Identification of Factors Affecting Ethical Internal Auditing

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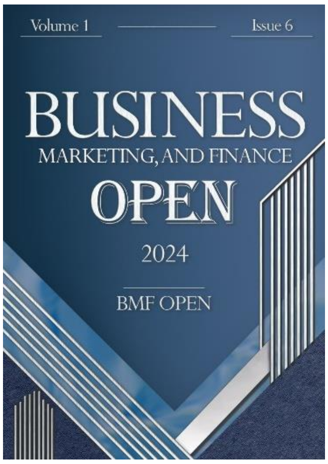

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Abstract: This study aims to investigate the ethical practices of internal auditing and the factors influencing auditors' judgments. Specifically, it explores the impact of legal, behavioral, professional, and committee-related factors on the quality of internal auditing and auditors' decision-making processes. The research adopted a descriptive analysis method, utilizing a survey-based approach. A sample of 384 auditors from auditing firms and organizations across Iran participated in the study. Data was collected using a structured questionnaire and analyzed through statistical methods to identify relationships between various factors and ethical decision-making in internal auditing. The study found that behavioral factors, such as the auditors' experience and gender, had a significant impact on ethical decision-making. Legal factors, particularly proficiency in using information systems and understanding relevant laws and regulations, were found to enhance auditors' judgment quality. Additionally, professional factors, including a comprehensive understanding of management's objectives and organizational goals, were crucial for auditors to provide effective judgments. The findings also indicated that committee-related factors, such as continuous training in information systems, improved auditors' ability to make informed decisions. The research concludes that ethical decision-making in internal auditing is influenced by a combination of behavioral, legal, professional, and committee-related factors. It emphasizes the importance of continuous professional development, ethical standards, and understanding the organizational context to enhance the quality and effectiveness of internal audits. Further research is needed to explore these relationships in other organizational settings and to investigate additional variables that might affect auditors' ethical decision-making.

Keywords: Internal auditing, Professional code of conduct, Professional ethics, Ethics, Accounting

1. Introduction

Ethics and adherence to professional ethics is a serious and critical issue in the field of accounting, directly impacting the integrity and ability of accountants to earn public trust. Especially, improper and unethical training can lead to unethical practices [1, 2].

Ethical misconduct can have detrimental effects on investments and financial markets, as people often argue that these actions result from the unethical behavior of accountants and their failure to understand ethical principles properly, leading to an ethical crisis in the accounting profession [3].

Given the numerous financial scandals in recent years, the focus on ethics in accounting has gained significant attention. Mistakes and ethical lapses observed in some auditors have caused many audit failures, drawing attention to the issue from the early stages of the auditing profession's emergence. While not all audit failures are linked to unethical behavior by auditors, many of them involve unethical or, at the very least, unprofessional actions by certain auditors (Clickman, 2019).

As a result, following audit firm failures, legislators have established laws and standards, such as the professional code of conduct, to promote ethical and professional behavior among auditors. In fact, accounting professional bodies have developed guidelines through the professional code of conduct to motivate auditors to enhance ethical behavior (Alin, Hadib, & Hanif, 2018).

Nevertheless, unethical behavior among auditors continues to occur, making the attention to ethics an essential matter. This is because, in addition to potentially violating the interests of shareholders through unethical conduct by accountants and auditors, accounting also plays a crucial role due to the fact that accounting information is an input for many economic decision-making systems [4, 5].

On the other hand, professional skepticism is an essential element of auditing. Professional skepticism is intrinsic to the exercise of professional judgment, and according to auditing standards, auditors must perform their work with doubt, not suspicion or distrust. Thus, maintaining a logical balance between the two sides of the coin is necessary [6]. The auditing profession has long recognized and emphasized the importance of professional skepticism in guiding audits. However, recent inefficiencies and audit failures have led to increased attention to the concept of professional skepticism. Moreover, the response from the Securities and Exchange Commission and the Public Company Accounting Oversight Board to these failures indicates that the concept of professional skepticism will be subject to further scrutiny. Accordingly, examining timely and useful factors that increase the likelihood of displaying appropriate levels of professional skepticism is beneficial [7, 8].

The auditing literature indicates that when auditors perform their role in accordance with professional ethics, it significantly affects their decisions. Professional ethics enhance the auditors' efforts to apply legal measures and professional skepticism in carrying out their duties [8, 9]. Additionally, professional ethics make auditors more conservative, meaning auditors are more likely to perform tasks with greater skepticism. Furthermore, when auditors behave in accordance with ethical standards, they make more conservative judgments. With the improvement of professional ethics, the auditing process conducted by auditors becomes more effective [10]. Therefore, the implementation of accounting ethics increases their professional skepticism, as auditors reason meticulously during the audit process and consider the issues deeply and even beyond the subject. In other words, professional ethics leads to an increased inquisitive search for necessary evidence by the auditor and enhances their professional skepticism [11, 12].

Actions in the public interest involve considering the legitimate interests of clients, government, financial organizations, employees, investors, the business and financial community, and other individuals striving to support the dignity and profession of accounting. Business, in short, is the primary reason for the need for accountants to adhere to ethical standards. It is only with professional ethics that financial and auditing work can be entrusted to an accountant or auditor, and this is a crucial point. Accountants deal with a wide range of issues on behalf of clients. They often have access to confidential and sensitive information. Auditors claim to maintain an independent perspective in their work. These ethical standards ensure that accountants and auditors can enjoy job security, as they cannot be accused of deviating from other accountants or the general standard. A distinguishing feature of the accounting profession is the acceptance of responsibility to act in the public interest. When acting in the public interest, a professional accountant must comply with the ethical requirements of this duty. A professional accountant is obligated to adhere to the fundamental principles of accounting and auditing, the first of which is maintaining professional integrity. Therefore, the objective of this research was to examine, identify, and rank the factors affecting ethical internal auditing.

2. Methodology

To identify the factors influencing ethical internal auditing, the fuzzy Delphi technique is employed. Subsequently, the CAP Land technique is used for ranking the challenges. Initially, the identification of factors affecting ethical internal auditing was conducted. Finally, through calculations in Excel software, the evaluation and ranking of these factors were performed.

In this study, first, the fuzzy Delphi method was used to identify the factors affecting ethical internal auditing, with input from experts. Afterward, the CAP Land method was applied to rank these factors. It is worth noting that these factors were extracted from the literature and prior research, and they were presented as semi-structured questions to the expert group.

3. Findings

In this section, the research question is addressed:

What are the factors affecting ethical internal auditing?

By examining the identified codes (open codes) extracted from the interviews analyzed in the final stage, themes were defined and named. The results of the analysis indicated that the factors affecting ethical internal auditing were categorized into four groups: legal factors, behavioral factors, professional factors, and audit committee factors. Each of these main components also has sub-components, and the results of this categorization are presented in Table 1.

Table 1. Main Components and Sub-Components Derived from Open Codes Extracted

Main Components	Sub-Components	Initial Extracted Codes
Legal Factors	Punitive Laws	Fear of the judicial system, fear of legal prosecution, severe legal consequences for auditors lacking ethical procedures, highlighting the role of punitive laws when auditors disclose information.
	Enforcement Mechanisms	Attention to professional principles in creating enforcement mechanisms, understanding internal auditors' activities, consideration of judgment by internal auditors, alignment with organizational strategies, objectives, and risks.
	Work Conscience	Feelings of regret in auditors, loyalty to commitments, adherence to good faith, impact on auditors' ethical sensitivity, auditors' work conscience, fair evaluation by auditors, resistance to personal interests, emphasis on auditors' internal conscience.
	Self-Efficacy	Auditor's self-efficacy, attention to internal auditors' flexibility, creating psychological capacity to withstand challenges, uncertainty, engagement, and failure, increased auditor progress and responsibility, loyalty to work values.
	Courage	Lack of auditor conservatism, fearlessness in stating the truth, moral courage of internal auditors, courage in internal auditors, courage to disclose the truth and reveal all positive and negative financial processes.
	Religious Beliefs	Belief in religious principles, development of religious beliefs among auditors to promote ethics, demonstrating adherence to ethical principles and values.
	Honesty	Observance of honesty by internal auditors, complete and honest presentation of financial information, commitment to ethical conduct by internal auditors, sensitivity to errors, respect for interests, and maintaining integrity in internal auditors' actions.
Behavioral Factors	Credibility and Work Quality	Influence on auditor's credibility, professional quality of auditor’s work, level of trust in the auditor, necessary knowledge, skills, and experience, attention to auditor competency, respect for the organization's operational and ethical goals, compliance with auditing standards, and enhancing internal audit quality.

	Disclosure of Truth	Disclosure of truth by auditors, revealing deficiencies in line with professional and legal standards, commitment to transparency, protecting auditors, and ensuring proper financial information reporting within the organization.
	Integrity	Impact of auditor's integrity, absence of opportunistic behavior, attention to conflicts of interest, and adherence to integrity principles by internal auditors.
	Confidentiality	Respect for ownership and confidentiality of information, protection of financial data, and non-disclosure of information for personal gain, adherence to confidentiality standards by internal auditors.
Professional Factors	Impartiality	Full adherence to impartiality by auditors, not participating in activities that could compromise auditor objectivity, avoiding distortion of facts, and maintaining impartiality and fairness in auditing processes.
	Auditor Independence	Legal support by senior management, laws ensuring independence of internal auditors, development of audit charters for internal auditors, creating organizational independence for auditors.
Audit Committee Factors	Monitoring and Evaluation	Monitoring and evaluation by the audit committee, assessing adherence to auditing values, and focusing on internal auditors' boundaries.
	Compensation and Rewards	Establishing appropriate auditing fees, focusing on the needs of the internal audit community, considering economic conditions, ensuring adequate income for internal auditors, providing rewards for ethical auditors, and creating motivation for auditors through incentives.
	Internal Audit Standards and Laws	Establishing mandatory internal auditing standards and guidelines for internal control by lawmakers, educating auditors on their responsibilities, and developing supportive regulations for whistleblowers.
	Internal Control and Support	Timely reporting of audit processes, internal audit committee's annual reports, evaluating internal control systems, and providing necessary suggestions for improving internal controls.

4. Discussion and Conclusion

Therefore, one solution for clients (audited companies) is to rely on other variables that do not require high costs for evaluation, yet are related to audit quality. DeAngelo (2020) defines audit quality as follows: the market's assessment (inference) of the likelihood that the auditor (1) will detect material misstatements in the client's financial statements or accounting system, and (2) will report the detected material misstatements. The probability that the auditor will detect material misstatements depends on the auditor's competence, while the probability that the auditor will report the detected material misstatements depends on the auditor's independence. DeAngelo (2020) believes that larger auditing firms have a stronger incentive to provide higher-quality audits because they are keen to build a better reputation in the market, and since they have a large number of clients, they are not concerned about losing clients. It is assumed that such firms, due to access to more resources and facilities for training their auditors and conducting various tests, provide higher-quality audit services [13]. From an economic perspective, the loss resulting from failure to detect and report material misstatements is significant for larger firms.

The results of their research showed that clients of industry-specialized auditors had lower levels of internal ethical auditing and internal ethical auditing compared to non-specialized auditors, and had a higher profit response coefficient (in other words, higher internal ethical auditing) than non-specialized auditors. If companies are more inclined to manipulate reported profits to meet projected profit goals, the internal ethical auditing will still be considered lower. These researchers report that internal ethical auditing is higher when the auditor is an industry leader.

Considering the impact of professional factors on internal ethical auditing, it can be said that this research is in line with the prior findings which that ethics and professional behavior are very important for the accounting profession. Without acceptance and gaining the trust of service users, accountants' services are futile [2, 4, 6, 9, 10, 13]. Trust in services is based on trust in the provider, which in turn depends on honesty and adherence to ethical principles. The aim of this research was to examine the impact of professional ethics on auditor professional skepticism. For this purpose, the impact of five components—professional principles and regulations, independence and impartiality, confidentiality, integrity and honesty, and competence and professional care—on auditor professional skepticism was analyzed using a questionnaire distributed among 119 auditors from the Audit Organization and member audit firms of the Iranian Association of Certified Public Accountants, including all partners, managers, and audit supervisors. The results indicated that all five components of professional ethics had a positive and significant impact on auditor professional skepticism; however, the greatest impact was related to the competence and professional care component. Therefore, auditing firms should focus on increasing the professional knowledge and skills of their employees to improve the quality of judgment and decision-making.

The limitations of this study stem from various factors, including the reliance on selected theoretical foundations, which may yield different results if other frameworks were used. Additionally, the research was conducted with 384 auditors, and changing the sample size could potentially alter the findings. Since the study was carried out in 2022, caution should be exercised when applying the results to other time periods due to possible changes in the context and environment.

It is recommended that internal auditors enhance their skills in utilizing information systems and their reporting capabilities to make more accurate and effective professional judgments. Internal auditors should base their decisions on established laws, regulations, and auditing standards, allowing them to defend their positions effectively in case of disagreements with organizational authorities. Furthermore, gaining a deeper understanding of management's goals and objectives will enable internal auditors to make more impactful judgments and align their audits with organizational priorities.

Future research could extend this study to other organizations outside the current research population to examine the broader applicability of the findings. Additionally, future studies could explore professional ethics as an independent variable to assess its impact on auditing practices. Given the dynamic nature of auditing and organizational environments, further research could investigate how these factors evolve over time and affect auditing outcomes in different contexts.

Authors' Contributions

Authors equally contributed to this article.

Ethical Considerations

All procedures performed in this study were under the ethical standards.

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Conflict of Interest

The authors report no conflict of interest.

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