



DETERMINANTS OF ETHICAL BEHAVIOUR AMONG
PUBLIC SECTOR AUDITORS IN MALAYSIA

BY

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ABSTRACT

Ethics is crucial to all professions, including accounting of both private and public sectors. This research sought to determine the determinants of ethical behaviour among public sector auditors in Malaysia. There are four research objectives for this study: (1) to investigate the influence of ethical climate professional commitment; (2) to examine the effect of professional commitment on ethical behaviour of public sector auditors; (3) to investigate the effect of corporate ethical values on ethical behaviour of public sector auditors; and (4) to examine the effect of ethical ideology on ethical behaviour of public sector auditors. The respondents of the study were public sector auditors from both federal and state levels of National Audit Department in Malaysia. Using a survey questionnaire comprising instruments about the ethical climate, corporate ethical values, professional commitment, ethical ideology and organizational misbehaviour, a total of 382 were received and usable. In order to achieve the research objectives, multiple regressions were performed. In terms of factors influencing the extent of ethical behaviour among public sector auditors in Malaysia, the results of multiple regression analysis reveal that seven variables have influence on ethical behaviour. These variables are law and independence climate, professional commitment, corporate ethical values, idealism, relativism, with one control variable, gender. The findings indicated that a significant positive influence of law ethical climate, professional commitment, corporate ethical values and idealism ethical ideology on ethical behaviour. In contrary, the study discovered that the independence ethical climate and relativism ethical ideology type has a significant negative influence on ethical behaviour. This study contributes to filling the research gap as research on public sector auditors is very few and scarce. In addition, it is expected that this will initiate future research on the ethics of public sector auditors as well as provide better understanding of the factors that can contribute to more ethical behaviour among Malaysian public sector auditors. More importantly, the findings of this current study may contribute to the government's understanding of how to foster an environment that can encourage ethical behaviour among public auditors in order to increase their credibility as public servants and thus enhance public trust in the government.

ملخص البحث

الأخلاق أمر بالغ الأهمية لجميع المهن، بما في ذلك المحاسبة لكل من القطاعين العام والخاص. تسعى هذه الدراسة إلى تحديد محددات السلوك الأخلاقي بين مدققي القطاع العام في ماليزيا. هناك أربعة أهداف لهذه الدراسة: (١) التحقيق في تأثير المناخ الأخلاقي على الالتزام المهني؛ (٢) دراسة تأثير الالتزام المهني على السلوك الأخلاقي لمدققي القطاع العام؛ (٣) دراسة تأثير القيم الأخلاقية للشركات على السلوك الأخلاقي لمدققي القطاع العام؛ (٤) دراسة تأثير الأيديولوجية الأخلاقية في السلوك الأخلاقي لمدققي القطاع العام. عينة الدراسة تتكون من مدققي القطاع العام من المستويين الاتحادي والدولة من دائرة الرقابة الوطنية في ماليزيا. باستخدام استبيان يضم أدوات عن المناخ الأخلاقي، القيم الأخلاقية للشركات، الالتزام المهني، الأيديولوجية الأخلاقية وسوء السلوك التنظيمي، الدراسة جمعت ٣٨٢ استبيان صالح للاستخدام. من أجل تحقيق أهداف البحث، الإنحدار الخطي المتعدد استعمل لتحليل البيانات. من حيث العوامل المؤثرة في مدى السلوك الأخلاقي بين مدققي القطاع العام في ماليزيا، نتائج التحليل تكشف أن سبعة متغيرات لها تأثير على السلوك الأخلاقي. هذه المتغيرات هي القانون ومناخ الاستقلال، الالتزام المهني والقيم الأخلاقية للشركات، المثالية، النسبية، والجنس. وتشير النتائج إلى أن هناك تأثير إيجابي كبير لمناخ القانون الأخلاقي، الالتزام المهني، القيم الأخلاقية للشركات والمثل الأيديولوجية الأخلاقية على السلوك الأخلاقي. علي العكس من ذلك، اكتشفت الدراسة أن إستقلال المناخ الأخلاقي و نوع الأيديولوجية الأخلاقية النسبية له تأثير سلبي كبير على السلوك الأخلاقي. يساهم هذا البحث في سد الفجوة في الدراسات السابقة لأن الدراسات المتعلقة بمدققي القطاع العام نادرة. وبالإضافة إلى ذلك، فمن المتوقع أن تؤدي هذه الدراسة إلى تحفيز الأبحاث المستقبلية حول أخلاقيات مدققي القطاع العام، فضلا عن توفير فهم أفضل للعوامل التي يمكن أن تؤثر أكثر على السلوك الأخلاقي بين مدققي القطاع العام بماليزيا. الأهم من ذلك أن نتائج هذه الدراسة يمكن أن تساعد الحكومة في فهم كيفية هيئة البيئة التي يمكن أن تشجع السلوك الأخلاقي بين مدققي الحسابات العامة من أجل زيادة مصداقيتهم كموظفين عموميين، وبالتالي تعزيز الثقة العامة في الحكومة.

APPROVAL PAGE

I certify that I have supervised and read this study and that in my opinion, it conforms to acceptable standards of scholarly presentation and is fully adequate, in scope and quality, as a dissertation for the degree of Master of Science in Accounting.

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Suhaiza Ismail
Supervisor

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DECLARATION

I hereby declare that this dissertation is the result of my own investigations, except where otherwise stated. I also declare that it has not been previously or concurrently submitted as a whole for any other degrees at IIUM or other institutions.

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CHAPTER ONE

INTRODUCTION

1.1 INTRODUCTION

This chapter provides an overview of this study on the ethics of public sector auditors. It is divided into six sections: Section 1.1 presents the background of the study; Section 1.2 introduces the problem statements; Section 1.3 discusses the motivation for the study; Section 1.4 discusses the research objective; Section 1.5 articulates the significance of the study; and, finally, Section 1.6 outlines the organisation of this dissertation.

1.2 BACKGROUND OF THE STUDY

The public sector has a great responsibility to public as it serves such basic needs as education, defence, health, communication and transportation. Budget allocations are made for each financial year, for each area, in order to deliver essential services to the nation and society at large. Audit of government entities is crucial to ensure effective utilisation of these allocations, and to provide well as transparent, policies and procedures to serve the people. The National Audit Department (NAD) is an independent executive authority that manages audit activities for government entities in Malaysia. According to the Audit Act 1957, NAD is authorized to perform the auditing of accounts of the central government and state governments (Malaysian Government, 2000, p. 180). The Auditor General of Malaysia, Tan Sri Dato' Setia Hj. Ambrin Bin Buang, has emphasized,

“Through quality auditing, the Government and citizens will obtain an objective and without prejudice, information on the weaknesses in managing public service” (Buang, 2014).

Therefore, the role of public sector auditors is crucial to help government organizations improve their level of quality, accountability and integrity (Buang, 2011).

To achieve quality auditing, auditors need to provide a true and fair opinion of the auditees' financial statements, as this will enhance credibility of the financial statements and thus allow owners, investors, bankers and other stakeholders to use them with greater confidence. Besides being knowledgeable about auditing, accounting and financial reporting, it is equally important for auditors to remain objective and ethical in their actions and decisions (Singh and Poduval, 2009). Ethics is the code of moral principles that govern an individual's behaviour in regards to what is ethically right or wrong (Aaker, 1989). Ethics is crucial to all professions, including accounting; ethical decision making is an essential professional attribute.

The importance of ethical decision making among accountants arises since they are responsible for safeguarding the public interest by ensuring appropriate management of private and public finances (Mohamed Saat et al., 2012). The President of the Malaysian Institute of Accountants' (MIA) has stated that ethical accountants are required as an instrument to boost assurance and confidence (Errol, 2013). Auditors are responsible for judging whether the set of accounts audited gives a true and fair view of the organization in accordance with the financial reporting framework. They must, therefore, make ethically sound decisions to provide assurance to the public. Public sector auditors in particular are expected to behave ethically in their day-to-day delivery of work. Many published studies address ethical issues and public service generally, but few focus on ethics among public sector auditors in developing nations such as Malaysia.

There are a number of factors influencing the ethical behaviour and decision-making of auditors. Hunt and Vitell's (1986) theory of marketing ethics has identified factors that influence ethical decision making. These factors are culture, industry, organizational environment and personal experiences.

This present study intends to investigate the determinants of work related ethical behaviour of public sector auditors. It proposes to investigate the effect of ethical climate, organizational commitment, professional commitment and ethical ideology on organizational misbehaviour of Malaysian public sector auditors.

1.3 PROBLEM STATEMENT

Recent court cases involving unethical activities such as fraud and corruption have put the spotlight on public sector auditors. The following example, a case involving the payment and collection of sales and payroll taxes, is detailed on the official website of the US Federal Bureau of Investigation (www.fbi.gov). In this case,

“business owners and the president of an accounting firm had been under-reporting the sales from various businesses by over \$10 million in order to avoid remitting sales tax to the state and local governments. In an attempt to conceal this massive scheme, the business owners and the accountant paid bribes to officials within the East Baton Rouge Parish Auditor's Office and agreed to bribe an auditor with the Louisiana Department of Revenue”

The case resulted in the conviction of five prominent businessmen, the president of an accounting firm, and a government auditor. Even worst, there is a case in UK whereby a public sector auditor goes bankrupt reported in 2005 (Simpkins, 2005). This UK case is typical of many high-profile cases throughout the developed world. The situation is perhaps even more worrying in parts of Asia. For instance, recent data from the Indonesian Government Internal Auditor Association (AAPI)

shows that 94 per cent of government internal auditors cannot detect fraud and corruption (Ashari, 2013).

Clearly, such unethical practices of public sector auditors can erode public confidence in government and the public service. There is, therefore, a crucial need for highly ethical accountants. However, as research by the ACCA's business intelligence unit suggests, the increasingly more complex nature of businesses presents a number of ethical challenges for accountants (Nasir, 2013). To address these challenges ethical behaviour among auditors must be actively promoted, with transparency being built in to every level of government systems (Labelle, 2014).

To date, there have been very few empirical studies related to ethical behaviour in Malaysia, particularly to the ethical behaviour of public sector auditors. The present study attempts remedy this scarcity of research by providing useful insights into the determinants of ethical behaviour among Malaysian public sector auditors.

1.4 MOTIVATION FOR THE STUDY

There are two main motivations for this study. First, as discussed at the Malaysian Public Sector Auditor Conference (2011), ethics in auditing is one of the five audit activities to be focused on in the next five years as an improvement of government audit in Malaysia. Ethics audit is a plan which will focus on the ethics of auditors, as well as investigating how companies, agencies, and the public sector conform to the ethical standards of society and industry. Thus, this study will examine the ethical behaviour of public sector auditors in Malaysia.

Secondly, although auditing ethics is a well- researched area, most prior studies have focused on private auditors. Also, most studies on the ethics of public

servants have generally been conducted in developed nations such as US and UK; research literature on the ethics of public sector auditors is still lacking in Malaysia. Thus, this current study aims to contribute to the literature on the ethical behaviour of public auditors and on the factors that influence this behaviour.

1.5 RESEARCH OBJECTIVES

Generally the aim of this study is to investigate determinants of public sector auditors' ethical behaviour in terms of organizational misbehaviour. To achieve the aim of the research, the research objectives (RO) have been formulated as follows:

- RO 1: To investigate the effect of ethical climate on ethical behaviour of public sector auditors
- RO 2: To examine the effect of professional commitment on ethical behaviour of public sector auditors
- RO 3: To investigate the effect of corporate ethical values on ethical behaviour of public sector auditors
- RO 4: To examine the effect of ethical ideology on ethical behaviour of public sector auditors

The following are four research questions (RQ) derived from the research objectives:

- RQ 1: Does ethical climate affect ethical behaviour of public sector auditors?
- RQ 2: Does professional commitment affect ethical behaviour of public sector auditors?
- RQ 3: Does corporate ethical values affect ethical behaviour of public sector auditors?
- RQ 4: Does ethical ideology affect ethical behaviour of public sector auditors?

1.6 SIGNIFICANCE OF THE STUDY

This study is important in a number of ways. Firstly, there were few prior studies pertaining to ethical behaviour among auditors (Aw, 2006; Zakari, 2010). In addition, the researcher has not come across any similar studies done on the ethical behaviour specifically among the public sector auditors in Malaysia. Thus, it is hoped that this study would fill the gap in the literature and produce more research pertaining to ethics of public sector audits in the future.

Secondly, the findings of the present study are important to the Malaysian Government and National Audit Department (NAD), which can enhance government's understanding on how to fostering ethical behaviour among public servant particularly among public sector auditors which thus can enhance their credibility as public servants and therefore raise public confidence trust on the government. Moreover, government can further nurture good environment that can influence auditors' behaviour in more ethical manner such as conducting by developing early plans and programs to improve ethical behaviour since the early stage such as by developing ethical programs among students in schools, universities as well as in private and public organizations. By identifying the factors that effecting ethical behaviour, government organizations can take appropriate precautions to enhance ethical behaviour among public sector auditors.

Thirdly, it provides better understanding related to the current ethical behaviour being practiced by the public sector auditors by assessing their perceptions on work related behaviour and requiring them to answer based on their level of awareness in regards with ethical issues.

This will help improve the overall ethical awareness and behaviour in the workplace not only in public sector, but also in private organizations as the ethical

vignettes used in this study are general work related misbehaviour that can also occur among employees in private organizations.

1.7 ORGANISATION OF THE STUDY

This study has been organised into six chapters. Chapter 1 provides an overview for this study. It comprises the background of this research, problem statements, research objective, motivation, and significance of this study. Chapter 2 reviews prior literature on ethical behaviour. Firstly, it outlines a general explanation pertaining to ethical behaviour, followed by a review of ethics among public sector auditors. Next, it discusses conceptual as well as empirical studies being carried out on ethical behaviour among public sector auditors. This chapter concludes by identifying the gap in the literature. Chapter 3 presents the theoretical framework underlying this study and a list of hypotheses based on prior literature.

Chapter 4 discusses the research method applied in the study. The discussion includes an explanation of the sample selection, data collection method, research design, pilot test, and statistical analyses. Chapter 5 focuses on the analyses of the research findings through the use of Statistical Package for Social Sciences (SPSS), presenting all relevant tables and diagrams, and also providing a thorough discussion of the demographic and findings. Chapter 6 consists of conclusions from the study, implications of the findings, limitations and contributions of the present research. Finally, it concludes with recommendations for potential future studies.

CHAPTER TWO

LITERATURE REVIEW

2.1 INTRODUCTION

This chapter reviews literature related to the present study. It consists of five sections: Section 2.1 provides a general explanation on ethics and ethical behaviour in the prior studies; Section 2.2 presents prior studies on ethics; Section 2.3 presents literature that is related to factors which influence ethical behaviour and judgment; Section 2.4 discusses the gap in the literature; and, lastly, Section 2.5 concludes this chapter.

2.2 DEFINITION OF ETHICS AND ETHICAL BEHAVIOUR

Ethics is defined as “the study of standards of conduct and moral judgment” and as a “reflection on the moral significance of human action” (Gandz and Hayes, 1988). Finn, Chonko and Hunt (1988) suggests that ethics means acting in ways consistent with what society and individuals typically think are good values. Aaker (1989) also defines ethics as the code of moral principles and values that govern the behaviour and beliefs of individuals with respect to what is ethically right or wrong. Pearce (1990) defines ethics as the correct procedures, based on the available facts and what can be adequately explained. Thus, ethics consists of procedures and rules used to guide and control the behaviour of people or society at large. In general, ethics is used to differentiate what is right (ethical) from what is wrong (unethical).

Ethics is closely related to the term “ethical behaviour”. Ethical behaviour refers to any behaviour which is shown to be objectively and morally correct. In the business and professional area, ethical behaviour is defined as correctness of behaviour based on moral awareness (Boomer, Gratto, Gravander and Tuttle, 1987).

In contrast, unethical behaviour, also known as misbehaviour, is defined by Ackroyd and Thompson (1999, p.2) as “anything you do at work you are not supposed to do”.

Vardi and Wiener (1996) define “organizational misbehaviour” as “any intentional action by members of organizations that defies and violates (a) shared organizational norms and expectations, and/or (b) core societal values, mores and standards of proper conduct” (p. 151). Other researchers have labelled it “deviant workplace behaviours” (Goldman, 1992; Robinson and Bennett, 1995; Robinson and Greenberg, 1998), “unconventional practices at work” (Analoui and Kakabadse, 1992), and “non-compliant behaviour” (Puffer, 1987).

Based on the above discussion, it is concluded that the term “organizational misbehaviour” is referred to as unethical behaviour which is non-compliant to organizational procedures and rules. For example, absent without reasonable justification and take longer break hours.

The current study will examine factors influencing ethical misbehaviour among Malaysian public sector auditors. The subsequent sections review literature on factors influencing ethical behaviour or ethical judgment.

2.3 PRIOR STUDIES ON FACTORS AFFECTING ETHICAL BEHAVIOUR

Numerous studies have been conducted to examine factors influencing ethical behaviour and the ethical decision making of individuals. Prior studies have analysed demographic variables such as age (Banerjee, Jones and Cronan, 1996; Honeycutt, Glassman and Karande, 2001; Roman and Munuera, 2005) and education (Honeycutt, Glassman and Karande, 2001; Roman and Munuera, 2005). Other factors tested include organizational learning capability (Camps and Majocchi, 2010), perceived ethical attitudes of managers (Kantor and Weisberg, 2002), methods of compensation

and control systems (Roman and Munuera (2005), existence of strong ethical standards (Cadogan, Tarkiainen and Sundqvist, 2009), managerial dependencies and organizational independence (Deshpande, Joseph and Prasad (2008) and performance appraisals (Jacobs, Belschak, and Hartog, 2014). Another study, which was conducted with tax professionals, found that regulation of professions, client-related issues, taxpayer preference, tax practitioners' credentials, technique competence, exposure to practice risk and information provided by the taxpayer can affect ethical behaviour (Nienaber, 2010).

As the present study focuses on determining the influence of ethical climate, professional commitment, corporate ethical values and ethical ideology factors on ethical behaviour, the subsequent sub-sections review literature specifically on each of these factors.

2.3.1 Ethical Climate and Ethical Behaviour

Prior studies have found different results in regards to the influence of ethical climate on ethical behaviour. Wimbush and Shepard (1994) have suggested that the ethical climate of an organization could be used to predict not only unethical behaviour but also counterproductive behaviour. Wimbush, Shepard and Markham (1997) conducted a survey to find the relationship between ethical climate dimensions and ethical behaviour in retail stores throughout the United States with approximately 4400 employees. By using "Within and Between Analysis", they found that there is a relationship between dimensions of ethical climate and ethical behaviour. Independence climate was negatively related to complicit, disobedient, and lying behaviours. Caring climates were negatively related to being an accomplice, disobedience, and stealing. The law and code climate was negatively related to

disobedience and stealing, and lying behaviours, whereas service climate was negatively related to lying and stealing behaviours. The only positive significant relationship was found between instrumental climate and complicit behaviour. Though none of the other behaviours was significantly related to an instrumental climate, all of the relationships were in the positive direction. Thus, in general, the instrumental climate was the most related to unethical behaviour (Wimbush et al., 1997).

In contrast, a study conducted by Vardi (2001) to examine the relationship between ethical climate and organizational misbehaviour among 97 Israeli supervisory and non-supervisory employees of a metal production plant found only one significant positive relationship of climate with misbehaviour. Vardi (2001) found the only importance facet of climate influencing organizational misbehaviour is law and rules, whereas the activities of misbehaviour reported by both managers and employees were negatively related to the rules, instrumental and caring dimensions of ethical climates.

Further, Andreoli and Lefkowitz (2008) surveyed 145 employed graduate and undergraduate students via web-based survey to examine the individual and organizational antecedents of misconduct in organizations. The findings suggest that formal organizational compliance practices and ethical climate are independent predictors of misconduct, while, compliance practices moderate the relationship between ethical climate and misconduct, as well as between pressure to compromise ethical standards and misconduct.

Similarly, Peterson (2002a) conducted a study to determine whether deviant workplace behaviour could possibly be predicted from the ethical climate of an organization. By using postal survey of ECQ, responses among undergraduate students from the college of business between the years 1983 and 1995 were gathered.

The results revealed that low adherence to company rules and laws would be more likely to foster deviant behaviour related to misuse of organizational property. Organizations that adopt a caring climate are less likely to experience problems such as gossiping and blame others. Meanwhile, rules climate can lead to misuse of organizations' belonging for personal use, and instrumental climate can lead to deviant such as work slower on purpose and doing personal things during work.

Huang, You and Tsai (2012) conducted a study to examine if ethical climate types can influence organizational behaviour. Questionnaires were distributed to 352 participants in the training program of the Taiwan Nurses Association. The results suggested that climate types of caring, law and code and rules climate lead to ethical behaviour within the hospital; in contrast an instrumental climate lead to unethical behaviour among nurses in Taiwan.

Fritzsche (2000) examined 285 managers from a high technology company for the purpose of extending studies in regards to the relationship between ethical climates and ethical decisions. The results revealed that efficiency led equally to ethical and unethical decisions, and people will take the most ethical decision when faced with various types of ethical dilemmas. It was also found that half of the high technology managers were guided by laws or professional codes. Deshpande and Joseph (2009) examined factors impacting ethical behaviour through a survey of 103 nurses in a hospital and discovered that independence climate had a significant impact on ethical behaviour of nurses. Other ethical climate types, such as professional, caring, rules, instrumental and efficiency, did not impact ethical behaviour.

Abdullah, Sulong and Mohd Said (2014) conducted a questionnaire survey to analyse the influence of ethical climate on ethical judgment and unethical behaviour in the Malaysian public sector. A total of 151 questionnaires were returned and analysed

using regression analysis; the result revealed a positive significant relationship between ethical climate and ethical judgment of employees' behaviour in selected public sector auditors.

Another study done by Peterson (2002b) analysed the relationship between unethical employee behaviour and ethical climate using the dimensions of the Ethical climate questionnaire (ECQ). 202 responses received from US alumni who graduated with a degree from a college of business. The results demonstrated that most of the ethical climate dimensions were clearly significantly related to an aggregate measure of unethical behaviour. Specifically, an egoism, particularly self-interest, climate had a significantly positive relationship with unethical behaviour. Thus, organizations that have higher self-interest need to alter the ethical climate in order to reduce unethical behaviour. By contrast, benevolence and principled climates were found to be negatively related to unethical behaviour.

Fu and Deshpande (2012) conducted a survey to examine factors impacting ethical behaviour in China. The study conducted among 208 Chinese employees of a state-owned steel company revealed that only a rules climate had a significantly positive impact on ethical behaviour. The study also found that between not for profit and for profit board of directors, moral reasoning was not different, but different types of ethical climates were exhibited.

Barnett and Vaicys (2000) conducted a survey to examine the direct and indirect effect of work climate on ethical judgments and behaviour. The survey was distributed to 1000 American Marketing Association professional members. The result indicated that organizations can positively affect ethical behaviour by establishing climates characterized by a utilitarian ethical criterion directed towards external constituencies, as well as rules and codes climate.