to exercise high integrity when carrying out their duties. This will help them to be effective and efficient in carrying out their duties. Integrity of internal auditors will help them not being engaged in collusion with county government accountants by either cooking books of accounts. This will help in improving financial accountability.

VI. ACKNOWLEDGEMENT

My acknowledgment goes to Kaimosi Friends University College for the scholarship they awarded me to pursue this master's degree. My sincere gratitude goes to my supervisors, Dr. Margaret Atieno and Dr. Denis Ouma for taking their time and attention to guide me throughout the writing of this thesis.

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