AUDIT COMMITTEE CHARACTERISTICS AND INTERNAL
AUDIT BUDGET: MALAYSIAN EVIDENCE

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BUDGET: MALAYSIAN EVIDENCE

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ABSTRACT

An audit committee is viewed as an essential self-regulatory internal governance instrument that is expected to provide an overseeing role over the entire process of financial reporting. An internal audit is also one of the corporate governance cornerstone that is essential for the effective monitoring of the operating performance of internal control. To ensure its effectiveness, the audit committee monitors the resources available to the internal audit, and internal control functions should be directly reported to the audit committee. This study is set out to explore the effect of audit committee characteristics (i.e. independence, expertise, meeting and tenure) on internal audit budget in Malaysia, where governance mechanisms are suboptimal. The study also opens the door to an unanswered question, that is, whether an audit committee index is related to internal audit budget. Data of 96 companies listed on Bursa Malaysia for a three-year period, 2012-2014, was utilized to achieve this end. The regression result shows that there is audit committee meeting and index are significantly and positively associated with internal audit budget. They also indicate that audit committee tenure has a significant and negative impact on internal audit budget. The theoretical, practical, academic and regulatory implications of these findings were discussed in details. On one extreme, the findings of the study supports the recent policy initiatives in relation to audit committee and internal audit. On the other extreme, the result serves as a wake-up call to policy makers in requiring more committed, competent and skilled members on the audit committee.

Keywords: Audit committee characteristics; internal audit budget; Bursa Malaysia
ABSTRAK


Kata kunci: Ciri-ciri jawatan kuasa audit; bajet audit dalaman; Bursa Malaysia
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Sincerely,

Almahdi Ali Mohamed Saleh Almagdoub
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<th>Full Form</th>
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<tr>
<td>MCCG</td>
<td>Malaysian Code of Corporate Governance</td>
</tr>
<tr>
<td>PCAOB</td>
<td>Public Accounting Oversight Board</td>
</tr>
<tr>
<td>IIAM</td>
<td>Institute of Internal Auditors Malaysia</td>
</tr>
<tr>
<td>BRC</td>
<td>Blue Ribbon Committee</td>
</tr>
<tr>
<td>MIA</td>
<td>Malaysian Institute of Accounting</td>
</tr>
<tr>
<td>PLCs</td>
<td>Board of Public Listed Companies</td>
</tr>
<tr>
<td>AOB</td>
<td>Audit Oversight Board</td>
</tr>
<tr>
<td>SEC</td>
<td>Securities and Exchange Commission</td>
</tr>
<tr>
<td>IAFNV</td>
<td>Investment in Internal Auditing</td>
</tr>
<tr>
<td>AC</td>
<td>Audit Committee</td>
</tr>
<tr>
<td>ACC</td>
<td>Audit Committee Characteristics</td>
</tr>
<tr>
<td>ACIND</td>
<td>Audit Committee Independence</td>
</tr>
<tr>
<td>ACEXP</td>
<td>Audit Committee Expertise</td>
</tr>
<tr>
<td>ACMEET</td>
<td>Audit Committee Meeting</td>
</tr>
<tr>
<td>ACTEN</td>
<td>Audit Committee Tenure</td>
</tr>
<tr>
<td>Acronym</td>
<td>Description</td>
</tr>
<tr>
<td>---------</td>
<td>----------------------------------------------</td>
</tr>
<tr>
<td>ACINDX</td>
<td>Audit Committee Index</td>
</tr>
<tr>
<td>ACSIZE</td>
<td>Audit committee size</td>
</tr>
<tr>
<td>LEV</td>
<td>Leverage</td>
</tr>
<tr>
<td>SIZE</td>
<td>Firm Size</td>
</tr>
<tr>
<td>INVEN</td>
<td>Inventory</td>
</tr>
<tr>
<td>OCF</td>
<td>Operating cash flow</td>
</tr>
<tr>
<td>IAFOS</td>
<td>Internal Auditing Source arrangement</td>
</tr>
<tr>
<td>OLS</td>
<td>Ordinary Least Square</td>
</tr>
<tr>
<td>CEO</td>
<td>Chief Executive Officer</td>
</tr>
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CHAPTER ONE
INTRODUCTION

1.1 Background of the Study

Following recent accounting scandals, deliberate manipulations and fraudulent activities of some corporations such as Enron, Worldcom, and Satyam that lead to accounting failure, internal auditing has increasingly became relevant as an important corporate governance mechanism (Carcello, Hermanson & Raghunandan, 2005; Coram, Ferguson & Moroney, 2008; Sarens & Abdolmohammadi, 2008). In response to these accounting failures, the Congress of the United States passed into law the Sarbanes Oxley Act of 2002 (SOX, 2002). This significantly affected several issues related to corporate governance and corporate financial reporting. Particularly, it pushed for more focus on internal controls and internal auditing. Hence, it is likely that a number of companies have shifted their concentration towards internal auditing during this period. In addition, the Public Accounting Oversight Board (PCAOB) asserted that an outstanding benefit of its standard on auditing an internal control is encouraging companies to invest in competent and objective internal audit function (PCAOB, 2004). Moreover, statistics show that internal audit budgets and number of internal audit staff grew by over 10 percent between 2001 and 2002 in the US (Carcello et al., 2005).

In a same token, internal auditing has become a very crucial component of global businesses. It is a vital constituent of the risk management, internal control structure of the organization (Anderson, Christ, Johnstone & Rittenberg, 2012). Internal auditing is
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Reference


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Ismail, W. A. W., Dunstan, K. L., & Van Zijl, T. (2009). Earnings quality and corporate governance following the implementation of Malaysian code of corporate governance. Available at SSRN.


Public Oversight Board (POB), 1994. In the Public Interest, POB, Stamford, CT


