

# **Evaluating The Independence Of The Internal Auditorcase: Case Study Of Al-Bariga Oil Marketing Company**

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## **Abstract:**

This study aims to examine whether or not the internal auditors in Al-bariga Oil Marketing Company (AOMC) operate in accordance with the necessary independence to permit the objective performance of duties and responsibilities. Qualitative approach was selected because it was found to be appropriate for this study and an interview guide was prepared and used to collect the necessary data during the interviews conducted with the director of internal audit (DIA), financial controller, internal auditors and internal audit coordinators. Accordingly, descriptive analysis of the data was adopted in order to examine the independence of the internal auditor within AOMC. It's concluded that the internal audit department (IAD) within the

company maintains its independence to a large extent which means that the independence of internal auditors can be considered as effective.

Based on results gained from the study, the AOMC recommended to having Audit Committee connected with the IAD to support the internal auditors independence.

**Introduction:**

The importance of the internal audit function in organisations has grown dramatically over the past decade and is expected to continue expanding. In recent years, the number of companies with internal audit departments has increased and the average size of their internal audit staff has grown [Schneider, 1985]. In the UK, an independent survey commissioned by Ernst and Young [1995] revealed that 61% of organisations had an internal audit department. 75% of retail, utility and financial services organisations had internal audit departments, while, in manufacturing, this decreased to only 45% [Liu et al., 1997]. In Libya, 65% of public enterprises (LPEs) have internal audit departments, but the other 35% do not. However, most of those which do have such departments still limit their role to the detection of fraud, with the emphasis on examining accounts before payment, collecting income and checking petty cash claims [Kilani, 1988].

In some years ago, internal auditing has been seen to emerge from a relatively underdeveloped professional status to one of major importance in terms of its size and level of contribution [Carmichael and Willingham, 1986]. During that time, it has been seen as covering primarily accounting and financial matters. Today it is concerned with all the different facets of internal control of the organisation. This process has transformed IA from being a minor player to occupying

the important position it holds in organisations today [Haimon, 1998, Carmichael and Willingham, 1986].

Almost every company of substantial size has a team of internal auditors, and many smaller ones have at least a single internal auditor [Cook and Winkle 1980]. These persons are fulfilling the function of IA, which has developed to help keep management informed about its operations as the top management feel that there has been a growth in the difficulties of driving and controlling the business operation at the grass roots level [Yan and Dunjia, 1997]. Both internal auditors and top management need continually to evaluate the activities of every section of their organisations to determine whether the goals and objectives of the organisation are being accomplished.

In this respect also, Higson [2004, p. 79] indicated that "the existence of an IA function does depend very much on the nature and size of the company being audited. It still tends to be the largest companies which make extensive use of them". As companies continued to grow, with increasing numbers of employees and widely scattered operations, the IA function developed to provide consultation to the owners and managers in relation to various activities of the organisation and assurance that internal operations were functioning properly [Cook and Winkle,1980; Arens,1997; Fernandes,2000].

Furthermore, internal auditors have been challenged not only to work on problems but also to work with management to recommend solutions [Rittenberg, 2000]. The IA has been described as the "window into the whole company"[ Church et al., 2004,p.196]. The new definition of IA defines the function as "an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation

accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes"[Albert and William 2002]. In this respect, Marks [2002, p. 2] indicated that, "in response to changing business demands, audit departments of the future are likely to be different in several key ways. For instance, we will audit faster and place more emphasis on real-time risk and controls consulting. Staffing will change accordingly, with more IT-proficient auditors. Instead of focusing on a list of audits from an audit schedule, we will be concerned primarily with assurance: providing peace of mind to our clients that business risk is being managed effectively-even, or especially, during turbulent times. Most importantly, however, we will need to start looking further ahead and rethinking our traditional approach to audits".

Therefore, for internal auditors to do so, they should be independent of the activities they audit. The concept of independence applies to both the internal audit activity and individual internal auditors. Appropriate organisational status ensures the activity's independence. Individual independence, however, depends on the objectivity of each internal auditor [Colbert 2002]. Therefore, this study aims to examine whether or not the internal auditors in AOMC operate in accordance with the necessary independence to permit the objective performance of duties and responsibilities.

### **Literature Review and Research Problem:**

The recent emphasis on consulting activities has brought new questions and concerns regarding the ability of internal auditors to function in an independent and objective manner [Richard & Jordan,

2000]. A key characteristic of an effective internal audit department is the independence with which it operates. Internal auditors should be free of organisational pressures that limit their objectivity in selecting areas to be examined or in evaluating those areas. Victor [1979, p.23] points out that *"One of the internal auditor's most important contributions to the organisation (and perhaps to society) is independence"*. Rittenberg [1977, p.20] developed the following comprehensive definition of internal auditor independence:

*"Internal auditor independence is the ability of a technically competent auditor to conduct and fully report on the results of an audit without personal bias or prejudice and with the ability to determine audit areas, audit scope, and audit procedures without adverse or controlling influence from the auditee or other managerial segments of the organisation"*.

As can be seen from this definition, the notion of internal auditor independence has two dimensions. The first is a personal attribute that deals with an auditor's integrity and competence. The second deals with the organisational environment to which the auditor belongs. This latter dimension affects the auditor's ability to maintain independence, which is contingent upon, or surrogated by, such factors as his organisational status, the availability of adequate resources, the attitude of auditees, the scope of audit and other organisational related factors.

The perceived independence of auditors is vital to the maintenance of public trust in the auditing. Independence of judgment has been defined as the ability of an individual to resist pressure and maintain an unbiased attitude when faced with pressure [Anandarajan & Umar, 2004].

The Institute of Internal Auditors (IIA) stresses the importance of organisational independence of the internal audit function with the chief internal auditor reporting to a level within the organisation that allows the function to fulfill its responsibilities [Goodwin, 2004].

When one looks at the definitions of IA provided by the IIA, it becomes apparent that they all contain the word "Independence". In this respect, Woolf [1983] indicated that auditors who have lost their independence have lost their *raison d'etre*; they have become dependent, and a dependent auditor is a contradiction in terms. To support these views, the IIA [2001] has stated that "*Internal auditors should be independent of the activities they audit*". Independence is the essence of auditing. An internal auditor must be independent of both the personnel and operational activities of an organisation. Otherwise, the integrity of his opinions, conclusions and recommendations would be suspect. So, independence is necessary for the effective achievement of the function and objectives of IA. One could argue that since the internal audit department is located within the company and its members are all employees of the company, it cannot be independent and is not in a position to take an independent attitude to examination and reporting.

In their discussion of practitioner independence, Mautz and Sharaf [1961, pp. 204-208] pointed out the following attributes as the main aspects of this independence:

- 1- Programming independence which means that the internal auditor is free to define how the selected areas will be audited and what procedures will be applied.
- 2- Examining independence which means that the internal auditor should have freedom to examine all areas that affect the organisations' activities.

- 3- Reporting independence which means that the right to report the full facts is seen as an important aspect of independence.

The independence or objectivity of internal audit has been identified by the IIA, the American Institute of Certified Public Accountants (AICPA), and others as crucial to the viability of the IA function.

The concept of independence is generally used to mean sufficient independence for the auditor to be fair and objective in his / her review and appraisal and not to be under undue pressure from any party to the extent that this could bias his / her opinion. Peter and Robert [1990] found that objectivity or independence was a significant variable in the evaluation of reliance if the status of the director of internal audit was such that the company's audit committee consulted him about the work of the external auditor. It is easy to argue that the internal auditors cannot be independent because they are employees of the company and therefore are not in a position to take an independent attitude to their examination and reporting. However, Sawyer [1995] indicated that although complete independence is not an attainable goal for the internal audit function, practical independence is possible and essential. Albrecht et al., [1988] indicated that an efficient IAD should be regarded as a good place to develop employees' careers, because internal auditors can understand the whole operation in a company. Therefore, if the internal auditor is to serve the organisation as a whole, it is important that independence is upheld.

Moreover, if the IA function cannot be established as an independent function, there is no purpose in even considering the setting up of a department. Therefore, to enable the internal auditor to perform his duties, independence has to be guaranteed. This independence is obtained mainly from the following two

characteristics identified by the IIA standards - organisational status and objectivity.

**Organisational Status:**

*"The organisational status of the internal audit department should be sufficient to permit the accomplishment of its audit responsibilities" [IIA, 2001].*

One of the most, if not the most, important elements that determine how well the internal audit department carries out its task is its organisational status. As suggested in the IIA's Statement of Responsibilities [IIA, 2001], the organisational status of the IA function and the support accorded to it by management are major determinants of its range and value.

Therefore, internal auditors should be positioned in the organisational structure of a company so that they may extend without restrictions their examination over all aspects of its operations. However, different organisations have different strategies as to where they locate their internal audit departments. Some internal audit departments fall under the control of the financial section, some under the accounting section, and others have IA as a section on its own.

Though the size of the organisation and the audit department itself play a role in determining the location of the department, ideally it should be a separate department that falls outside the control of any other. This means that the director or manager of the internal audit department will be directly responsible to and report to the highest authority in the company. It is important that internal auditors report to an authority that is in a position to take action on the recommendations in their report.

Personal Objectivity:

The IIA's Statement [2001] states that "*Internal Auditors should be objective in performing audits*". It defines the objectivity as an "*Independent mental attitude which internal auditors should maintain in performing audits. Internal auditors are not to subordinate their judgment on audit matters to that of others*". Objectivity is essential to the IA function. Therefore, internal auditors should not develop and install procedures, prepare records, or engage in any other activity which they would normally review and appraise and which could reasonably be construed to compromise their independence. It is important to mention here that Statement of Auditing Standards (SAS.No. 9) identified objectivity as one of the three general factors which the external auditors should consider when evaluating the strength of IA as a basis to determine the degree of reliance.

Most previous studies have found that external auditors perceived independence as the most important factor when evaluating the effectiveness of the IA function. For example, Brown [1983] who studied factors that might be considered important in evaluating the reliability of an IA function, as well as the degree to which use is made of them found that two factors dominated the external auditors' judgments, namely, (1) the independence of the IA function and (2) satisfaction with that function during previous audits. He also found that, of these two, independence was the primary factor used to evaluate the reliability of an IA function. Also independence and previous satisfaction accounted respectively, for an average of 19% and 25% of the judgment variance across all auditors. Boyle [1993] studied the external auditor's reliance on IA as a part of his study. When he asked the participants to grade a number of reliance criteria, the external auditors rated the independence and the objectivity of

internal auditors in second place, but he found that the internal auditors believed that their working papers were a more important factor for the external audit firm's evaluation of reliance. Campfield [1960; 1965; 1971] agreed that independence is one of the most important standards for internal auditors. He also stated that it is a very difficult responsibility since the internal auditor is employed by the company which he is examining. He feels that a large part of this responsibility must be borne by the individual auditor through the maintenance of a very high degree of independence in his attitude. Recently, Rittenberg [2001] issued a call for research to determine whether internal auditors are able to maintain objectivity in this expand role.

Despite the importance of controlling and evaluating the independence of the internal auditors in various economic activities in Libya, no formal guidelines are provided to support this evaluation. Therefore, the next requirements identified by the IIA [2001] will be used as guidelines to evaluate the internal auditor independence in Al-bariga Oil Marketing Company:

- The organisational status of the IAD should be sufficient to permit the accomplishment of its audit responsibilities.
- The decision to appoint or remove the DIA should be made by the highest level.
- The DIA should report directly to the highest level.
- The DIA should has the right to discuss the report with the level that he responsible to.
- The internal audit staff should has unrestricted access to all information and personnel.
- The internal auditors should carry out their work freely and objectively.

- The DIA should decide what subjects will or will not appear in the audit work plan.
- The DIA should produce the audit plan without restrictive amendment.
- Internal auditors should not be involved in non-audit work for the company during the year.
- The DIA should has the right to attend all the regular meetings within the company.
- The DIA should has top management support for his work and recommendations.
- The top management should issued statement requiring all departments and managements within the company to follow the internal audit recommendations.
- The DIA should has a direct communication link to the highest level of management.
- Internal audit staff should not assume designing or operating responsibility.
- Persons transferred to or temporarily engaged by the internal auditing department should not be assigned to audit those activities they previously performed until a reasonable period of time has elapsed.

Based on the forgoing discussion, the main question underlying this research study is:

***Do the Internal Auditors in Al-bariga Oil Marketing Company Operate in Accordance with the necessary Independence to permit the Objective Performance of Duties and Responsibilities?***

To answer the main question, the following two sub-questions have to be answered:

- *Dose the organisational status of the IAD sufficient to permit the accomplishment of its audit responsibilities?*
- *Are the internal auditors objective in performing audits?*

**Previous Studies:**

It may be useful at this point to present a summary of the previous studies on the evaluation of the IA function (shown in table 1-1). It is quite clear that the majority of them concentrate on the factors of competence, objectivity and work (referred to as performance in some studies). Besides examining the importance of independence, they attempted to investigate the factors perceived as important in indicating that internal auditors are maintaining their independence, and which of these factors is more important than the others. It was believed that this investigation might provide some insights into the understanding of the independence of internal auditors and that it would be important for two reasons. The first was that, since the major function of internal auditors is to monitor various activities for the benefit of the organisation, it is likely that the persons in charge of these activities will exercise pressures on the internal auditors because of a conflict of interests between the two parties. The major sources against which the internal auditor can "balance" the pressures from auditees are the indicators which characterise organisational settings. Therefore, in order to achieve an enhanced understanding of the effectiveness of these factors in maintaining internal auditor independence it was necessary to know how they are perceived by the participants. The second reason was that little was known about

whether the external and internal auditors shared common views on how internal auditor independence should be evaluated.

**Table 1.1 Summary of Findings of Previous Studies**

<b>Researcher</b>	<b>The aim of the study</b>	<b>The empirical results</b>
Gibbs and Schroeder (1980)	Determining what criteria are important in determining the competence, objectivity, and performance of audit work.	Three ranked lists of criteria to assess the competence, objectivity, and performance of audit work.
Clark et al., (1981)	Ranking the five criteria in order to evaluate the objectivity of internal audit staff.	Independence is the most important of the five criteria.
Brown (1983)	Determine the factors considered important by external auditors in evaluating the reliability of IA.	The dominant factors are independence and previous audit work.
Abdel-khalik et al., (1983)	Determining the factors considered important by external auditors in evaluating the reliability of an IA function.	The level to which internal audit staff reports is the most significant factor.
Schneider (1984)	Determining how external auditors evaluate the IA function.	The IA work factor is most important, followed by the competence and the objectivity factors.
Schneider (1985a)	Studying the relationship between external auditors' evaluation of IA and their reliance in audit-planning decisions.	Competence and work performance are almost equally important. The objectivity factor is less important.
Schneider (1985b)	Examining the degree of consensus among external auditors in evaluating the IA.	Work performance, then competence, then objectivity.

<b>Researcher</b>	<b>The aim of the study</b>	<b>The empirical results</b>
Margheim (1986)	Examining the factors that external auditors consider important in their decision to rely on IA.	Competence and work performance (combined) significant. Objectivity and interaction not significant.
Messier & Schneider (1988)	Examining the relative importance of the attributes that are considered important by external auditors in evaluating the IA.	Competence is the most important attribute, then objectivity, then work performance.
Daruish (1990)	Evaluating the internal auditor's role in Libyan industrial companies.	1- The internal auditors are not independent; 2- They are not sufficiently qualified; 3- They do not perform all the required tasks; and 4- They do not adopt the proper manner when performing their tasks.
Maletta (1993)	Examining the factors considered by external auditors.	Internal audit competence was the most significant followed by objectivity and work performance.
DeZoort et al., (2001)	Considering how the type of work that the IA routinely performs and the IA compensation structure affect external auditors' evaluations of IA objectivity.	External auditors perceived that the IA was less objective when its role was primarily consulting or when its auditors had the opportunity to receive incentive compensation.
Ganesh (2001)	Examining whether the reliability of the audit procedure employed by the IA affected the external auditor's evaluation of IA work performance, and whether that evaluation was contingent on the level of IA	When audit procedure reliability was high, the evaluation of IA work performance was differentially sensitive to alternate indicators of IA competence and objectivity. When audit procedure reliability

Researcher	The aim of the study	The empirical results
	objectivity and competence.	was low, the evaluation of IA work performance was low, regardless of IA objectivity and competence.
Ganesh (2002)	Presenting a multistage model for the evaluation of the IA function and to understand how the three IA factors (competence, objectivity and work performance) interact and combine in the evaluation judgment.	In the Bayesian context, it is futile to attempt a ranking of the factors since no single factor will dominate under all conditions. When either (or both) objectivity or competence was negative, little importance was placed on work performance.
Akers & Maher (2003)	Examines the participants' views of the role of IA in systems development projects and whether consulting impacts on the independence of the IA function.	The findings indicate that the respondents believe IA should be involved with the testing of the operating effectiveness of the systems, including their accuracy.
AL-Twajjry et al., (2003)	Examines the development of internal audit in Saudi Arabia.	Internal audit departments have restrictions on their degree of independence.
Alfatemy (2004)	Evaluate the effectiveness of IAD.	The requirements of independence have been met.
Abobaker (2005)	Determining the role of IA in supporting control structure in economic units.	- Weakness of IA. -Absence of standards for the professional practice of IA.
Masaud (2010)	Determining to what extent the standards for the professional practice of IA are applied in Jamhuriya bank (in Libya).	The requirements of the independence have not been met.

**Objectives of the research:**

The main objective of the research is to examine the independence of the internal auditor within Al-bariga Oil Marketing Company.

**The Population of the Study:**

Since the objective of this study was to examine the independence of the internal auditor within Al-bariga Oil Marketing Company, about thirteen interviews were conducted with the DIA, whose job is to manage the work within the IAD, financial controller, whose job is to control financial activities within the company, seven internal auditors whose jobs are to audit all the activities within the company and four internal audit coordinators whose jobs are to coordinate the internal auditors efforts. They were selected because they are concerned of IA and most of them were reasonably informed about IA.

**Research Approaches and Data Collection:**

Qualitative research is described by Amaratunga et al., [2002] as a source of well grounded rich descriptions and explanations of processes in identifiable local contexts. Some writers [e.g. Haralambos and Holborn, 1991; Hague and Jackson, 1996] support the use of qualitative research by stating that compared to quantitative data, qualitative data are usually seen as richer and, more essential, as having greater depth and being more appropriate for providing a clear and true picture of a way of life. Qualitative research, on the other hand, is not numerically, but experientially based, and is intended not to definitively answer a question, or even necessarily to provide a generalisation, but to highlight and draw attention to a group of people or phenomena.

Collecting information through a survey usually involves one or more of the following data gathering methods: (1) interviews, (2) questionnaires, (3) observation and (4) documentary analysis. Since the concern of this study was to examine the independence of the internal auditor within Al-bariga Oil Marketing Company as a case study, interviews considered to be one of the most effective data collection methods, because an interviewer can communicate directly with the respondents. Yin [1989] pointed out that interviews are one of the most important sources of data collection when conducting a case study. The literature review reveals that structured and unstructured interviews were initially felt to be inappropriate for the purpose of this research. It also shows that semi-structured and unstructured interviews are the ones most commonly used in qualitative research studies. Therefore, a semi-structured interview format was selected as the main means of gathering interview data, as this is seen as the most relevant research tool for this purpose. Semi-structured interviews allow respondents to express themselves at some length, but offer enough shape to prevent aimless rambling. In order to collect the necessary data for this study, interview guide was prepared and used during the interviews conducted with participants. It lists the questions and issues that are to be discussed during the interview. The questions included in this interview guide are related to the requirements of independence that need to be met. Those questions were directed to the participants according to their Jobs and their relationship with the IA. Therefore, If those requirements were met, that means the internal auditors within AOMC maintain their independence, and if not, that means they are not independent.

### Results and Discussion:

Several questions were included in the interview guide to discover whether and how internal auditors within the AOMC maintain their independence. One such question directed to the DIA and related to the organisational status read as follows:

*What is the organisational status of your IAD? Do you think that this status is sufficient for the fulfilment of its tasks?*

In replying to this question, the DIA indicated that he is directly responsible to a board of directors. It is quite clear from his response during the interview that he accepted the organisational status of the IAD as adequate for the job. He believed that he was encouraged to maintain his independence and to report all compliance violations. However, he also believed that complete independence is impossible due to the many different relationships which exist within the company and because independence can easily be infringed. He went on to say that the primary role of IA is to help the board of directors to achieve the company's objectives. To fulfil this responsibility, a programme should be set up by management that will allow the internal auditor as much independence as possible. Another factor that affects the independence of the internal auditor is the interpersonal relationships developed between individuals within the company. Although the IAD is located at the highest management level, one might still ask how it can be protected from the pressures of that highest level of management. The Financial Controller supported this argument when he indicated that the current situation is problematic. For example top management can prevent internal auditors checking a particular topic by instructing them to investigate another one. Also they can, if they wish, easily neutralise the internal auditors by not

giving them the tools they need to perform their job. The Financial Controller added that he does not expect that the internal auditors can check items that are directly connected to the Chairman of the Board. He believes that the present situation does not make it possible for internal auditors to be truly independent, because they are in fact dependent on the Chairman of the Board. One of the internal audit coordinators stated the following in this respect:

*We can get to a conclusion that the present organisational status of the IAD in our company is quite satisfactory and fundamental to consideration of recommendations by board of directors. However, it should be clear that such status does not lead to the mechanical implementation of recommendations implied in the report, because the board of directors is the only body that has the right to accept or reject the audit recommendations.*

Another element which may enhance the independence of the IAD within the company is the identity of the person or persons who have the right to appoint or remove the DIA. The researcher asked who has the right to make decisions on this matter. The results from the interviews reveal that the board of directors is the only body within the company that has the right to appoint and remove the DIA. It is worth mentioning here, that the internal auditors within the company have not been offered special advantages in terms of their salaries and / or other job benefits. All officers within the company are subject to the Salaries Law No. 15 of 1980, which applies to all Libyan officers within all Libyan public institutions, be they commercial, industrial or service related.

The next factor that may potentially have an impact on the acquired level of independence is the level to which the DIA reports. The DIA was asked to indicate the management level that he should submit his audit reports to, and whether or not he reviews/discusses those reports with this management level. He pointed out that any one will of course report to the level or the body that he is responsible to. As a DIA is responsible to the board of directors, he has to submit his audit reports directly to this body. However, he pointed out that he has also been encouraged by this board to discuss with them the audit conclusions and recommendations before issuing the final report.

One of the most important factors that affect independence is the free access of internal auditors to people and places. The internal auditors within the company were asked to indicate whether or not they had unrestricted access to personnel and all management information needed to carry out their work. They indicated that they have been given the right of access at all times to the company's accounts, records, archive and systems and to all its areas. They added that they are entitled to require the company's officers to provide them with such information and explanations that they believe necessary for the purposes of their task, and which can be considered as the evidence necessary to support their findings regarding the subject under review and audit. However, the board of directors within the company provides the IAD with all the necessity facilities to make the IA tasks as easy as possible and to contact any officer or responsible person at any level of management. However, when the Financial Controller was asked to express his opinion regarding this matter, he pointed out that:

*Although the IAD at present is unable to audit all areas of company operations, the DIA as I see it is not free in reality to choose the areas he wants to be inspected.*

He further explained that in saying that the IAD within his company may possibly have the right of access to people and places and all areas within the company, he does not believe that it can audit any subject which directly concerns the actions of the board of directors or their close circle. This means that the DIA cannot maintain complete independence since he is responsible to some management level within the company. The DIA was also requested to indicate whether or not the internal auditors carry out their work freely and objectively. In response, he stated the following:

*As a DIA, my duty is to control the performance of the audit staff; I could say that the internal auditors have tried hard to keep their examinations completely unbiased. But being part of the company and having personal and official relations with other personnel within the company, it is not easy for an internal auditor to perform his work one hundred percent neutrally. In other words his assessment will not be completely objective.*

From his perspective, the relationship that the internal auditors have with the auditees will affect their degree of objectivity so that sometimes they cannot express their opinions as freely as the situation demands. Accordingly, whenever relationships with people are established, independence is no longer complete. In general, the DIA believes that his internal audit staff have sufficient independence to enable them to be fair in their evaluation of their auditees' performance and that they are not under such pressure from their auditees as to bias their opinions.

Expressing a very similar viewpoint, the Financial Controller indicated that the internal auditors may encounter a situation in their operations that involves a conflict of interest and thus interfere with their objectivity. He quoted the case of an internal auditor who may find himself in a conflict of interest situation. "If the personnel management has to approve the promotion of the internal auditors and the internal auditors perform an audit in the personnel management, this could lead to some tension in ensuring a completely unbiased approach".

The DIA was also requested to indicate whether he decides what subjects will and will not appear in the work plan of the IAD and the extent to which top management participates in establishing the overall internal objectives and topics. His reply was as follows:

*It is my choice as DIA to decide which subject will be included in audit programmes for different departments. Yet, the part that the board of directors plays in this matter is to highlight only general objectives.*

**He added that:**

*Although the board of directors controls the objectives of the IAD, we have been given a total freedom to plan our audits and fulfil our duties.*

Thus the response of the DIA implies that it is he who decides what subjects will appear in the work plan of the IAD.

The results further revealed that the IAD has a policy of not assigning its personnel to other areas of the company to perform non-internal audit work, and in reality this happens infrequently. The DIA indicated that, in some cases, he assigns members of the internal audit staff to a specific committee established by top management to make

an inventory of material storage or to observe the problems related to the company activities. Tasks such as these require an internal audit member to be included in this committee. The researcher asked the DIA if any of internal audit staff has assigned to audit those activities they previously performed during the year, he indicated that officers who transferred from other departments within the company to work in the IAD are not allowed to review or audit any activities they were previously prepared or performed until the financial year ends.

When the researcher asked the DIA to evaluate the degree of support received by his internal auditors from top management, he indicated that they have been given all the authority required to carry out their tasks and have received total support from top management. He also indicated that the board of directors plays a vital role in determining the apparent independence of the internal audit staff by supporting them and therefore enabling them to ensure a broad range of coverage without objections and by giving adequate consideration to taking effective action regarding the audit findings and recommendations. However, one of the internal audit staff was not satisfied with the top management as it did not provide the IAD with sufficient support. He indicated that they are not sure what top management expected from them because they do not have enough support from top management. In this connection, the Financial Controller commented as follows:

*The internal auditor derives his success from the extent of cooperation and support given to him by company management. It should be clear to the personnel subject to auditing and to the administration as well, that the auditor is a part of the company and acts mainly for its interests in a loyal and sincere way.*

Thus there is a contrast here between two points of view. The DIA's view that he received total support from top management is very different from the lack of support referred to by one of his staff. This may be a problem of communication between the DIA and his subordinate or it may simply be that the researcher has discovered a dissatisfied employee. The results from the interviews reveal that the board of directors has issued a statement which requires all departments and management within the company to cooperate with the internal auditors by providing all the information they need to carry out their task, and to follow their recommendations. This support from top management will of course enhance the internal auditors' independence. The explicit instruction from the board of directors that everyone is to co-operate with the IA function should both enhance its status and make the work easier.

In response to the question about the DIA's right to attend all the regular meetings within the company, it was indicated that he has regular access to the board of directors and, as the IAD is considered as senior management within his company, the DIA has the right to attend all the regular meetings like any other member. During the discussion with the DIA, he was asked to indicate whether he has a direct communication link to the board of directors. He indicated that, although he has the right to contact any responsible person in the highest level of management at any time and from any place. It is not always necessary to contact them, because the problems disclosed by audits will usually be resolved at the middle management level. Therefore, it will not be necessary for the board of directors to be contacted and consulted directly. In particular, nowadays with the ever-increasing complexity of business practices, top management has

no time to spend resolving small matters which could be resolved at middle or sometimes lower management levels.

The internal auditors were asked to indicate whether they assume operating responsibility for designing or operating systems within the company. They said that they have never been informed and consulted about any proposed changes in systems of internal control. Also, they have not been asked to make any recommendations on the standards of control to be applied in the development of the systems and procedures under review. They believe that they could provide some advice on the controls to be incorporated in new or revised systems before their implementation. This should not prejudice their objectivity in reviewing the system. They should not be directly responsible for the development or implementation of new systems, or engage in any activity which they would normally review and appraise, since this could compromise their independence.

In general, the above results can be summarised as following:

- 1- The IAD is located at the highest level (board of directors).
- 2- The decision to appoint or remove the DIA is made by the board of directors.
- 3- The DIA report directly to the board of directors.
- 4- The DIA has the right to discuss the report with the board of directors.
- 5- The internal auditors have unrestricted access to all information and personnel.
- 6- internal auditors carry out their work freely and objectively. They have tried hard to keep the examinations completely unbiased.

- 7- The DIA decides what subjects will or will not appear in the audit work plan.
- 8- The DIA produces the audit plan without restrictive amendment.
- 9- The DIA attended all the regular meetings within the company.
- 10- The DIA has top management support for his work and recommendations.
- 11- The DIA has a direct communication link to the board of directors.
- 12- Internal auditors are not involved in non-audit work (designing or operating responsibility).
- 13- Internal auditors had never been informed and consulted about any proposed changes in systems of internal control.
- 14- Internal auditors had not been asked to make any recommendations on the standards of control to be applied in the development of systems and procedures under review.
- 15- Persons transferred to or temporarily engaged by the internal auditing department are not assigned to audit those activities they previously performed until a reasonable period of time has elapsed.

It is clear from the above results that most of the requirements of independence are met by the company. Therefore, it can be said that the IAD within the company maintains its independence to a large extent which means that the independence of internal auditors can be considered as effective.

**Conclusion and Recommendations:**

Based on the literature review, there were some requirements of independence that need to be met. Therefore, in order to evaluate the independence of the internal auditor, These requirements have been

examined based on the empirical data collected from the case study. The following conclusion can be drawn at this point. The first factor is organisational status. The results of the case study revealed that the IAD is located at the highest level of management within the company (the board of directors) and the DIA has direct responsibility to this board and consequently reports directly to it. The results also indicate that the decision to appoint or remove the DIA is made by this board and nobody else. It was noticed during the interviews that the DIA accepted that the organisational status of his IAD was adequate for the job. He believed that he was encouraged by the board of directors to maintain his independence and to report all compliance violations. The board of directors support for the IAD was also confirmed by the DIA. The internal auditors have been given all the authority required to carry out their tasks. This high level of visibility was enhanced by the company regulations, in which the board of directors issued a statement requiring all departments and management within the company to cooperate with the internal auditors by providing all the information they need to carry out their task. Another indication of this support is that the DIA has the right to attend all the regular meetings. The next factor examined that may enhance independence was unrestricted access to all the information needed. The results indicate that all the internal auditors within the company have been given the right of access to all the company's accounts, records, archives, systems and areas at all times. The empirical data reveal that the board of directors within the company provides the IAD with all the necessary facilities to make it as easy as possible to complete internal audit tasks and to contact any officer or responsible person at any level of management. The internal auditors' objectivity was also examined; the results reveal that they have tried hard to keep their examinations completely unbiased. However, being part of the company and having personal and official relations with other

personnel within it, internal auditors do not find it easy to perform their work a hundred percent neutrally. Finally, one of the things which is usually seen to have an influence on independence is the internal auditors' involvement in the planning and design phases of projects for systems development. The results revealed that the internal auditors had never been informed and consulted about any proposed changes in systems of internal control. Also, they had not been asked to make any recommendations on the standards of control to be applied in the development of systems and procedures under review. It is important to mention here that one potential problem with internal auditors acting as consultants for systems - related projects is that their independence could be impaired. Although the IIA has developed standards for both independence and consultation, the IA literature is not clear as to how top management views the role of the internal auditors in project systems development. One viewpoint is that top management places more importance on the internal auditor's role as a consultant than on his/her objectivity. Akers & Maher, [2003] argues that independence is more important and that consulting activities should not impair the internal auditor's objectivity. In their study, which examines the participants' views of the role of IA in systems development projects and whether consulting impacts on the independence of the IA function, the findings indicate that the respondents believe IA should be involved with the testing of the operating effectiveness of the systems, including their accuracy. While this finding is inconsistent with the consulting perspective, it is consistent with the respondents' views on independence. The respondents were essentially indifferent about IA's involvement in the planning and design phases and did not support IA involvement in the development, implementation and maintenance phases.

Finally, based on the above results, it is necessary for the AOMC to have Audit Committee connected with the IAD. This will enhance and support the independence of the internal auditors.

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## APPENDIX A

LIST OF ABBREVIATION USED	
DIA	Director of the Internal Audit
AOMC	Al-bariga Oil Marketing Company
IA	Internal Auditing
IAD	Internal Audit Department
IIA	Institute of Internal Auditors

## APPENDIX B

### INTERVIEW GUIDE FOR EVALUATING THE INTERNAL AUDITOR INDEPENDENCE WITHIN AL-BARIGA OIL MARKETING COMPANY AS A CASE STUDY

- 1- What is the organisational status of your internal audit department?
- 2- Do you think that this status is sufficient for the fulfilment of its tasks?
- 3- In your company, who has the right to make the decision to appoint or remove the director of the internal audit?
- 4- As director of the internal audit, to whom do you submit the audit reports?
- 5- Do you review/discuss the audit report with the management level that you should report to?
- 6- Do the internal auditors have unrestricted access to personnel and all management information needed to carry out their work?
- 7- Do they carry out their work freely and objectively?
- 8- If you prepare an audit plan:
  - (a) Do you decide what subjects will or will not appear in the audit work plan?
  - (b) Do you produce the audit plan without restrictive amendment?
  - (c) Do you involve management in planning the objectives of the audit?
- 9- Have members of the internal audit staff been involved in non-audit work for the company during the year?
- 10- If yes, were they informed that they should not consider themselves as internal auditors when they carry out these tasks? Please give details.

## Evaluating The Independence Of The Internal Auditor \_\_\_\_\_

- 11- Do you have the right to attend all the regular meetings within the company?
- 12- As director of the internal audit, does the highest level of management within the company offer you support in carrying out your management tasks?
- 13- Has the top management issued any statement requiring all departments and managements within the company to follow the internal audit recommendations?
- 14- Do you have a direct communication link to the highest level of management within the company?
- 15- Do your internal audit staff assume responsibility for designing or operating systems?
- 16- Has any internal auditor assigned to audit those activities they previously performed during the year?