

Internal audit in the federal organizations of Malaysia: is there light at the end of the long dark tunnel?

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ABSTRACT

Internal audit is supposed to help members of organizations to improve their business activities. But the findings from in-depth interviews with internal auditors from a total of 40 federal government ministries, departments and agencies in Malaysia, conducted in the middle of 2004, have revealed a number of serious shortcomings. Most notable of these shortcomings are that many internal audit units have a shortage of staff, and that the audit staff lack internal audit skills. In addition, a majority of the audit units still employ outdated audit practices, and have failed to get the right level of support and assistance from the Treasury. Worse still, their operational effectiveness and efficiency is threatened by the high-handed conduct of the National Audit Department which arbitrarily and unilaterally shuffles staff between the body and internal audit units. With national and public sector surrounding leaving much to be desired for in regard to transparency and public accountability of the major actors and the fact that Malaysia is a large power distance society, it may not be too far fetch to expect the internal audit quagmire to continue to take place into the foreseeable future.

Key words

Internal audit; federal government organizations; in-depth interviews; Malaysia

INTRODUCTION

The history of modern internal auditing effectively starts in 1941 when the Institute of Internal Auditors (IIA) was formed in the United States of America. This professional body has, for well over half a century, published standards and a code of ethics for the practice of internal auditing. Today, these standards and the code are in use in thousands of organizations in more than 100 countries, across all business and public sectors (Ridley & Chambers 1998:xxix-xxx). Unfortunately, as noted by Ridley and Chambers (1998:3), many organizations have failed to bring significant change to their internal auditing practices. They state (p. 3): "True, there are now more internal audit units; yet most of their practices are still based on fundamental auditing principles, as developed in the early years of the twentieth century." They also specifically note the following (p. 3): "Despite a 1990s focus on rapid change within many organizations, in some internal audit units technology has still not penetrated deeply into auditing practices, while in

others internal auditors are still not seen as part of the management team."

In Malaysia, a catalogue of ongoing organizational failures and mismanagement highlight both the need for, and current general lack of effectiveness of internal audit in both the public and private sectors. To date, there have been several research reports on the status of internal audit in general. However, there are none that specifically probe the nation's public sector. (The exception is perhaps in regard to internal audit at the level of state and local governments. See below.) This is despite it being the well documented responsibility of the management of public sector organizations to maintain an effective system of internal control, including the use of the internal audit function (e.g. Dowsett & Morris 1981; Buttery 1985; Coombs & Jenkins 1994; Jones & Pendlebury 2000). And this has also arisen in spite of the requirement that the public sector entities in Malaysia have an internal audit function which was published as early as 1979 in the form of Treasury Circular No. 2: Implementation of Internal Auditing in Federal

Government Agencies and which was replaced in October 2004 with Circular No. 9: Implementation of Internal Auditing in Federal Ministries and Departments and State Governments (*New Straits Times* 18 December 2004).

This new circular is directed at not just the relevant parties in the federal government but also those in the state governments. It is noticeable that the new circular (which may be found in the Treasury website: www.treasury.gov.com) has nearly twice as many paragraphs as the old one. Reading just a few paragraphs one becomes conscious of the strong desire of the authorities to achieve a marked improvement in internal audit practice in the public sector.

However, regardless of the 1979 and 2004 Treasury Circulars, it should be obvious that the need for a review of the current state of internal audit operations in the federal government is long overdue. Such a review could lead to the identification of problems and obstacles that have confronted, and continue to confront internal audit, and thereby focus efforts on achieving more substantial reform than the mere issuance of an official document such as the new (2004) internal audit circular. Further justification for such a study arises from the nation's need to find ways to be more competitive in all sectors of the economy following the implementation of the Asean Free Trade Area (AFTA) in early 2003. Internal audit that achieves its potential may actually be one of the tools for all sectors to employ in their pursuit of such competitiveness.

LITERATURE REVIEW

In public sector organizations, the internal audit function holds high potential for promoting accountability and improving government performance. Thus, not surprisingly, several countries have developed policies aimed at strengthening public sector internal audit functions to enhance their capacity for contributing to these goals (Auditor-General of Australia 1990; Office of the Auditor General of Canada 1993 & 1996; Light 1993; Newcomer 1994 & 1998). Policy measures include the following: requiring the establishment of internal audit units; establishment of standards for the professional conduct of audit work; training; resource allocation; expanding reporting arrangements and broadening mandates to make auditors responsible for performance assessment. Also, the understanding that internal auditing is an important tool for accountability has led, in the case of the United States, to the traditional internal audit functions being transferred to Inspectors-General who report findings to both the Executive and to Congress. Thus, in the United States, internal audit is currently also a tool for external accountability - no more a mere tool of internal accountability intended to aid senior management of the government organizations.

Nonetheless, available evidence on the reality of internal audit operations in recent time provides the picture that shows there is much room for improvement. In the United States, Canada and

Australia, the common findings include: inadequate audit coverage, particularly of areas of major significance and high risk; a tendency to focus audits on compliance and regularity to the detriment of the performance of audits of economy, efficiency and effectiveness; and little attention being given to audit findings within agencies by senior managers. Furthermore, in Canada and Australia there exist deficiencies in the professional qualifications of audit staff and in the involvement of senior management in audit planning. As for the United States, based upon his study of the work of the nation's Inspectors General, Light (1993:224) concludes that "government appears no more accountable today than before the IG Act."

As is perhaps to be expected, the dichotomy of internal audit ideals and their realities do not just exist in these three developed western countries. This is easily deduced from research conducted in recent years in their counterparts in the developing world: Sudan, Israel and South Africa. In fact, the situation may be considered extremely bad in Sudan.

As noted by Brierley *et al* (2001:73-4), in the developing country of Sudan, in North Africa, the typical internal audit department is largely engaged in the routine authorisation of transactions, is staffed by inexperienced and untrained personnel, and has insufficient credibility, independence and authority to act in the manner expected of internal audit personnel. Employing interview and observation research methods, Brierley concludes that in the few places where internal audit may be in operation, it has failed to meet any one of the five core standards of the Institute of Internal Auditors (IIA 1979) in terms of independence, professional proficiency, scope of work, performance and management.

As for Israel, the picture of internal audit in the public sector is also not that encouraging even though it may not be as bad as in Sudan. As noted Schwartz and Sulitzeanu-Kenan (2002), in that country the recent efforts to strengthen internal auditing through top-down legislation "... have not significantly improved the overall performance of audit units in the lion's share of ministries and statutory authorities." After employing a variety of research methods, including in-depth interviews with 25 internal audit units of government ministries and statutory authorities in order to collect the data, they conclude that internal audit units operate "well below reasonable capacity and accepted practices."

Finally, as far as South Africa is concerned, the *Public Finance Management Act* (PFMA 2000) places a statutory duty on public sector organizations such as national and provincial departments, public entities and Constitutional Institutions to establish and maintain an internal audit function. This internal audit requirement is complemented by more detail requirements in the *Treasury Regulations* (2004) which are issued in terms of the PFMA. Quite recently, National Treasury, as the body assigned with the duty to oversee the implementation, has noted the following regarding the development of the internal audit functions (Nair 2008):

During July/August 2006, the National Treasury conducted a survey amongst all National and Provincial Departments to determine aspects relating to the functioning of their internal audit functions and audit committees. The survey revealed that most departments met the legislative prescripts related to internal audit and audit committees. It was, however, notable that several vacancies still exist within internal audit units whilst it was also found in several instances that the positions of Chief Audit Executive were also not at an appropriate level of seniority.

In Malaysia very little is known on the state of internal audit in the public sector. The same may also be said for internal audit in the private sector. To date, there appear to have been very few research studies conducted. What was possibly the first one was conducted by the Malaysian Institute of Accountants (MIA) in June 1988 – less than a year after the statutory body was activated in September 1987 (MIA 1989). The study involved the sending out of questionnaires to the heads of internal audit of 658 organizations across private and government sectors, and including all companies listed at the Kuala Lumpur Stock Exchange (KLSE) (now, Bursa Malaysia). The response rate was 37 percent (241 organizations). The outcome of this study was published as Report No. 1, issued in July 1989. Following the publication of this report, the MIA in August 1989, conducted another study which it says was more in-depth than the earlier one (MIA 1991).

In the second study two sets of questionnaires were sent out: one to internal audit managers and another to chief executives. The 106 responses (19 percent) were received from the internal audit managers and 133 (24 percent) from the chief executives. The ensuing Report No. 2, issued in January 1991, discloses that these questionnaires were sent to 555 organizations covering both listed and unlisted companies, statutory authorities and government departments (MIA 1991:3). In contrast to Report No. 1, it does not disclose how many from the government sector actually responded. It also appears that the report was defective in that it glossed over various issues uncovered by the study, issues such as the definition of the areas within an organization covered by the internal auditors. In an attempt to justify the almost primitive internal audit function Malaysia had then, the MIA somewhat evasively described the activity as an “emerging one” (p. 2) and an “emerging profession” (p.10).

Besides these two studies conducted by the MIA in late 1980s, there appears to be just another two studies conducted in the next decade. One was by a group of Australian academics (Mathews *et al* 1995) on internal audit in both private and government organizations (and which later was used in a benchmarking study by Cooper *et al* 1994), and another in late 1999 by a joint effort between the audit firm Ernst & Young, the Malaysian Institute of Corporate Governance (MICG), and the Institute of Internal Auditors Malaysia (IIAM) (Ernst & Young *et al* 2000). The latter investigated internal audit in companies listed at the KLSE and Malaysian

Exchange of Securities Dealing & Automated Quotation Bhd. (MESDAQ). While the MIA studies were concerned with an “overview” of internal audit, the next two focused on the nation’s internal audit “profile”. But just like the MIA studies, the latter two studies do not really provide much detailed information of the actual operation of internal audit in Malaysia.

In recent years, a team of researchers headed by the one conducting the present study had embarked upon a similar study on internal audit in the state and local governments of Malaysia (Azham *et al* 2007). The findings from in-depth interviews conducted with internal auditors from 35 state and local governmental bodies (SLoGBs) located in Peninsular Malaysia in the third quarter of 2003 show that the audit function faces numerous challenges. This is in addition to the fact that a mere 35 out of the then 202 SLoGBs had an internal audit capacity. The problems range from staff, skills and training shortages to premeditated obstruction of the auditors in their attempts to perform their duties.

All in all, it is probably not an exaggeration to say that major questions have remained unanswered when it concerns the practice of internal audit in the nation’s federal government. This is simply not conducive to any serious effort to squarely face the challenges of globalisation. Thus, this study shall attempt to shine a light into that “black hole” of understanding, thereby contributing to real and sustained efforts for national development.

There are numerous models for this type of study besides the ones conducted on Sudan and on Israel mentioned earlier. Among the notable recent research projects, found through search made through internet, are those taking place in Canada (Canadian Treasury Board Secretariat 2000) and Malta (National Audit Office 2000).

RESEARCH OBJECTIVES

The present study of internal audit in federal government ministries, departments and agencies is number two in a series of three studies which is concerned with the internal audit function in Malaysia’s public sector. Its primary objective is to delineate audit weaknesses found in the organization. Following this description of audit weaknesses, there is an attempt to explain the reasons for their occurrence.

RESEARCH DESIGN

Population and survey sample

The government hierarchy has three levels: federal, state and local. Local governments include the city, town and local councils, depending on the territory’s population. As mentioned above, a previous internal audit study conducted by the authors covered the state and local governments located in Peninsular Malaysia (see Azham *et al* 2007). The current study covers internal audit operation found in 40 organizations forming a large section of the federal

government: 22 ministries, 9 departments and 9 agencies. (See Appendix A for the list of the organizations.)

Methods of data collection

The main form of data collection was through face-to-face interviews with the internal auditors in the federal government organizations. (Appendix B provides the list of positions held by these auditors.) Out of a total of 40 auditors interviewed, 27 or more than two thirds hold the post of head of the internal audit unit or department.

There are four parts to the questionnaire: (A) Background information; (B) Organizational Audit Practice; (C) Efforts in Support of Organizational Audit Practice; and (D) Internal Audit in the Organization and Government Sector as a Whole. There are a total of 60 questions: 51 close-ended structured type (Parts B and C) and 9 open-ended semi-structured type (Part D). A total of 12 of the close-ended questions have more than one sub-part - (a), (b), etc. - to them. A majority of the close-ended questions also have spaces for participants to express their (unstructured) comments.

In regard to the categories of questions asked, the close-ended, structured type questions (Sections B and C) are concerned with the following: *facts*, such as the number of internal audit staff; *perceptions*, such as knowledge elements needed by internal auditors to ensure the fulfillment of their present roles; and, the *extent of agreement with various statements*. As for the open-ended, semi-structured type of questions (Section D), they may be divided into three categories: the history and future of internal audit operation in the organization; weaknesses and strengths of the internal audit unit in the organization; obstacles and potential for change in the operation of internal audit in the public sector as a whole.

Numerous resources were referred to in developing this questionnaire. For details, see Appendix A in Azham et al (2007).

FINDINGS

Arising from the face-to-face interviews conducted with internal auditors (the majority working in audit units, and a small minority working in audit departments) through May, June and July of 2004, a number of discouraging facts were discovered. These were primarily concerned with staff shortages in the audit units, and the level of competence in internal audit functions. But other issues were also identified. Overall, it was apparent that there is much room for improvement in the practice of internal audit in the federal organizations.

Staff shortage

As can be seen in Table 1, forty percent of the units have five or fewer personnel.

Table 1: Audit personnel available

	Total	%
Fewer than 3	2	5.00
Between 3 and 5	14	35.00
Between 6 and 10	11	27.50
Over 11 people	12	30.00
Total	40	100.00

Thus, not surprisingly, many auditors interviewed were not happy with the number of audit staff. To be more exact, seventy percent of the auditors interviewed claimed that they had insufficient staff members for them to be able to successfully perform their duties. See Table 2.

Table 2: Audit personnel sufficiency

	Total	%
Yes	12	30.00
No	28	70.00
Total	40	100.00

Among those experiencing staff shortages, one auditor said:

The shortage of staff is so severe and this has affected the operation of the internal audit department itself.

In an open-ended part of the interview, the same person said that due to the staff shortage, which is at a "critical" level, the audit unit failed to cover the broad audit scope in its operation. Another auditor mentioned that the main problem faced by the unit was related to broad audit coverage, or too many parts of the organization which need to be audited in comparison to the number of staff in the audit unit. As a result, not all parts of the organization could undergo the broader audit scope. Yet another auditor said that the unit was not able to do a more comprehensive audit due to the staff shortage. He or she said that many audit programs, ideas, and other components of the audit plan were not implemented because of staff shortages.

A question may be asked as to the kind of audit that these auditors are able to perform, given their limited staff resources. One auditor stated that the unit had focused on financial audit, and nothing else over the years. Another response in the open-ended part of the interview reiterated this view:

The main problem faced by internal audit is that there is not sufficient number of staff considering the work load that the department is supposed to handle. As a result, the department gives focus on financial audit. As for management or operational audit, it will only be conducted on sections of the organization which are having problems or which need attention.

The seriousness of the staff shortage is easily apparent from the table below: more than twenty percent of those organizations indicating that they were short of audit staff indicated that they need more than 11 additional staff in order to achieve operational competence. See Table 5.

Table 3: Audit staff shortage

	Total	%
Inadequate by 3 or less	12	42.86
Inadequate by 4 to 5	7	25.00
Inadequate by 6 to 10	3	10.71
Inadequate by over 11 staff	6	21.43
Total	28	100.00

It is depressing to find within this very category that two organisations are 20 and 22 staff members short, and that their audit workload is being carried by fewer than 5 members of staff. At the extreme, one unit with 2 members requires 24 members, while another unit with fewer than 30 audit staff actually needs more than 120 members to cover the audit assignments competently.

These figures support the responses given in the open-ended part of the interviews that the main problem facing auditors is the staff shortage.

Discussing the reasons for audit weaknesses, one of these auditors placed the blame squarely on the National Audit Department (NAD) (in the Malay language, it is known as Jabatan Audit Negara or JAN). In his/her experience the root cause is the shortage of audit staff that individual organizations are not at liberty to address. As he/she puts it:

When it concerns staff shortage, the NAD could perhaps do better in filling the internal audit posts. It is the NAD which appoints the internal audit officers – not the organization itself.

This may well be the key point. After all, in the Auditor General’s Circular No. 1/2002, addressed to heads of the various public sector organizations, paragraph 1.4 states:

Right now, almost 80 percent of the posts in the internal audit units are filled by officers from the National Audit Department, in the form of either secondment or “cadre”.

Another auditor suggested that one way of addressing the audit staff shortage could be by having the audit head attend administrative meetings (where presumably he or she could raise the staffing issue). Perhaps he or she has a point here. In response to the same question a respondent from another organization stated:

The problem arises from too frequent shifting of audit staff, and sometimes top management or administrators fail to fill the vacant post.

Lacking in competency in internal audit

The importance of having the right skills can never be emphasized enough. But a significant number of the auditors blamed the audit units’ inability to function competently, and consequently failing to fulfill their organisations’ expectations, on inexperienced audit staff or staff lacking in audit competence. This skills shortage appears to have been addressed in that auditors from each and every federal organization interviewed said, in the close-ended interviews, that their staff participate in training and development programs. A significant majority also said that these programs are conducted both internally and externally. See Table 4.

Table 4: Types of staff training and development programs

	Total	%
Internal only	2	5.00
External only	6	15.00
Both internal and external	32	80.00
Total	28	100.00

Auditors mention several external bodies (non-government) providing courses to audit staff in addition to BNPK (see below) in the Treasury, NAD, INTAN and MAMPU. For certain federal departments, the internal audit units located at the ministerial level provide the training courses. A minority of auditors have also undergone training programs developed by other entities overseas and locally, including the MIA and IIA Malaysia (IIAM). Not everyone however gets the chance to attend externally provided training and development programs. When asked to identify the main problems facing his audit unit, one auditor responded:

The main problem is to get staff with experience because most of the staff sent by NAD have been newly hired. Furthermore, the budget for internal audit unit training and courses is a mere RM 5000 per year. Even though the strategy to enhance the internal audit performance is by providing courses and training to these new staff, there is a limited budget and they could only attend internally arranged courses.

Auditors from a majority of the organizations appear to have a good opinion of the three aspects of their training and development programs: sufficiency, completeness and current relevance. (See Table 5.) Nonetheless, 25 percent hold a negative view or no view with regard to the programs’ sufficiency and completeness, while a mere 15 percent believe the programs lack current relevance, or do not comment.

Table 5: Opinion on staff training and development programs

	Sufficient		Complete		Current	
	Total	%	Total	%	Total	%
Yes	29	72.5	29	72.5	33	82.5
No	7	17.5	9	22.5	4	10
No Comment	3	7.5	1	2.5	2	5
No Answer	1	2.5	1	2.5	1	1
Total	40	100	40	100	40	100

These opinions on staff training and development programs are generally positive. However, for a number of auditors, despite the optimistic view given in the close-ended part of the interviews, where they claim the programs to be sufficient, complete and of current relevance, a few minutes later, in the open-ended part of the interviews, their views are the opposite. Three examples follow:

The first, in response to the question on the main problems faced by his or her internal audit unit, the auditor claimed these to be among others the lack of knowledge in effective audit techniques and in areas such as ICT. Next, he/she said:

There is a need for certain parties to provide courses/workshops which could lead to effective audit techniques being acquired, including the writing of audit reports, and ensuring that there are sufficient staff who are experts in finance and ICT areas.

Later, in response to another question on the reasons behind these problems, he or she said:

There is no special training centre or specialist who can provide effective audit training to new auditors.

The second example is from an auditor responding to the question on the weaknesses of the audit unit:

The weaknesses of the internal audit arise from the lack of exposure to new audit techniques such as risk management, forensic accounting, IT, etc., needed to enhance the auditor's knowledge of auditing.

The third and final example is particularly interesting since the auditor made it clear early on in the open-ended part of the interview that the main problems were the following:

There is no advance auditing course offered in Malaysia, especially in the field of IT and Investment Operation and Treasury.

Later, he or she claimed that the audit unit's weakness rested upon having audit staff who were lacking in experience in these two areas, and who were thus in need of the exposure.

Such views that auditors are lacking in competency, and the fact that the training and development programs available are actually not quite sufficient, complete or of current relevance, were supported by numerous other auditors. Unlike the previous three examples, however, many of these auditors were consistent in their responses in both the close-ended and the open-ended parts of their interviews, maintaining that everything was far from perfect regarding the training programs. Three more examples.

The first involves an auditor who claimed in the close-ended part of the interview that the staff training and development programs were neither sufficient nor complete, though they were of current relevance.

Then, in the open-ended part of the interview, he or she mentioned the following:

The internal audit weakness is related to its inability to conduct financial audits because it does not possess the expertise in handling the computerized accounting system used by the organization.

And the source of this weakness is this:

The lack of exposure and training in current audit approach especially in computerized auditing.

The second example is an auditor who maintained that there were insufficient training and development programs. He/she did not have a problem with the criteria of completeness and current relevance of those few programs that were on offer. In the open-ended part of the interview, he or she identified the lack of training in computerized auditing and in performance audit as key factors contributing to the audit unit's weakness. He/she saw the situation as dire since most of the audit staff were new faces and lacking in expertise, which in turn demanded a lot of guidance and training. This means the unit was not able to complete its tasks in an expeditious manner.

The third example is the auditor who responded "No Comment" on whether staff training and development programs were sufficient, complete and current. In the open-ended part of the interview, he/she said:

The problem faced by the internal audit unit is the lack of expertise and experience leading to problems in satisfying organizational expectations of the audit function.

Finally, from among those who consider the staff development and training programs to be inadequate, insufficient and lacking in current relevance, there is one auditor who does not fault the providers of these programs, but instead places the blame on those inside his or her organization. It seems that those tasked with ensuring that audit staff receive appropriate training have failed to do their job. As a result, not only are there too few staff members, but they are also short in experience and knowledge in internal audit.

Less than advanced audit mode

The original definition of internal auditing provided by the United States based IIA in its Standards for the Professional Practice of Internal Auditing (SPPIA) states (IIA 1979):

Internal auditing is an independent appraisal function established within an organization to examine and evaluate its activities as a service to the organization. The objective of internal auditing is to assist members of the organization in the effective discharge of their responsibilities. To this end, internal auditing furnishes them with analyses, appraisals, recommendations, counsel and information concerning the activities reviewed.

In its more recent definition the body provides a broader goal for internal auditing (IIA 2003):

Internal auditing 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 effectiveness of *risk management*, control and governance process. (Emphasis added.)

It seems however that this new definition of internal auditing has little relevance in the day-to-day operation of the auditors in the Malaysian federal organizations. On reviewing current knowledge elements professed by those interviewed, the responsibilities or tasks specified in the organizations' audit charters, and finally on specific activities undertaken when auditing, these are among the

areas that showed that auditors from a significant proportion of the organizations do not have much awareness of the importance of risk as part of the new manner of conducting an audit.

Specifically, on the matter of knowledge elements which an internal auditor needs in order to perform his or her "current" role in the organization, a majority of those interviewed provided answers demonstrated either a "traditional" or a "modern" mode of internal auditing, as opposed to that of the more appropriate "advanced" type (see Ridley & Chambers 1998). Table 6 shows that subjects such as auditing, financial accounting and control are the favoured areas of focus and competence, in contrast to risk vocabulary, concepts and management techniques, globalization and forensic auditing.

Table 6: Current knowledge elements

Knowledge Elements	Total	%
Auditing and analytical skills	39	97.50
Financial accounting	37	92.50
Communication techniques	36	90.00
Interrogation techniques	35	87.50
Types of controls (preventive, detective, directive and corrective)	35	87.50
Ethics	35	87.50
Computer technology	34	85.00
Red flags (indicators of fraud such as unauthorised transactions, overrides of controls, unexplained pricing exceptions or unusually large losses)	32	80.00
Laws	30	75.00
Types of fraud	30	75.00
Cost accounting	26	65.00
ISO framework	21	52.50
TQM	21	52.50
Risk vocabulary, concepts and management techniques	20	50.00
Globalisation	17	42.50
Forensic auditing	6	15.00
Others	5	12.50

Another sign that audit practice is taking place in less than "advanced" mode in many federal organizations is revealed when the auditors were questioned about their audit charters. The presence of an audit charter may be considered of utmost importance for internal auditors and for those with whom they interact. This is because this document should, at the very least, be able to clarify many matters that come under the purview of the internal auditors. All except for one organization have developed such a document. The specific areas of responsibility or tasks disclosed in

audit charters, are presented in Table 7. It is in the detail that it becomes obvious that at best the majority are operating in "current" mode, and not "advanced". The most popular areas include assessing compliance with policies, plans, procedures and law, and appraising the adequacy and effectiveness of internal controls. As for the less popular (more "advanced") tasks, these include fraud investigation, assessment of risks faced by the organization and IT audit.

Table 7: Responsibilities or tasks specified in audit charter

Responsibility/Task	Total	%
Assess the extent of compliance with policies, plans, procedures and law	37	94.87
Appraise the adequacy and effectiveness of internal controls – covering both accounting and administrative – that are applied in all the activities of the organization	35	89.74
Hand in objective and timely reports to the department head so that he or she is made known of the relevant aspects of the organizational position and performance	35	89.74
Verify the existence of assets and proper safeguards for their protection	33	84.62
Ascertain the accomplishments of established objectives and goals	33	84.62
Appraise the economy and efficiency with which resources are employed	33	84.62
Contribute towards the organization's governance process by making evaluation and improvement of the manner that organizational values and goals are established, communicated and preserved and accountability ensured	30	76.92
Ascertain the proper dispensing of government revenues	28	71.79
Provide information to the relevant outside party (such as the BNPK)	27	69.23
Suggest steps in improving the working of the governmental body	26	66.67
Review information reliability and integrity	26	66.67
Conduct financial auditing activities separate from those conducted by the external auditors	25	64.10
Conduct financial auditing activities in close cooperation with the external auditors	24	61.54
Provide advice in setting up policies and procedures	21	53.85
Investigate frauds	20	51.28
Identify and assess "risks" faced by the organization and analyse and evaluates controls established to respond to such risks	19	48.72
Conduct information technology audits (IT Audit)	19	48.72
Assess the presence of adequate criteria used by the governmental entity in determining whether its objectives have been accomplished	17	43.59
Conduct special projects	15	38.46
Conduct detailed checks on expenditures prior to payment	12	30.77
Some other responsibilities	6	15.38

Regarding IT audit in particular, many auditors mentioned in the open-ended part of the interviews that they have failed to implement it due to the lack of specific knowledge. As said by an auditor in defining the main problem faced by his or her audit unit:

The main problem faced by the audit unit is the lack of expertise and knowledge and experience especially in IT audit.

Another auditor says the following:

The lack of competency and experience in IT audit has caused a limitation on the internal audit scope.

Still another sign of current use of outmoded audit practice became apparent when the auditors answered questions on the specific tasks done while conducting the audit. Those which should perhaps be most prominent, such as maintaining awareness over the potential for fraud during audit planning stage, and the use of risk assessment techniques, are performed by auditors from fewer than half of the organizations contacted. See Table 8.

Table 8: Specific activities undertaken while auditing

	Total	%
Prepare audit report	39	97.50
Discuss recommendations with auditee	38	95.00
Evaluate the relevance, sufficiency and competency of evidence	38	95.00
Conduct interviews	38	95.00
Prepare annual audit plan detailing the auditable areas, the resources required and duration of each audit activity during a calendar year	38	95.00
Develop recommendations when appropriate	37	92.50
Use audit aids such as flowcharting, internal control questionnaires and checklists	37	92.50
Develop work papers	37	92.50
Review prior audit reports and other relevant documentations	36	90.00
Perform follow-up audits on all audit findings sometime after the issuance of the audit report	34	85.00
Monitoring the progress of audit work	34	85.00
Require written response from auditee (to include among others, a plan for corrective action and the date by which action will be implemented)	34	85.00
Disseminate audit outcome to the appropriate individuals	33	82.50
Review of audit work papers by senior auditors	30	75.00
Execute judgmental sampling	29	72.50
Use computer	26	65.00
Maintain an awareness of the potential for fraud while auditing	25	62.50
Execute statistical sampling	24	60.00
Use risk assessment technique to inform the audit planning and resource allocation process	19	47.50
Perform Analytical Review Procedures	18	45.00
Consider the potential for fraud during planning stage	16	40.00
Others	2	5.00

In the open-ended part of the interviews, many auditors also made various remarks which give evidence to the less than advanced audit mode which they are working in – and the reasons leading to such situations. Some of these remarks have been raised earlier. Others are detailed out next coming from two auditors. The following remark was made by the first auditor interviewed, in describing the work performed by his or her audit unit:

Internal audit is mostly focused on the financial audit, in comparison to performance audit related to IT management development, which is still under the NAD.

Why is this the case?

This is related to staff shortage and inadequacy of skills, making it impossible for the internal audit unit to conduct their audit as thoroughly as that of the external auditor.

As for the following remark from the second auditor interviewed, in discussing the weaknesses of the audit unit, he or she said:

In regard to equipment and facilities these are not conducive in that the internal audit staff not only have to use old computers but also to share with each other in using them. In addition, they also face weaknesses in regard to having very few staff with sufficient experience and expertise, especially in a field such as IT audit.

Next, when talking about the fundamental reasons leading to those weaknesses, he or she provided the following list:

The lack of support and attention from the relevant sections in the organization, which probably do not think much of internal audit, and which do not fully understand the internal audit function; the lack of staff training due to the limited amount allocated for that purpose; and, the lack of exposure in current audit techniques.

Finally, it is notable that there are also auditors who hold contrarian viewpoints on the reasons why auditors in the federal organizations are still working in out of date audit modes. One of these auditors avoided the easy way of blaming other parties. Instead, he or she blames the auditors themselves for the present situation. In his or her view, the present situation is caused by auditors' lack of exposure to the latest trends, and their failure to read about and research an issue or problem.

Another contrarian explanation was offered for the "elementary competence level" situation in public sector audit practice. This auditor mentioned early on in the interview that the reason is that most of the auditors do not possess professional qualifications and they are not members of the IIAM. Membership of the IIAM would require them to have current expertise and audit knowledge. In his or her view, this situation is caused by the fact that the government does not recognise those possessing professional

qualification from bodies such as the IIAM. Nor are there any grants or bursaries from government to enable auditors to study further, or to join the IIAM. This means that there are very few in the public sector with the interest in pursuing the professional qualification.

Treasury's failure

In the 1979 Treasury Circular No. 2, it is stated, in paragraph 5, that the Financial Management System Unit, located in the Budget Department in the Treasury of the Ministry of Finance, is responsible for the development, administration and coordination of the internal audit practice in the whole government. Their four listed duties are: to issue general policy directives; to provide guidelines on audit practice; to coordinate audit efforts; and to give advice. Recently, on the website of the Ministry of Finance (Treasury Malaysia 2004), it was stated that the Malaysian Treasury (BNPK) is the central authority in internal audit with the responsibility to monitor and coordinate the implementation of internal audit in the federal ministries, departments and statutory bodies. In the 2004 Treasury Circular No. 9, the responsibilities mentioned in both the old Circular No. 2 and on the website are clearly noted within paragraph 9 which has a list of four items. But it seems the reality on the ground is something different. A small minority of auditors are more or less satisfied with BNPK, while many others are clearly unhappy.

Perhaps the most interesting and revealing reaction to BNPK's failures comes from an auditor who says:

There are so many things which could and should have been done for internal audit The BNPK needs to keep in touch regularly with internal auditors. But now what is happening is that the contact takes place only once per year. BNPK has failed to get to know about the problems faced by internal audit ... at the beginning of the year it asks for the audit plan; at the end of the year, it asks for the audit report – but there is no feedback whatsoever. I think there is a lot more which it can implement especially on training.

Note also the agitation in the tone of this auditor's view on the BNPK's failure in fulfilling its functions:

In regard to the administrative side, it is hoped the Treasury will play an important role in training, in increasing the number of audit staff available and in monitoring internal audit.

On audit training in particular, BNPK's role appears to be reactive, showing a lack of knowledge and insight into internal audit, rather than taking the lead from a position of informed vision. This is what the auditor says:

Instead it asks us which courses we would like them to organize.

As for internal audit monitoring, the implicit failure of BNPK to carry out its duty is obvious from this auditor's comments:

There are cases where an auditor is conducting non-audit activities – being a member of the Quality Award Committee, a Quality Officer, a Sport Officer. Currently, BNPK is doing the monitoring, but there is no black and white ... From the aspect of monitoring, it is not that good. It gets the annual audit report. That is all it wants.

It is notable that other than the deficiencies in the training programs for internal auditors, the other area which clearly brings a lot of dissatisfaction with the BNPK is its monitoring function. This is not surprising since auditors from mere five out of a total of 40 organizations mentioned the involvement of BNPK in some sort of evaluation program which covered *all* aspects of internal audit activities and which *always* monitored the effectiveness of the audit function.

Further proof that BNPK has failed in its duties is suggested by the lack of uniformity in audit practice in the public sector. The perceived importance of uniformity in audit practice was stressed by several auditors in the open-ended section of the interview. In response to the question on the direction internal audit should be taking, one auditor saw uniformity across all audit units in the ministries and departments as a priority. This standardization should extend across financial audit, performance audit and ICT audit. Another auditor saw the state of current audit practice in the public sector as follows:

There is improvement but there is still a lot of room for improvement. For example, no standardization in audit structure exists across the government entities; nor is there a standardized manual, and there are so many other cases of the lack of standardization in audit practice in the government sector.

Unlike these two auditors who have implicated the BNPK indirectly, there is an auditor who does not mince his or her words over the failure of BNPK in ensuring uniformity in audit practice in the federal organizations. The following is what he or she says:

The Treasury as a “central body” needs to issue standards or do the monitoring so that everyone will do the same and have the same “bench mark”.

The threatening NAD?

A number of audit units seems to have quite a close relationship with the external auditor, the National Audit Department. One auditor for example, listed the following five forms of interaction taking place between his or her audit unit and the body. These are: information sharing; planning the whole of the audit program together; allocating specific tasks between NAD and internal audit unit; serving as assistant to the external auditors in preparing schedules; and, receiving training from the external auditor. Another auditor mentions four different ways of interaction between the internal and external auditors: the first three are the same as the previous auditor's, and in addition assisting the external auditors with the year-end audit work.

There is also an auditor who provides a list of actions demonstrating the close working relationship between the internal and external auditors. The list includes:

1. Giving out a copy of the internal audit report to and receiving the external audit report from the external auditor.
2. Giving external auditors places in training programs conducted by the Internal Audit Department.
3. Having meeting twice per year.

All in all, only three organizations reported having no interaction whatsoever between the internal auditors and the NAD while another five organisations reported having “very little interaction” with the NAD. The substantial majority of internal auditors therefore appear to have some sort of working relationship with the NAD. (See Table 9 for the tabulation of the different forms of internal auditor - external auditor relationship.) It is also significant that internal auditors from a total of 17 organizations (or over 42 percent) claimed that their close relationship with the NAD continues throughout the year.

Table 9: Internal Auditor - External Auditor Working Relationship

	Total	%
Information sharing	29	72.50
Internal auditors participate with the external auditors in planning the whole of the audit programmes which are subsequently divided between them for implementation	13	32.50
External auditors provide training to internal auditors	12	30.00
External auditors provide suggestions for reviews	9	22.50
Internal auditors assist with year-end audit of the external auditors	3	7.50
Internal auditors serve as assistant to the external auditors in preparing schedules, etc.	2	5.00
Internal auditors perform their work in conformity with an auditor programme prepared by the external auditors	1	2.50

The fact that 80 percent of the internal audit units have some sort of working relationship with the external auditor, and that internal auditors from more than half of these units claim a *close* working relationship with the external auditor is not surprising at all. This is because, as previously stated, 80 percent of the posts in the internal audit units are filled with officers from the NAD. The working

relationship between the two types of auditors is in accordance with the 2002 Auditor's General Circular.

On the surface this high degree of implementation of policy should be quite encouraging news. What is not encouraging, and is in fact quite alarming news stated in many interviews, is the high-handed manner in which the NAD moves its officers in and out of the

federal organizations' audit units without giving proper consideration to the needs of these units. Said one auditor:

The internal audit head is also facing a control issue over its staff since those who are filling in a "cadre post" may be taken back by the NAD whenever it wants to.

Worse, the NAD is always shifting experienced and capable auditors out from the internal audit units, replacing them with those who have little experience and knowledge of audit! This phenomenon was noted by an auditor when talking about problems faced by his or her audit unit:

There are also problems in the organization where the experienced staff are taken back by the National Audit Department since most of the internal audit staff in the ministries and departments are holding "cadre post". This automatically means that the internal audit department is "losing" experience staff and is forced to train new staff.

A similar observation comes from another auditor:

The auditors sent in are mostly still fresh – without any experience whatsoever. But the NAD is "smart", for they do not want to send in those with experience to internal audit units since they themselves need the experienced officers to conduct external audit. Those sent in to internal audit units are to learn stuff while working ... Once I raised this issue at a meeting in the NAD. That is, the head of audit unit should never be a fresh face but somebody with at least five years work experience as auditor. The new face will only bring down the NAD's reputation.

In the final analysis, what the NAD is doing appears to have contributed to the staff competency problems in internal audit units. This may be inferred from the remark made by an auditor in explaining the reason behind the problem faced by his or her audit unit:

The problem is to become competent since competency is derived after being in the job over a period of time. For new officers, they will need time to be competent whereas internal audit needs people or officers who are already competent.

But it seems the NAD has chosen to ignore the need for competent staff in the internal audit units. It would appear that, as far as the NAD is concerned, the internal audit units are mere training grounds for its inexperienced staff who are appointed to the cadre post. In other words, its staff are sent into the internal audit units to prepare them to be external auditors, and once they have gained experience they are brought back into the NAD.

Many auditors note and lament this state of affairs which, while it profits the NAD, is also causing the internal audit units to "hemorrhage" competent staff. In talking about the weakness experienced by the audit unit caused by the frequent shifting of staff, an auditor says:

If there is a frequent shifting of staff, it will affect the smoothness of the work done because the unit will need to go through the process of training new staff all over again, so that they could reach the level of competency possessed by the more senior staff.

In response to the question of responsibility for the situation, he or she says the following:

It is up to the Auditor-General himself since he is the one who issues the transfer order. If there is a frequent shifting of staff, it will affect both the audit unit and the auditee.

It is notable however that not every single auditor interviewed held the NAD to be solely responsible for the lack of internal audit skills amongst new audit staff. One auditor, in the open-ended part of the interview stated:

The first problem concerns the appointment of new staff who are lacking in training, experience and familiarity with the operation of the organization.

When asked for the fundamental reason leading to such a situation, he or she said:

It is because of the lack of coordination between the PSD (Public Service Department), NAD and the organization itself, in bringing in staff who can really fulfill the needs of the internal audit unit.

DISCUSSION AND CONCLUSIONS

In Malaysia, the internal audit function in many federal organizations studied have a number of serious shortcomings. The two areas that need most urgent attention are the staff numbers in the audit units or departments, and the competency of the audit staff. There is a high percentage of these organizations where the internal audit units or departments are not able to operate effectively as a result of the acute shortage of staff and of staff lacking in appropriate audit skills. Furthermore, while the world trend, and including some members of Malaysia's listed companies, is that internal auditors have moved to risk-based auditing, in a majority of Malaysia's federal organizations, the internal auditors are still performing financial management audits. Compounding the inefficiencies of operating an outdated system, the BNPK has failed in its duty to coordinate, train and monitor the staff of all government internal audit units. As for the NAD, their cynical exploitation of the internal audit units as simply training grounds for their staff requirements, further undermines the effectiveness and credibility of the internal audit units in all government departments and agencies.

Perhaps the clearest summary of the fundamental factors leading to the debilitating state of affairs in the internal audit function in the public sector was made during the open ended interview with an auditor:

There is no coordination in the practice of internal audit in the government sector. In addition, there are too many parties such as the NAD and the BNPK which are supposed to be responsible for

monitoring the audit units. In the end, one can conclude simply that there is no good and effective coordination that would raise the quality and the added value of the internal audit function, and nor have any best practices been published, or Parliamentary Act promulgated to support the internal audit practice in the government sector.

This view, also held by a few other auditors, appears to define the direction that needs to be taken to deal with the myriad problems which they are currently facing. Unfortunately it also appears that those who have the power to effect these changes have chosen not to take up this challenge.

In order for audit to achieve its potential, its primary requirement is a surrounding where operational transparency and public accountability are the normal occurrence. Azham (1999) has made this vividly clear in regard to the practice of external auditing. The same may easily be inferred for internal auditing in the public sector in Malaysia. Unfortunately, Malaysia is still far away from this ideal of transparency and accountability and which arguably contributes to the worsening corruption in the public sector over the years. No less than Tan Sri Ramon Navaratnam, the current president of Transparency International - Malaysia, has spelt this out recently (*The Star Online* 7 May 2008):

Transparency International – Malaysia commends the intention of the Penang State Government to be the first to introduce Freedom of Information legislation in Malaysia. The absence of this legislation and the presence of the Printing Presses and Publication Act has severely curtailed press freedom and cramped the growth of its development and progress in our country. This has led to unhealthy “closed” as opposed to “open” debate and discussions on vital national and public policy issues and has therefore inhibited the evolution of a more transparent democracy and greater national integrity and accountability. *All these negative trends have contributed to increasing corruption and the considerable wastage of public funds. As a result, corruption is debilitating our economy and eroding our national competitiveness.* (Emphasis added.)

Malaysia in 2006 ranks 44th (down from the 39th position it occupied in 2005) among 163 countries in the Transparency International Corruption Perception Index 2006 (*New Straits Times* 7 November 2006). In the following year, the country improved its ranking from 44th to 43rd. Its score of 5.1 was a minimal improvement from the 5.0 recorded in 2006 (*The Star Online* 27 September 2007). However, the slight positive change stopped almost a decade of downward trend in the rankings.

Though the index is not an assessment of actual corruption in any country, but is an appraisal of the perception of corruption amongst businessmen and other groups, it should be obvious that such perception is largely based on the first hand experiences of those parties interviewed. For the last decade Malaysia's score has hovered around five, the

borderline figure below which a serious corruption problem is deemed to exist. In comparison with other countries which are ranked higher, Malaysia is arguably a significantly corrupt country.

Recently this was pointed out in Parliament by the current chief minister of Penang, Lim Guan Eng. He claimed that in 2004 the international investments and finances services giant Morgan Stanley had estimated that as much as US\$100 billion (then RM380 billion) had been squandered through corruption over the past two decades (*Malaysiakini* 24 June 2008).

That corruption, lack of transparency and accountability are all part and parcel of Malaysian life was made clear in an interview given by Tunku Abdul Aziz Tunku Ibrahim with the *New Sunday Times* (24 October 2004). He was then the executive president of the Malaysian chapter of Transparency International, and had been responsible for setting up the Kuala Lumpur Society for Transparency and Integrity in 1995. In response to the question whether he was happy with what was being done to curb corruption within the country, he said: “I feel our country can do better,” supporting an earlier comment that “... the perception still is that we are not serious about curbing corruption.”

That there is a lack of transparency and public accountability in the public sector was substantiated during a workshop presentation at the Universiti Utara Malaysia (Zakaria 2004) made by Zakaria Haji Mohammad Nor, NAD's Audit Director in the state of Kedah at that time. He mentioned various problems and challenges that he and his colleagues from the NAD had had to face in trying to improve accountability in the public sector. A key challenge was the lack of accountability on the part of the heads of these public organizations, manifested in their regular failure to attend the audit exit conference, to respond to audit observations and directives, and to take appropriate actions upon cases reported.

With leadership of this (dubious) quality other challenges and problems abound. These include the lack of cooperation given to the auditors by the rest of their organizations' staff, particularly by those being audited, and their failure to rectify their mistakes. In his view, this behaviour is almost unavoidable given that the following situations exist: the Public Accounts Committee (PAC) is particularly weak; the penalties for failure to complete departmental accounts and for deliberately concealing its books have never been imposed (see also *New Straits Times* 18 October 2004); and, a lack of transparency within the government administration prior to Datuk Seri Abdullah Badawi becoming the Prime Minister on 31 October 2003.

All in all, the conduct of those in power, and of those who put them there can be explained respectively by the “politics of accountability” theory, and by Hofstede's “cultural dimension of power distance”. Under the politics of accountability theory, political representatives, appointed officials, administrators and workers have good reasons to resist attempts to

expose their work to scrutiny. As stated by Schwartz and Sulitzeanu-Kenan (2002), their interests in organizational stability, budget maximization and the promotion of favorable image, contribute to a general desire to oppose accountability mechanisms such as internal audit that might portray deficiencies in their work.

But to place the blame for the dire state of internal audit operations solely on the powerful would be to miss an important Malaysian dimension. Hofstede (1991) discusses five important cultural dimensions that explain the general similarities and differences in cultures around the world. One of these is "power distance", a concept that helps explain the behavioral interrelationship between the less powerful and the more powerful members of a society. Specifically, the concept of power distance refers to the degree to which people are willing to live with unequally distributed power within and across their institutions and organizations. A high score on the power distance index indicates a national culture that has a high tolerance for inequality. In short, the people accept a strongly hierarchical order in which everybody has a place, and which needs no further justification. Hofstede (1983) conducted two surveys between 1968 and 1973, involving employees from subsidiaries of IBM in sixty-four countries, and 116,000 questionnaires in twenty languages. In the final analysis Malaysia received the highest score, ranking it first for power distance, or tolerance of unequal distribution of power.

With such being the case, it may be inferred that a majority of Malaysians are barely aware of, or silently accept situations where the powerful disdainfully disregard any call to explain their conduct. This is in stark contrast to the accepted norm in societies where the power distance is small. More to the point, when it concerns internal audit in the federal organizations,

which may be considered a tool of internal accountability, and even after half a century of independence from Britain, the norms in society in general appear to explain the "neither here nor there" attitude to accountability. The powerful continue to flaunt their lack of internal accountability, made possible by, among others, the (often forced) inadequacies of the internal audit function. On the other hand, the powerless members of the organizations, and the society as a whole, appear to be resigned to their state of impotence.

A final word: it appears unreasonable to expect the future of internal audit in the federal organizations to be much different from its present. This would be because, in societies with significant inequalities in power distribution, there is an apparent psychological need for dependence on the part of those without power, and there is a complementary need on the part of those in power to be depended on. In other words, the value symbols of the two groups are complementary.

Surprisingly however, the majority of the auditors interviewed has maintained their optimism regarding the future of internal audit, not only in their own respective organizations, but also in the government sector as a whole. In fact, so many of them are supportive of the various ideas proposed to strengthen the audit function, and full of their own ideas on new directions and strategies in support of the improvement of internal audit. If it were left to them alone, progress would be unavoidable. But, since it is not up to them, it can safely be said that, for the foreseeable future the functioning of internal audit in the federal organizations will not be much different from the past and present. Only the volume of rhetoric and number of official documents issued on the subject, and immediately ignored, might increase. *There is no light at the end of the long dark tunnel.*

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APPENDIX A

LIST OF FEDERAL GOVERNMENT ORGANIZATIONS

MINISTRY	DEPARTMENT
Prime Minister's Department	Public Service Department of Malaysia
Ministry of Energy, Water & Communications	Immigration Department of Malaysia
Ministry of Youth & Sports	Royal Customs and Exercise Department Malaysia
Ministry of Home Affairs	Department of Islamic Development
Ministry of Domestic Trade & Consumer Affairs	Attorney General's Chambers of Malaysia
Ministry of Rural & Regional Development	National Registration Department of Malaysia
Ministry of Works	Prisons Department of Malaysia
Ministry of Health	Department of Statistics Malaysia
Ministry of Foreign Affairs	National Library of Malaysia
Ministry of Education	
Ministry of Tourism	
Ministry of Entrepreneur & Co-operative Development	AGENCY
Ministry of Information	Central Bank of Malaysia
Ministry of Transport	The Inland Revenue Board of Malaysia
Ministry of International Trade & Industry	Armed Forces Fund Board
Ministry of Defence	Pilgrims Fund Board of Malaysia
Ministry of Agriculture & Agro-Based Industry	Putrajaya Holdings
Ministry of Housing and Local Government	Treasury Malaysia
Ministry of Plantation Industries & Commodities	Implementation Coordination Unit
Ministry of Science, Technology & Innovations	Kuala Lumpur City Hall
Ministry of Natural Resources & Environment	Bank Simpanan Nasional
Ministry of Human Resources	

APPENDIX B
LIST OF POSITIONS OF INTERVIEW PARTICIPANTS

POSITION	TOTAL
Internal Auditor	3
Senior Internal Auditor	1
Audit Head	1
Internal Audit Head	10
Head of Internal Audit Department	1
Head of Internal Audit Unit	9
Head of Internal Auditing Unit	1
Director	1
Audit Director	1
Internal Audit Director	1
Director of Audit and Compliance Department	1
Director of Department of Inspectorate	1
Audit Assistant	1
Assistant to the Internal Audit Head	1
Assistant to the Registration Officer	1
Assistant to the Officer in Charge	1
Assistant to the Head of Internal Audit 1	1
Secretary to the Internal Audit Section	1
Secretary to the Internal Audit & General Investigation Section	1
Deputy Head of Internal Audit	1
Deputy Head of Internal Audit Unit	1
Total	40

