EFFECTIVENESS OF AUDIT COMMITTEES IN ACHIEVING INDEPENDENCE OF INTERNAL AUDIT:
A CASE STUDY OF TANZANIA PETROLEUM DEVELOPMENT CORPORATION (TPDC)
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A CASE STUDY OF TANZANIA PETROLEUM DEVELOPMENT CORPORATION (TPDC)

By
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A Dissertation Submitted in Partial Fulfillment for the Requirements for the Award of the Degree of Master of Science in Accounting And Finance (MSc A&F) of Mzumbe University.
CERTIFICATION

The undersigned certifies that he has read and hereby recommends for acceptance by Mzumbe University a dissertation titled: *Effectiveness Of Audit Committee In Achieving The Independence Of Internal Auditors: The Case Study Of Tanzania Petroleum Development Corporation* in partial fulfillment of the requirements for the degree of Masters Of Science In Accounting And Finance

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DECLARATION

I, Mkwe Thomas Vendelin, declare that this dissertation is entirely a result of my own original work except where acknowledged in the text and that it has not been presented and is not currently being presented to any other University for a similar or any other degree.

Signature…………………………
Date……………………………..
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And above all, my vast gratitude to the Almighty GOD who gave the researcher health, strength and a privilege to pursue this degree
DEDICATION

This work is dedicated to my Late Dady Mr. Vendelin Mkwe Mkenda for the efforts and support he gave me to make sure I reach to my goals, my family for their inspiration towards my career achievement and my son Tevin.
I love you so much.
The role of the audit committee and the internal audit function in corporate governance has grown in recent years. In that context, the audit literature and practice has underlined the increasingly important role of support and interaction between the audit committee and the internal audit with the aim to improve the corporate governance quality.

The purpose of this paper is to examine the effectiveness of audit committee in achieving the independence of internal auditor.

Data were collected by means of questionnaires and interviews addressed to chief internal auditor, auditors, TPDC staff and the audit committee also by means of documentary sources.

The results suggest that the expertise and frequency of meetings of the audit committee have a positive impact on audit committee interaction with internal audit, while the size of the audit committee affects negatively this interaction. However, audit committee independence has no effect on audit committee relation with the internal audit function.
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LIST OF ACRONYMS

IA – INTERNAL AUDIT
AC – AUDIT COMMITTEE
CAE – CHIEF AUDIT EXECUTIVE.
CEO – CHIEF EXECUTIVE OFFICER
CFO – CHIEF FINANCE OFFICER
IIA – INSTITUTE OF INTERNAL AUDITORS
NBAA – NATIONAL BOARD OF ACCOUNTANTS AND AUDITORS
TPDC – TANZANIA PETROLEUM DEVELOPMENT CORPORATION.
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CHAPTER ONE
INTRODUCTION

1.1 Introduction
The Chapter one is the introductory part which comprises of background information to the research problem, statement of the problem, research objectives, research questions, significance of the study, scope of the study and limitations of the study.

1.2 Background of the study
In practicing effectively their duties internal auditor has to be independent and has to be seen to be independent. Auditors in TPDC are seen to be independent since they work freely and objectively in their day to day activities. The researcher on examining the audit committee working system in TPDC and internal auditor reporting structure he realized that there may be a chance that audit committee knowingly or unknowingly is not working effectively in achieving that independence to internal auditors, and internal auditors though they are seen to be independent but there is chance that they are not achieving their independence effectively due to the loop holes seen on reporting structure and the management influence.

To assist in assessing Internal Audit’s independence in TPDC, audit committees consider engaging an experienced external party to perform a strategic assessment of Internal Audit. A strategic assessment primarily focuses on optimizing Internal Audit to bring the most value to the company and the audit committee. It also help the audit committee answer tough questions about Internal Audit’s performance and practices a thing that seen by the researcher to be questioning the internal auditors independence when is not practiced in effective way.

It is therefore important for the audit committee to distinguish between the role of management and that of internal audit department so as to work effectively.
Management has primary day-to-day responsibility for managing risk and for the operation of internal controls within an organization. Internal audit’s role is separate and independent from management. The internal audit function is generally considered independent when it can carry out its work freely and objectively.

Tanzania Petroleum Development Company is a large parastatal company in Tanzania deals with exploration of gas and oil in Tanzania. It has the organization structure that include the internal audit department which report to the Board of Directors via audit committee.
The audit committee in TPDC assess whether the internal auditors are monitoring critical controls, identifying and addressing emerging risks. The specific expectations for internal audit functions vary by organization, but in TPDC they include the elements like: To objectively monitor and report on the health of financial, operational, and compliance controls, To provide insight into the effectiveness of risk management, To offer guidance regarding effective governance, To become a catalyst for positive change in processes and controls, To deliver value to the audit committee, executives and management in the areas of controls, risk management, and governance to assist in the audit committee’s assessment of the efficacy of programs and procedures and Coordinate activities and share perspectives with the independent auditor.

1.3 An overview of TPDC
The Tanzania Petroleum Development Corporation - TPDC Is the Tanzanian State corporation through which the Ministry of Energy and Minerals implements its petroleum exploration and development policies. TPDC has manpower strength of about 130 and is organized into four directorates, namely: Exploration, Production and Technical services, Finance and Administration, Managing Director and Marketing and Investment.
The Tanzania Petroleum Development Corporation was established under the Public Corporations Act No.17 through the Government Notice No.140 of 30th May 1969. The Corporation began operations in 1973. TPDC is a wholly owned Government parastatal, with all the shares held by the Treasury Registrar.

1.3.1 TPDC Mission statement
To participate and engage in the exploration, Development, production and distribution of oil and gas and related services, facilitate a fair trading environment safeguard the national supply of petroleum products at the same time developing quality and safety standards to protect people property and environment.

1.3.2 Vision
To become a leading integrated national oil and gas company competing nationally, regionally and globally in an environmentally responsible manner to the benefit of all stakeholders.

1.4 Statement of the research problem
On formation of audit committee, TPDC apart from other roles, the committee work in relation to internal audit To develop and approve the internal audit mandate, goals and mission, review the (re)appointment, promotion or dismissal of the head of internal audit, and the determination of his/her qualifications, reporting hierarchy and compensation monitor whether the internal audit function has adequate resources, follow up on the internal audit department’s scope, the results of its operations and recommendations, and on management’s responses thereto, and Regularly evaluate the internal audit department’s objectivity and independence of judgment. Also to monitor and assess the role and effectiveness of the internal audit function in the overall context of the company’s risk management system; and review and assess the annual internal audit work plan.
With these roles the internal audit need to work independently and free from the management under the guidance and support from the audit committee. It is seen most of the time in some organizations goals and expectation are not reached due to the fact that audit committee effectiveness fail to give clear cut between the internal audit as in relation to the management and internal audit fail to recognize her safety as far as management is concerned, hence the internal audit fail to operate independently.

The researcher therefore taking TPDC as case study due to the seen structure, functions and operation wants to examine if audit committee is working effectively in achieving internal auditors independence and that there are no management effect on the internal auditor in acquiring the independence. The effectiveness of audit committee can help the internal audit in achieving their independency. Since the independence of internal audit is of vital important on risk management and internal control of an organization.

1.5 Objectives of the study

The objectives of the study are identified in two categories; general objective of the study and the specific objectives of the study. They are explained as follows;

1.5.1 General objective of the study

The study was conducted with an objective of assessing the effectiveness of audit committee in achieving independence of internal audit. whereas the performance of the audit committee duties where being examined in relation to the independence of internal audit.
1.5.2 Specific objectives of the study

The specific objectives of the study were:

1. To examine the roles of audit committee in enhancing the independence of internal audit
2. To assess effectiveness of Audit Committee roles in enhancing the independence of internal audit
3. To assess on the way to improve the independence of the internal audit

1.6 Research questions

1. How do roles of audit committee enhance the independence of internal audit?
2. Are the audit committee roles effectively provide for internal auditors independence?
3. How is the audit committee work with the management and other staffs to provide internal auditors independence

1.7 Significance of the study

The findings of research have benefited the Tanzania Petroleum development corporation itself, as well as other companies. The research activity has also generated new knowledge to the researcher in the field of audit committee and internal audit functions and be able to apply the knowledge in other organization where he will happen to work.

1.8 Scope of the study

The study was conducted in Tanzania petroleum Development Corporation. This is because it is a large corporation which has internal audit department and audit committee reporting to the Controller and Auditor General (CAG) office for external auditing. Therefore the data collected from there were expected to be reliable and of good quality.
1.9 Limitation and delimitations of the study

1.9.1 Limitations

Limitation of the study was on the access to the organization information due to confidentiality and organization protocol. Also the willingness to corporate the selected sample was another big challenge that a researcher encountered during the research.

1.9.2 Delimitations

The researcher provided questionnaire with questions that can cover the whole area that is not accessible due to confidentiality and from the answer received he can draw conclusion. Also the special recommendation from the head of faculty to introduce the researcher to the company management which stated the clear purpose of the research and that all the confidential information will remain confidential after the use.

To gain staff cooperation the researcher volunteered to work with the staff helping some office work, provide advice where necessary and explain to them the clear importance of the research to them and to the organization at large.
CHAPTER TWO
LITERATURE REVIEW

2.1 Introduction.
Here researcher has given an overview of the existing literature and some previous studies on the interaction between audit committees and internal audit in order to give an overview of possible expectations audit committee members can have vis-à-vis the internal auditor(s) and that helped the researcher to undergo the research on the effectiveness of audit committee in achieving the independence of internal audit.

2.2 Theoretical literature review
2.2.1 What is internal audit?
A commonly used definition for internal audit is:
‘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’.

This definition recognizes two roles for internal audit:
To provide an independent assurance service to the board, audit committee and management, focusing on reviewing the effectiveness of the governance, risk management and control processes that management has put into place.
To provide advice to management on governance risks and controls, for example, the controls that will be needed when undertaking new business ventures.

2.2.2 Relationship between the audit committee and the internal auditor(s)
The relationship between the audit committee and internal audit is an important one, with a reciprocal strengthening of each other’s function (Goodwin and Yeo, 2001). In other words, the audit committee can strengthen the internal audit function and internal audit can in turn be an important resource to the audit committee in fulfilling its
responsibilities (Turley and Zaman, 2004). Based on their analysis of audit committee charters and reports, Carcello et al. (2002) found that although internal audit can be a valuable resource for the audit committee, disclosures suggest a possible under-emphasis on internal audit.

Moreover, the committee is regarded as a liaison between the Board of directors and the internal auditors, which allows it to reduce the information asymmetry that exists between them. The efforts of the Tunisian accounting and legal authorities to strengthen the role of the audit committees are expressed in the promulgation of Law No. 2005-96 of October 18, 2005 on strengthening financial relations securities. According to this law, the permanent audit committee is composed of at least three members, designated as appropriate by the Board of Directors or the Supervisory Board from among their members, and it is prohibited for the Chief Executive or the Chief Executive Officer to be a member of the committee.

The audit committee is responsible for several issues relating to the audit and in particular the relationship of the organization with its auditors. As part of its responsibilities, it will review the internal control procedures and the risk management system. These areas fall under the remit of the internal audit function, which means that an effective working relationship between the two parts is a key to sound corporate governance (Davies, 2009).

Goodwin and Yeo (2001) affirm that the importance of working relationship between the audit committee and the internal audit resides in reciprocal strengthening of each others function. In other words, the audit committee can strengthen and monitor the internal audit function (Goodwin, 2003) and internal auditors may in turn serve as an important resource for the audit committee in fulfilling its responsibilities (Turley and Zaman, 2004).
From an international perspective, the importance of a working relationship between the audit committee and internal audit is reinforced by the Sarbanes Oxley Act of 2002 in the US where “audit committees must make informed choices about the quality of work it receives from the auditors” (Rittenberg, Schwieger and Johnston, 2008). Similarly, the BRC (1999) emphasizes the importance of a strong working relationship between the audit committee and internal audit in preventing misstatements in financial reporting. In order to better understand the relationship between the audit committee and internal audit, researchers explained the role of internal audit in support of the audit committee, the audit committee's role in strengthening the internal audit, and the interaction between the audit committee and internal audit.

Audit committees have a crucial role to play in providing oversight to the internal audit function. Their main objective is to determine whether internal audit is doing an effective job (Schneider, 2010) and to improve the quality of its work. They must therefore assess the internal audit organizational structure and ensure that the function has sufficient staff to fulfill its mission (Bailey, 2007). Moreover, effectively functioning audit committees have to play a key role in strengthening internal audits independence (Marx, 2008). In fact, audit committees, as part of their internal audit oversight role, protect and enhance the independence of the internal audit function by means of reviewing the appointment, promotion or dismissal of the head of internal audit, and the determination of his compensation (Sarens and De Beelde, 2006) and acting as an independent forum for internal auditors to raise matters affecting management (Goodwin and Yeo, 2001). Audit committees are also entitled to monitor the work performance of the internal audit function. They should review and approve internal audit reports such as internal audit charter, internal audit plan and programs, internal audit budget and evaluate the internal audit results. Similarly, according to Marx and Voogt (2010), audit committee should review the cooperation between internal and external audit, whether internal audit has unrestricted access to the chair of the audit committee, and whether internal audit has unrestricted access to the chair of the board.
2.2.3 The role of internal auditors in supporting and assisting the audit committee

A strong internal audit function can increase the effectiveness of the audit committee in carrying out its tasks (Bishop, Hermanson, Lapides and Rittenberg, 2000; Turner, 1999). Therefore, audit committees often rely in the exercise of their responsibilities on the internal audit function that can help them with assurances regarding controls, independent evaluation of accounting practices and processes, risk analysis, and fraud analysis (Hermanson and Rittenberg, 2003).

Moreover, the internal audit function can provide comfort to audit committees, specifically, with respect to internal control and risk management system (Sarens, De Beelde and Everaert, 2009; Gendron, Bédard and Gosselin, 2004; Gendron and Bédard, 2006). Indeed, audit committees feel uncomfortable about internal control in high-risk areas and risk management system because of the evolution in the company’s risk management and internal control approach.

Internal auditors, due to their specific knowledge and expertise in internal controls and their privileged position within the organization, can help audit committees to understand how internal auditors evaluate the system of internal control and the effectiveness of internal controls of the company (Rezaee and Zabihollah, 1993).

Furthermore, the internal audit function’s role in formalizing the risk management system can also be a crucial source of comfort for the audit committee. Regulators have recently highlighted the growing role of internal audit in support of the audit committee to ensure the integrity and quality of financial reporting.

The internal audit function is considered as a mechanism that reduces the principal agency problems between the audit committee and the operational people in the organization, including management (Raghunadanan et al, 2001; Scarbroughet al, 1998). In fact, the audit committee (principal) often lack information about the status of specific questions of the organization, such as risk management and internal control, which are the responsibilities of operational (agent) which may lead to uncertainty in their ability to fulfill their own supervisory role (Sarens, De Beelde and Everaert, 2009).
Therefore, the internal audit, considered as valuable resource that provide the information needed for audit committees, can reduce the problems of asymmetric information between the members of the audit committee and operational people within the organization (Bishop et al., 2000).

2.2.4 The extent of interaction between the audit committees and the internal audit function
Interactions between internal audit and the audit committee are an important element of sound corporate governance (IIA, 2002; Bishop et al., 2000; Scarbrough et al., 1998). This interaction is, however, a broad concept and that includes a variety of activities. Previous studies (Scarbrough et al., 1998; Raghunandan et al., 2001, Goodwin, 2003, Zain, Subramaniam and Stewart, 2006) focused on the following three main aspects: (1) frequency of meetings between the audit committee and the Chief Internal Auditor, (2) audit committee involvement in the dismissal of the CIA, and (3) review of internal audit work.

2.2.5 Frequency of audit committee meetings with the chief internal auditor
The audit committee has to have effective communication with the internal audit function by having frequent meetings with the chief internal auditor to discuss and review specific issues on a timely basis (Raghunandan et al., 2001; Scarbrough et al., 1998). Regular meetings between audit committee and internal auditing helps the audit committee to remain informed and knowledgeable about relevant issues of accounting, finance and auditing, thus enabling it to assist the internal auditors to resolve any problems identified.

More frequent meetings also provide opportunities undertake in-depth discussions on ways to improve an organizations financial reporting system (Zain, Subramaniam and Stewart, 2006). From a regulatory perspective, The Institute of Internal Auditors (2002) suggest that open lines of communications must be kept between internal audit and the
audit committee to achieve maximum benefit for the organization. In addition, Bailey (2007) argues that the meetings between the audit committee and the chief internal auditor, without the presence of management, can help to improve communication between the two groups. Similarly, Braiotta (2000) points out that private meeting between the audit committee and the audit manager would improve and protect the independence of internal auditors as the auditor may provide more complete information to the audit committee because it is free from any influence of the direction.

2.2.6 Audit committee involvement in the dismissal of the chief internal auditor
The audit committee can interact with the audit committee function through its involvement in the decision of dismissing the chief internal audit. The involvement of the audit committee in key decisions such as the replacement of the Chief Internal Auditor strengthens the authority and accountability of the internal function (Zain, Subramaniam and Stewart, 2006). Such involvement enhances the independence of the internal audit function, making more difficult for management to dismiss the chief internal auditor for raising sensitive audit issues (Scarborough et al., 1998). In other words, management influence over the internal audit function decreases and consequently internal auditors would feel more confident in undertaking audit investigations, particularly when dealing with more sensitive issues that may involve senior management.

2.2.7 Audit committee review of the internal audit work
The audit committee is responsible for ensuring that management has designed and implemented an effective internal control system and internal audit program (BRC, 1999). To fulfill this responsibility effectively, audit committees are required to review the internal audit proposals related to programs and plans, internal audit budget and internal audit coordination with external auditors.
Further, the audit committee also has the responsibility of reviewing the internal audit results insofar as they relate to financial reporting, internal controls and compliance with laws and regulations (Raghunandan et al., 2001).

According to Zain, Subramaniam and Stewart (2006) the greater is the extent of audit committee review of the internal audit programs and processes, the greater is the possibility of identifying weaknesses in the internal audit activities, and consequently of improving the internal monitoring function. Bailey (2007) indicates that the best practices regarding audit committee review of internal audit work consist in reviewing the internal audit charter, plan, budget as well as the internal controls and the financial statements of the company.

2.2.8 Effects of audit committee to organization.
Several studies have examined the effect of audit committee presence or absence on various measures of financial reporting quality. Evidence of a positive link between audit committee existence and the quality of financial reporting has been provided by analysis that indicates that earnings overstatements are less likely among companies having audit committees (DeFond and Jiambalvo, 1991), and that companies that manipulate their earnings are less likely to have an audit committee

Evidence also has been documented that audit committees are associated with a reduced incidence of errors and irregularities in financial statements (McMullen, 1996). Furthermore, Gwilliam and Kilcommins (1998) found that the presence of audit committees creates a perception of enhanced auditor independence, and more reliable financial reporting among financial statements users
2.2.9 Internal audit independence and the role of Audit committee

Goodwin (2003) indicate that independence is further enhanced if members of the audit committee in addition to being independent have the technical expertise to understand the work of the internal audit. This supports the earlier study by Raghunandan Red and Rama (2000) who found that committees comprise solely of independent directors and at least one member having accounting or finance expertise were more likely to have longer meetings with the chief audit executive to provide access to the chief audit executive and to review internal audit programs and result.

An important responsibility arising out of this reporting relationship that can have an effect on auditor independence is the responsibility for hiring and firing the chief audit executive. Bariff (2003) argues in his research done that the independence of the internal audit function is at risk if an auditee such as the CFO has responsibility for the hiring and firing of the chief audit executive, based on the principal that the internal auditor may be indebted to the CFO for his appointment and may be hesitant to criticize the CFO for fear of being fired. McHugh and Rughunandan (1994) in their study identified that a strong majority of internal auditors indicated that vesting the hiring firing authority with the audit committee would enhance internal auditor independence improve oversight by the audit committee and improve the ability of the internal auditor to get action on audit findings.

This is reflected in the institutes advisory guidelines (IIA 2001b, 2002c) for the Board Audit Committee participate in these responsibilities.

2.2.10 Audit committee in financial disclosure

An underlying assumption of exercising sound AC in the firm is that it has a positive effect on the quality of financial disclosure. Previous empirical researches documented a positive association between AC and the quality of financial information.
A well functioning AC system leads to the improvement of corporate financial reporting and the decrease of earnings management or financial frauds, as well as the increase of unqualified auditor reports. Some researchers noted that existence of AC reduces errors and irregularities in financial statements and enhances the credibility of financial reporting. It is axiomatic that poor standards, for instance ineffective or non-existent ACs, facilitate abuses such as fraudulent financial reporting. AC’s effectiveness in achieving independence of internal auditors has been highlighted in many studies.

2.3 Empirical literature review

2.3.1 Internal auditors independence in reporting line

Goodwin and Yeo (2001) support this view through their research findings that an effective audit committee can strengthen the position of the internal auditor function by acting as an independent forum for internal auditors to raise matters affecting management.

In addition to the presence of audit committees and access to them is a requirement to report to them directly to maintain independence. This is reinforced through a study by Bariff (2003) who noted that traditionally internal auditors were functionally reporting to the Chief Financial Officer (CFO) or Chief Executive Officer (CEO). Studies conducted a few years ago indicate that this practice still exist (Leung et al. 2004; Paape et al., 2003), although in lower proportions. Bariff (2003) asserts through the findings of his study that the reporting line to the CFO is based on the theory that there was the need for the CFO to know what is right and wrong with their finances and operations within their scope of accountability and responsibility and that this historical reporting relationship between internal auditing and the (CFO) began to change during the 20th century. Bariff (2003) further asserts that due to the increasing frequency of financial reporting and external auditing failures, the internal auditing profession was motivated to seek greater independence for its actions and judgments through an appropriate functional reporting line. Findings from earlier studies support this view (Schneider and Wilner, 1990; Hanson, 1997).
These research studies suggest that in settings where the internal audit function is independent, in terms of reporting level, an improved control environment and reduction in reporting errors results.

Gramlings (2004) confirms this by identifying that independence through an appropriate reporting relationship is typically viewed as the most important criterion describing objectivity. The importance of the independence status of internal auditors through an appropriate reporting line was reinforced by the IIA (2004) who strongly insists that the Chief Audit Executive (CAE) should report functionally to the audit committee to promote good corporate governance and administratively to the Chief Executive Officer (CEO) of the organisation. This further supports the view of Braiotta (1999) who argued that private meetings between the audit committee and the chief audit executive serve the purpose of enhancing and protecting the independence of internal auditors. This reasoning is based on its standing that the functional reporting line for the internal audit function is the ultimate source of independence and authority. The Audit Committee has been suggested as the functional reporting line because it is a sub committee of the Board consisting of members who are independent of the management function.

2.3.2 Internal audit value to audit committee

The increased organizational status and power of the audit committee may enhance the status of the internal audit function. It may also deflect cost control pressures from management who may view internal audit as a cost centre (Quarles, 1994). Based on empirical research, Spira (1999) argues that one benefit of audit committee establishment is the raising of the status of the internal audit function. Internal auditors interviewed in her study particularly valued audit committee support and sought to be proactive in achieving it, sometimes through ‘educating’ audit committee members. An effective audit committee can strengthen the position of the internal auditor(s) by acting as an independent forum for internal auditors to raise matters affecting management (Goodwin and Yeo, 2001). Therefore, the IIA (2004) strongly insists that the Chief Audit Executive (CAE) should report functionally to the audit committee, which is critical to good corporate governance.
Internal auditing is a valuable resource for audit committees to meet their mandate related to financial reporting (Bishop et al., 2000). “Audit committee characteristics and investment in internal auditing” For example, the National Association of Corporate Directors remarks that “the audit committee can look to today’s internal auditing function to provide independent, objective assurance and consulting activities designed to add value and improve the organization’s operations” (NACD 1999, p. 47). Recent enforcement actions have stressed the important role of internal auditors in the corporate governance and monitoring processes. Despite the policy and practice related importance of internal auditing and the role of audit committees in internal auditing, the relevant empirical literature is small but growing.

2.3.3 Audit committee characteristics and investments in internal auditing

Audit committees are responsible for providing oversight over the financial reporting process, including the system of internal controls. Regulators encourage audit committees to rely extensively on both the external and internal auditors to ensure more effective monitoring. Since internal auditing is a key component of the internal monitoring process, we expect that the composition of the audit committee will be associated with the extent of investment in internal auditing. Further, prior research suggests that audit committee characteristics are associated with support for the external auditor (DeZoort et al., 2003),”Audit committee support for auditors” and with external audit fees (Carcello et al., 2002b; Vermeer et al., forthcoming). A natural corollary is that audit committee characteristics are likely associated with the nature of the committee’s interactions with, and the extent of investment in, internal auditing.

An effective audit committee can strengthen the position of the internal auditor(s), by acting as an independent forum for internal auditors to raise matters affecting management (Goodwin and Yeo, 2001). In their journal “Two Factors Affecting Internal Audit Independence and objectivity”, says The lines of communication and reporting should encourage internal auditors to speak freely, regularly and on a confidential basis.
with the audit committee. The CAE should be invited to audit committee meetings to present and discuss the audit planning, findings and observations.

2.3.4 Meeting between audit committee and internal auditor

Braiotta “The audit committee handbook” (1999) argues that private meetings between the audit committee and the CAE serve the purpose of enhancing and protecting the independence of internal auditors. National Board Of Accountants and Auditors (NBAA) gives an overview of the specific aspects of the internal audit oversight role of the audit committee.

- The audit committee should develop and approve the internal audit mandate, goals and mission;
- review the (re)appointment, promotion or dismissal of the head of internal audit, and the determination of his/her qualifications, reporting hierarchy and compensation;
- monitor whether the internal audit function has adequate resources;
- follow up on the internal audit department’s scope, the results of its operations and recommendations, and on management’s responses thereto;
- regularly evaluate the internal audit department’s objectivity and independence of judgement;
- monitor and assess the role and effectiveness of the internal audit function in the overall context of the company’s risk management system;
- and review and assess the annual internal audit work plan.

2.3.5 Roles of internal auditors

Bishop et al. (2000)” give an overview of more specific (theoretical) roles of internal auditors to support the audit committee.
• general assistance could include: facilitating the information flow to the audit committee or performing special projects or investigations, as requested by the audit committee

• financial reporting assistance could include: supporting the audit committee in its evaluation of whether or not the company has satisfied its internal and external reporting objectives, supporting the audit committee in its assessment of the quality of financial reporting, providing information and insight regarding the strength of controls over the quarterly reports or assuring audit committee members that they are receiving reports with relevant and timely business performance measures;

• risk and control assistance could include: supporting the audit committee in its evaluation of whether the company has satisfied its control objectives, providing information that will help the audit committee monitor the company’s control environment, and providing information that will help the audit committee monitor key financial and business risks facing the organisation.
Facilitating effective audit committee performance in acquiring independence of internal audit requires a framework that encompasses all key participants and processes. Ultimately, this framework should support a flow of information to enhance the audit committee's ability to meet its oversight objectives on a consistent, timely, and ongoing basis.

It is clear that audit committees and their members are facing significant challenges. In today's complex and evolving business environment, audit committees can contribute tremendously to a “no surprises” environment.
Rules and regulations increase virtually on a daily basis, with perhaps the greatest challenge being to strike the right balance between enforcement and compliance. An audit committee that operates effectively is a key feature in a strong corporate governance culture, and can bring significant benefits to a company especially when it can work to attain the independence of internal auditor While the audit committee may first consider whether internal audit is effectively using available resources, it may also want to assess whether the function is appropriately funded and staffed to meet expectations. One consideration is whether internal audit has the appropriate mix of skills and certifications to achieve strategic objectives and proactively identify and address current and emerging risks.

An effective evaluation by the audit committee of the appropriateness of resources is not limited to the internal audit team, but also includes the CAE. The reporting structure of the CAE can also be considered in evaluating the effectiveness of internal audit. In many organizations, the CAE reports functionally to the audit committee and administratively to the CFO or CEO. This reporting structure, can present real or perceived issues in terms of independence and effectiveness. Audit committees can help mitigate this challenge through having an open and transparent relationship with internal audit that allows the CAE to regularly and freely discuss issues and concerns outside the presence of management, and through actively participating in the CAE’s performance evaluation and compensation process.
CHAPTER THREE
RESEARCH METHODOLOGY

3.1 Introduction
This is the way of systematically solving the research problem. The research studied various steps that generally adapted in studying the research problem along with the logic behind them. This chapter presents research procedure and methodology; it includes some explanation about the research design, unit of inquiry, research instrument, methods of data collection, data processing and analysis.

3.2 Type of the study
This is the way of investigating an empirical topic by following a set of pre-specified procedures. The study type intended to be used is Case Study research approach. Due to the available case study which is reliable.

3.3 Study area
The area in which the study was conducted is Tanzania petroleum Development Corporation. Because the TPDC as a case study is large company with internal audit department work with the management and audit committee, therefore the use of it as a case study is appropriate for the researcher had realizable information for making decision, draw conclusion and give suggestion. Also since the researcher has been working with the company therefore he is familiar with that particular area.

3.4 Study Population
The targeted population used was 130 people who are the staffs working with the Tanzania Petroleum Development Corporation and the audit committee members of the corporation. The study population extended further to the board of directors members of the corporation.
3.5 Units analysis
The units of inquiry chosen have been from:-
(i) Audit section
(ii) The accounts section
(iii) Audit committee
(iv) Board of directors

3.6 Sampling size and sampling Techniques
The researcher used judgmental sampling technique as an approach in selecting his sample units. This is a non-probabilistic sampling technique. The sample size was 34 people provided that they had at least level of education Advanced Diploma or First Degree in Accountancy and/or Finance field from recognized institutions.

3.7 Types and source of data
This study was designed to use both primary data and secondary data.

3.7.1 Primary data
Kothari (1996) defines primary data. Is the researchers collected fresh data to use in solving a specific problem under study. They are original and used to describe directly an occurrence by person who actually observed or witnessed the occurrence.
In this study, primary data will be collected through personal interviews and questionnaire.

3.7.2 Secondary Data
Secondary data involves data that have already been collected by someone else, and have already been processed (Kothari, 1996). These were extracted through reviewing various documents e.g. donors audited accounts, textbooks, journals, periodicals and other published information that were available.
3.8 Data Collection Methods

The researcher, in conducting the research he used data collection techniques such as interviews, questionnaire, and documentary sources.

**Interview**

This was used on those top officials of the corporation such as Managing director, Director of internal audit and some board members. The researcher used this technique because it enabled him to obtain detailed information about how they operate meetings, how often, what are the modalities and what is the participation of audit unit in the meetings. This information enabled the researcher to measure the access of internal audit to the management.

**Questionnaires (Appendix 1 & II)**

Under this method of data collection, the researcher used it to different people. Such as auditors, accountants and other staff having the knowledge and experience concerning audit committee of the corporation. Both open ended and close-ended questions was used. This method enabled the researcher to reach many people in a short period of time and the information acquired, allowed a researcher to analyze how effectiveness of audit committee can have an impact on the performance of internal auditor and the independence of internal audit in organization.

**Documentary source**

The researcher used this technique so as to review the minutes of the audit committee, auditors’ reports and board meeting reports. Here the researcher checked the consecutive report finding out the agreements and recommendation made by internal auditors on pre report or meeting are being implemented and being presented on the fore meetings and reports.
3.9 Validity and reliability issues

“Validity refers to the extent to which a test measures what we actually wish to measure. Reliability has to do with the accuracy and precision of a measurement procedure … …” (Kothari 2004). The procedures below will indicate the validity of the instruments in this study. The researcher asked an expert and group of experts among the respondents to comment on the representativeness and suitability of the questionnaires and the interview guide for data collection. The instruments will also be further presented to my research supervisor for intellectual comments and suggestions so as to obtain accurate, correct and meaningful data.

As reliability is the accuracy or precision logging in data without making errors, then reliability will concern with data collected from the selected sample of TPDC’s employees which will be careful logged in the computer by the researcher himself to avoid any possibility of coding wrong information.

3.10 Data analysis and presentation technique

Both qualitative and quantitative data was analyzed by using the Statistical Package for Social Science (SPSS) software to compute percentages, tabulation and cross-tabulation of responses.

SPSS was applied by the researcher because it is reliable on data analysis and user friendly it also can cope with the data collection technique expected to be applied by the researcher.
CHAPTER FOUR
PRESENTATION AND DISCUSSION OF RESEARCH FINDINGS

4.1 Introduction
In this chapter the research findings are discussed and analyzed. Findings were analyzed by referring to the results obtained from the interviews, questionnaires, documentary analysis and observation. The findings of the study were analyzed in line with the specific objectives.
The study aimed at assessing the effectiveness of audit committee in achieving the independence of internals auditors whereby the performance of audit committee was examined.

Thus the study specifically looked at the role of audit committee in enhancing the independence of internal auditors and the effectiveness of audit committee roles in enhancing the independence of internal auditors’

The study was conducted at TPDC which is parastatal company which deals with exploration of gas and oil and has the internal audit department and the audit committee team.

4.2 The Profile of Respondents for Members
General information of respondents in this study shows that both female and male employees were involved, and both attained different levels of education and positions in TPDC. In this study however male were 24(72%) and 10(28%) were females. Among them 9(26.4%) were Directors, 5(14.7%) were managers and 20 (58.8%) were other staff . The study showed that 7(20.5%) of the employees have worked with TPDC in a period less than 5 years, 18(52.9%) within 8 years and only 9(26.4%) above 8 years. The study revealed that all the staff selected knows about audit committee and the internal audit operations in the company.
Table 4.1: Characteristics of respondents

<table>
<thead>
<tr>
<th>Sex</th>
<th>No. of employees (N=34)</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Female</td>
<td>10</td>
<td>29.5</td>
</tr>
<tr>
<td>Male</td>
<td>24</td>
<td>70.5</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>34</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Position</th>
<th>No. of employees (N=34)</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>High level(Directors)</td>
<td>9</td>
<td>26.4</td>
</tr>
<tr>
<td>Middle level(Managers)</td>
<td>5</td>
<td>14.7</td>
</tr>
<tr>
<td>Low level</td>
<td>20</td>
<td>58.8</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>34</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Working experience</th>
<th>No. of employees (N=34)</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of years</td>
<td></td>
<td></td>
</tr>
<tr>
<td>0-5 yrs</td>
<td>7</td>
<td>20.5</td>
</tr>
<tr>
<td>5-8yrs</td>
<td>18</td>
<td>52.9</td>
</tr>
<tr>
<td>8 and above</td>
<td>9</td>
<td>26.4</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>34</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Source; Field data, 2013

4.3 Data collection

The researcher conducted interview with the internal auditors and the Director of Internal Audit and the questionnaire were provided after the interview where the researcher was interested to find out the coordination between them and audit committee. The focus was on meeting reports and committee obligation to internal audit, the interviews lasted from 60 to 90 minutes. All interviews were tape recorded and transcribed immediately after the interview took place in order to support data and enhanced the reliability of conclusion.
Contrary to the internal auditors, it was not easy to reach these other individuals to arrange an interview with them therefore the researcher issued some questionnaire for them to fill whereas the questionnaire mainly focused on finding out how the effectiveness of audit committee provide to the independence of the internal auditors.

The researcher obtained copies of several archival materials, like the internal audit charter and internal audit planning, as well as even more confidential documents like internal audit reports, business control guides, audit committee reports, and so on. The company was reluctant to release some confidential documents like internal presentations and some risk matrices.

4.4 Data analysis
The research results were extracted and analyzed using the SPSS software and thereafter compiled in tabular form. The results were thereafter critically analysed against existing literature and best practice guideline to identify evidence of effectiveness of audit committee in achieving independence of internal auditors.

All interview transcripts and documents were coded. Next, the most important observations were summarized and sent back to the interviewees to obtain their confirmation about the researchers interpretations. They were afforded the opportunity to react openly and add new elements if necessary.

4.5.1 Measurement of results
Each of the research questions were addressed as follows:

**How do roles of audit committee enhances the independence of internal audit?**
Three research questions dealt with this aspect of the research. These questions (research question 8-10, Appendix 1) were concerned with the structure and personnel of the Audit Committee. These questions would provide some insight into the structure and composition of the audit committee including the level of internal audit committee involvement relative to its role with the internal audit function.
In addition, questions were posed to the research participants to determine if there were any direct influences through their relationship with the audit committee that impacted on internal audit independence. These questions (research questions 11-17, Appendix 1) would provide some insight into internal audit’s reporting line and the level of internal audit committee involvement relative to its role with the internal audit function.

**Are the audit committee roles effectively provide for internal auditors independence?**

In order to respond to the above broad research question and identify any direct or indirect management influences that would impact on audit committee and internal audit’s independence, the researcher identified various characteristics which were explored through seven specific research questions (Questions 1-7, Appendix 1). These characteristics included:

- The organizational status of the internal audit department, i.e., the hierarchical level.
- The management practice of the internal audit department, which includes staff movements, budgets and the role of CEO’s and CFO’s on audit planning.
- The perception of people within the organization on internal audit as a partner.

**How is the audit committee work with the management and other staffs to provide internal auditors independence?**

On this question also researcher posses appendix ii questionnaire where general question where filled by TPDC staff members to see their respond on how they perceive the work relationship between management audit committee and staff at large
4.6 Discussion and interpretation of the research findings

The research results are discussed through the following descriptive analysis. 100 % of respondents indicated they knew about audit committee in TPDC. The respondents identified that there were a minimum of 0 and a maximum of 6 qualified accountants in the audit committee. While the results indicate that there is a somewhat trend towards moving to best practice principles that promote independence, there is still a fair amount of inconsistency in this area. This is especially with a lack of legislative backing providing for audit committee structural set ups that facilitate internal audit independence. These include compliance in respect of all members being independent and at least one being a member with an accounting qualification.

The roles of audit committee in enhancing the independence of internal audit was examined next.

Table 4.2 – Findings

<table>
<thead>
<tr>
<th>No</th>
<th>Research Questions</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>No</td>
</tr>
<tr>
<td>RQ</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>What is the hierarchical level of your internal audit department?</td>
<td>34</td>
</tr>
<tr>
<td></td>
<td>Corporate group level</td>
<td>0</td>
</tr>
<tr>
<td></td>
<td>Intermediate level</td>
<td>0</td>
</tr>
<tr>
<td></td>
<td>Local Level</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Is it common for internal auditors to move to other functions within the company?</td>
<td>19</td>
</tr>
<tr>
<td></td>
<td>Yes</td>
<td>13</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td>No comments</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>On average how many years does an internal auditor stay within your internal audit department?</td>
<td>4</td>
</tr>
<tr>
<td></td>
<td>Less than 2 years</td>
<td></td>
</tr>
</tbody>
</table>
Between 2-4 years | 15 | 48
---|---|---
Between 5-7 years | 7 | 22
Between 8-10 years | 2 | 6
More than 10 years | 4 | 12

6 Do people within the organization perceive internal audit as their partner?
- Strongly disagree | 10 | 29
- Somewhat disagree | 12 | 35
- Neither agree/disagree | 2 | 6
- Somewhat agree | 5 | 15
- Strongly agree | 3 | 9

Table 4.3 - Findings

<table>
<thead>
<tr>
<th>No</th>
<th>Research Questions posed to respondents</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>RQ</td>
<td></td>
<td>No</td>
</tr>
<tr>
<td>5</td>
<td>Does your company have an Internal Audit Committee?</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>No</td>
</tr>
<tr>
<td>8</td>
<td>How many members are there in the Audit Committee?</td>
<td><em>there was a minimum of two, a maximum of 15,</em></td>
</tr>
<tr>
<td>10</td>
<td>How many of the Audit Committee members are professionally qualified accountants?</td>
<td>All are qualified accountants</td>
</tr>
<tr>
<td></td>
<td></td>
<td>50% of members or more are qualified accountants</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Non of members are qualified accountants</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Less than 50% of members are qualified accountants</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Did not respond</td>
</tr>
<tr>
<td>13.</td>
<td>Is the CAE regularly invited to the audit committee meetings?</td>
<td></td>
</tr>
<tr>
<td>-----</td>
<td>-------------------------------------------------------------</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Yes</td>
<td></td>
</tr>
<tr>
<td></td>
<td>No</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Yes</td>
<td></td>
</tr>
<tr>
<td></td>
<td>No</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>14.</th>
<th>Does the CAE have regular private contacts with the audit committee (chair/ or individual members)?</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Strongly agree</td>
</tr>
<tr>
<td></td>
<td>Somewhat agree</td>
</tr>
<tr>
<td></td>
<td>Strongly disagree</td>
</tr>
<tr>
<td></td>
<td>Somewhat disagree</td>
</tr>
<tr>
<td></td>
<td>Neither agree or disagree</td>
</tr>
<tr>
<td></td>
<td>Strongly agree</td>
</tr>
<tr>
<td></td>
<td>Somewhat agree</td>
</tr>
<tr>
<td></td>
<td>Strongly disagree</td>
</tr>
<tr>
<td></td>
<td>Somewhat disagree</td>
</tr>
<tr>
<td></td>
<td>Neither agree or disagree</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>16.</th>
<th>On an annual basis, what percentage of their time does the audit committee spend on internal audit topics?</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>A minimum of 10% and a maximum of 80%</td>
</tr>
</tbody>
</table>
To the question, whom does the internal audit department report functionally, the results indicate that there is room for management to influence the internal auditors. While 37% of the respondents indicated that they report functionally to the audit committee, some also identified multiple reporting lines in addition to the AC depending on the issue being discussed. In addition to reporting to the audit committee, 18% of respondents also indicated a functional reporting line to the CEO, 9% to the CFO, 9% to both the CFO and CEO and 12% to the CEO, CFO and the BOD’s. 6% of the respondents indicated that they only report to the CEO and a further 9% indicated that they report to others (e.g. company secretary, Head of Risk Management, Chief Operating Officer). The maximum of 37% indicate internal audit report functionally to audit committee which imply that there is independence room to internal audit on reporting rather than to the management.

**FIGURE 4.1 TO WHOM DOES INTERNAL AUDIT REPORT FUNCTIONALLY**

![Bar Chart](image_url)

Source: Field data, 2013

With regards the question, to whom does the internal audit department report administratively, 6% of the respondents identified that they report administratively to the
audit committee, 29% to the CEO, 23% to the CFO, 3% to the BOD’s and 6% to the company secretary. It appears that the lack of legislation on the structural set up has also provided for a range of administrative reporting lines. This if taken together with the varied functional reporting line, could provide further room for management influence especially when the functional and administrative reporting line is the same.

FIGURE 4.2 TO WHOM DOES INTERNAL AUDIT DEPARTMENT REPORT ADMINISTRATIVELY

![Bar Chart]

Source: Field data, 2013

When the respondents were posed with the question as to who is mandated to appoint, dismiss and evaluate the head of the internal audit function, a majority of respondents (50%) indicated that the audit committee is mandated to carry out the above duties, while a further 21% indicated that the audit committee carries out these duties in conjunction with the CEO, CFO or BOD’s. The results also indicate that there is a work culture where in some firms this duty is carried out by the CEO (15%), CFO (3%), CFO and CEO (3%). This also indicates that in the absence of legislative backing towards this
guideline, management has room to carry out this duty without audit committee oversight and hence negatively impact on internal audit independence.

With respect to the question, is the CAE regularly invited to the audit committee meetings, 97% indicated that they are regularly invited to the Audit Committee meetings, providing strong evidence of this positive trend to maintain independence. This is supported with the result of the next question, does the CAE have regular private contacts with the audit committee (chair/ or individual members), where 67% and 15 % of respondents agreed that they regularly meet or somewhat agreed that they privately meet with AC members.

The positive influence of the audit committee was further supported by the response to the following question, does the audit committee give input to the internal audit planning?. The results indicated57% and 37% agree and somewhat agree respectively that the AC provides input to the planning.
Despite having a large number of meetings and a sufficient number of members with financial expertise, one of the AC members suggests sometimes committee is a rather theoretical and obligatory concept without much decisive influence: “I have to confess that, in some cases, the audit committee is running after the facts”. Instead of considering the internal auditor as a valuable and independent information provider, AC prefers to rely almost exclusively on the external auditor. Consequently, the reciprocal relationship between the AC and the internal auditor clearly is underdeveloped, which can be considered to be a missed opportunity for both parties in particular internal auditors independence.

On the question, on an annual basis, what percentage of their time does the audit committee spend on internal audit topics, the results were a minimum of 10% and a maximum of 80% indicating a positive response. “I perceive internal audit as extremely important for our company and attach a lot of importance to the function”. Naturally,
they have a very large added value for our company. I think we can say that more than 50% of our time is devoted to internal audit.”. This high level of AC support improves the acceptance of the IA findings and recommendations, which contributes to the maturity of the function as a whole and to the independence of internal auditor.

The researcher reveal that AC meeting reports often spend a very limited proportion of their time on these topics. This was also confirmed by one of the interviewed internal auditors who expressed regret over this situation: “If an AC meeting takes two hours, they talk about the financial results for more than one hour and 45 minutes, so they (can) only spend five to ten minutes on internal audit topics”. Remarkably, AC members are convinced that they show enough interest in IA topics, whereas most internal auditors complain about the limited interaction that they have with AC members. This is understandable, as they have high expectations vis-à-vis the AC.

In summary, while there is a positive trend towards audit committee involvement in internal audit affairs and the level of interaction between the chief audit executive and audit committee which enhances independence, the lack of any legislative backing as to its structural set up appears to have provided for a number of loopholes that could impair internal audit independence. There are still avenues for structural setups for audit committee’s to have non independent members or not even one with an accounting qualification. In addition, there are possibilities for internal audit to report to the CEO, CFO, and also for these parties to be involved in the appointment and dismissal of the chief audit executive with no audit committee oversight. The loopholes identified provide avenues for management to influence internal audit independence.
Table 4.4 Distribution of respondents basing on whether is Internal Audit sufficiently independent of management

<table>
<thead>
<tr>
<th></th>
<th>Frequency</th>
<th>Percent</th>
<th>Cumulative Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Valid</td>
<td>Yes</td>
<td>23</td>
<td>67.6</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>11</td>
<td>32.4</td>
</tr>
<tr>
<td>Total</td>
<td>Total</td>
<td>34</td>
<td>100.0</td>
</tr>
</tbody>
</table>

**Source:** Research Data 2013

100% of respondents reported that their internal audit function was placed at the corporate/group level as opposed to being in the intermediate management level. This is in line with best practice guidelines (Bariff, 2003). While this indicates that in practice internal audit functions are well placed in the hierarchical level to maintain independence, the following additional questions were posed to the participants to identify if there were any indirect threats to independence.

When asked if it is common for internal auditors to move to other functions within the company, 56% of respondents implied that there is a culture within the organization for internal audit staff to move to other management functions within the organization. This is supported by 48% of the respondents who indicated that on average internal auditors stay between 2-4 years and 12% of respondents who indicated that auditors on average stay for less than two years. A long term commitment was rare and is supported by only 22% of respondents who indicated that auditors stay between 5-7 years in the organization, 6% of respondents who indicated that auditors stay between 8-10 years and only 12% of respondents who indicated that auditors stay for more than 10 years in the internal audit department.
The above analysis points towards an implied assumption that internal audit is used as a training ground or a jumping stone for internal auditors to further their career progress as the majority only stay between 2-4 years. This supports the view of earlier studies by Goodwin and Yeo (2001) that internal audit is used as a training ground. What is of concern is the effect this would have on internal auditor independence as it raises the question on whether the internal auditor can raise reports against management independently and objectively knowing that he or she is dependent on management for a career in an operational role in the future.

Other indirect negative influences on internal audit independence were noted when the results identified the potential for management influence on internal audit work. 17% of respondents reported that the Chief Executive Officer (CEO) is responsible for approving the IA budget while 12% reported that the Chief Financial Officer (CFO) approves the IA budget. Only 24% reported that the Audit Committee was solely responsible for approving the IA budget, while 32% indicated the approval was made by the Audit Committee in conjunction with the CEO, CFO, Board of Directors (BOD), the Company Secretary or overseas parent company in various combinations.
Management influences on audit planning was also noted when 32 % somewhat agrees that the CEO provides input for the IA planning, while a further 32 % strongly agrees that the CEO provides input to the IA planning. Only 3 % strongly disagrees and 15 % somewhat disagrees that they provide input for the IIA planning. With regards input by the CFO, 29 % of respondents strongly agree that the CFO provides input for the IA planning, while a further 35 % somewhat agrees that the CFO provides input to the IA planning. Only 6 % strongly disagrees and 15 % somewhat disagrees that they provide input for the IIA planning.

While the CEO and CFO’s input to internal auditing may not necessarily directly indicate impairment to internal audit’s independence, it does indicate a possible indirect influence especially when taken into account with other indirect influences such as them being in a position to control the career paths of internal auditors, the budget for the internal audit department and if the internal audit function were to functionally and/or
administratively report to them (identified as being possible in this study through an analysis of Table 2 in page 17 of this report).

It is also noted that a majority of respondents (50%) agreed and (6%) somewhat agreed that people within the organization perceive internal audit as a partner. It is argued by the authors, that this culture may indirectly put additional pressure on internal audit (a function that is subject to the same budgeted resources of the organization as all other functions) to work with management to achieve a common goal rather than act as a separate independent body checking on them.

In summary, while the results indicate that there is a trend towards internal audit departments being organizationally positioned to maintain independence, there, however, exists within firms a work culture that facilitates possible management influence on internal audit work. This includes the indirect ability of management to influence the career prospects of internal auditors, the internal audit budget and its planning when the internal audit function reports functionally to management rather than the audit committee. This is exacerbated by internal auditors themselves using the function as a stepping stone to further their career path in operational roles. It is also argued by the authors that the independence concept may be lost in such a culture especially if it were to be combined with people within the organization perceiving internal audit as a partner, subjecting them to the same budgeted resources, and pressures of each function rather than recognizing internal audit as a separate independent and resourced function.

4.6.3 What do audit committee (AC) members expect the role of internal auditors (IA) to be?

The researcher found out that AC members have high expectations about the role of internal auditors in the organization. AC members want internal auditors to demonstrate, as much as possible, their specific contributions to the monitoring and functioning
(efficiency) of the organization. More specifically, they expect internal auditors to work towards the achievement of specific results in a limited number of areas. The following paragraph from an AC meeting report clearly illustrates the fact that AC members do not feel comfortable when there are too many audits “in the pipeline”: “The current audit strategy of having multiple parallel audits is not ideal, not for the organization nor the internal auditor. The audits last too long and due to the fragmented input have diminished quality and coherence”.

More over the researcher found out that AC members, want internal auditors to become (more) like “translators” or “communicators” between the operational levels and the monitoring level (of which the AC is part) of the organization, in order to compensate for their lack of information about “what generally is going on in the organization”.
This shortage often is considered to be a serious constraint in the fulfillment of their responsibilities. More specifically, in the course of their work, internal auditors are expected to signal and communicate clearly all recognized risks and problems, as well as shortcomings in the internal control system. In order to achieve this, internal auditors should be able to communicate with everyone in the organization, which necessitates an open and friendly attitude. Moreover, they expect internal auditors to be facilitators for whistle blowing. Where as internal audit are being less independent due to lack of cooperation from other staffs

**Risk management**
During the interview with audit committee members the researcher also reveal that audit committee members expect internal auditors to be important, active and proactive players in risk management. More specifically, they want internal auditors to focus on specific high risk areas (e.g. inventories, foreign subsidiaries, IT applications), as these also are their areas of interest, especially when these have a direct or indirect impact on financial results.
After a thorough assessment of these risks, internal auditors should review the adequacy and effectiveness of the related internal controls, as well as compliance with existing policies and procedures, followed by the formulation of focused suggestions for improvements and even assistance with the implementation of these suggestions. AC members do not consider this last aspect to be a potential threat for the independence of internal auditors. In other words, AC members expect internal auditors to be specialists in risk assessment, and to develop and exhibit sufficient expertise to play a valuable advising or even more proactive role in the management of these risks.

4.6.4 Reasons for the differences in expectations and perceptions between audit committees and internal auditor

the researcher found that except from the one sample mentioned in the previous paragraph, all others show, to some extent, a mismatch of interests between the AC and the internal auditors. As a result, the reciprocal strengthening between both parties is far from optimal which hinder the independence of internal auditor. Whereas this mismatch of interests and the resulting limited interaction is more perceived by the internal auditors than the AC members. This can be explained by the internal auditors being more dependent on AC support, whereas the AC has other (potential) sources of information, like external auditors which diminishes its effectiveness to internal auditor independence.

Looking for reasons to explain this mismatch of interests, our interviewees as well as several AC meeting reports indicate that, despite the broader range of audit committee responsibilities suggested by the Code on Corporate Governance, ACs still focus strongly on financial results and related reporting issues. Conversely, the internal auditors’ work is more oriented towards the review and improvement of the risk management and internal control system. Although the monitoring of the risk management and internal control system clearly is mentioned in most corporate governance charters as an AC responsibility
4.6.5 How can the interaction between the audit committee and internal auditors be improved? In other words, how can we obtain better alignment of interests?

Based upon suggestions offered by the interviewed AC members and internal auditors, we can formulate specific suggestions to reduce the gaps between the expectations and perceptions about the effectiveness of audit committee and the internal auditors independence since the gaps between the expectations is one factor that researcher found to be hindering the independence of internal auditor.

First, since internal auditing remains as a profession both parties will benefit from clear communication about the specific roles and mission of IA, for example, through dissemination of the internal audit charter or a formal presentation of the function. Well-considered marketing of the IA function contributes to the creation of realistic expectations about IA and a more realistic evaluation of IA performance. One AC meeting report clearly mentions this need: “AC member X is wondering whether the internal audit function is clear within the company. AC member Y responds by stressing the importance of marketing the internal audit function”. Moreover, the sometimes opposite perceptions about the interaction between the AC and the internal auditors necessitate a critical and formal evaluation of their relationship (e.g. by means of a satisfaction questionnaire), which will provide both parties with opportunities to express their needs and expectation hence the independence of internal auditor.

Second, it becomes clear that both parties should broaden their areas of interest in a converging way and both should work out to maximize their effectiveness and independence. The independence is well seen to internal auditors when the audit committee work effectively accordingly.
CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION, AND RECOMMENDATIONS

5.1 Introduction
The study investigated the effectiveness of audit committee in achieving the independence of internal auditors. The case study of Tanzania Petroleum Development Corporation. The specific objectives were tackled through the three research questions. Firstly, the study examined what are the roles of audit committee in enhancing the independence of internal audit. Secondly, the study identified how does audit committee competent enough to bring performance to the internal audit. Finally, how is the interaction between the audit committee and internal auditors perceived by audit committee members, as well as internal auditors.

In this chapter, the summary and conclusions derived from the research findings of the study are presented. Recommendations derived from the findings are made and suggestions are given.

5.2.1 Summary of findings
The study involved female and male who joined TPDC in different periods. Males form the majority of the TPDC members of staff. Majority of TPDC staff are in the permanent contract employment and some of them have been employed for more than ten years in different levels.

The results indicate an interesting analysis. While it indicates that there is a trend towards adhering Effectiveness of audit committee to internal auditors independence, it also provides evidence that organizations are able to operate in an environment that compromises internal audit independence. This is brought about by a lack of statutory backing for internal audit’s structural set up along lines to maintain its independence.
As a result of the lack of such legislative backing and consequent consistency in its structural setup to enhance internal audit independence, there is a mix in internal audit structural setups and services. This has inevitably given rise to loopholes for independence to be breached as evidenced through this study.

5.2.2 Conclusion

It is noted that while there is a positive trend towards audit committee involvement in internal audit affairs and the level of interaction between the chief audit executive and audit committee which enhances independence, however, the lack of any legislative backing as to its structural set up appears to have provided for a number of loopholes that could impair internal audit independence. There are still avenues for structural setups for audit committee’s to have non independent members or not even one with an accounting qualification. In addition, there are possibilities for internal audit to report to the CEO, CFO, and also for these parties to be involved in the appointment and dismissal of the chief audit executive with no audit committee oversight. The loopholes identified provide avenues for management to influence internal audit independence discourage audit committee effectiveness on that.

The reporting structure of the CAE is being considered in evaluating the effectiveness of audit committee. In TPDC the CAE reports functionally to the audit committee and administratively to the CEO. This dual reporting structure, particularly when considered with the effects of rotational models and performance and compensation processes driven by the CEO, can present real or perceived issues in terms of independence and effectiveness. Audit committees can help mitigate this challenge through having an open and transparent relationship with internal audit that allows the CAE to regularly and freely discuss issues and concerns outside the presence of management, and through actively participating in the CAE’s performance evaluation and compensation process. The perception of the experience and knowledge of the CAE and the internal audit team can also affect how internal audit is regarded and respected in the organization. If the
CAE is viewed as not having the appropriate stature in the organization, or if the CAE or the internal auditors are viewed as lacking the necessary business acumen, internal audit may not have the respect and visibility needed to be independent.

In TPDC, the audit committee is responsible for approving the internal audit budget, and this approval is typically based on management’s recommendation. How often does the audit committee challenge the recommended internal audit budget? Internal audit, like other areas of the organization, is under pressure to contain or decrease its expenses while responding to emerging risks and the expectations of audit committees and management to expand coverage.

In providing the above comments, a number of general limitations to the study are identified. Firstly, the respondents were only Staff of Tanzania Petroleum Development Corporation and the board members of the company therefore the researcher had to broaden the views to come to the best conclusion. Secondly, respondents were not directly asked the question as to whether they were independent or provide independent; rather internal audit’s independence status has been gauged through trends established from a series of questions that examined internal audit’s relationship with audit committee and the two with the company at large.

5.2.3 Recommendations

An effective relationship between the audit committee and internal audit is fundamental to internal audit’s success, with the audit committee clearly setting and articulating expectations of strategic focus, providing the appropriate level of support for achievement, and holding internal audit accountable. Key performance measures will vary significantly depending on internal audit’s strategic emphasis; however, an evaluative approach that measures quantitative and qualitative factors should be considered.
In addition to regularly reviewing performance metrics and recalibrating internal audit’s activities when appropriate, the audit committee and internal audit may consider periodically revisiting the alignment of expectations and how internal audit supports the strategic and operational objectives of the organization.

Communication is an important component in maintaining an effective relationship between the audit committee and internal audit. Clear articulation by the audit committee of its expectations regarding both formal and informal communications can help facilitate a successful relationship and support internal audit in meeting its objectives. Internal audit’s communications should be timely, actionable, and relevant, with a priority on the implementation of recommendations and resolution of issues.

Few components of oversight are as critical to effective and successful audit committee oversight of internal auditing as is two-way communication with the internal audit activity. Because of their position and role within an organization, internal auditors possess a good and objective understanding of the culture, system of internal control, operations, and industry. Hence, the audit committee should rely upon them for important information about the organization’s control environment and processes, including significant control process issues, potential improvements, and resolution; as well as the overall adequacy of internal controls.

Specifically, the audit committee should ensure the lines of communication are open with the internal auditors to discuss significant issues that have been brought to the attention of management and the resulting responses. Should management place limitations on the scope of internal audit processes that have been authorized by the charter, the audit committee should be informed by the CAE. Such discussions will provide valuable information that will help the audit committee in its role of management oversight.
discussion include the reliability of operational information, safeguarding of assets, appropriate disclosures, and compliance with contracts, regulations, and laws.

And because of their extensive knowledge and based on their observations of accounting decisions, policies, and any complex or unusual events, transactions, and operations, the internal auditors also can help the audit committee evaluate various policies and practices. Inherent in the audit committee charter is its responsibility for monitoring and reviewing the performance of the internal audit activity. Because the input of the internal auditors is so critical to the success and potentially, the very survival of an organization, it is important for the audit committee to have a clear picture of the internal audit activity’s performance, and ensure that it is functioning well. Clearly, the CAE should report to the audit committee on the performance of the audit plan. But this is not sufficient to ensure quality and independence of the entire internal audit activity. Internal audit activity, should have in place a Quality Assurance and Improvement Program. Not only does such a program help ensure the activity is on the path to optimal quality and the independence of internal auditor, but it also sets an example of excellence for all audit customers and stakeholders, by demonstrating the activity’s commitment to confronting areas in need of improvement, and taking steps to make the requisite changes.

**Auditing the Internal Auditors**

The internal audit activity is a part of an organization’s risk universe, and should be assessed. Although the audit committee clearly is responsible for internal audit oversight, it is not the committee’s role to “audit” the activity. The audit committee’s oversight is at a much higher level. So who audits the internal auditors? That is the role of the external quality assessment (QA) team an independent group of professionals who are well-versed in best internal audit practices, under the leadership of an experienced and professional project manager.
The objectives of an external QA team are to evaluate the efficiency and effectiveness of the internal audit activity within the organization, to make best-practice recommendations for improvement, and to determine whether the activity is in conformance with the Standards. This is especially important, as it sends the message to everyone that the internal audit activity systematically submits itself to the same level of scrutiny that the rest of the organization undergoes through internal audits. This represents the internal audit activity’s commitment to excellence and dedication to quality. In addition, the external QA validates for the CAE, executive management, and the audit committee the level of the internal audit activity’s performance. It also provides assurance that enables the audit committee to report to the board with the highest level of confidence that internal auditing is functioning as it should.
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MZUMBE UNIVERSITY

APPENDIX 1

QUESTIONNAIRE ON EFFECTIVENESS OF AUDIT COMMITTEE IN ACHIEVING THE INDEPENDENCE OF INTERNAL AUDITOR.

I am Mr. Mkwe Thomas V a student pursuing Master Degree of Science in Accounting and Finance at Mzumbe University. In final year of my program, I am required to conduct a study in partial fulfillment of the requirements for the award of my Masters degree.

The main aim of this study is to find out the effectiveness of audit committee in achieving the independence of internal auditor. The findings are expected to be catalyst for rectifying the mentioned situation in all organization audit committee and internal audit operations in Tanzania.

So, you are hereby kindly asked to assist the research by simply filling in this questionnaire. I assure you that all information you provide will be guarded with high confidentiality and will only be used for academic purposes and not otherwise.
RESEARCH QUESTIONS

Instruction:
Please, answer by putting (√) in front of the answer you find correct. Likewise, explain or mention by writing in the place you are asked to explain or describe

QUESTIONS

1. Is Internal Audit appropriately funded and staffed

   (i) Yes               [ √  ]

   (ii) No             [       ]

2. Does Internal Audit have a clear set of performance expectations that are aligned with the success measures of the audit committee, and that are measured and reported to the audit committee?

   (i) Yes               [ √  ]

   (ii) No             [       ]

3. Does Internal Audit have a charter that is periodically reviewed and approved by the audit committee?

   (i) Yes               [ √  ]

   (ii) No             [       ]
4. Is Internal Audit sufficiently independent of management?
   (i) Yes [ ]
   (ii) No [ ]

5. In delivering the annual internal audit plan, is Internal Audit flexible and dynamic in promptly addressing new risks and the needs of the audit committee?
   (i) Yes [ ]
   (ii) No [ ]

6. Is Internal Audit highly regarded and respected within the organization?
   (i) Yes [ ]
   (ii) No [ ]

7. What do audit committee members expect the role of internal auditors to be?
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8. What are reasons for the differences between the expectations and perceptions about the interaction between the audit committee and internal auditors?
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9. How is the interaction between the audit committee and internal auditors perceived by audit committee members, as well as internal auditors?

**Audit committee members**

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**Internal auditors**

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10. How can the interaction between the audit committee and internal auditors be improved?

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THANK YOU FOR YOUR COOPERATION
RESEARCH INTERVIEW QUESTIONS

1. What is the hierarchical level of your internal audit department?
2. Is it common for internal auditors to move to other functions within the company?
3. On average how many years does an internal auditor stay within your internal audit department?
4. Who approves the internal audit budget?
5. Does the CEO give input for the internal audit planning?
6. Does the CFO give input for the internal audit planning?
7. Do people within the organization perceive internal audit as their partner?
8. How many members are there in the Audit Committee?
9. How many of the Audit Committee members are independent members?
10. How many of the Audit Committee members are professionally qualified accountants?
11. To whom does the internal audit department report functionally?
12. To whom does the internal audit department report administratively?
13. Who is mandated to appoint, dismiss and evaluate the head of the internal audit function?
14. Is the CAE regularly invited to the audit committee meetings?
15. Does the CAE have regular private contacts with the audit committee (chair/ or individual members)?
16. Does the audit committee give input to the internal audit planning?
17. On an annual basis, what percentage of the audit committee’s time is spent on internal audit topics?

THANK YOU FOR YOUR COOPERATION