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# The Impact of Audit Activity and Internal Control Effectiveness on Public Finance Management in Gambia

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***Abstract***

***Research aim :*** *This study addresses the impact of audit activity and internal control effectiveness on public finance management in The Gambia. Utilising empirical studies and theoretical frameworks, the study delves into the intricate dynamics of financial governance.*
***Design/Methode/Approach:*** *The study used the purposive sampling method for its specificity, allowing the selection of relevant and valuable respondents. This approach acknowledges that certain individuals or groups possess the information required by the study and, thus, choose its respondents to provide the needed data.*
***Research Finding:*** *The study highlights the crucial role played by robust internal controls and effective audit practices in fostering financial transparency, accountability, and efficiency. The findings underscore specific challenges, including management's limited commitment to implementing audit recommendations.*
***Theoretical contribution/Originality:*** *This study makes a noteworthy contribution by validating theoretical frameworks, specifically Agency, Control, and Resource Dependency theories. The empirical findings align with these theories, showcases their applicability to the dynamics of public finance management in The Gambia. This validation enhances the theoretical understanding of how audit activities and internal controls operate within the context of a developing country like the Gambia.*
***Practitionel/Policy implication:*** *To enhance financial governance, the study recommends updating the Public Finance Act, developing a policy for audit recommendation implementation, empowering internal audit units, and establishing an investigative institution.*
***Research limitation:*** *The small sample size constraints may introduce potential biases, and the perspectives expressed may not fully represent the diversity of viewpoints in Gambia's public finance management and lack generalization potentials.*
***Keywords : Audit, Internal Control, Public Finance, Public Finance Management***

## 1. Introduction

Public finance management is critical to sustainable development and economic growth in any country. Effective public finance management requires transparency, accountability, and efficient utilisation of public resources. However, poor management of public finances can lead to corruption, misappropriation of funds, and poor service delivery. Despite being in power for the last six years, the current government has made little progress in resolving the political, social, and economic challenges plaguing the Gambia. Political and economic experts warned that the country remains unstable and prone to crisis, particularly regarding corruption, transitional justice, and major reforms needed to foster sustainable socio-economic and political development, national reconstruction, and integration (Omotosho & Senghore, 2018). Like many developing countries, the Gambia has struggled with public finance management issues for many years. The country has experienced significant challenges in managing public resources, including poor budgeting, inadequate financial reporting, and lack of transparency and accountability. These challenges have adversely affected the country's economy and social development (Sallah, 1990). The Gambian government has implemented various reforms to address issues to improve public finance management. One of these reforms includes strengthening audit activity and internal control effectiveness. Audit involves examining financial records, transactions, and procedures to determine whether they comply with established policies and procedures. On the other hand, internal control effectiveness refers to the efficiency and effectiveness of internal controls in ensuring the reliability of financial information and compliance with laws and regulations (The Institute of Internal Auditors [IIA], 2017).

Public Finance Management refers to the processes, systems, and policies that manage government financial resources. Challenges in PFM in countries like The Gambia include weak expenditure controls, limited transparency, and risks of corruption. Effective PFM systems enhance resource allocation, accountability, and government efficiency. According to Lawson (2015), robust PFM frameworks mobilise revenue, allocate public funds, and conduct financial audits, thus improving service delivery and minimising corruption. Internal audit as defined by the Gambia Financial Regulation (2016), is an independent and objective activity aimed at improving governance, risk management, and internal control. It plays a crucial role in promoting sound governance by assessing the responsible management of public resources, which enhances accountability and operational improvements. Empirical studies (Mihret & Yismaw, 2007; Mwanza, 2022) highlight the importance of organisational support, auditor competence, and effective communication for audit success in the public sector. Internal and external audits are complementary but distinct. While internal audit focuses on enhancing organisational controls, external audit provides independent assurance on the accuracy of financial statements and internal control effectiveness. Coordination between both audits can improve efficiency and accountability. Various studies emphasise that strong audit activity and internal control mechanisms enhance public finance management by improving accountability and reducing financial mismanagement as in Diamond (2002) and Mwanza (2022) affirms that effective auditing leads to better financial transparency and control in the public sector.

The agency theory theory explains the principal-agent relationship, where the government (principal) delegates financial management responsibilities to public officials (agents). There is a risk of misalignment between the interests of principals and agents, leading to financial mismanagement. Internal audits and control mechanisms help mitigate this by enforcing accountability and transparency, aligning the interests of public officials with the government's goals (Adams, 1994). The control theory focuses on the mechanisms organizations use to ensure that their activities align with objectives. It categorizes control into input, process, and output controls, emphasizing the importance of balanced and adaptive controls to minimize deviations from desired outcomes (Simmons, 1997). Effective internal control systems help governments manage public resources efficiently. The resource dependency theory highlights the reliance of organizations on external resources to achieve their objectives. In public finance management, government institutions depend on financial resources, expertise, and technology, often influenced by external factors (Davis & Cobb, 2010). Effective internal auditing and financial management help mitigate risks associated with resource dependencies and improve organizational performance.

The previous studies largely focus on compliance-based evaluation of auditing, and there is a need for more comprehensive research that assesses the broader impact of audits on governance and financial performance over time. Furthermore, limited empirical studies exist that explore internal audit effectiveness across different cultural and institutional contexts. The effectiveness of audit activity and internal controls is critical to improving public finance management in the Gambia. However, there is a lack of empirical evidence on the impact of these mechanisms on public finance management in the country (Aikins, 2011). This study seeks to fill this gap by examining the impact of audit activity and internal control effectiveness on public finance management in the Gambia. In doing so, the study objective is to provide insights that can inform policy and practice on improving public finance management in the country. The study examined the impact of Audit activity and internal control effectiveness on public finance management in The Gambia.

### 1.1. Statement of Problem

Around the globe, especially in Africa, most countries face the challenges of fraud, mismanagement of public funds, corruption, embezzlement, and ineffective and inefficient management of government projects and funds within public institutions (Campos & Pradhan, 2007). The Current Gambia Government has made little or no effort to fight corruption in the country. The annual audit report of the Auditor General (National Audit Office) and the Directorate of Internal Audit from 2017 to 2022 fiscal year indicated that most of the Ministries, Departments, Agencies, Parastatals, State-owned Enterprises (SoEs) and Local Government Authorities (LGAs) are mismanaging and misappropriating government funds. The improvements in financial management and compliance with laws and regulations and the introduction of effective internal control in government Ministries, Departments, Agencies, Parastatals, SoEs and LGAs remain minimal despite these entities being in charge of implementing key Government programs. From 2017 to 2021, there is a huge reluctance from the senior management of public institutions to implement audit recommendations (Conteh & Hamidah, 2021). Therefore, the above issues from the research problem have been examined to determine the impact of audit and effectiveness of internal control on public finance management, given that most government institutions still have shortfalls in the management of public finances. The study specifically addresses the state of audit activity in the Gambia's public finance management and assess its effectiveness in promoting financial transparency and accountability; existing internal control mechanisms in the Gambia's public finance management and determine their effectiveness in preventing fraud, mismanagement, and financial irregularities; the relationship between audit activity, internal control effectiveness, and the overall efficiency of public resource allocation and utilisation in the Gambia and management's reluctance to implement audit recommendations and its effects on public finance management in the Gambia.

### 1.2. Research Objectives

The specific objectives of the study are to:

a. Identify the current state of audit activity in the Gambia's public finance management and assess its effectiveness in promoting financial transparency and accountability.
b. Evaluate the existing internal control mechanisms in the Gambia's public finance management and determine their effectiveness in preventing fraud, mismanagement, and financial irregularities.
c. Analyse the relationship between audit activity, internal control effectiveness, and the overall efficiency of public resource allocation and utilization in the Gambia.
d. Investigate into management's reluctance in implementing audit recommendations and its effects on public finance management in the Gambia.

## 2. Method

This study adopts a quantitative approach to examine the cause-effect relationship between audit activity, internal control effectiveness, and public finance management in The Gambia. The study utilises a descriptive research design, aiming to explain the impact of audit activities and internal control mechanisms on the management of public finances within selected government institutions, including Ministries, Area Councils, and State-Owned Enterprises. The study measures three key variables:

**Audit Activity**: This variable encompasses the processes and procedures for examining and evaluating financial records, transactions, and internal control systems. Measures include the number of audits performed annually, the types of audits conducted (financial, performance, compliance), the depth and coverage of audit procedures, and the timeliness of audit reports and management responses.

**Internal Control Effectiveness**: This variable assesses the efficiency of internal control mechanisms in safeguarding assets, ensuring compliance, and promoting operational efficiency. Key measures include the existence and implementation of documented internal control policies and procedures, segregation of duties, financial management personnel's competency and training, and monitoring activities' effectiveness.

**Public Finance Management**: As the dependent variable, this involves government entities' overall management and utilisation of public funds and resources. The study evaluates budget execution, revenue collection efficiency, expenditure control, procurement practices, and accountability and transparency in financial transactions.

Data was collected through questionnaires distributed to senior employees responsible for finance, accounting, procurement, and auditing within public institutions. A total of 50 questionnaires were designed and distributed specifically to personnel employees (permanent secretaries and directors) of government ministries and agencies involved in public finance management. The data analysis techniques involves both descriptive and inferential statistics. The hypotheses were tested through correlation analysis, and regression analysis to explore the relationship between the dependent and independent variables.

## 3. Results and Discussion

The study targeted a sample of 50 senior employees respondents, and the achieved response rate was commendable, with 42 individuals participated in the research by responding to the questionnaires. This represents 84% response rate and as noted by Saunders, (2012), a response rate exceeding 35% is deemed acceptable. The 84% response rate highlights the robustness of the collected data and enhances the credibility of the study's findings.

The study's gender distribution is characterized by a predominant representation of males, constituting 64% of the respondents, with a total of 27 male participants. In contrast, females make up 36% of the respondents, equivalent to 15 female participants. This gender distribution is designed to establish a representative sample, minimizing the potential for gender bias in the study.

In order to establish the relationship between audit activity, internal control effectiveness, and the overall efficiency of public resource allocation and utilization in the Gambia requires the adoption of correlational and regressional analysis as the main thrust of the study the results and explanation of which is as follows.

Table 1. Correlation Analysis Between Audit Effectiveness, Internal Control Effectiveness and Public Finance Management.

| | **Public Finance Management** | **Audit Effectiveness** | **Internal Control Effectiveness** |
|---|---|---|---|
| Public Finance Management | 1 | | |
| Audit Effectiveness | 0.331790669 | 1 | |
| Internal Control Effectiveness | 0.697132936 | 0.128358692 | 1 |

Sources: Authors' Computation (2024)

A strong positive correlation between internal control effectiveness and public finance management (PFM) in The Gambia would suggest that as internal control systems improve, public finance management outcomes also improve in a directly proportional way. The following factors could explain this:

*Improved Accountability and Transparency*: Internal control mechanisms are designed to ensure that financial transactions are properly recorded, monitored, and reported. In the context of The Gambia, improved internal controls would increase transparency in how public funds are used. With greater transparency, public finance management becomes more efficient, reducing opportunities for misuse of funds or corruption. This leads to better budgetary outcomes and resource allocation, hence the strong positive correlation.

*Reduced Financial Mismanagement*: Strong internal controls help detect and prevent fraud in financial processes. In a system with effective internal controls, irregularities such as overspending, unauthorized transactions, or misallocation of resources are minimized. This directly strengthens public finance management by ensuring that public funds are used for their intended purposes, improving financial sustainability and trust in government institutions.

*Compliance with Financial Regulations*: Internal control systems promote compliance with established financial laws, regulations and policies. In The Gambia, adherence to financial rules and regulations ensures that public spending aligns with national development goals and international standards. Proper internal control helps the government meet its fiscal targets, leading to better-managed public finances.

*Increased Donor Confidence*: Strong internal controls instil confidence in external donors and investors. Like many developing countries, the Gambia relies on external funding for many public finance projects. When internal control systems are robust, donors are more likely to support initiatives, knowing their funds will be managed properly, thus strengthening the public finance system.

Finally, the strong positive correlation between internal control and public finance management in The Gambia reflects the significant role that internal controls play in ensuring efficient, transparent, and effective use of public funds. Strengthening internal control frameworks leads to more reliable financial information, reduced corruption, and better overall management of public resources, all of which enhance public finance management outcomes.

The weak correlation between audit effectiveness and public finance management in The Gambia highlights the challenges in translating audit findings into tangible improvements in financial practices. Factors like poor implementation of audit recommendations, insufficient audit capacity, political interference, and lack of public engagement reduce the potential impact of even effective audits on public finance management. To strengthen the correlation, The Gambia would need to focus on enforcing audit recommendations, increasing audit scope and frequency and improving the transparency and accountability of its public finance management systems.

The very weak correlation between internal control and audit effectiveness in The Gambia can be attributed to several factors, such as the lack of integration between these processes, narrow internal control scopes, independent auditing practices, and inconsistent implementation of controls. To strengthen the relationship between internal control and audit effectiveness, there needs to be better alignment between internal control systems and audit frameworks and greater attention to the quality and consistency of internal controls across institutions. Additionally, auditors and internal control managers could collaborate more closely to ensure that internal controls support effective and efficient audits.

Table 2. Regression Analysis of Public Finance Management (Y) on Audit Activity ($X_1$) and Internal Control ($X_2$)

| *Regression Statistics* | |
|---|---|
| Multiple R | 0.73870891 |
| R Square | 0.54569086 |
| Adjusted R Square | 0.52239295 |
| Standard Error | 0.66636849 |
| Observations | 42 |

| ANOVA | *df* | *SS* | *MS* | *F* | *Significance F* |
|---|---|---|---|---|---|
| Regression | 2 | 20.80121585 | 10.40061 | 23.4223149 | 0.00000021 |
| Residual | 39 | 17.31783177 | 0.444047 | | |
| Total | 41 | 38.11904762 | | | |

| | *Coefficients* | *Standard Error* | *t Stat* | *P-value* |
|---|---|---|---|---|
| Intercept | 0.72251205 | 0.586190747 | 1.232555 | 0.22512082 |
| Audit Activity ($X_1$) | 0.22680976 | 0.100191443 | 2.263764 | 0.02922846 |
| Internal Control ($X_2$ | 0.62418642 | 0.102073008 | 6.115098 | 0.00000036 |

Multiple R (0.7387)**:** This is the correlation coefficient that shows the strength of the linear relationship between public financial management and independent variables, i.e., audit activity and internal control. A value of 0.7387 indicates a strong positive relationship. R-Square (0.5457)**:** The coefficient of determination shows that approximately 54.57% of the variance in public finance management is explained by the independent variables of audit activity and internal control. Thus, this suggests a moderately good fit for the model. The adjusted R Square for the number of predictors in the model. It is slightly lower than R Square (52.24%), showing that when adjusted for the number of predictors, the model still explains a significant amount of the variance in the dependent variable (public finance management).

The regression equation can be written as:

**Y = 0.7225 + 0.2268(X1) + 0.6242(X2) + Ɛ**

Intercept (0.7225)**:** This is the predicted value of the dependent variable when both audit activity and internal control are zero. In this case, when all predictors are zero, the dependent variable would be approximately 0.7225. audit activity coefficient (0.2268)**:** For every one-unit increase in audit activity, holding internal control constant, the dependent variable increases by 0.2268. The P-value (0.0292) is less than 0.05, indicating that audit activity has a statistically significant relationship with the dependent variable. Internal control coefficient (0.6242)**:** For every one-unit increase in internal control, holding audit activity constant, the dependent variable increases by 0.6242. The P-value is extremely small, meaning internal control is highly significant in explaining the dependent variable.

Finally, The model explains about 54.57% of the variability in the dependent variable ($R^2$ = 0.5457). Both predictors, audit activity and internal control, have significant positive relationships with the dependent variable, but internal control has a much stronger influence (coefficient = 0.6242) compared to audit activity (coefficient = 0.2268). Overall, the model is statistically significant, as indicated by the F-statistic and the significance of the individual predictors. The intercept suggests that even when both predictors are zero, the dependent variable would have a base value of approximately 0.7225.

Table 3. Correlation Analysis between Internal Control, Management Responsiveness and Implementation of Audit Recommendations.

| | **Internal Control** | **Management Responsiveness** | **Implementation of Audit Recommendations** |
|---|---|---|---|
| Internal Control | 1 | | |
| Management Responsiveness | 0.10993746 | 1 | |
| Implementation Audit Recommendations | 0.143794029 | 0.17541488 | 1 |

Source: Authors' Computation (2024)

A very weak correlation between internal control and management responsiveness in The Gambia suggests that improvements in internal controls do not significantly influence how management responds to issues, risks, or opportunities. Several factors could explain why this correlation is weak despite internal control systems generally being designed to improve organizational accountability and responsiveness. Here are possible reasons for this weak relationship.

Internal Control Systems May Not Be Linked to Decision-Making: In many cases, internal control systems focus on ensuring compliance with rules and regulations, detecting errors, and preventing fraud rather than being used to inform management decisions. If management views internal controls merely as a regulatory requirement rather than a tool for improving operations, they may be slow to respond to the risks or insights identified by these controls, leading to a weak correlation.

Lack of Timely Information Flow: For internal controls to influence management responsiveness, they must provide timely and accurate information that management can act upon. If there are delays in reporting or communication breakdowns between internal control departments and management, the controls may not effectively prompt quick or meaningful responses. This would weaken the impact of internal controls on management responsiveness.

Lack of a Culture of Accountability: A weak organizational culture of accountability could explain why management is slow to respond to internal control findings. In some public or private institutions, there may be a lack of emphasis on taking corrective action or being accountable for financial or operational risks. If management does not feel pressured to act on internal control information, the responsiveness remains weak, resulting in a very weak correlation.

Political or Bureaucratic Constraints: In public sector settings like The Gambia, management responsiveness may be hindered by political or bureaucratic constraints. Even when internal controls identify urgent issues, management may be constrained by political considerations, legal requirements, or slow bureaucratic processes that delay action. This can reduce the effectiveness of internal controls in driving timely responses, contributing to the weak correlation.

The very weak correlation between internal control and the implementation of audit recommendations in The Gambia can be attributed to several factors, including misalignment between the focus of internal controls and audit recommendations, resource constraints, management resistance, political and bureaucratic barriers, and poor communication. To strengthen this relationship, it is important to ensure that internal controls are continuously updated to reflect audit recommendations, that resources are available for implementation, and that there is a culture of accountability and cooperation between auditors and management.

The very weak correlation between management responsiveness and the implementation of audit recommendations in The Gambia can be associated with several factors, including a lack of resources, competing priorities, bureaucratic or political obstacles, and organizational resistance to change. Management might respond to audit findings on the surface but face significant challenges in translating that responsiveness into action. There needs to be better alignment between management’s responsiveness and capacity for action, stronger accountability frameworks, and more systematic follow-up on audit recommendations.

Table 4. Regression Analysis of Internal Control (Y) on Management Responsiveness ($X_1$) and Implementation of Audit Recommendations ($X_2$)

| *Regression Statistics* | |
|---|---|
| Multiple R | 0.167573837 |
| R Square | 0.028080991 |
| Adjusted R Square | -0.02176101 |
| Standard Error | 1.099124722 |
| Observations | 42 |

ANOVA

| | *df* | *SS* | *MS* | *F* | *Significance F* |
|---|---|---|---|---|---|
| Regression | 2 | 1.361259466 | 0.680629733 | 0.563400158 | 0.573834278 |
| Residual | 39 | 47.11493101 | 1.208075154 | | |
| Total | 41 | 48.47619048 | | | |

| | *Coefficients* | *Standard Error* | *t Stat* | *P-value* |
|---|---|---|---|---|
| Intercept | 3.100747707 | 0.422510809 | 7.338860078 | 0.000000007 |
| Management Respoı | 0.090572728 | 0.166164833 | 0.545077597 | 0.588803983 |
| Implementing Audit | 0.119016419 | 0.148559675 | 0.801135428 | 0.427907284 |

Souces: Author’s Computation (2024)

The regression output contains key statistical measures that help interpret the relationship between Management Responsiveness ($X_1$), Implementation of Audit Recommendations ($X_2$), and the dependent variable.

Multiple R (0.1676): This represents the correlation between the predicted and actual values of the dependent variable. A value of 0.1676 indicates a very weak positive correlation, meaning that the independent variables (management responsiveness and implementation of audit recommendations) have little relationship with the dependent variable. R-squared represents the proportion of the variance in the dependent variable that is explained by the independent variables, i.e., management responsiveness and implementation of audit recommendations. Here, only 2.81% of the variation in the dependent variable is explained by management responsiveness and implementation of audit recommendations, which is very low. Adjusted R Square (-0.0218): This value adjusts R-squared for the number of predictors in the model. A negative adjusted R-squared suggests that the model performs worse than just using the mean as a prediction. This further confirms that the independent variables do not explain the dependent variable well.

Intercept (3.1007): This is the predicted value of the dependent variable when all the independent variables are 0. It suggests that if management responsiveness and implementation of audit recommendations were 0, the predicted value of the dependent variable would be approximately 3.1. Management Responsiveness ($X_1$) (0.0906, p-value = 0.5888): The coefficient of 0.0906 means that for every one-unit increase in management responsiveness, the dependent variable is expected to increase by 0.0906 units, assuming all other variables remain constant. However, the p-value (0.5888) is much greater than 0.05, indicating that this relationship is not statistically significant. Implementing Audit Recommendations (X2) (0.1190, p-value = 0.4279): The coefficient of 0.1190 suggests that for every one-unit increase in the implementation of audit recommendations, the dependent variable is expected to increase by 0.1190 units, assuming other variables are constant. However, the p-value (0.4279) is also much greater than 0.05, showing that this relationship is not statistically significant either.

Overall model is not statistically significant (Significance F = 0.5738), meaning that neither management responsiveness nor implementation of audit recommendations significantly explains the dependent variable. Both independent variables, management responsiveness (p = 0.5888) and implementation of audit recommendations (p = 0.4279), do not have a statistically significant relationship with the dependent variable. R-squared is very low (2.81%), indicating that the model does a poor job of explaining the variation in the dependent variable. The results suggest that management responsiveness and implementation of audit recommendations have a very weak and no significant effect on the dependent variable. This implies that other factors not included in the model might better explain the variation in the dependent variable.

## 4. Conclusion

The study's objectives have been thoroughly addressed through an analysis of empirical data collected via questionnaires. The results indicate that both control effectiveness and audit activity are crucial in influencing public finance management. The findings emphasize the significant impact of robust internal controls and effective audit practices on enhancing financial transparency, accountability, and efficiency in managing public resources.

The literature supports these findings, highlighting a positive correlation between effective audit activities and improved financial management practices. For instance, Diamond (2002) underscores that strong internal controls and audit mechanisms contribute to better financial management and transparency. Similarly, Mihret and Yismaw (2007) find that internal audit effectiveness is critical in promoting accountability and operational improvements in public sector organizations. However, the study did not find statistically significant evidence supporting the negative impact of the second hypothesis. This discrepancy suggests that the relationship between audit activity, internal control effectiveness, and public finance management is complex and context specific. As noted by Mihret and Yismaw (2007), various factors can influence audit outcomes and their impact on financial management, indicating a need for further investigation into these dynamics, particularly within the context of The Gambia.

A significant issue highlighted by the responses is the lack of management commitment to implementing audit recommendations. Respondents expressed concerns about inadequate management engagement in leveraging audit findings to improve financial management. This aligns with Agency Theory, which addresses conflicts of interest between principals (e.g., government entities) and agents (e.g., public officials), shedding light on challenges related to management commitment and the alignment of interests (Adams, 1994). In the public sector, the importance of a robust internal control framework is emphasized in the literature. Effective internal controls are essential for assessing and measuring performance, as well as for evaluating the broader impact of audit activities on public finance management (Simmons, 1997). The theoretical framework integrating Agency Theory, Control Theory, and Resource Dependency Theory provides a comprehensive understanding of the factors influencing audit activity and internal control effectiveness. This framework helps identify underlying mechanisms, challenges, and opportunities, and forms the basis for developing hypotheses, research questions, and analytical frameworks for further empirical investigation.

These detailed insights derived from the objectives and the literature review contribute to a more comprehensive understanding of the challenges and opportunities inherent in public finance management in The Gambia. The diverse nature of the findings suggests that future strategies for improvement should consider a holistic approach, addressing not only the technical aspects of internal controls and audit activities but also the organisational and managerial commitment essential for successful financial governance. The existing gaps in the literature, as identified in the literature review, further emphasise the need for continued research to fill these voids and enhance our understanding of the complex dynamics involved in public finance management.

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