

# Intellectual Discourse

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# *Intellectual Discourse*

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Volume 31

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## Transliteration Table: Consonants

Arabic	Roman		Arabic	Roman
ب	b		ط	ṭ
ت	t		ظ	ẓ
ث	th		ع	‘
ج	j		غ	gh
ح	ḥ		ف	f
خ	kh		ق	q
د	d		ك	k
ذ	dh		ل	l
ر	r		م	m
ز	z		ن	n
س	s		ه	h
ش	sh		و	w
ص	ṣ		ء	’
ض	ḍ		ي	y

## Transliteration Table: Vowels and Diphthongs

Arabic	Roman		Arabic	Roman
اَ	a		اَ، اِيَّ	an
اُ	u		اُو	un
اِ	i		اِي	in
اَ، اِ، اِيَّ	ā		اُو	aw
اُو	ū		اِيَّ	ay
اِي	ī		اُو	uww, ū (in final position)
			اِيَّ	iyy, ī (in final position)

*Source: ROTAS Transliteration Kit: <http://rotas.iium.edu.my>*



# Objectivity Threats: Would it Jeopardise Malaysian Internal Auditors’ Risk Judgment Quality?

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**Jamaliah Said\*\***

**Razana Juhaida Johari\*\*\***

**Norizelini Ibrahim\*\*\*\***

**Abstract:** In the realm of internal auditing, the rise of Risk-Based Internal Auditing has heightened the demand for auditors to excel in risk assessment. Failing in this role not only endangers audits but also exposes companies to significant losses and reputational harm. Internal auditors entrusted with critical decisions grapple with objectivity challenges that impede their ability to assess a company’s risks accurately. This study investigates objectivity challenges in Malaysian internal auditing and their impact on risk assessment. Employing experimental tasks of varying complexity, it reveals that all nine objectivity threats outlined in the “International Standards for Professional Practices of Internal Auditing (IPPF): Practice Guide on Independence and Objectivity” are prevalent in Malaysia. These threats negatively affect risk assessment,

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regardless of task complexity. Prominent objectivity threats include social pressure, familiarity, and intimidation. Crucially, these threats have a more significant impact on risk assessment during simpler tasks, especially when auditors assess familiar, less intricate areas. These highlight the urgent need for internal auditors to manage objectivity effectively, strengthening their role as impartial, dependable risk assessors.

**Keywords:** Objectivity Threat, Risk Judgment Performance, Internal Auditor, Malaysia

**Abstrak:** Dalam bidang pengauditan dalaman, perkembangan dalam Pengauditan Dalaman Berasaskan Risiko telah meningkatkan permintaan juruaudit untuk cemerlang dalam penilaian risiko. Kegagalan dalam peranan ini bukan sahaja membahayakan audit tetapi juga mendedahkan syarikat kepada kerugian besar dan kemudaratannya reputasi. Juruaudit dalaman, yang diamanahkan dengan keputusan kritikal, bergelut dengan cabaran objektiviti yang menghalang keupayaan mereka untuk menilai risiko syarikat dengan tepat. Kajian ini mengkaji cabaran objektiviti dalam pengauditan dalaman Malaysia dan kesannya terhadap penilaian risiko. Menggunakan tugas eksperimen dengan kerumitan yang berbeza-beza, ia mendedahkan bahawa semua sembilan ancaman objektiviti yang digariskan dalam “Piawaian Antarabangsa untuk Amalan Profesional Pengauditan Dalaman (IPPF): Panduan Amalan Kemerdekaan dan Objektiviti” berleluasa di Malaysia. Ancaman ini memberi kesan negatif terhadap penilaian risiko, tanpa mengira kerumitan tugas. Ancaman objektiviti yang menonjol termasuk tekanan sosial, kebiasaan, dan intimidasi. Yang penting, ancaman ini mempunyai kesan yang lebih ketara terhadap penilaian risiko semasa menjalankan tugas yang lebih mudah, terutamanya apabila juruaudit menilai bahagian audit rutin dan kurang rumit. Ini menyerlahkan keperluan mendesak bagi juruaudit dalaman untuk menguruskan objektiviti dengan berkesan, mengukuhkan peranan mereka sebagai penilai risiko yang tidak berat sebelah dan boleh dipercayai.

**Kata Kunci:** Ancaman Objektiviti, Prestasi Penilaian Risiko, Juruaudit Dalaman, Malaysia



## **Introduction**

The incidents of corporate collapses due to the fiduciary negligence of corporate governance actors have continuously reduced the public trust in the overall corporate governance system. The persistence of corporate failures has raised apprehensions about internal audits' efficacy in both identifying and mitigating critical risks and in delivering the value they are anticipated to provide. In some cases, there appears to be a misalignment between the expectations set by industry standards and the actual performance of internal audits in practice (Kotb et al., 2020). Internal auditors, considered among the cornerstone actors of corporate governance, have faced mounting criticism for their perceived shortcomings in discharging their duties diligently. This criticism has been substantiated by the exposure of high-profile scandals involving well-established conglomerates, such as Toshiba, which overstated profits by a staggering USD1.8 billion, and Silver Bird Berhad, where the falsification of invoices amounting to RM64.7 million came to light. In both of these instances, the failure of internal auditors to effectively assess accounting irregularities and fraud risks resulted in undetected fraudulent activities, causing significant financial losses and severe damage to the reputation of the companies involved. This failure contradicts the concept of audit quality (Deangelo, 1981).

In addition to genuine failures, there are instances where internal auditors successfully identified and raised concerns about irregularities but faced undue pressure to suppress their findings within the internal audit reports. A recent example of this occurred with The Star Entertainment Group, which became the subject of an investigation by the Independent Casino Commission in New South Wales, Australia. The allegations included money laundering, organized crime connections, and fraud taking place at its Pymont casino. The internal auditor had flagged these concerning indications, but they were unfortunately disregarded by the top management (Wootton, 2022).

This clearly indicates that the primary underlying factors responsible for the shortcomings in an internal audit's risk assessment can be attributed to a lack of objectivity (Chambers, 2015:AL Fayi, 2022). The issue of "objectivity" becomes prevalent in the internal audit context due to the uniqueness of the internal audit's dual role functions, which, on the one hand, acts as an agent to monitor the

effectiveness of the governance system (independence assurance on the effectiveness of internal control), whereas on the other hand acts as one of the management partners (consulting and advising management on governance matters). The dual roles of an internal auditor (i.e., providers of both assurance services within the organization and consultancy services to managers) expose them to conditions that threaten objectivity (Jameson, 2011). The situation deteriorates when internal auditors compromise their professional values as independent assessors in favour of their commercial interests, leading them to align more closely with the top management at the expense of other stakeholders (Khelil & Khlif, 2022). Specifically, in making judgments, the internal auditor may be influenced by objectivity threat, which is “situations, actions or relationships that are likely to lead the internal auditor to subordinate their judgment on the audit matters to that of others” (Jameson, 2011). By upholding objectivity, the internal auditor successfully resisted any external pressures that could have compromised the quality of the internal audit, including any attempts to manipulate or alter the audit report’s findings (AL Fayi, 2022). Internal auditor’s objectivity could be further enhanced if the independence at the internal audit function level is preserved, which indirectly leads to the overall internal audit effectiveness (Alqudah et al., 2023).

As the sources of information highly relied upon by multi-stakeholders such as the Board of Directors (BOD), Audit Committee (AC), and external auditors (Trotman, 2013), the issue of an internal auditor’s objectivity needs to be addressed thoroughly, especially on how it could reduce internal auditor’s ability to make sound risk judgment. The impact of objectivity on internal auditors’ risk judgment performance might vary depending on the level of complexity of the task given. As such, this study is set up to examine the relationship between objectivity threat and internal auditors’ risk judgment performance in both scenarios, namely low- and high-complexity risk judgment tasks. Specifically, the present study will provide the answer to two research questions. Firstly, it will answer the question of whether Malaysian internal auditors encounter objectivity threats and highlight the most prevalent objectivity threats they experience. Secondly, it will provide an answer on whether the objectivity threats will cause a detrimental effect on internal auditors’ risk judgment performance in two levels of

task complexity that could contribute practically to the internal audit profession.

## **Literature Review and Hypothesis Development**

### ***Risk Judgment Performance***

The auditing process is described as a sequence of processes (Bamber, 1980) which requires internal auditors to exercise their professional judgment. A study on audit judgment is crucial to evaluate the need for improvement and to identify the sources of internal and external factors and the remedies for such impairment (Bonner, 1999; Libby & Luft, 1993; Trotman, 1998). The importance of risk judgment is clearly stated in the International Standards for Professional Practices of Internal Auditing (ISPPIA), particularly in the planning stage, where the Chief Audit Executive (CAE) is required to establish a risk-based plan to direct the internal audit activity (IIA, 2016). CAE would usually depend on the input from the risk judgment made by subordinates. The expertise of both the CAE and the internal audit staff members in forming a sound risk judgment will determine the result of the risk assessment exercised, which is undertaken at least once a year. Specifically, ISPPIA states that an internal auditor “must be alert of significant risk affecting the objectives, the operation and resources” (IIA, 2016), be it the existing risk or emerging risk (Ibrahim, 2016; KPMG, 2008; Soh & Martinov-Bennie, 2011; Taha, 2023).

Kotb et al. (2020) have aptly underscored the necessity for future research endeavors aimed at exploring the evolving role of internal auditors within risk-based corporate governance. Such research should delve into how this role can be best defined, evaluated, and adapted in response to contemporary business developments. Concurrently, Hazaea et al. (2022) have passionately emphasized the urgent need for an investigation into the integral role played by internal auditors in the realm of risk management, given their pivotal function in ensuring the long-term sustainability and stability of organizations. The weight of responsibility carried by internal auditors in this context is undeniably substantial. Collectively, both studies have illuminated the critical importance of conducting in-depth research on the topic of internal auditors' risk judgment within the domains of governance, risk management, and control (GRC).”

Low-quality judgment is presented in the form of inconsistency, inaccuracy, and lack of consensus among auditors in their judgment (Iskandar & Isellin, 1996; Trotman, 1985, 1998). The case of Toshiba, Olympus, and Silver Bird Berhad present real case examples of low judgment quality by an internal auditor (Bhattacharyya, 2015; Chambers, 2015; Ibrahim, 2016; Tabuchi, 2012; The Star, 2012; Wootton, 2022). With the growing criticism of internal auditors' ability to make sound risk judgments, there is a crucial need to identify the source of flaws, especially objectivity threats.

### *Objectivity Threat*

Agentic Perspectives of Social Cognitive Theory (APSCT) argues that in many conditions, people do not have direct control over the social conditions and institutional practices that affect their day-to-day lives (Bandura, 2001). This limits the chances to secure the outcomes they desire with the given scarceness of time, energy, and resources. In an internal auditing context, the internal auditor is surrounded by social conditions (the organization's member attitude towards internal audit practices) and institutional practices (the reporting structure) that fall beyond their control. Specifically, in discharging his or her duties, an internal auditor may be influenced by objectivity threats, which are "situations, actions, or relationships that are likely to influence internal auditors to subordinate their judgment on audit matters to that of others" (Jameson, 2011). The variances in quality of assurance made by an internal auditor depend so much on individual auditor differences in exercising "objectivity" or "unbiased mental attitude" and response toward the objectivity threat from its environment.

A study by Miller and Rittenberg (2015), "The Politics of Internal Auditing", provides evidence that threats come in many forms; they can be managed and mitigated but not eliminated. The authors highlighted that professional competence alone is not sufficient to manage or mitigate threats. It also depends so much on the individual internal auditor's adherence to Standards and their commitment towards internal audit professions. Internal auditors' commitment to ethics, especially objectivity, was found to minimize audit quality behavior (Yulianti et al., 2023). Specifically, higher adherence to the Internal Audit Core Principles by internal auditors is associated with a lower likelihood of being pressured to modify audit findings (Calvin, 2021). As one of the

key corporate governance actors whose opinions are highly relied upon by the other key corporate governance actors (BODs, AC including external auditors), internal auditors need to be able to manage the objectivity threats to provide confidence in their services as independent assurers. Ashfaq et al. (2022) conducted interviews with stakeholders of internal auditors, revealing that objectivity is a pivotal factor contributing to the trust that external auditors and stakeholders place in the work of internal auditors. It serves as a determining factor in their effectiveness. This observation is further reinforced by the findings of a regression analysis, which identified a significant positive relationship between the objectivity of internal auditors and both its effectiveness and the degree of reliance placed on it by external auditors. It is thought-provoking to consider how much the job of internal auditors is influenced by the competing interests of different groups of people and the necessity to uphold their organization's credibility by maintaining a balance between being independent and objective, as suggested by Kotb et al. (2020). The enduring challenge of upholding objectivity remains a subject of scrutiny, as there exists skepticism regarding the tendency of internal auditors to align more closely with management interests, often to the potential detriment of other stakeholders (Khelil & Khelif, 2022).

IPPF Practice Guide on Independence and Objectivity (Jameson, 2011) listed nine main objectivity threats that could impair the internal auditor's objectivity. The details of each threat are depicted in Table 1.

*Table 1: Types of Objectivity Threats*

Threat	Detail
Social Pressures	Social pressure threats may arise when an auditor is exposed to, or perceived to be exposed to, pressures from external parties.
Economic Interest	This threat may arise when the auditor has an economic stake in the performance of the organization. An auditor may fear that significant negative findings, such as the discovery of illegal acts, could jeopardise the entity's future and, hence, the auditor's own interests as an employee. This threat also arises when the auditor audits the work or a department of an individual who may subsequently make decisions that directly affect the auditor's future employment opportunities or salary.

Threat	Detail
Personal Relationship	This threat may arise when an auditor is a close friend or relative of the manager or an employee of the audit client. The auditor may be tempted to overlook, soften, or delay reporting negative audit findings to avoid embarrassing the friend or relative.
Familiarity	This threat may arise because of an auditor's long-term relationship with the audit client. Familiarity may cause an auditor to lose objectivity during an audit by making the auditor overly sympathetic to the client. Alternatively, familiarity may cause an auditor to prejudge an audit client based on previous problems (or non-problems) and assume a posture consistent with the prejudgment rather than taking a fresh, objective look.
Cultural, Racial and Gender Biases	This threat may arise from cultural, racial, or gender biases. For example, in a multidivisional organization, a domestically based auditor may be biased or prejudiced against audit clients located in certain foreign locations. Alternatively, an auditor may be unduly critical of different practices and customs or an audit client managed or staffed by employees of a particular race or gender.
Cognitive Biases	This threat may arise from an unconscious and unintentional psychological bias in interpreting information depending on a person's role in a situation. For example, if someone takes a critical audit perspective, he or she may overlook positive information. Conversely, if someone takes a positive facilitative perspective, he or she may discount negative information. In addition, an auditor may come with certain preconceived notions and tend to see evidence confirming such notions.
Self-Review	Self-review threats may arise when an auditor reviews his or her own work performed during a previous audit or consulting engagement. For example, an auditor may audit a department repeatedly or in consecutive years, or the auditor may provide consulting services in connection with a system implementation that he or she subsequently must audit. Furthermore, the auditor may provide recommendations for operational improvements

Threat	Detail
	and subsequently review processes that were changed in accordance with those recommendations. All of these examples represent situations in which the auditor could conceivably become less critical or observant of the errors or deficiencies due to the difficulty of maintaining objectivity when reviewing his or her own work.
Intimidation	Intimidation threats arise when an auditor is deterred from acting objectively by threats—actual or perceived—or being overtly or covertly coerced by audit clients or other interested parties.
Advocacy	Advocacy threats arise from auditors acting biased in promoting or advocating for or against the audit client to the point that subsequent objectivity may be compromised.

Source: IPPF: Practice Guide on Independence and Objectivity (Jameson, 2011)

Comparing the listed objectivity threats, the most highly cited objectivity threats in the academic literature are the social pressure threat, familiarity threat, and self-review threat resulting from certain conditions, especially the internal audit's organizational status, dual roles (assurance versus consulting) and the use of internal audit as a management training ground (Stewart & Subramaniam, 2010). A study conducted in the Middle East found that social pressure is present in the form of persistent workplace bullying over an extended period, which has a detrimental impact on an internal auditor's ability to confidently voice valid opinions and identify flaws, mistakes, and unethical conduct (Taha, 2023). At times, internal auditors may find themselves compelled to offer somewhat partial information and reports in an attempt to evade bullying from senior managers. Additionally, they may face isolation as they hesitate to openly discuss the challenges they encounter in the workplace. These factors collectively contribute to a diminished dedication to improving internal audit processes and practices (Taha, 2023). In Malaysia, Razali et al. (2016) found the most prevalent objectivity threats are social pressure threats, cognitive biases threats, and intimidation threats. The result of the study indicates a loophole in the governance of internal audit, particularly in the aspect of the reporting line (Chambers & Odar, 2015), which need to be addressed to ensure that internal auditor can discharge their duties objectively. The

results supported Ali et al. (2012) and Shamsuddin et al. (2014), who found that internal auditors are threatened to the extent that they are hindered from performing their duties efficiently and effectively.

Samagaio and Felício (2023) found that the quality of internal auditing is boosted when internal auditors can perform their work without threats of self-interest, intimidation or otherwise. When the objectivity of the internal auditor is threatened, they tend to subordinate their judgment on audit matters (Jameson, 2011; Khelil & Khelif, 2022). Objectivity threats have been proven to have a negative impact on external auditor judgment performance (i.e., accuracy, consistency, and consensus). In both scenarios, low- and high-complexity tasks and the level of social pressure experienced by an individual internal auditor will explain the variance in their risk judgment performance. While the existence of social pressure in the Malaysian internal audit environment is known (Ali et al., 2012; Razali et al., 2016; Shamsuddin et al., 2014), its influences on internal auditor's risk judgment performance are yet to be explored. This argument leads to the following hypothesis:

H<sub>1</sub>: Internal auditor's objectivity threats negatively influence internal auditors' risk judgment performance.

## **Research Methodology**

### ***Participants***

The questionnaires of this study were randomly sent to internal auditors of 300 Public Listed Companies and 300 Government Agencies located around Wilayah Persekutuan, Selangor, and Wilayah Persekutuan Putrajaya. A booklet containing the research instrument was distributed to 600 potential respondents. Of the distributed booklets, 274 completed instruments were returned, indicating a 45.6% response rate.

### ***Data Collection***

A sample of 274 individuals working as internal auditors in the private sector (188 samples, 69%) and public sector (86 samples, 31%) organizations in Wilayah Persekutuan, Selangor and Wilayah Persekutuan Putrajaya were collected. Table 2 presents the selected demographic characteristics of the respondents in this study.



*Table 2: Demographic Information*

Demographic	Detail	Sector				Total n = 274	
		Private Sector		Public Sector		Frequency	Percent
		Frequency	Percent	Frequency	Percent		
Gender	Male	85	45.2	43	50	128	46.7
	Female	103	54.8	43	50	146	53.3
Race	Malay	140	74.5	78	90.7	218	79.6
	India	14	7.4	5	5.8	19	6.9
	Chinese	33	17.6	1	1.2	34	12.4
	Others	1	0.5	2	2.3	3	1.1
Position	Chief Audit Executive	8	4.3	2	2.3	10	3.6
	Senior Manager	22	11.7	8	9.3	30	10.9
	Manager	50	26.6	6	7.0	56	20.4
	Assistant Manager	28	14.9	15	17.4	43	15.7
	Senior Executive	50	26.6	16	18.6	66	24.1
	Executive	29	15.4	37	43.0	66	24.1
	Others	1	0.5	2	2.3	3	1.1
Experiences	Less than 5 years	78	41.5	47	54.7	125	45.6
	5 to 10 years	72	38.3	29	33.7	101	36.9
	10 to 15 years	21	11.2	8	9.3	29	10.6
	More than 15 years	17	9.0	2	2.3	19	6.9
Professional Qualification	Certified Internal Auditor (CIA)	30	16.0	7	8.1	37	13.5
	Chartered Accountant (CA)	27	14.4	13	15.1	40	14.6
	Certified Public Accountant (CPA)	5	2.7	2	2.3	7	2.6
	Certified Global Management Accountant (CGMA)	7	3.7	1	1.2	8	2.9
	No Professional Qualification	119	63.3	63	73.3	182	66.4

Out of the total respondents, 128 were males (Private: 85, Public: 43) and 146 were females (Private: 103, Public: 43). The 274 internal auditors comprised ten (Private: 8, Public: 2) Chief Internal Auditors (CIA), thirty (Private: 22, Public: 8), senior managers, fifty-six (Private:

50, Public: 6) managers, forty-three (Private: 28, Public: 15) assistant managers, sixty-six (Private: 50, Public: 16) senior executives, sixty-six (Private: 29, Public: 37) executives, and four respondents under other positions. Meanwhile, 54.4% of the respondents have more than five years of experience (101 less than ten years; 48 more than ten years); 33.6% of the respondents possess a professional qualification, while the rest have no professional qualifications.

### ***Research Instrument***

The employed research instrument contained three main sections. The first section presented the audit task for the experiment. The task related to risk judgment has two levels of complexity: high and low. Respondents were required to perform both high-complexity and low-complexity audit tasks. The second section contained items concerning “objectivity threat”. The last section concerned respondent’s demographic characteristics, which also included questions on experience.

This study used risk judgment associated with the internal control findings related to procurement and collection procedures, as this area is reported to be susceptible to irregularities and fraud. The instrument was placed in a booklet together with a cover letter and prepaid envelope. Prior to the actual survey, the contents of the audit task that were to be used as the experimental instrument were validated by experts comprising six internal auditors (with more than 10 years of experience as an internal auditor) and five senior accounting lecturers. The objective of the validation was to ensure that the information and statements contained in the instruments were realistic and reflected the actual nature of risk judgment performed by internal auditors. Based on the experts’ feedback, improvements were made in both cases concerning word choice, sentence structure, and case format. The participating experts agreed that the two cases differ in their level of complexity.

### ***Operationalization of Variables***

#### ***Risk Judgment Performance***

The measurement for risk judgment performance used in the main study is presented via two risk judgment task scenarios, namely Audit Task 1 (less complex) and Audit Task 2 (complex). Bonner (2008) stated that the task factors could influence one’s judgment. Accordingly, Shaw (1981), as cited in Kim and Soergel (2006), stated that the chances of the outcome

of the task being substandard increases as task difficulty increases. Therefore, to provide a robustness of the result, Audit Task 1 has been specifically developed to be less complex than Audit Task 2. Audit Task 1 involves the risk judgment on internal control deficiencies in property, plant, and equipment procedures, whereas Audit Task 2 involves the risk judgment on internal control deficiencies in collection procedures. The potential risk for property, plant, and equipment procedure in Audit Task 1 has been developed to be direct and straightforward, thus enabling the auditor to easily perform risk judgment without exercising extra cognitive effort. Risk judgment performance on the less complex task is evaluated based on the percentage of the correct answers to questions on the risk associated with property, plant, and equipment procedure, as depicted in Figure 1.

<p><b>Panel A: Potential Risk</b></p> <ul style="list-style-type: none"> <li>• Misappropriation of assets.</li> <li>• Unrecorded property, plant, and equipment.</li> <li>• Financial loss due to unexpected damages.</li> <li>• Misclassification to conceal unauthorized purchases.</li> <li>• Unauthorized purchase of property, plant, and equipment.</li> <li>• Overstatement of property, plant, and equipment.</li> <li>• Unauthorized disposal of property, plant, and equipment.</li> <li>• Physical loss of equipment.</li> </ul>
<p><b>Panel B: Internal Control Deficiency</b></p> <ul style="list-style-type: none"> <li>• Authority limits for procurement (manual and system) are not updated in line with the latest authorization limit approved by the Board of Directors. Five out of ten properties purchased exceeded the manager's approval limit.</li> <li>• Three incidents of capital expenditure (all items above RM10,000 have been expenses under "Miscellaneous Expenditure" in the Statement of Income. The payment has been approved by the Head of Department.</li> <li>• All items are disposed of with prior approval from authorized personnel. However, there is no procedure for the sale of the disposed assets (i.e., quotation from the potential buyer of wreckage, and recordings of the disposal's proceedings).</li> </ul>

- The insurance coverage for material properties is not consistently monitored (i.e., expiry, no insurance coverage, etc.)
- The Property, Plant and Equipment Listing does not tally with the General Ledger.
- The useful lives of the assets are not consistently applied to similar assets.
- Properties are recorded in the Property, Plant, and Equipment Listing but they do not exist.
- The equipment is not properly tagged.

*Figure 1: Audit Task 1 (Less Complex task) - Risk Judgment on Internal Control Deficiencies for Property, Plant and Equipment Procedure*

On the contrary, the potential risk for the collection procedure in Audit Task 2 has been constructed to be long and detailed. It has also been constructed to be closely related to each other, thus indirectly forcing internal auditors to exercise extra cognitive effort. The instrument has been validated by an expert to ensure that the level of difficulties and level of cognitive effort for completion of the task differs between Audit Task 1 and Audit Task 2. This is crucial since the level of task complexity might explain variance in the internal auditor's risk judgment performance. The risk judgment performance of the highly complex task is determined based on the percentage of correct answers to questions on the risk associated with the collection procedure, as depicted in Figure 2. The total scores for each task were pre-determined based on the answers developed following a series of discussions with professionals and senior academics.

**Panel A: Potential Risk**

- Collection on misappropriated accounts, concealed by debits into other accounts besides cash accounts (e.g., expense account) or by incorrect issue of credit note.
- Invalid or incomplete data and information could possibly cause delays in the decision-making process.
- Collectable accounts are written off or otherwise credited; customer remittances are misappropriated.
- Lack of audit trail on the handover of cash.

<ul style="list-style-type: none"><li>• Cheques received are deposited but not recorded; cheques written to employees for the same amount are also not recorded.</li><li>• Fictitious customers or invoices are added to the trade debtor's master file.</li><li>• Unauthorized disposal of property, plant, and equipment.</li><li>• Delays in the detection of the manipulation of accounting entries to perpetrate fraud.</li></ul>
<b>Panel B: Internal Control Deficiency</b>
<ul style="list-style-type: none"><li>• There is no segregation of duties in the collection process. The designated Accounts Clerk received (cash/cheque), recorded it in the Collection Register and prepared an official receipt.</li><li>• A review of the data entry for cash receipts from January 2015 to December 2015 discovered that important information (i.e., official receipt number, payer name) was left blank. This contributes to unresolved, long outstanding, unreconciled items.</li><li>• There is no segregation of duties between the Cashier and Debtor Officers (responsible for sending monthly statements to all or overdue customers). Complaints are handled by the same person.</li><li>• Long unreconciled transactions are not promptly investigated.</li><li>• The sharing of the password for data entry of the sales transaction.</li><li>• No limits for the approval of customer credit notes (including write-offs) in the system.</li><li>• A daily reconciliation does not include the procedure to match proof of cash deposit/cheque bank-in to the journal ledger and cash collection register.</li></ul>

*Figure 2: Audit Task 2 - Complex task - Risk Judgment on Internal Control Deficiency in Collection Procedure.*

### Objectivity Threats

Objectivity threats were measured by nine (9) items representing nine (9) types of objectivity threats, as listed in the IPPF Practice Guide on Independence and Objectivity (Jameson, 2011) (see Table 1 for details). The respondents were asked to indicate on a 7-point Likert scale (i.e., 1= never; 7=always) the frequency of possible threats that they have encountered in task situations with an auditee.

### Manipulation Check

The manipulation checks on the task complexity are measured by three different questions: whether the task requires coordination among different activities, whether the task is complex, and whether the task is mentally demanding. These items were adapted from Iskandar and Sanusi (2011). Upon completion of the task, respondents were requested to rate each of the questions on a 7-point Likert scale (i.e., 1= strongly disagree; 7=strongly agree).

### **Results**

#### *Descriptive Statistics*

Table 3 presents the descriptive statistics on risk judgment performance for low- and high-complexity audit tasks. The mean value of risk judgment performance is the percentage of the total scores of the correct answers obtained by each participant over the overall scores assigned to each task.

*Table 3: Descriptive Statistic-Risk Judgment Performances*

Variables	Low Task Complexity n=274				High Task Complexity n=274			
	Mean	Std. Dev	Lowest Mean	Highest Mean	Mean	Std. Dev	Lowest Mean	Highest Mean
Risk Judgment Performance	55.931	24.935	12.5	100.0	40.967	16.417	12.5	75.0

The mean value of risk judgment performance for low-complexity tasks is 55.9%, ranging from 12.5% to 100%. Meanwhile, the mean value for risk judgment performance for high-complexity tasks is 41.0%, ranging from 12.5% to 75%. The variance of the means score between low- and high-complexity tasks reflects a higher level of difficulty and effort needed to perform high-complexity tasks.

Table 4 presents the descriptive statistics of social pressure experienced by Malaysian internal auditors. Out of 274 respondents, 76.3% agreed that they had been directed to suppress or significantly modify valid internal audit findings or reports ( $M=3.201$ ,  $SD=1.708$ ). More than half of the respondents (68.2%) agreed on the fact that the

situation that led to such pressure was due to “operational audits that would reflect badly on key operational management” ( $M=3.058$ ,  $SD=1.811$ ). Other situations that led to pressure to suppress or significantly modify valid internal audit findings or reports include a) financial reporting issues conflict with the external auditor or the Chief Financial Officer (59.5%,  $M=2.577$ ,  $SD=1.680$ ), b) the executive’s misuse of corporate funds (52.6%,  $M=2.431$ ,  $SD=1.683$ ), and c) the executive’s misuse of travel-related funds (53.3%,  $M=2.343$ ,  $SD=1.621$ ).

*Table 4: Descriptive Statistics-Objectivity Threats Experienced by Internal Auditor*

Types of threats	Mean Score	SD	Percentage of respondents who reported that objectivity threats occur at least sometimes
Social Pressures	4.507	1.404	97
Cognitive Biases	3.989	1.658	90
Intimidation	4.033	1.754	90
Familiarity	4.398	1.469	88
Personal Relationship	3.307	1.559	87
Self-Review	3.927	1.564	93
Economic Interest	3.781	1.395	95
Advocacy	3.799	1.480	93
Cultural, Racial and Gender Biases	3.945	1.490	93

The analysis and discussion of the results were structured around the answers to the two research questions specified above. Thus, the response relating to RQ1 allowed us to conclude that objectivity threats existed in the Malaysian internal auditing environment. Data from Table 4 addressed RQ1 and indicated that internal auditors in Malaysia did encounter all nine objectivity threats (social pressure, economic interest, personal relationship, familiarity, cultural, racial and gender biases, cognitive biases, self-review, intimidation, and advocacy), as listed in the IPPF: Practice Guide on Independence and Objectivity (Jameson, 2011). Furthermore, the results showed 97% of respondents admitting to social pressure threats (mean=4.51, 97%) as being the most prevalent threats in the Malaysian internal audit environment. This is followed by familiarity threats (mean=4.39, 88%), intimidation threats (mean=4.03,

90%), and cognitive biases (mean=3.89, 90%). Social pressure, by definition, is a threat that may arise when an internal auditor is exposed to or perceives that he or she is exposed to pressures from external parties. Meanwhile, intimidation threat is the threat that may arise from actual or perceived pressures or being obviously or secretly pressured by audit clients or other interested parties (Jameson, 2011). This finding was consistent with Miller and Rittenberg (2015), who found that internal auditors were pressured to omit high-risk areas and were directed to purposely audit low-risk areas. The result of the current study indicates a loophole in the governance of internal audit, particularly in the aspect of the reporting line (Chambers & Odar, 2015), which need to be addressed to ensure that internal auditor can discharge their duties objectively. The results also supported Ali et al. (2012), Shamsuddin et al. (2014), and Taha (2023), who found that internal auditors were threatened to the extent that they were hindered from discharging their duty efficiently and effectively.

In contrast to social pressure and intimidation, cognitive biases originate from the internal auditors themselves. Cognitive biases are defined as threats that may arise from an unconscious and unintentional psychological bias in interpreting information (Jameson, 2011). In this condition, an internal auditor may have a predetermined notion and tend to find evidence confirming the notion while neglecting important information. This finding might indicate a lack of attention to the need for professional scepticism in the internal audit profession. While IPPF is silent about the concept of professional scepticism, ISA 200 (applicable for external auditors) stresses the need for “*an attitude that includes a questioning mind, being alert to conditions, which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence* (ISA 200: Para 13(l): page 79)” (IFAC, 2009). Overall, in addressing RQ1, the results are consistent with the study done in other jurisdictions, which reported social pressure threats (Stewart & Subramaniam, 2010) as the major objectivity threat. However, Malaysian internal auditors experienced a low occurrence of self-review threats (mean=3.85) as compared to other jurisdictions, for instance, in Singapore (Goodwin & Yeo, 2001). This is supported by Ahmad and Taylor (2009), who found that Malaysian internal auditors did not perceive a conflict between their assurance and consulting roles and thus experienced low self-review threats.



**Data Analysis**

To test the model developed, we used the partial least square (PLS) approach. PLS is a second-generation multivariate technique (Hair et al., 2012) that can simultaneously evaluate the measurement model (the relationships between constructs and their corresponding indicators) and the structural model (the relationships between construct and construct).

Measurement Model

The current study used partial least squares (PLS) modeling using the SmartPLS 3.3.3 version (Ringle et al., 2015) as the statistical tool to examine the measurement and structural model. We followed the suggestions of Anderson and Gerbing (1988) to test the model developed using a 2-step approach. First, we tested the measurement model to test the validity and reliability of the instruments used, following the guidelines of Hair et al. (2019) and Ramayah et al. (2018). Next, we ran the structural model to test the hypothesis developed.

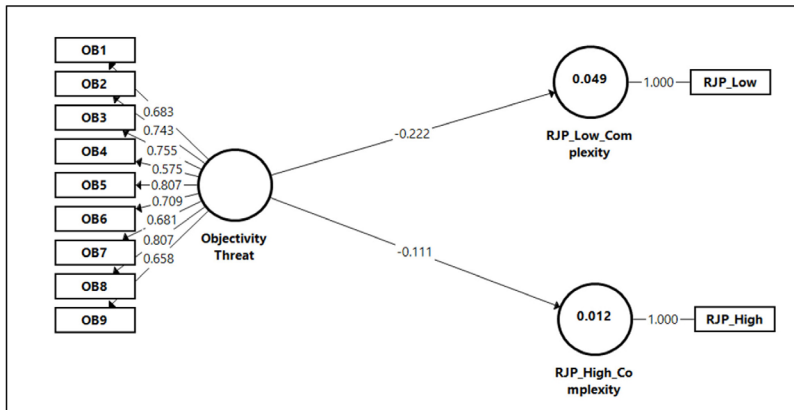


Figure 3: The PLS Algorithm Results

Before interpreting the results of our structural models, we evaluate the quality of our measurement models. Objectivity threat was measured reflectively by 9 indicators: social pressure, economic interest, personal relationship, familiarity, cultural, racial and gender biases, cognitive biases, self-review, intimidation, and advocacy. The measurement model of the study is depicted in Figure 3. As summarized in Table 5, the reflective measurement model for objectivity threat performs well

with regard to standard quality criteria. All outer loadings are above the 0.70 threshold except for social pressure (0.68), familiarity threat (0.58) and economic interest (0.68), which is adequate as long as the AVE meet the threshold of 0.50 (Thurasamy et al., 2018). The average variance extracted of 0.513 exceeds 0.50, indicating appropriate convergent validity of the construct. Finally, the composite reliabilities are above 0.90 but below 0.95, indicating appropriate construct reliability. The discriminant validity of the objectivity threat construct fulfils the criterion of HTMT 0.90 (Gold et al., 2001), thus signifying that discriminant validity has been ascertained. Besides, the result of HTMT inference also shows that the confidence interval does not show a value of 1 (Henseler et al., 2015), which also confirms discriminant validity. Taken together, both these validity tests show that the measurement items are both valid and reliable.

*Table 5: Reflective Measurements and Quality Criteria*

Reflective and Single-item measure	Loading > 0.70	AVE > 0.50	CR > 0.70	HTMI CI without 1
<b>Objectivity Threat</b>				
Social Pressures	0.683	0.513	0.904	RJP_High [0.056:0.175]
Cognitive Biases	0.743			RJP_Low [0.105:0.175]
Intimidation	0.755			
Familiarity	0.575			
Personal Relationship	0.807			
Self-Review	0.709			
Economic Interest	0.681			
Advocacy	0.807			
Cultural, Racial and Gender Biases	0.658			
Risk Judgment Performances	1			

Note: AVE average variance extracted, CR composite reliability, CI 90% bias-corrected confidence interval, HTMT heterotrait-monotrait-ratio

Structural Equation Model-Partial Least Square

To evaluate the structural models' predictive power,  $R^2$  was calculated to represent “the amount of variance in the dependent variable explained by all the independent variables linked to it” (Hair Jr et al., 2017, p.209). Internal auditor's objectivity threats explained 5% of the variance in the low-complexity risk judgment performance, whereas it explained only 1.2% of the variance in high-complexity risk judgment performance. Using a bootstrapping technique with a re-sampling of 500, the path estimates and  $t$ -statistics were calculated for the hypothesized relationships.

Specifically, RO2 of the present study is to examine the effect of objectivity threat on internal auditor's risk judgment performance. As depicted in Figure 4, it was found that social pressure was negatively related to audit judgment performance regardless of the level of complexity of the risk judgment task performed (low complexity:  $B = -0.222, p < 0.05$ ; high complexity:  $B = -0.111, p < 0.10$ ).

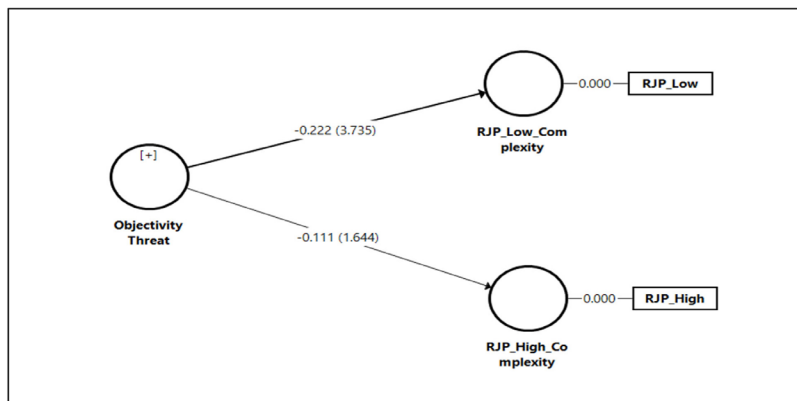


Figure 4: Structural Model

The impact of social pressure on risk judgment performance is higher in the low-complexity task ( $B = -0.222$ ) than in the high-complexity task ( $B = -0.111$ ). This result indicates that the severity of the objectivity threats in influencing risk judgment performance is higher when internal auditors perform risk judgment in the area that they are familiar with and less complex. On the other hand, in a high-complexity task that involves a high level of uncertainty in performing the task successfully, the internal auditor might exercise a high level

of scepticism and precaution to reduce the risk of making improper risk judgments. Hence, in this condition, the severity of the objectivity threat on the risk judgment could be minimized. Thus, H1 is supported in both low- and high-complexity tasks. The result of hypothesis testing is depicted in Table 6 as follows:

*Table 6: Hypothesis Testing*

Hypothesis	Beta	SE	t-value	p-value	Decision
H1 Objectivity threat -> Risk Judgment Performance (Low Complexity)	-0.222	0.059	3.735*	0.000	Supported
Objectivity threat -> Audit Judgment Performance (High Complexity)	-0.111	0.068	1.644**	0.050	Supported

Notes: \* $p < 0.05$ , \*\* $p < 0.10$

## Conclusions and Practical Implications

Recently, there has been growing criticism toward internal auditors (as one of the key corporate governance actors) for their failure to discharge their responsibility diligently. Internal auditors' failure to assess the existence of accounting irregularities and fraud risk led to fraud when undetected, causing huge company losses and reputation damage. The main root cause might be the influence of objectivity threat, which is "situation, actions or relationships" that are likely to lead internal auditors to compromise their judgment on the audit matters to that of others. This study yielded persuasive empirical evidence of the existence of all nine objectivity threats listed by IPPF (social pressure, economic interest, personal relationship, familiarity, cultural, racial and gender biases, cognitive biases, self-review, intimidation, and advocacy) in the Malaysian internal audit environment. Malaysian internal auditors perceived that social pressure threat, familiarity threat, intimidation threat, and cognitive biases were the most prevalent threats that existed in their environment. The existence of social pressure and intimidation threats signal loopholes in the current governance, especially in the context of the reporting line of internal auditors. Internal auditors are hindered from discharging their fiduciary duty independently and objectively. The condition worsens with the existence of familiarity threats. This might be the main cause of internal auditors' failure to detect and report frauds and irregularities objectively. In contrast to

social pressure and intimidation threats, internal auditors also concede the existence of cognitive biases (psychological threats), which signal the need for more attention to be paid to the importance of the concept of professional scepticism in the internal audit profession. Most importantly, the existence of objectivity threats has been proven to cause detrimental effects on the internal auditors' risk judgment performance, especially when the threats are imposed by those entrusted to govern internal audit activity in an organisation, such as the audit committee.

Practically, this empirical evidence is important to create awareness among the individual internal auditors as well as their stakeholders on the negative impact of objectivity threat on the internal auditors' risk judgment performance. In order to perform risk judgment with an unbiased mental attitude, individual internal auditors should recognise the possible action, situation or relationship that could induce social pressure. Implementation of possible mitigating measures that may reduce or eliminate the social pressure should be undertaken to increase internal auditors' ability to perform risk judgment, thus enhancing the quality of assurance made. Since the impact of objectivity threat on risk judgment performance is severe in the low complexity task as compared to high complexity task, mitigating measures such as rotation of audit assignment assigned to an individual could be implemented. Governance of internal audit should be strengthened so that the loopholes that lead to the existence of objectivity could be improved. Quality assurance by an external independent party, such as the Institute of Internal Auditor Malaysia, can be an alternate mitigating measure that could oversee the quality of internal audit governance in an organization. For instance, the quality of the audit committee (such as competency of audit committee members, conflict of interest, etc.) will be monitored in the quality assurance exercise. Given the findings derived from this current study, future studies could explore the individual internal auditors' characteristics that could reduce the impact of objectivity threats on internal auditors' risk judgment performance. Future research could also consider environmental factors that could minimize the impact of objectivity threats, such as external quality review so that internal auditors could provide high-quality risk-based assurance on an organization's governance, risk management, and control.

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