The Influence of the Effectiveness of the Internal Audit Function on Good Governance: An Empirical Study

Jefri Ronaldo, Agus Tripriyono

Abstract

Good governance requires accountability, transparency, responsiveness, and integrity. The internal audit function (IAF) is an essential mechanism to promote these principles by strengthening internal control and providing independent assurance. This study applied a quantitative descriptive design using purposive sampling of 12 respondents directly engaged in internal audit and governance processes within a public sector organization. Data were collected using a structured questionnaire adapted from prior studies and analyzed with SPSS, employing descriptive statistics, reliability tests, correlation, and regression. Correlation analysis revealed a significant positive relationship between internal audit effectiveness and good governance ($r = 0.687$, $p < 0.05$). Regression analysis showed that internal audit effectiveness explained 47.2% of the variance in governance ($R^2 = 0.472$, $\beta = 0.687$, $p = 0.014$). The findings demonstrate that effective internal audits significantly enhance good governance. Strengthening auditor independence, competence, and resources is essential for improving accountability and transparency. Despite the small sample size, the study provides valuable insights for policymakers and public organizations. Future research should use larger samples and advanced statistical methods such as SEM.

***Keywords**:* Internal Audit Effectiveness, Good Governance, Public Sector, SPSS.

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Introduction

Good governance has become an essential benchmark for evaluating the performance of governments, institutions, and organizations worldwide. The concept underscores principles such as accountability, transparency, participation, efficiency, equity, and integrity, which together enhance trust between institutions and stakeholders (World Bank, 1992; OECD, 2015). In both the public and private sectors, governance is not merely about compliance with rules and regulations but about ensuring that resources are managed responsibly, decisions are made inclusively, and operations contribute to sustainable outcomes. As governance demands intensify, oversight mechanisms play a vital role in ensuring that organizations adhere to the principles of good governance. Among these mechanisms, the internal audit function has gained increasing recognition as a central pillar of governance structures (Institute of Internal Auditors [IIA], 2017). Internal audit is defined as an independent, objective assurance and consulting activity designed to add value and improve organizational operations. It achieves this by systematically evaluating risk management, internal controls, and governance processes to ensure their adequacy and effectiveness.

The effectiveness of the internal audit function is critical for achieving organizational objectives and sustaining good governance. An effective internal audit function ensures that financial reports are reliable, that organizational activities comply with laws and ethical standards, and that resources are utilized efficiently (Mihret & Yismaw, 2007). According to Arena and Azzone (2009), the effectiveness of internal auditing depends on several factors: 1) Independence and objectivity **–** auditors must be free from undue influence to provide unbiased evaluations, 2) Competence of auditors – adequate knowledge, skills, and experience are essential for effective audit practices, 3) Resource adequacy – sufficient staffing, budget, and technology enhance audit performance, adnd 4)Management support – organizational leaders must value and act on internal audit recommendations.

When these conditions are met, the internal audit function becomes a powerful mechanism for improving accountability, reducing corruption, and strengthening overall governance frameworks (Alzeban & Gwilliam, 2014).

The principles of good governance and the objectives of internal auditing are closely aligned. Good governance emphasizes accountability, transparency, participation, and effectiveness **(**OECD, 2015). Internal auditing supports these principles by Providing independent assurance that organizational policies and procedures are followed, Promoting accountability by evaluating how well resources are managed. Enhancing transparency through reliable reporting and disclosure, Supporting effectiveness by recommending improvements to processes and controls.

Several studies underscore this relationship. Cohen and Sayag (2010) found that internal audit effectiveness was strongly correlated with governance outcomes in Israeli organizations. Similarly, Christopher, Sarens, and Leung (2009) highlighted that internal audit independence enhances accountability and transparency, particularly in the public sector. In developing countries, where governance challenges are often acute, internal audit serves as a safeguard against inefficiencies, fraud, and corruption (Alzeban & Sawan, 2013).

Despite its importance, the internal audit function often struggles with challenges that undermine its effectiveness. In many organizations, particularly in the public sector of developing countries, internal audit units face limited resources, inadequate training, and lack of authority to enforce recommendations (Mihret & Yismaw, 2007). Furthermore, internal auditors may lack independence due to their reporting lines within management structures, reducing their ability to provide objective assessments (Christopher et al., 2009). These challenges not only weaken the internal audit function but also reduce its contribution to governance. Without effective auditing, risks of mismanagement, fraud, and poor accountability increase, ultimately undermining stakeholder trust and organizational credibility.

Empirical studies demonstrate the link between effective internal auditing and the realization of good governance.

1) Mihret and Yismaw (2007) showed that in Ethiopian public sector organizations, internal audit effectiveness significantly improved decision-making and accountability.
2) Alzeban and Gwilliam (2014) revealed that in Saudi Arabia, internal audit effectiveness was positively associated with governance, especially in terms of transparency and accountability.
3) Arena and Azzone (2009) emphasized that organizations with adequate resources and management support for internal auditing reported stronger governance structures.
4) Together, these studies confirm that internal audit effectiveness is not an isolated operational concern but a governance imperative.

Research Gap

While the importance of internal auditing for governance is well recognized, gaps remain in the literature. First, much of the empirical research is concentrated in developed countries, with limited evidence from developing economies where governance reforms are most critical (Alzeban & Sawan, 2013). Second, many studies adopt a narrow focus on financial accountability, overlooking broader governance dimensions such as responsiveness, rule of law, and ethical compliance. Finally, few studies integrate multiple dimensions of internal audit effectiveness with multiple indicators of good governance in a comprehensive framework. This study seeks to address these gaps by empirically analyzing how the effectiveness of the internal audit function influences good governance, taking into account a multidimensional perspective of both constructs.

The primary objective of this research is to examine the influence of internal audit effectiveness on good governance. Specifically, the study aims to:

1) Assess the current state of internal audit effectiveness in selected organizations.
2) Evaluate the extent to which good governance principles are implemented.
3) Analyze the relationship between internal audit effectiveness and good governance across multiple dimensions.

This research is expected to contribute both theoretically and practically. Theoretically, it enriches the literature by providing evidence from developing country contexts. Practically, it provides policymakers, auditors, and managers with insights into strengthening governance structures through effective internal auditing.

Literature Review

2.1 Internal Audit Effectiveness

The internal audit function (IAF) has evolved from a compliance-focused activity to a strategic governance mechanism. The Institute of Internal Auditors (IIA, 2017) defines internal auditing as an independent, objective assurance and consulting activity designed to add value and improve operations. Its effectiveness depends on multiple dimensions, including independence, auditor competence, resource adequacy, and management support (Arena & Azzone, 2009).

Cohen and Sayag (2010) argued that independence and objectivity are critical determinants of internal audit effectiveness, as auditors must operate free from management influence to evaluate governance processes accurately. Similarly, Mihret and Yismaw (2007) identified technical competence as a significant driver of effectiveness, noting that auditors must possess the skills and experience to identify risks and provide constructive recommendations. Furthermore, resource adequacy—including staff size, training, and access to technology—has been linked to audit performance outcomes (Alzeban & Gwilliam, 2014).

2.2 Good Governance

Good governance is widely recognized as a framework that emphasizes accountability, transparency, participation, effectiveness, and adherence to the rule of law (World Bank, 1992; OECD, 2015). It is a multidimensional construct that guides both public and private sector organizations toward ethical and efficient practices. Governance ensures that decision-making processes are inclusive and transparent, resource allocation is equitable, and institutions remain accountable to stakeholders (OECD, 2015).

Internal audit effectiveness contributes directly to these governance principles. For example, by monitoring compliance with regulations, internal auditors strengthen accountability. By ensuring the reliability of financial and operational information, they enhance transparency (Christopher, Sarens, & Leung, 2009). Furthermore, by evaluating internal controls and recommending improvements, internal auditing supports efficiency and responsiveness in governance structures (Alzeban & Sawan, 2013).

2.3 Empirical Studies Linking Internal Audit and Governance

A growing body of empirical evidence highlights the relationship between internal audit effectiveness and good governance. Mihret and Yismaw (2007) found that effective internal audits enhanced accountability and improved decision-making in Ethiopian public sector organizations. Alzeban and Gwilliam (2014) demonstrated similar outcomes in the Saudi public sector, where audit effectiveness was strongly associated with improved transparency and accountability.

Cohen and Sayag (2010) examined Israeli organizations and found that the perceived effectiveness of internal auditing was positively correlated with governance performance. Arena and Azzone (2009) emphasized that internal audit units with strong management support and adequate resources reported more significant contributions to governance effectiveness. Together, these studies suggest that internal auditing plays a pivotal role in institutionalizing good governance practices.

2.4 Conceptual Framework

Based on the reviewed literature, the conceptual framework of this study posits that internal audit effectiveness influences good governance. The independent variable (internal audit effectiveness) consists of four dimensions: (1) independence and objectivity, (2) competence of auditors, (3) adequacy of resources, and (4) management support. The dependent variable (good governance) is represented through principles of accountability, transparency, rule of law, responsiveness, and effectiveness.

Research Methodology

3.1 Research Design

This research adopts a quantitative descriptive design with an explanatory purpose to analyze the relationship between the effectiveness of the internal audit function and good governance. The design is appropriate because it allows testing hypotheses about the influence of one construct on another using statistical tools (Creswell, 2014).

3.2 Population and Sample

The study population consists of employees involved in internal audit and governance processes within a public sector organization. Using purposive sampling, 12 respondents were selected based on their direct role and knowledge in internal auditing and governance. The small sample size reflects an exploratory approach and is suitable for pilot-level empirical studies (Saunders, Lewis, & Thornhill, 2019).

3.3 Data Collection

Primary data were collected using a structured questionnaire adapted from prior studies (Cohen & Sayag, 2010; Arena & Azzone, 2009). All items were measured on a five-point Likert scale (1 = strongly disagree, 5 = strongly agree).

3.4 Data Analysis

Data were coded and analyzed using SPSS (Statistical Package for the Social Sciences). The following steps were applied:
Descriptive Statistics – to summarize respondents' demographic characteristics and perceptions of internal audit and governance (mean, standard deviation, and frequency).

1. Reliability Test – Cronbach's Alpha was computed to evaluate the internal consistency of measurement scales, with values above 0.70 considered acceptable (Nunnally & Bernstein, 1994).
2. Correlation Analysis – Pearson correlation was applied to examine the strength and direction of the relationship between internal audit effectiveness and good governance.
3. Regression Analysis – a simple linear regression was conducted to test the influence of internal audit effectiveness (independent variable) on good governance (dependent variable).
4. Although the number of respondents is limited, SPSS provides robust tools for analyzing small datasets, and results are interpreted with caution regarding generalizability.

3.5 Ethical Considerations

Respondents participated voluntarily and were assured of anonymity and confidentiality. Data were used strictly for academic purposes, and ethical approval was obtained prior to distribution of the questionnaire.

Results

1.

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.687[a]	.472	.419	1.775

a. Predictors: (Constant), Efektivitas Fungsi Audit Internal

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	28.167	1	28.167	8.942	.014[b]
	Residual	31.500	10	3.150		
	Total	59.667	11			

a. Dependent Variable: Good Governance
b. Predictors: (Constant), Efektivitas Fungsi Audit Internal

Coefficients[a]

Model		Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.
1	(Constant)	31.167	2.943		10.589	<.001
	Efektivitas Fungsi Audit Internal	2.167	.725	.687	2.990	.014

a. Dependent Variable: Good Governance

4.1 Correlation Analysis

The correlation results show that the effectiveness of the internal audit function (IAF) has a positive and significant correlation with good governance ($r = 0.687$, $p = 0.014 < 0.05$). This indicates that improvements in the effectiveness of internal audit functions are associated with better governance practices. Several individual indicators of the internal audit function (e.g., P6, P9) also demonstrated significant relationships with the construct of audit effectiveness, reinforcing the construct validity. On the governance side, indicators such as Y1, Y4, and Y7 had significant correlations with overall governance, suggesting that internal audit contributes particularly to accountability, transparency, and organizational integrity.

4.2 Regression Analysis

The regression analysis further confirms this relationship. The model summary indicates an R^2 of 0.472, meaning that 47.2% of the variance in good governance is explained by the effectiveness of the internal audit function. The ANOVA test shows the regression model is statistically significant ($F = 8.942$, $p = 0.014$).

The regression coefficient ($B = 2.167$, $\beta = 0.687$, $t = 2.990$, $p = 0.014$) demonstrates that internal audit effectiveness significantly influences good governance. This suggests that for every one-unit increase in audit effectiveness, good governance improves by approximately 2.167 units.

The findings of this study empirically support the theoretical proposition that effective internal audit functions are a cornerstone of organizational governance. Internal audit provides independent assurance, risk assessment, and recommendations for improvement (IIA, 2017). In this study, the strong correlation and significant regression results indicate that when internal audit functions are implemented effectively—through independence, competence, adequate resources, and systematic audit processes—they contribute meaningfully to the realization of good governance principles such as accountability, transparency, and compliance.

This result aligns with prior research. Cohen and Sayag (2010) found that effective internal auditing enhances organizational performance and control, which indirectly strengthens governance structures. Similarly, Alzeban and Gwilliam (2014) highlighted that internal audit effectiveness is positively associated with accountability and trust in public institutions. The current study, despite having a smaller sample size (12 respondents), confirms these earlier findings and provides localized evidence that supports the universal role of internal audit in promoting governance.

The R^2 value of 0.472 suggests that while the internal audit function is a critical determinant of governance quality, other factors also play significant roles, such as leadership commitment, regulatory compliance, organizational culture, and external oversight (Mihret & Yismaw, 2007). Nonetheless, the significant effect size ($\beta = 0.687$) in this study underscores that strengthening internal audit functions should be a strategic priority for organizations seeking to enhance governance practices.

Another noteworthy point is that not all indicators of internal audit correlated strongly with governance. This indicates potential areas for improvement in specific dimensions of the audit function. For example, while audit process integrity (P6) was strongly associated with effectiveness, other indicators such as independence and resource adequacy may require further organizational reinforcement to maximize impact.

Conclusion

This study concludes that the effectiveness of the internal audit function has a significant and positive influence on good governance. The findings reveal that 47.2% of governance quality can be explained by the effectiveness of internal audits. Practically, this emphasizes that strengthening internal audit independence, resourcing, and methodology will directly improve governance outcomes.

Theoretically, the results reinforce agency theory and stakeholder theory perspectives, where internal audit acts as a monitoring mechanism to reduce information asymmetry and align organizational behavior with stakeholder interests.

Future research should involve a larger sample size and possibly use structural equation modeling (SEM) to capture the multidimensional effects of internal audit on various governance constructs. Additionally, qualitative insights could enrich the understanding of contextual challenges that affect the audit-governance nexus.

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