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The American University in Cairo
School of Global Affairs and Public Policy

**ADOPTION OF INTERNAL AUDITING IN
DEVELOPING COUNTRIES: EGYPTIAN PUBLIC
SECTOR**

A Thesis Submitted to the

Public Policy and Administration Department

**in partial fulfillment of the requirements for the degree of
Master of Public Administration**

By

Samar Yousry El-Tahan

SID: 800 10 1321

Spring 2016

DEDICATION

This study could not have been written without the incredible and relentless support of my father, *Yousry*, and my mother, *Menna*, who have continued to provide me with endless support, love, and encouragement. Without them, I could have never had the strength or confidence to follow my dreams and complete my academic research.

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I dedicate my thesis to all of you.

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**ADOPTION OF INTERNAL AUDITING IN DEVELOPING COUNTRIES:
EGYPTIAN PUBLIC SECTOR**

Samar Yousry El-Tahan

Supervised by: Dr. Racha Helwa

ABSTRACT

The establishment of an independent internal audit system has become increasingly important as a means to promote governance, enhance institutional efficiency and promote public services. This research examines the extent of internal audit adoption in the Egyptian public sector. Moreover, it investigates the factors and barriers affecting this adoption and provides some solutions and recommendations for overcoming these obstacles. The study adopts qualitative methodology, as the researcher conducted in-depth semi-structured interviews with those individuals who are embedded in the process of internal auditing in Egypt. The findings highlight negative consequences of change. As the Egyptian internal auditing has a very low level of independence and qualifications of internal audit staff. In addition, the role of the internal auditors is strictly limited to financial audit and compliance with laws, where in the meantime, the modern definition of internal auditing sheds the spotlight on the performance based audit as well as it sheds the spotlight also on the financial audit. To conclude, Egypt has no any successful independent internal auditing system, and will not have any successful internal audit system, unless, the administration methodology is changed radically, once most of the focal issues have been resolved, Egypt will be able to hold a successful independent internal audit system.

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List of Acronyms

IAF	Internal Audit Function
IDI	In Depth Interviews
IIA	Institute of Internal Audit
ENCC	Egyptian National Competitiveness Council
PSIAS	Public Sector Internal Audit Standards
CAE	Chief Audit Executive
RIASS	Relevant Internal Audit Standards Setters
IAQAF	Internal Audit Quality Assessment Framework
GIAA	Government of Internal Audit Agency
ACA	Administrative Control Authority
ASA	Accountability State Authority
EFSA	Egyptian Financial Supervisory Authority
MoF	Ministry of Finance
NAO	National Audit Office

Chapter One: Introduction

This chapter describes the nature of the research as well as discusses the research question, objectives and methodology.

1.1. Nature of Research

Internal Auditing has a vast range of definitions that have developed over the time. Ramamoorti (2003) drew an outline for the evolution of the role and responsibilities of Internal Auditing Function (IAF) over time. He suggested that at the early stage of development of the internal auditing concept, the understanding of ‘auditing ‘was strictly limited to financial compliance. By 1947 however, the *Statement of Responsibilities of Internal Auditing* clearly suggested that Internal Auditing does not only deal with the financial facets but also englobes the operational and performance aspects of an organization. The definitions, role and scope of activities of the IAF continued to progress over time. By the turn of 1981, Sawyer framed internal auditing as a process of independent assessment of the various procedures and actions within an entity, to determine whether acceptable policies and operations are being followed, whether important ground standards are met, assets are used efficiently and the organization’s overall mission and vision is being matched. As a result, in 2005 the IIA defined internal auditing as:

“An independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes”.

Therefore, the establishment of an IAF within the public sector is significantly important as it provides critical assurance techniques and develops instruments for

monitoring and assessing management undertakings in public organizations. IAF also helps government agencies to ensure accountability and integrity, improves the execution of government platforms and develops a sense of trust and confidence among citizens and the various stakeholders in the public sphere (Baharud-din *et al*, 2014).

Internal auditing is designed to enable public organizations meet their objectives (Plicher *et al*, 2013). If internal auditing in public sector is well designed, it will improve the workflow and serve as a valuable guideline promoting public governance.

We can conclude that internal auditing has a critical purpose in improving the proficiency of the public sector. In Egypt however, the public sector seems to lack a well-functioning internal auditing mechanism. Almost none of the public institutions in Egypt have an internal audit principles and standards department. In addition, there is a lack of academic research and empirical work on the internal auditing in the public sector in Egypt. As most of the existing literature on Egypt tackles the definition of internal auditing at large and discusses its importance in the Egyptian context, but it does not go deep in the analysis to address the reason behind the deficiency of the public sector in introducing an IA system that monitors the performance of public institutions and ensures the quality of policy deliverables. In addition, existing research equates between public and private sector institutions while both categories follow different dynamics. Furthermore, the wider literature on IA focuses on case studies from developed nations. This leads to the gap that creates the *raison d'être* of this research. The main aim of the research is to discuss the deficiency of establishing a well-functioning system in Egypt, and to analyze the

opportunity cost resulting from this absence. The research uses best practice country comparison and develops related policy recommendations.

1.2. Research Problem

Recently, the importance of IA has witnessed a rapid escalation among private, governmental entities and non-profit organizations over the last six decades (Ramamoorti, 2003). Also, the significance of IA actually lies in the role IA plays in providing the management of any organization with the essential information necessary for a more efficient and adequate organization (Diamond, 2002). Moreover, Internal auditing usually promotes good governance in public sectors by providing objective assessment of whether the public resources are adequately utilized in order to achieve favorable results.

According to Nnenna, the functions of IA include ensuring that all necessary guidelines adopted by the administration are implemented, and also to make sure the accuracy and reliability of information provided to upper management (2012). Consequently, the lack of IA principles in any given public or private sector organization is actually at risk.

The reason behind the risky situation that lack of IA principles cause lies in that auditors help the public sector organizations to attain liability and integrity and improve operations (IIA, 2012). We can conclude that elements of IA ranging from oversight, insight and foresight are the integral pillars of providing proper internal auditing in public sectors. Henceforth, complete absence of IA will lead to the lack of oversight, which in turn leads to distrust among common citizens and stakeholders. In addition, the lack of principals of IA executed in the public sectors leads to an increase in fraud and financial misstatements, also, the reports given to administration

will be inaccurate and unreliable as there is no internal auditing to vouch for the credibility of these reports (Nnenna, 2012).

The problem that this research confronts is that the Egyptian public sector lacks the codes of internal auditing within its establishments; whether it was governmental institutions or public holding companies. Moreover, upon the revision of preceding literature, the researcher found that the predominately focused on testing the significance of the impact of some variables on the internal auditing and its effectiveness in the public sector (Alzeban and Gwilliam, 2014; Mihret and Yismaw, 2007). Extensive research has been conducted an assessment between private and public companies in the context of internal auditing (Goodwin, 2004; Cohen and Sayag, 2010; Lori, 2011; Neu *et al*, 2013). Most literature has shed the spotlight on a comparison between internal and external auditing in public sector companies (e.g. Plicher, Gilchrist and Singh, 2013). In addition, the focal point of the debate has been concerned with the internal auditing in public companies (e.g. Goodwin, 2004; Zakaria *et al*, 2006; Zain and Subramaniam, 2007; and Vijayakumar and Nagaraja, 2012; Christooher, 2012; Plicher, Gilchrist and Singh, 2013; Alzebban and Gwilliam, 2014) and internal auditing in the government and public financial management (e.g. e.g. Diamond, 2002; and Gansberghe, 2005; Asare, 2009; Akikins, 2011; Aikins, 2013; Neu *et al*, 2013; Plicher, 2014).

Therefore, prior studies showed that there are many articles that can explain the role of internal auditing in the public sector, however these articles overlook IA main functions and how IA is implemented in developing countries especially Egypt. This study will examine the level of adoption of internal auditing in the Egyptian public sector as a first step. The second step will be analyzing this adoption and determining the factors affecting the implementation of internal auditing. As a result, this will

further instill confidence among citizens and increase the efficiency, effectiveness, accountability and credibility of the Egyptian public institutions.

1.3. Research Question

The main research question addressed in this research is:

- What is the level of adoption of internal auditing in the Egyptian public sector?

The following sub-question can be extended from the major question:

1. What are the factors affecting the success of internal auditing?
2. What are the obstacles and barriers facing the public sector in adopting internal auditing?

1.4. Research Objective

This study aims to pave the way for the Egyptian public sector to effectively adopt concepts of the internal auditing by reducing the theory-practice gap between Egypt's lack of IA standards and well defined procedures. In order to have efficient public sector governance and improved public sector performance, Egypt must have a well-designed function of internal auditing. The latter is the core objective of this research which can be accomplished by fulfilling the sub-objectives. The first sub-objective is to empirically examine the extent of internal auditing adoption in the Egyptian public sector. The second sub-objective is to investigate the factors and barriers affecting this adoption and provide some solutions and recommendations for overcoming these barricades.

1.5. Research Methodology

Library Research

This involves investigating all the theoretical reports and articles that argue the progression of internal audit, responsibilities, role, and definition. Research is targeted towards internal public sector audits in both developing and developed countries. An overview for the Egyptian case is studied providing the researcher with the required data to determine the level of adoption of internal auditing in the Egyptian public sector.

Moreover, at this point, the researcher measures comparative internal audits performance between Egypt public sector and one of the developed countries that have a solid internal audit mechanism, mainly the United Kingdom. This is done by conducting interviews, inspecting government documents that are directly related to the internal audit function in both countries (Mohamed, 1997).

Field work

This phase consists of data gathering. The researcher gathers data by adopting the qualitative methodology. In-depth semi-structured interviews will be shown with external auditors and those who are responsible for applying the principles of internal audit mechanism in Egypt. The interviewees will be questioned on internal auditing and whether they view IA as an important instrument for enhancing good governance. Interviewees will be asked if the internal audit departments in the public sector meet the abstract role of internal audit function. Additionally, questions as to the role of internal auditing, the level of adoption of internal auditing, the factors affecting the adoption, the barriers facing it and the recommendations for enhancing it will be asked.

1.6. Thesis Structure

The research is divided into five chapters. The first chapter familiarizes the themes of internal auditing and classifies the research problem, objective, question, and ends with the research outline.

The second chapter presents a review of the literature. The literature part gives the required background about similar studies. The literatures include studies linked to definitions of internal auditing, its characteristics, its effectiveness, internal auditing in public sector, internal auditing in UK and the background of the Egyptian case study.

Chapter Three discusses the research methodology, with techniques and instruments used; as well as limitations encountered in the process of data collection.

Chapter Four presents the findings and analysis of the gathered data; and provides a relevant overall discussion.

Chapter Five concludes the thesis by providing recommendations for improvement of the internal auditing mechanism in the Egyptian public sector.

Chapter Two: Literature Review

2.1. Internal Auditing: Overview

Internal auditing began in the United States in the early forties. According to Friedberg (1998) both public and private sectors in the United States in 1941 encountered rapid growth accompanied by failures, difficulties and problems in many areas. Therefore, this situation required the development of a new function which currently known as "internal audit" (Brink and Witt, 1982). Early research on internal auditing investigates the phases of its evolution, including the founding of the Institute of Internal Auditing "IIA" in 1941, the definition of internal auditing based on the principle of "operational auditing" almost two decades after the establishment of the IIA (Brink and Cashin, 1958). In 1978, the approval of the IIA to the *Standards for the Professional Practice of Internal Auditing*. By 1981, the *Statement of Responsibilities of Internal Auditing* noted that internal auditing is a form of control which functions by examining and evaluating the effectiveness of other controls (Ramamoorti, 2003).

Internal auditing is defined as an independent, objective assurance and consulting activity that adds value to an organization while improving organizational operations (IIA, 2005). Ramamoorti (2003), internal auditing has gained an increasingly important role within organizations, whether private, governmental, or nonprofit over the last 60 years. Diamond (2002), suggests that internal auditing is important because it provides the organization's management with information about the adequacy and effectiveness of the organization's system. The revised Statement of Responsibilities of Internal Auditing issued by the Institute of Internal Auditors (1990) states:

"The objective of internal auditing is to assist all members of management in the effective discharge of their responsibilities by furnishing them with analyses,

appraisals, and recommendation pertinent comments concerning the activities reviewed."

Prior research on the role of internal auditing reveals that internal auditing plays a critical task in promoting good governance (Woodard, 2002; Brody and Lowe 2000; Diamond, 2002; Ramamoorti, 2003; Gansberghe, 2005; Carey *et al.* 2006; Zain and Subramaniam, 2007; Leung *et al.* 2011; Christopher, 2012; Plicher *et al.*, 2013; Neu *et al.*, 2013). Furthermore, the function of internal auditing has extended to encompass assurance, risk management and consulting services (Leithhead 1999; Brody and Lowe 2000; Walker *et al.* 2003; Ramamoorti, 2003; Gansbergh, 2005; Carey *et al.* 2006; Leung *et al.* 2011; Simona and Elisabet, 2013; Neu *et al.*, 2013). Moreover, in an early study conducted by Reinstein and Gabhart in 1987 that was further elaborated by many researchers, stated that internal auditing strengthens the function of internal control and is responsible for establishing the audit committee.

2.2. Characteristics of Internal Auditing

In order to understand the role of internal auditing and to identify its characteristics, experts recommended a number of criteria in order to measure the effectiveness of internal audits e.g. degree of independence (Chrisopher, 2012; Burnaby and Hass, 2011; Mihret and Yismaw, 2007; Zakaria *et al.*, 2006; Gansbergh, 2005; Ramamoorti, 2003 and Friedberg, 1998), source of authority (Burnaby and Hass, 2011; Mihret and Yismaw, 2007; Zakaria *et al.*, 2006; Fischer and Montondon, 2005; Gansbergh, 2005 and Friedberg, 1998), scope of work or the compass of the audited organization (Alkafaji *et al.*, 2010 and Fischer and Montondon , 2005), professional proficiency, the performance of the audit and management of internal audit department as cited by Ramamoorti (2003), Diamond (2002) and Friedberg (1998). According to Acrons and Popanz (2012), the top five characteristics of high functioning international audit

organization are: Aligning audit with strategic risk, continuous auditing, competency development, leadership development and performance measurement. However, Zain and Subramaniam (2007) argue that internal auditors must have integrity and courage, team work and communication skills. They must be curious and open to diversity. In light of the relationship between internal auditing/auditors characteristics and the criteria needed to perform and evaluate the audit process, newly identified activities emerged including corporate governance reviews, enterprise risk management audits, reviews of linkage of strategy and company performance, ethics audits and migration to IFRS (IIA, 2011).

2.3. Effectiveness of Internal Auditing

Empirical evidence examines the effectiveness of internal auditing in the private sector and even fewer in the public sector. Among studies that examined IA effectiveness of internal auditing in the private sector a study sponsored by the Institute of Internal Auditing (IIA), in which, fifteen factors measure the effectiveness of internal auditing were identified including the fit between the goals set by the management and the audited work and the qualifications of internal auditors (1988). Moreover, the factors associated with internal audit effectiveness can be categorized into three groups; each group is assigned to each stage of the auditing process, planning, fieldwork and review (Lampe and Sutton, 1994; Cohen and Sayag, 2010). On the other hand, in one of the studies that have examined internal auditing effectiveness in the public sector, the authors tested the association between internal audit effectiveness in the Ethiopian public sector with four key factors, which are management support, organizational settings, audited attributes and internal audit quality using a case study method in public universities of Ethiopia (Mihret and Yismaw, 2007). In 2014, Alzebban and Gwilliam examined also the effectiveness of

internal audit in Saudi Arabia public sector but by using different variables, including methods to measure the level of competence of the internal audit department, size of internal audit department, relationship between internal and external auditors, management support for internal audit and independence of internal audit.

2.4. Internal auditing in public sector

It is worth noting that internal auditing in public sector has been given a great attention by most of the authors.

The role of internal auditing in public sector has been argued by most of the authors for decades, where it was stated by Plicher in 2014 that the principal role of IA is to deliver effective performance which debatably is going to overlap with righteous governance

In municipalities, Internal audits play a crucial role in promoting good governance. The overview of growth accounting in local government definitely has extra complexity and additional risks, with cases of fraud, corruption and high risk investments in several Australian public entities being reported periodically by the media. Also it was cited by Aikins in 2011 regarding the role of internal auditing sector that the effort of government internal audits leads to enhancements in government financial transactions. Broken economic downturn and deteriorating state aid to local governments has left many public directors looking for ways to progress financial oversight and operational productivity. Even if the internal audit is one range with the proficiency to assess effective utilization of financial assets and helps develop oversight and financial acts, public management research has paid little attention to the role of internal audit in the financial management process. And last, but not least the descriptive article that Simona and Elisabeta wrote in 2013, which

states that it has concentrated mainly on assessing internal control and not on the process of risk management and corporate governance. The aim of this literature is to analyze and assess the role of the internal auditing in risk management in community establishments.

On the other hand, some of the studies discuss the public sector's internal audit in the framework of IA effectiveness (Lampe and Sutton, 1994; Woodard, 2000; Mihret and Yismaw, 2007; Cohen and Sayag, 2010; Alzebban and Gwilliam, 2014; Baharud, Shokiyah and Ibrahim, 2014; Hailemariam, 2014; Shamsuddin, 2014).

2.5. Internal Auditing in UK

Since, some studies and researches used UK as a benchmark for setting up a model, therefore studying the British literature is important for enhancing the understanding the internal audit department according to Liu, Boo and Bonsu in 1997. In this study, the author discussed the methodology for setting up a new division, and its necessities. He defined the construction and the staff of the internal audit department and argued the scope and obligation of IA. Finally, he offered recommendations in order to have a highly effective internal audit department.

The United Kingdom's literature is divided into two major sub-divisions, First academic articles and second auditing in the British educational system has received little attention. As stated by Vinten in 2004 when, he wrote an article discussing the future of UK internal audit education, as most of the concern –in his point of view- is given to higher education.

El-Kheir in 1997 compared between the internal and external audit systems in his country and those of UK in his research. This comparison helped him figure out the

weaknesses in the studied internal audit system and find recommendations to solve them.

Many reports were issued by the UK government as for the purpose of IA in public sector. Moreover, there reports that address the internal audit standards in the public sector the report states that a professional, independent and objective internal audit service is one of the key elements of good governance, as recognized throughout the UK public sector.

This document is therefore addressed to Accounting Officers, Accountable Officers, board and audit committee members, heads of internal audit, internal auditors, external auditors and other stakeholders such as chief financial officers and chief executives.

Moreover, a study made by the World's Bank Institute outlined the role of internal audit in the UK. Gansberghe in this study stated that during the last three decades, the UK has progressed their internal audit from internal checks, "turn and tick", to a system's based approach, which monitors the achievement of well-defined goals and objectives/ The UK's IA also ensures compliance to relevant laws and regulations with a great deal of reliability and transparency of for more economically effective use of assets. There are currently ten principals, half linked to organizational status and the other half to operational approach. The details of these standards include the scope of IA, independence, risk management control, audit strategy and due professional care.

2.6. Background of the Egyptian case

I will be given a historical overview of Egypt due to the fact that Egypt is currently the main focus of this paper, I will discuss Egypt as a case study of a developing country in the Middle East and in the Arab world.

El-Kheir mentioned in 1997 that auditing has always been known in Egypt as far back as 5500 years. Early Egyptians required the actual beholding of corn being brought to the granaries and demanded that receipts of corn be certified. [Sawyer, 1988: 18] Nowadays, there is little that study has to offer about auditing in Egypt.

Ebaid (2011), in his study aimed to discover the nature and features of internal audit function in Egyptian Private Sector firms and evaluate IA's ability to fulfill its role in corporate governance. The findings of the study reveal that a large fraction of Egyptian private sector listed firms have internal audit function, but IAF in these firms is less developed. IAF has low levels of organizational individuality, administrative support, and qualification of internal financial audit and internal controls compliance and has not yet moved towards the expanded new role explained in Institute of Internal Auditors' new definition. Finally, the results indicate that there is a weak level of interaction between internal and external auditors in Egypt. These results suggest that internal audit function in Egyptian private sector listed firms, in its current status, can come along with many hardships that affect negatively its efficiency in corporate governance.

The objective of the country-office audit is to provide assurance as to whether there are suitable and effective controls, risk-management and governance processes over a number of strategic areas in the office. In addition to this assurance service, the audit

report identifies, as appropriate, noteworthy practices that merit sharing with other UNICEF offices. (Office of Internal Audit and Investigations (OIAI) Report 2013/33)

To conclude, there has been some research on the comparison between private and public companies in the context of internal auditing (Goodwin, 2004; Cohen and Sayag, 2010; Lori, 2011; Neu *et al*, 2013), while some other articles focused on the comparison between internal and external auditing in the public sector companies. Researchers explained that internal audit has an advantage over external audit in discovering the problems in an early stage and obtaining the information more quickly (e.g. Plicher, Gilchrist and Singh, 2013; Xiangdong, 1997; Spaarkman, 1997). However, the main debate of this issue was between internal auditing in public companies (e.g. Goodwin, 2004; Zakaria *et al*, 2006; Zain and Subramaniam, 2007; and Vijayakumar and Nagaraja, 2012; Christooher, 2012; Plicher, Gilchrist and Singh, 2013; Alzebban and Gwilliam, 2014) and internal auditing in the government and public financial management (e.g. Diamond, 2002; and Gansberghe, 2005; Asare, 2009; Akikins, 2011; Aikins, 2013; Neu *et al*, 2013; Plicher, 2014). Prior literature indicates that there are many articles that explained the role of internal auditing in the public sector, but these articles ignore its role in the developing countries especially Egypt. Therefore, the study will examine the extent of which internal auditing is adopted in the Egyptian public sector and the factors impacting this adoption, this in turn will help improve public sector performance especially after the period of the successive revolutions.

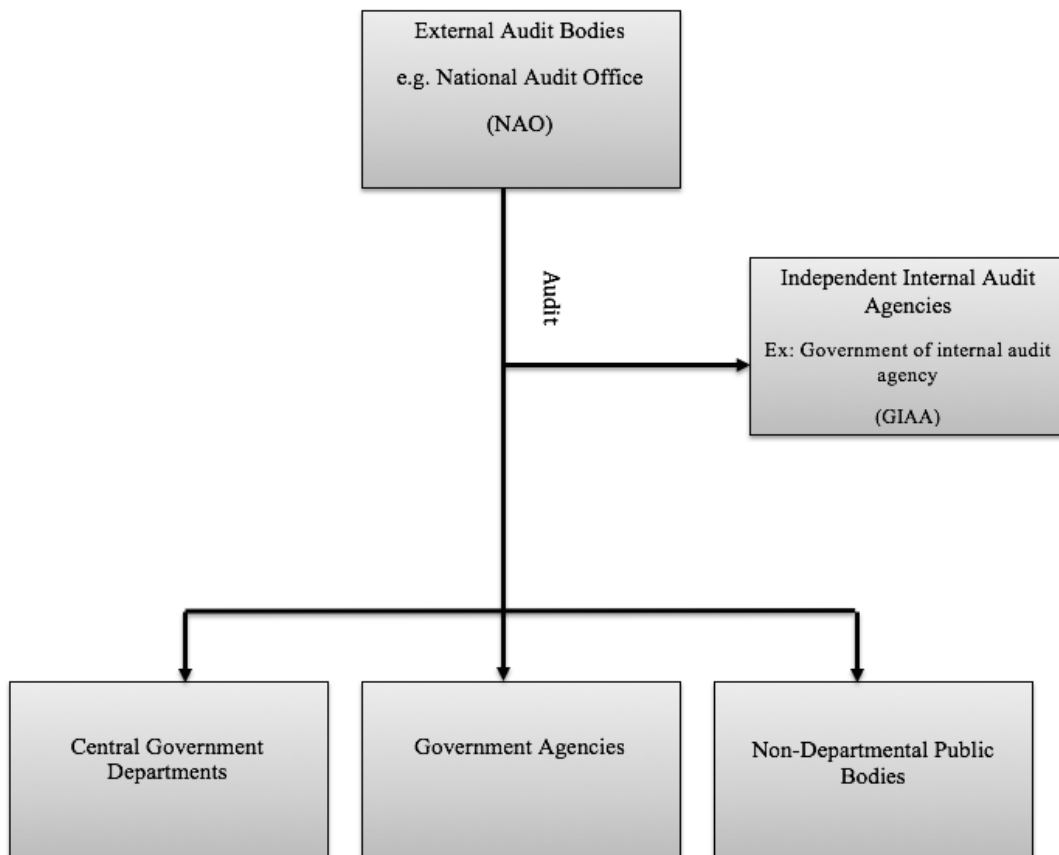
Chapter Three: Research Methodology

3.1. Research Framework

The researcher draws a comparison between the current state of internal auditing in Egypt and United Kingdom as it has one of the most comprehensive internal audit systems. According to the National Audit Office website, UK spends over \$70 million dollars a year on internal auditing. The independent internal auditing system in UK, which acts as an intermediate preventive body for frauds and violations, while external audit bodies complements the work of the internal auditing in terms of assurance and maintaining control. Moreover, most of the Egyptian institutions were built and developed under the English occupation. From 1911 to 1936, Egyptian administration was brought under the supervision of Europeans and most of the Egyptian systems were developed under the British rule, for example: The judicial system in Egypt is based on European legal concepts and methods (Innes, 1986).

Although this comparison is outdated but it raises the question of why they have developed each and every single policy and the state of Egypt is yet to have the prerequisites of internal auditing and still many public organizations do not have an internal audit department. Another reason for choosing the United Kingdom as a benchmark model is that the UK has, recently, inserted a set of standards that are applicable to its public sector (PSIAS).

Structure of Auditing in UK



[Figure 3.1] Structure of Auditing in UK, Developed by the author

External Auditing: National Audit Office (NAO)

The National Audit Office (NAO) is an independent parliamentary body in the United Kingdom which is responsible for auditing central government departments, government agencies and non-departmental public bodies.

The National Audit Office scrutinizes public spending for Parliament. The public audit perspective helps Parliament hold the government accountable for public

services

The audit work of the NAO has two main purposes:

- Reporting audit results to Parliament, to help to hold government departments and other bodies to account for how they use public money.
- Through value-for-money work, NAO reports on whether departments and other bodies have used public money efficiently, effectively and with economy.

The Comptroller and Auditor General (C&AG), Amyas Morse, leads the NAO and is an Officer of the House of Commons. He and the staff of the NAO (are independent of the government.

The C&AG use his powers to:

Decide which value-for-money examinations to carry out;

- Decide how to report results to Parliament; and
- Use rights of access to documents and staff to get information and explanations.

NAO focuses on three strategic objectives:

- To develop and apply our knowledge;
- To achieve high performance;
- To increase our influence.

To achieve these strategies, we gain insight about what enables and inhibits good performance in departments and across government sectors in Egypt. Using our expertise, we use this knowledge to help departments and the public sector to improve their performance.

Overview of the internal audit function in UK

From April 1, 2013, the Relevant Internal Audit Standards Setters (RIASS) has adopted a common set of standards that aims to establish a framework for providing

internal audit services and for evaluating internal audit performance. These standards are the Public Sector Internal Audit Standards (PSIAS) which encompass the required elements of the Institute of Internal Auditing (IIA) as follows:

- Definition of Internal Auditing
- Code of ethics
- International standards for the professional practice of internal auditing

However, additional requirements and interpretations have been adopted for the United Kingdom public sector.

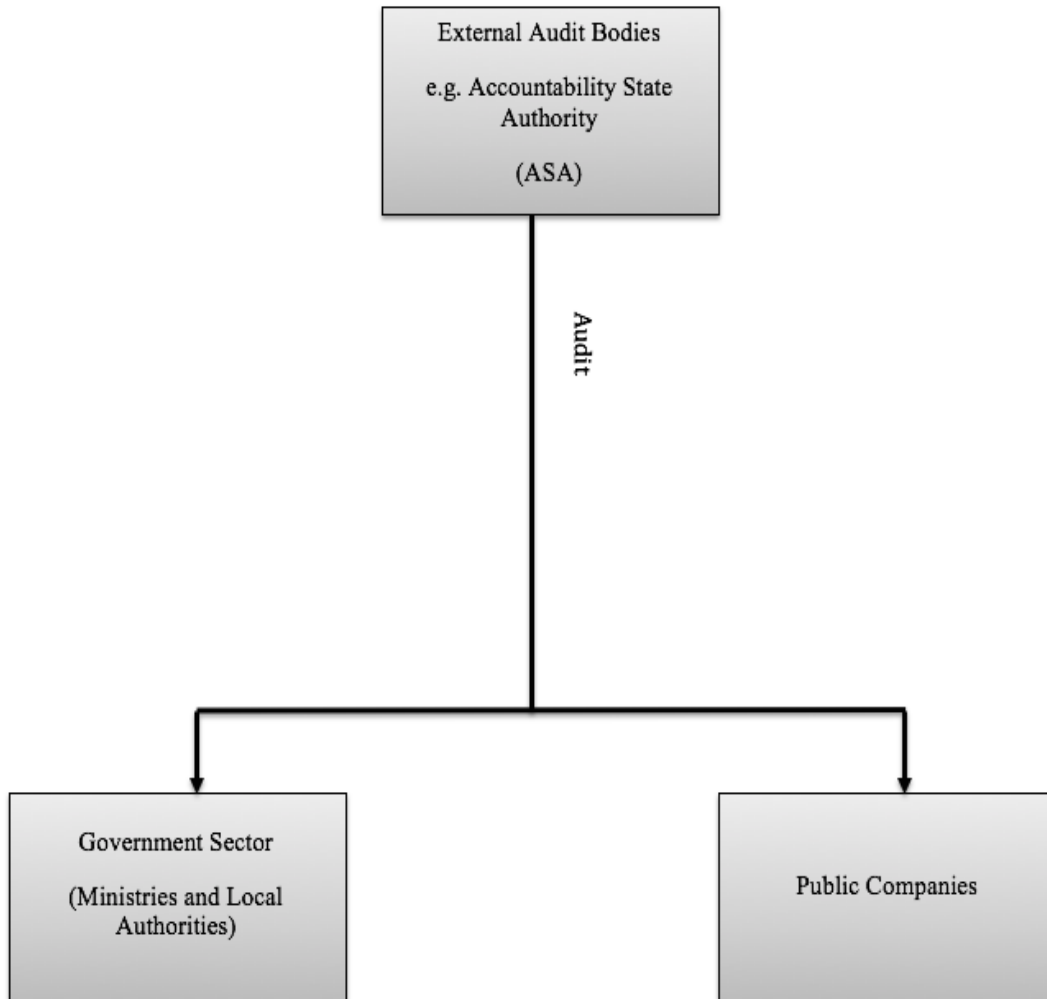
The Chief Audit Executive (CAE) must apply these standards in the internal audit department in each public sector organization.

Moreover, a framework for evaluating and assessing the internal audit quality must be performed periodically in order to provide feedback on the quality of the internal audit service. This framework is the Internal Audit Quality Assessment Framework (IAQAF) which has four sections reflecting the purpose, the structure, the audit execution and the impact of the internal audit service on the governance and the control risk within the organization.

After applying the PSIAS and the IAQAF, the chief audit executive of the internal audit department provides feedback to the head of government internal audit profession and to the government of internal audit agency (GIAA) which on the other hand reviews the functions and activities of the government and public sector organizations, makes recommendations for improvement and adds value to the public service.

To conclude, internal auditing in the United Kingdom acts as an intermediate preventive body between the external audit function and the government as well as public sector organizations. This in turn will lead to enhancing governance, improving operations and achieving integrity and accountability.

Structure of auditing in Egypt



[FIGURE 3.2] Structure of Auditing in Egypt, Developed by the author

External Auditing

External Auditing and Internal Auditing are the two types of audit that are performed in the Egyptian public sector.

There are three bodies that are in charge of external auditing:

1. Accountability State Authority (ASA)
2. Ministry of Finance (MoF)
3. Administrative Control Authority (ACA)

Overview of internal auditing in Egypt

Internal Auditing in the public sector is performed by the internal auditors within each public entity.

Internal auditing in Egypt does not have a structured workflow. The auditors do not follow internal audit standards; they only audit each financial transaction prior to issuance (pre-spending). However, some public departments and organizations have their own guidelines on the practice of internal auditing; these guidelines are issued to assist internal auditors operate for the department or organization and to provide guidance for those auditors while they are performing their auditoria duties.

The discrepancy between the two models is that the Egyptian public sector lacks the principles of internal auditing. The intermediate preventive role of internal auditing is absent in the Egyptian government as well as its public sector organizations.

Moreover, as shown in the two diagrams, Egypt does not have an independent body or agency for the internal audit function. In addition, most of the public sector organizations do not have an internal audit department. Prior research indicated that the absence of internal audit principles is very critical. This is due to a lack of oversight, insight and foresight advocates a lack of confidence among citizens and stakeholders. In addition, the absence of internal auditing directives along with the related-enforcement mechanisms in the public sector leads to an increase in the levels

of fraud and financial misstatements in the public sector. Work reports that are presented to senior management of public institutions become unreliable as there is no internal auditing mechanism to vouch the credibility of these reports (Nnenna, 2012).

This research addresses the absence of a structured internal auditing system in Egypt and assesses the opportunities that the Egyptian government can use to address this problem by building on the expertise of the comprehensive External-Internal Audit system in the United Kingdom. The research highlights the need for the development of a fraud-preventive mechanism similar to the one in the UK as it finds that piecemeal auditing techniques have not been effective.

3.2. Research Design and Data Collection

In order to address the research question, the study adopts a qualitative methodology. The researcher conducted in-depth semi-structured interviews with those individuals who are responsible for the external bodies and responsible for implementing the principles of internal auditing in the Egyptian public-sector in order to explore whether public sector in Egypt applies the principles of internal auditing or not. The interviewees were asked about their perception of internal auditing and if they viewed IA as an important tool for enhancing good governance. Then, they were asked if the internal audit departments in the public sector meet the theoretical role of internal audit function. Moreover, questions as to the role of internal auditing, the level of adoption of internal auditing, the factors impacting the adoption, obstacles facing IA and recommendations for enhancing IA were discussed

The quantitative methodology is not applicable for this research paper due to the numerical data that can be obtained. When examining whether the public sector in Egypt applies internal audit principles most probably the result will be the lack of

principles in the public financial management and public holding companies.

Therefore, the only type of data that can be obtained is explanatory and descriptive data. However, quantitative survey method may be utilized. But, in this case the researcher should follow up with results obtained from the survey which combines quantitative and qualitative methodologies. The alternative methodologies that can be used in this study will be discussed in more detail. One of the methodologies that can be utilized to address the research question is a questionnaire with open ended questions. In this questionnaire the participants in this study, who are the internal auditors, the managers of the audit department and the public officials, will be asked to answer several questions in order to find out whether the governmental sector or the public holding companies in Egypt apply the principles of internal auditing effectively. If these principles are not implemented, they will be asked what the prerequisites for introducing them are, whether implementing these principles important in the Egyptian public sector context, and what their recommendations to apply them effectively are.

The researcher can use alternative methodology that can address the research question. This methodology is a survey with close-ended questions. A survey that is designed to explore the existence of internal audit departments in the Egyptian public sector. Questions regarding the principles of internal auditing, its prerequisites, the recommendations to be applied in the Egyptian society will be asked providing answers of a scale from one to five, whether the participants strongly agree, agree, neutral, disagree or strongly disagree. The results of the survey can be followed up by the researcher, in order to get more interpretation from the participants of the study.

Focus groups, groups of internal auditors can also be interviewed. Each group may contain from six to twelve internal auditors and they will be asked by the researcher

several questions to know their opinion in how to introduce the principles of internal auditing in the Egyptian public sector, what are the benefits of introducing these principles, and how can this be done.

The case study method can be used. It enables the conduct of detailed analysis using multiple sources of data (Mihret and Yismaw, 2007). If the researcher chose the case study method, a large number of public sector institutions will be selected. Primary data can be collected by conducting in depth interviews with the managers of the audit departments if existed or with those personnel who are responsible for implementing the internal audit function in those institutions. Moreover, the researcher can distribute questionnaire to the internal auditors and the public officials in order to explore whether or not these organizations apply the principles of internal auditing. Also, to know what their recommendations are in order to introduce these principles in the Egyptian public sector, and which of these principles are applicable within the Egyptian context and which are difficult to be applied. Besides, if these organizations have internal audit department, then the researcher must review some documents related to it, such as, audit programs, audit plans, audit reports, audit manuals, and working papers. All these documents will serve as a secondary source of data. At the end of the day, the researcher will have multiple sources of data that can be used in order to answer his research question.

The qualitative methodology is used in this study, because the researcher is seeking in-depth interpretation for the prerequisites of introducing internal auditing in the public sector of developing countries in general and Egypt in specific. Moreover, unlike the results of any qualitative methodology, the results in this study can be generalized in all public sector companies in Egypt, as the researcher is trying to examine the level of adoption of internal audit function and the factors impacting their

adoption and the results will be the same in the Egyptian public sector as a whole. The researcher chose the interview method in particular as the researcher is trying to explore the views of the managers of audit departments and internal auditors to the internal audit principles and how should they be implemented in Egypt. Besides, the interview method shed light on aspects that could not be included in any other type of methodology.

Institutions:

The public sector in Egypt is divided into: Governmental sector (e.g. Ministries and Agencies), the public companies sector (e.g. Public Holding Companies), and the non-governmental organizations (NGOs). Purposeful sampling was adopted in this study, as a sample was taken from each sector. Firstly, from the governmental sector (ministries and agencies), the researcher chose the “Accountability State Authority”, the “Administrative Control Authority” and the “Ministry of Finance” as her first sample. These institutions were chosen as they are the external audit bodies in Egypt and they are responsible for any reform initiative considering internal audit function in the public sector.

Secondly, from the sector of the public companies, the researcher chose the “Holding Company for Food Industries”. It was selected as an example for the publicly held companies in order to identify the policies applied in their departments and to investigate the level of adoption of internal auditing in the Egyptian public-sector organizations.

Thirdly, from the non-governmental organizations (NGOs), the researcher chose the Egyptian National Competitiveness Council (ENCC). The ENCC is the first non-governmental organization to focus primarily on the issue of competitiveness in Egypt

and the Middle East. Moreover, it is currently concerned with the problem of internal control and improving the efficiency of financial audit function in Egypt.

Participants:

Although the researcher has interviewed only fourteen interviewees, she assured diversity in the participants in order to guarantee reliability and trustworthiness. From the “Accountability State Authority”, the persons interviewed were responsible for different types of tasks; one was in charge of auditing the electricity sector. Another, audits the “Insurance Company” sector, two of them audited the food industries sector and the fifth one was responsible for auditing the newspapers and the media and the press organizations. All of them hold high positions in the ASA. Furthermore, the researcher interviewed the head of financial sectors of the holding Company for food industries that is in charge of all the financial matters of all the subsidiary companies under this holding company. In addition, another two participants holding a high confidential position in the ‘Administrative Control Authority’ were interviewed. Moreover, a representative of the ministry of finance who has a “General Account Manager” position was interviewed and four managers from different departments were interviewed. In addition, an informant interview was conducted with a board member in the selected NGO.

The interviews were in-depth in order to get more interpretative information about the principles and the prerequisites of internal auditing in order for it to be implemented in the Egyptian public sector and to assess the internal audit function in Egypt. Also, interviewing the managers helped the researcher know how to change the culture of the Egyptian society to make it easier for these principles to be adopted, and to make the public institutions accept this change easily.

Accountability State Authority	5 IDIs
Administrative Control Authority	2 IDIs
Egyptian National Competiveness Council (ENCC)	1 IDI
Ministry of Finance	5 IDI
Holding Company for Food Industries	1 IDI

[Table 3.2] Summary of Interviews

3.3. Research Limitations

The research has faced some challenges, some of which pose limitations to the study. These limitations can be introduced by the lack of the academic writings and the empirical studies of the internal auditing in the Egyptian public sector. This lack of previous literature makes it a little bit difficult to analyze the function of internal auditing in the Egyptian public sector. Moreover, theoretical data collection generally helps the researcher in all parts of his study and its lack is considered one of the main limitations facing any research.

The second limitation is the difficulty of access to the public holding companies. This made it difficult for the researcher to take a representative sample from these companies. As a result, the researcher interviewed only one official holding managerial position in one public-holding company. In fact, the researcher intended to

interview the CEOs and the internal auditors of –at least- three public holding companies.

Another limitation is related to the research technique and the sample size which affect the degree to which research results can be representative to the target population. With regards to the use of interviews, and in addition to their advantages –previously discussed- which justify the research’s choice, some limitations do exist. Generally, in an interview method, the sample size is limited to the number of qualified respondents within the selected field. Moreover, the researcher only interviewed representative participants from the bodies which are responsible for implementing an effective internal audit function in the Egyptian public sector. Nevertheless, the researcher intended to conduct interviews with the internal auditors themselves to get more interpretative data about their perception to the internal audit function as they are the ones who are subjected to this policy.

The Egyptian culture also can be considered from the limitation of this study. In Egypt, we do not find the urge to change. Therefore, when the researcher introduces the recommendations for having a good model of internal auditing that will change the function and the structure of the public organizations, this may be faced by many barriers as Egyptians always have the fear to change even if the change is to the better. The political and economic instability of Egypt is another type of limitation that may negatively affect both the process of data collection and the implementation and adoption of the internal auditing principles.

Chapter Four: Data Findings, Analysis and Discussion

The data acquired from the interviews were analyzed according to the processes of qualitative analysis (Christopher, 2012). Questions as to the existence of internal audit department, its role, the qualifications and independence of internal auditors were asked in an open-ended style followed by an extensive and interpretative conversation (Christopher, 2012). Likewise, exploratory questions were asked after the general ones in order to get more interpretative data.

Interviewees were to be interviewed for the duration of half an hour; still, the interviews always took more time than that which ensures that they viewed it as a thought-provoking topic. Furthermore, in order for the interviews' results to be trustworthy and valid, all the interviewees were given a consistent understanding for the UK model with which the researcher compares the Egyptian one. They were also provided by a definition of internal audit and its role in public sectors.

Based on examining government documents and legislations that affects the internal audit profession (EL-Kheir, 1997), based on analyzing the comparison made between the two previously mentioned countries (Egypt and UK) and based on interviewing fourteen interviewees from different institutions related to the external audit bodies the following data were obtained. Moreover, the data acquired from the interviews were summarized and analyzed in a thematic way (Christopher, 2012) as follows:

4.1. Auditing in Egyptian public sector

Auditing is the official inspection and examination of accounts and records.

External and internal Auditing are the two types of audit that are performed in the Egyptian public sector.

There are two bodies that are in charge of external auditing:

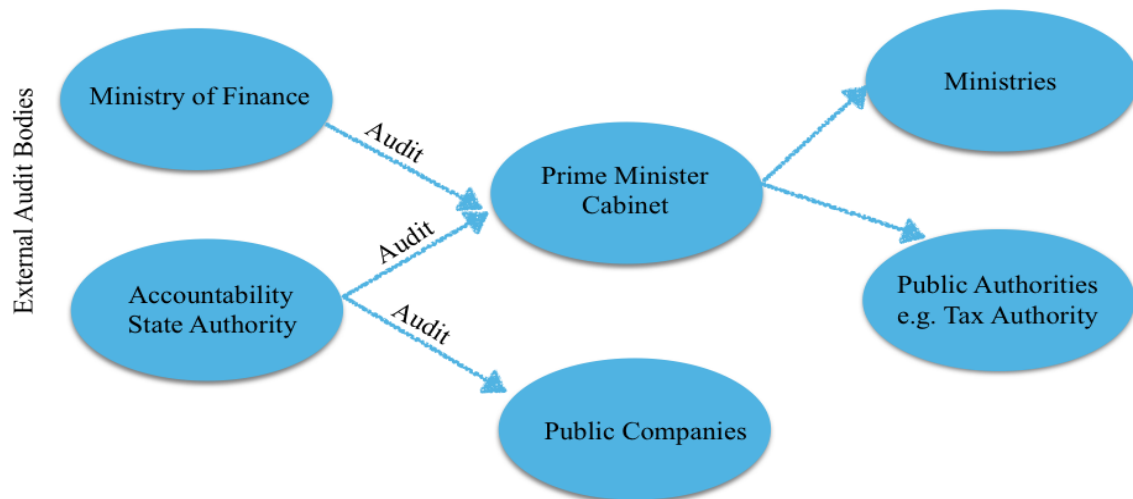
1. Accountability State Authority (ASA)
2. Ministry of Finance (MOF)

The external auditing cycle in Egypt is labelled below in [Figure 4.1].

To illustrate the diagram below, it is seen that the Ministries and the Public Authorities are audited mainly by the Accountability State Authority. Moreover, Ministry of Finance has a department which is called “Central Audit Department”. This department sends representative to each and every Ministry and Public Authority that is responsible for auditing and monitoring the financial affairs in these areas. Those Ministry of Finance’s representatives do not exist in the public business sector companies; therefore, these companies are audited by only the ASA.

Meanwhile, the external auditors of the ASA get a sample of the financial records and inspect them according to the Egyptian auditing standards, in order to issue the annual report that includes the result of the examination.

The role and the scope of these two bodies will be discussed in more detail in the following section.



[Figure 4.1] External Auditing Cycle in Egypt, Developed by the author

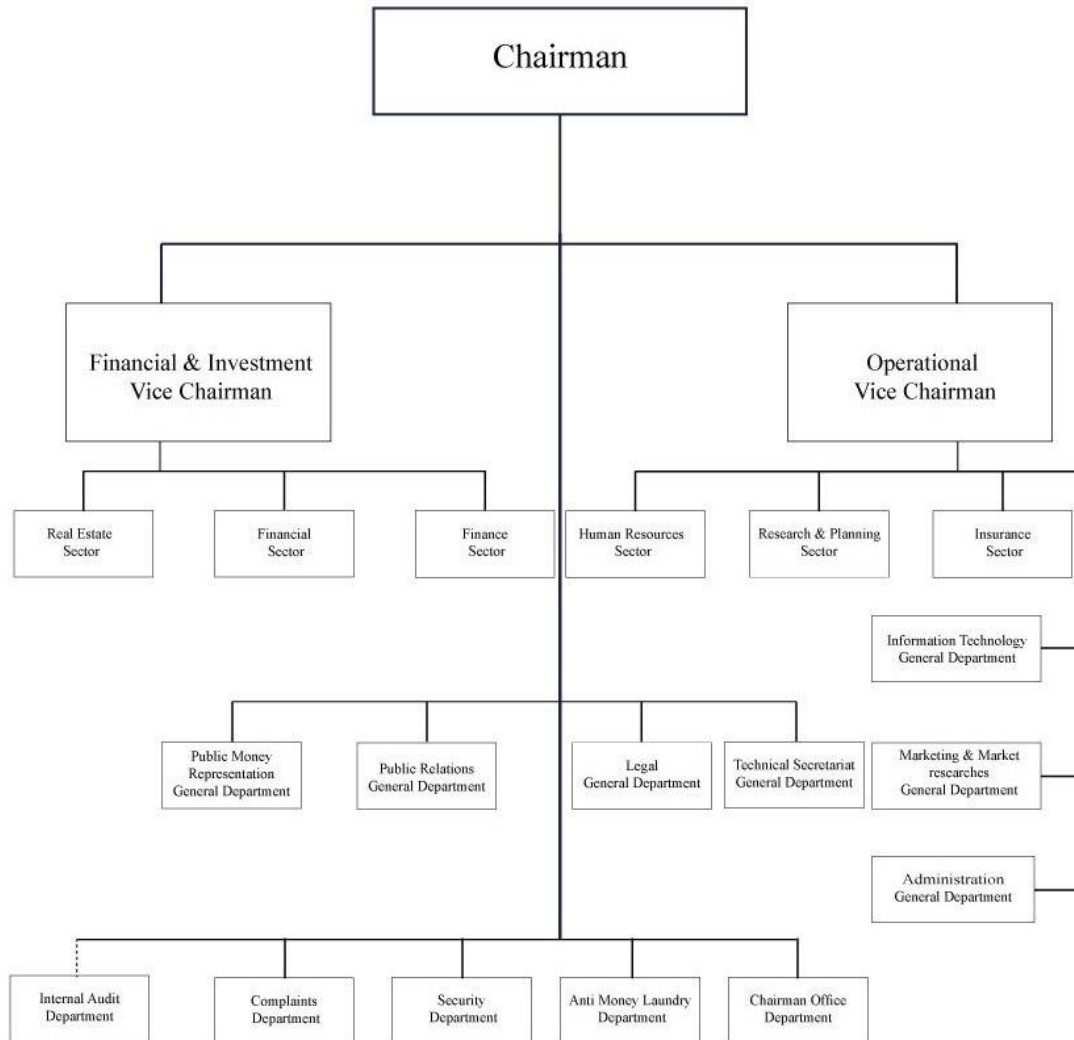
In the meantime, internal Auditing in the public sector is performed by the internal auditors within each public entity.

Internal auditing in Egypt does not have a designed workflow. The auditors do not follow internal audit standards; they only audit each financial transaction before it is actually done (pre-spending).

After conducting all the interviews, the researcher has found out that all the publicly held companies in Egypt has an internal audit department which is responsible for auditing all the financial transactions of the company.

Above and beyond, interviewing the representative of the Accountability State Authority in the Insurance sector in Egypt, it was found that all the companies have an internal audit department which reviews and audits each financial transaction in the company before it was actually done. This internal audit department offers the required assurance to the external auditors, since the external auditors cannot audit each and every transaction. These departments must be shown in the organizational structure of any company as seen in [Figure 4.2].

In [Figure 4.2] is given the organizational structure of “*Misr Insurance Company*” as an example to all the insurance companies in specific and to all the Egyptian public companies in general.



[Figure 4.2] Organizational Restructure of Misr Insurance Company, Printed from: http://misrholding.co/Pages/167/org_structure.html

Quoting the interviewee, she stated that the Egyptian insurance sector is a *clean sector*, and it has the importance of the banking sector and this is for two reasons. The first reason is that it is controlled by the Egyptian Financial Supervisory Authority.

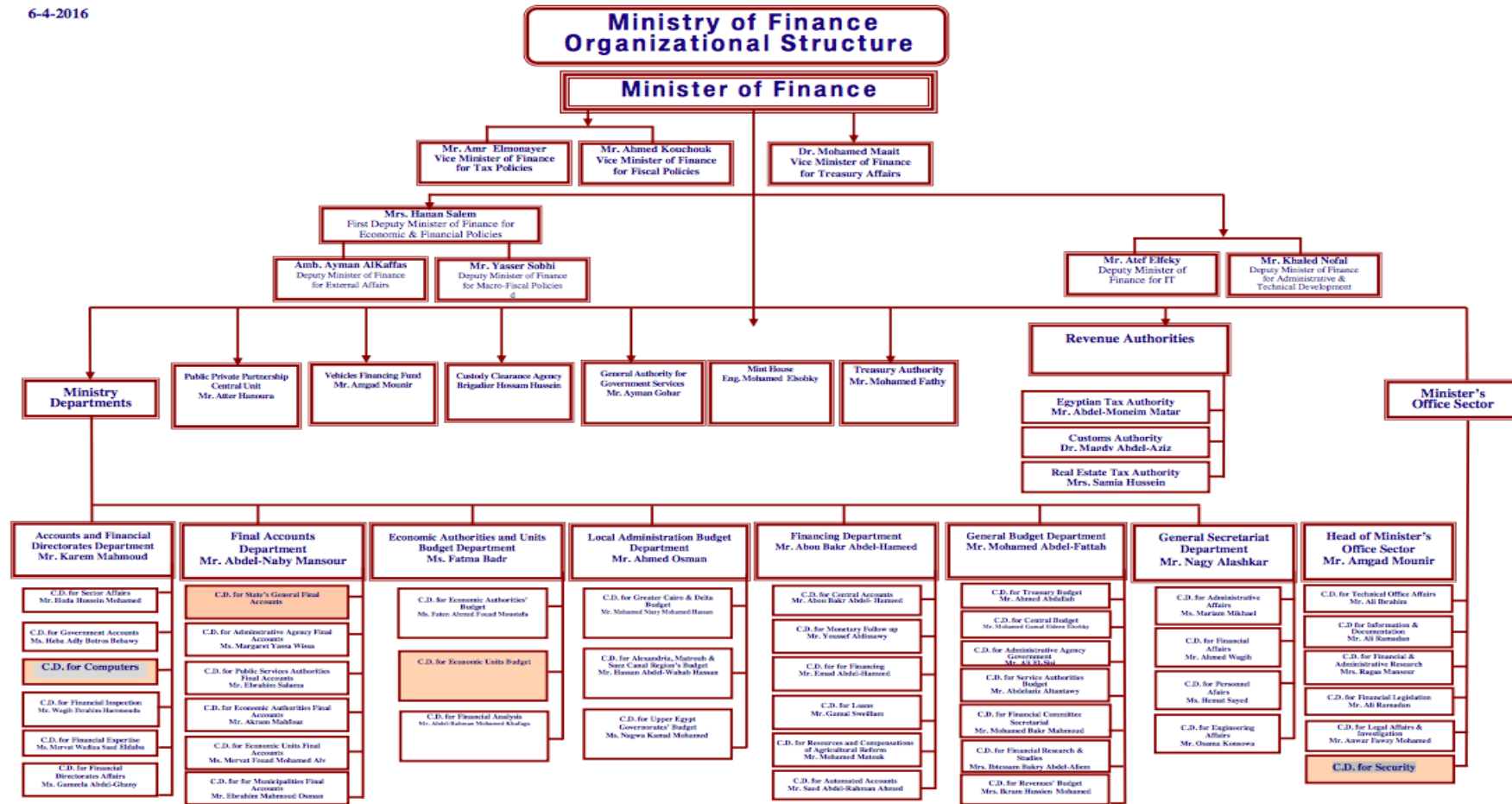
According to the interviewees, the insurance sector is not only audited by the Accountability State Authority, but also it is controlled by an external independent

body which is called *Egyptian Financial Supervisory Authority* (EFSA). The latter's role is regulating non-banking financial markets and instruments, including the Capital Market, the Exchange, and all the actions related to the Insurance services. In fact, the role of this authority is not related to the internal audit issue, conversely, it gives an indication that the presence of an external independent body offers the required regulations and assurance for the efficiency of the organizations of which it controls. The second reason is that most of the Insurance companies in Egypt are jointly owned by the public and the private sector. There are only two companies that their capital is 100% owned by the Egyptian government. These two companies are: *Misr Insurance Company* and *Misr Life Insurance Company*.

Referring to the fact that this sector is an unsoiled one, therefore, this can show the gap of efficiency between the public and the private sectors.

Talking about the governmental sector; including ministries and the public authorities, it was found that some of them have an internal audit department, others do not. Yet those entities which do not have an internal audit department have one or two internal auditors in the financial departments whose role is to audit the financial matters of that entity.

Given in [Figure 4.3], the organizational structure of the Ministry of Finance as an example of the governmental sector in Egypt. By having a deep look in this organizational structure, the researcher has found that it does not have a separate internal audit department. Nevertheless, by the extensive research inside the Ministry of Finance, the researcher has found that internal auditing in this entity is a small sector from the financial department.



[Figure 4.3] Organizational Structure of the Ministry of Finance, Printed from: <http://www.mof.gov.eg/MOFGallerySource/English/MOF-Organizational-Structure7-4-2016.pdf>

To conclude, all public companies and most of public entities have a department which is called “Internal Audit” department. But, the questions here are: What is the competency of the internal auditors who work there? What is the level of independence of internal auditors working in the internal audit departments? Do these departments meet the international standards of internal auditors? What is the level of efficiency of these departments?

Regarding the competency of internal auditors in the Egyptian public sector, it can be measured by their scholastic qualifications, skills, training and development and proper knowledge for the standards by which they are working (Christopher, 2012; Shamsuddin, 2014; Alzebban and Gwilliam, 2014).

When asking the interviewees about the qualifications of internal auditors especially the educational ones, the answers were that internal auditors may have a bachelor degree in commerce and may have only a diploma in commerce, but none of those holding diplomas hold managerial positions.

Talking about the training of these auditors and the training plan of each public organization, the interviewees mentioned that each organization has a *‘Training and Development Department’* which is responsible for training all the employees in the organization, and this department has a yearly plan for the training. However, these plans are not implemented.

Sufficient and efficient staff in the internal audit department leads to higher quality of internal audit. Moreover, unqualified staff in an internal audit department is considered an obstacle towards the success of the internal audit function and is previewed as the severest issue facing internal auditing (Ali *et al*, 2007; Alzeban and Gwilliam, 2014).

Besides, after conducting the interviews, the researcher has found that the internal auditors in the departments established in the Egyptian public sector perform the tasks that are assigned to them by their heads; however, they are not aware about the standards of internal audit function. Meanwhile, compliance with internal audit standards is one of the main factors associated to the effectiveness of the internal auditing in the public sector (Christopher, 2012; Shamsuddin, 2014; Alzebban and Gwilliam, 2014), and the Egyptian public sector lacks this factor though.

Hence, in order for the internal auditors to execute their duties and carry out their responsibilities successfully, they must be qualified, well trained, and aware by the standards of the internal audit profession.

The most important aspect that determines efficiency of internal audit function is independence. According to Shamsuddin, independence is a very crucial aspect whether to external or internal auditors in both private and public sectors. It is very important to the success of the internal audit function (2014).

By researching the Egyptian public sector in the context of internal audit mechanism, it was discovered that none of the internal auditors is independent and this may have negative consequences. Correspondingly, all these departments are dependent to the management. In other words, internal audit departments in the Egyptian public sector companies lack independence and this may have many concerns. Since the employees working in these departments are from the same company which they are auditing internally, conflict of interest may occur between management and internal auditors, which leads to a great level of biasness.

Previous studies (Bchayf, 2000; Brierley et al, 2001; Mihret and Yismaw, 2007) highlighted that lack of independence affects the internal audit department strength.

Moreover, according to Shamsuddin (2014), he stated that the internal auditor effectiveness is affected by the independence of internal auditors, and he added that if the internal auditors were not independent, they will produce a biased report which is impractical in improving transparency and accountability of the public sector as a whole.

To conclude, as long as the internal auditors are employees in the entity they audit, therefore, it will be difficult to achieve independence.

One of the common observations from the interviews is that internal auditing in the Egyptian departments are strictly limited to financial compliance audit and ignored the new definition of internal auditing which is concerned with the performance based audit as well as policies implementations and achievability of goals.

In addition, from the interviews conducted and all the data gathered, it was found that assessing the effectiveness of any internal auditing system is based on several aspects.

For one, as the extent of independence of the internal audit system is higher, the effectiveness will consequently increase. Regrettably, in Egypt there are no independent internal auditing systems.

For seconds: the qualifications of the internal auditors, the higher skills and qualifications they have got, the more successful the entity will become. In Egypt, disappointingly, most of the dependent internal auditors are under qualified.

For thirds: and most importantly, the relation between internal and external auditors, as the relations between them is better and more professional, the easier the business will be conducted and done more efficiently, but unfortunately, in Egypt the only relation the gathers the external auditors with the internal ones is the final signature of

the internal auditors on the financial document that provides assurance to the external ones.

And last: the management support, in order to conduct professional business transactions, the management of the entity to be audited should be willing to help the internal auditors by all means.

So, it is concluded that Egypt has a long run ahead of it to be able to hold a successful internal audit system.

4.2. Role of external audit bodies

4.2.1. Accountability State Authority (ASA)

Accountability State Authority (ASA) is an independent auditing body that is associated to the presidency. Its main role is to have financial control over the state and public entities as decreed by law¹.

According to the interviewees and as assured by the law of the ASA, the role of the ASA is to:

- Audit financial matters after the transaction is done and the money is spent
'Financial Control'
- Evaluate the performance of the audited companies *'Performance Control'*
- Take any legal action when there is financial violation *'Legal Control'*

"We are responsible for auditing every public entity and public individuals including the parties, unions and the elections"

¹Accountability State Authority, Act number 144 of 1988

According to the law number 144 for year 1988, subject number 3, the ASA audits the following:

- ✓ The Government (Ministries and Authorities)
- ✓ Public sector enterprises and their subsidiaries
- ✓ Companies with capital of no less than 25% owned by public sector
- ✓ Syndicates and unions
- ✓ Political parties and national newspapers
- ✓ Any organization whose laws requires it to be audited by the ASA

ASA has a department which is called “Performance evaluation department”. This department issues an annual report which includes financial indicators for the company they audit. Although this report is discussed in the General Assembly but the interviewees assured that it does not have the importance of the audit report.

4.2.2. Ministry of Finance

After investigating the ministry of finance documents and as assured by the interviewees, the ministry of finance carries out its audit in three different ways that were also mentioned in El-Kheir’s study in 1997:

- Decentralized Audit
- Centralized Audit
- Control through the central bank

The decentralized audit is done by the ministry of finance from within the audited entity. It is a pre-spending audit which is carried out by different levels of authority, whose responsibilities are determined by the ministry of finance. This process is organized by Act No. 127 for 1981. The Act states that "the ministry of finance will

appoint a financial manager in every province; he would be helped by the heads of finance in the different areas of the province. The ministry will also appoint a financial controller at every ministry and he would be also helped by the heads of the financial hierarchy in the ministry. They are all responsible for the implementation of this Act or any other relevant Acts without contradicting any regulations which might exist within the audited entity". The Act defines the different levels of authority as: The financial controllers, the financial managers and the financial agents.

Centralized audit is carried out by the central department for government accounts, the central department for treasury and the agency for budget affairs.

Control through the central bank is achieved when the central bank is in control of all the revenues and expenditures of the public entities.

Based on this information and on the interviews, it was proven that those representatives and these types of audit perform the preventive role of internal auditing.

4.2.3. Administrative Control Authority²

The Administrative Control Authority (ACA) was established in 1964 as an independent organization affiliated with the Prime Minister following Law 54/1964.

According to the interviewees and as assured by the law, the functions of the Administrative Control Authority are:

1. Researching and verifying the causes of insufficiency of business and production and suggesting the means susceptible to remedy.
2. Revealing the imperfection of administrative, technical, and financial systems

²Administrative Control Authority, Law number 54 for year 1964

which hinder the regular Functioning of public organizations.

3. Following-up the execution of laws, and ensuring that the decisions, regulation and systems applied, are sufficient for realizing the objective of their establishment.
4. Detecting the administrative and financial contravention as well as the criminal actions committed by employees during the accomplishment of their function, and taking the necessary precautionary measures to avoid such occurrences within preparation, and denouncing those already accomplished.
5. Verifying the complaints presented by citizens about contravention to law, or negligence in the accomplishment of functional duties; also the observations and suggestions made by them with the aim of amelioration the service, and regularizing the flow of business and the quick accomplishment.
6. Following-up and studying the publications of the press about complaints, and journalistic investigations revealing cases of negligence, lack of due care Abuse of power or exploitation, as well as other cases and aspects handled by the different mass media.
7. Providing the Cabinet Ministers, and to Governors, the information, data, and studies may demand, and for effecting any other supplementary work.
8. Assisting Conducting investigations on candidates for top management posts or candidates to be decorated
9. Conducting investigations on illegal gain cases.
10. Conducting investigations on suspicious financial operations that might include money laundering crimes by coordinating & exchanging information with Anti Money Laundering Unit in the Central Bank of Egypt.

In addition, its area of jurisdiction is:

- 1- State Administrative Bodies
- 2- Public Business Sector.
- 3- Public Associations & Institutions
- 4- Private Sector undertaking any public work.
- 5- Organizations to which the State contributes in any form.

4.3. Room for improvement

In the Egyptian public sector, there are many weaknesses which have had a major role in the prevalence of an ineffective audit mechanism. For one, the weak internal control on public institutions which is presented in lack of an efficacious system for periodic check on the commitment to the rule, lack of deterrent penalization system in violations and cases of irregularities and lack of control to the financial allocations of resources. For second, the weakness of administrative skills for the public sector managers which results in redundancy, indolence and laziness, providing high probability for manipulation and misstatements. As a result, improvements were vital.

So, the government worked out three reforming initiatives to broach these dilemmas. Firstly, the *National Anti-Corruption Strategy (2014-2018)*. This strategy set out a work plan for several goals. Some of these goals are highly related to and greatly concerned with the aspect of internal auditing, such as: Raising the governmental and administrative performance of the state, improving the public services and setting the ground rules for integrity and transparency. The initial step in these goals' execution procedures is to "Develop Internal Control" which in turn will enforce internal audit mechanism.

Secondly, *legal act number 122 for 2015³ for attaining financial and administrative compliance and improving the efficiency of government spending*. Although this act is concerned mainly by the financial and administrative issues, the focus on improving the internal auditing system hasn't been mentioned in its fifteen subjects.

Thirdly, as stated in 2030's vision of Egypt in the goal of Transparency and Efficiency of Governmental Institutions: *"By 2030, Egypt has a well-organized and flexible administrative system; extremely capable of maximizing the use of its assets, provides high quality aids, utilizes technological mechanisms and applies a clear and transparent governmental monitoring system that is fair and effective, contributing positively to economic growth"*. This goal will be delivered by combating corruption, increasing government savings, enhancing institutional efficiency and promoting the services providing by non-government organizations.

Although none of the mentioned above initiatives address the core of the internal audit system, they help forming minor changes that may lead to having an effective function of internal audit system.

The previously stated efforts from the government and the proposed model to have an independent internal audit body would have been effective if it wasn't for the challenges and obstacles facing the Egyptian public sector. These obstacles are represented in the following issues:

Legal Issues. This type of issues forms a great obstacle to execute the independent internal audit system in Egypt.

³The prime minister council legal act no. 122 for 2015

Because for Egypt to institute an independent body that regulates internal audit, it would require a lot of legislation and setting up a new bundle of laws.

Economic Issues. There are a lot of economic issues that would face us if we were to execute the internal audit mechanism.

For one, there is an annual deficit in Egypt's annual budget.

For seconds: Egypt is indebted to a lot of countries

For thirds: very low annual per capita income which is an indicator for the poor economic condition of Egypt.

For fourths: Misallocation of resources.

Therefore, executing the independent body of internal audit will cost a lot of money, which Egypt cannot afford in the current economy.

However, in 2013 it was discovered that Egypt suffered from tax evasion by the cost of sixty-one billion in that year from the total of 366 billion that should have been collected from tax receipts, which is equivalent to 16.7% of tax evasion (Najjar, 2014).

This dilemma proved that preventing the taxes fraud is way less costly than the actual occurrence of corruption and investigating the irregularity.

Political Issues. Egypt has been facing a lot of increasing instabilities since 2011 because of the successive revolutions, which has been hindering the process of development and evolution in Egypt.

Moreover, one of the most important political problems for the internal audit system to succeed, that it requires transparency and updated data and information, which will not be offered by some of the public institutions in Egypt.

As an example for the public institution that wouldn't offer the needed help to the internal audit system is the Ministry of Interior, as authority's abuse of its power, might contradict with the final opinion of the independent internal audit mechanism.

Administrative Issues. Administrative issues are the real obstacle because it represents the corruption in most of the administration in Egypt's public sectors, and as long as there is corruption in these institutions, there is no hope for the independent internal audit system and the reformed initiatives to succeed in Egypt. As this corruption is an indicator of all what might happen to the administration of the independent internal audit if it was to be executed.

Here is short list that shows some of the weaknesses in administrations.

For one: the immensely poor performance in Egypt's public sectors.

For seconds: in public sectors, variable salary is not based on performance, so there are no performance incentives which is a huge weakness because by giving off the incentives not based on performance, the administration is equaling between non-compatible employees.

For thirds: neither hiring nor firing the workers is based on the assessment of the employees, as hiring employees is not built on the skillfulness of the individual, and also public sectors employees are rarely fired.

For fourths: weak internal control on the employees of the public sectors by the administration and the complete absence of deterrent penalization if an employee needs to be punished.

For fifths: public sectors suffer greatly from the bureaucratic concerns and immensely complex procedures, which creates a suitable environment for the corruption of the administration to grow.

Cultural Issues. It is a fact that a nation can't change itself without itself wanting to change, and the people in Egypt don't have the urge to change in their nature, so, how are we supposed to expect that the system of independent internal audit will succeed if the prospect of change is unacceptable for us. How are we supposed to want to execute the independent mechanism of internal audit if we can't bear the thought of being bossed around?

So the main matter of the cultural issues is a matter of mind, the system of the independent internal audit won't make it if we don't destroy our inhibitions and start thinking fresh.

Chapter Five: Conclusion and Recommendations

5.1. Conclusion

This study provides evidence that shows the importance of having an independent internal audit system, in terms of enhancing governance and improving the public services. But, as the Egyptian public sector lacks the principles of internal auditing, for it was essential to try and effectively adopt the principles of the internal auditing by providing the trial to reduce the theory-practice gap between the well-known standards of internal auditing and the Egyptian situation, and by offering solutions and recommendations based on extensive researches of Egyptian internal audit department and external audit bodies sector. Results of various studies also highlight the role of internal auditing which as it has a critical role in improving the proficiency of the public sector. So, this study enhances understanding of the role nature of how internal auditing could make a difference in Egypt and of those factors underlying independent internal auditing.

Literature in this study offers descriptive information about, the definition of internal auditing, as well as the internal auditing's characteristics, it also provides a real assessing comparison between the internal audit and the internal control. It also offers detailed interpretation on the internal audit in UK as well as, internal audit in Egypt. Another benefit from the literature in this study, is to help the researcher analyze the facts about the internal audit system, and that will help get all the closer to his goal.

The main methodology that this study adopts is the qualitative methodology, where the researcher conducted fourteen in-depths semi-structured interviews, with fourteen individuals, from different institutions. The researcher also drew a comparison between the state of internal and external auditing in UK as well as in Egypt. But, in

order to make this comparison happen, he firstly wrote an overview on both, the states of internal and external audit in both UK and Egypt. Inevitably, this study has methodological limitations. It is interview-based so it's not necessarily 100% reliable and it's not uncommon to come face to face with methodological limitations. The first limitation that came up in the researcher's way is the limitation that can be introduced by the dearth of the academic writings and the empirical studies of the internal auditing in the Egyptian public sector. This lack of previous literature makes it a little bit difficult to analyze the function of internal auditing in the Egyptian public sector, and last and most important limitation is the difficulty of access to the public holding companies. This made it difficult for the researcher to get a representative sample from these companies.

Based on the conducted interviews and analysis, it was discovered that all the companies in Egypt have a dependent internal audit department, where the departments are under qualified, because, first, they lack the independence that is the key element of the effectiveness of internal auditing, also, the departments lack the proper qualifications of its employees, and the role of the internal auditors is strictly limited to financial audit and compliance with laws, where in the meantime, the modern definition of internal auditing sheds the spotlight on the performance based audit as well as it sheds the spotlight also on the financial audit, all while regarding the government's policies implementations and acquiring their objectives. As a result of the vitality of executing the independence of internal audit in Egypt, the government came up with three reformed initiatives to apply the independent internal audit system. However, these three reformed initiatives would have been applicable if it wasn't for the common obstacles that came up the researcher's way, from these obstacles, are the legal issues where this type of issues forms hinders the process of

execution of the independent internal audit system in Egypt as it would require a lot of legislation. The second type of obstacles that faced the researcher is the political issues, where Egypt has been facing a lot of increasing instabilities since 2011 because of the successive revolutions, which has been hindering the development and evolution in Egypt. The third type of obstacles is the economic issues there are a lot of economic issues that would face Egypt if it was to execute the internal audit mechanism. For one, there is an annual deficit in Egypt's annual budget. For seconds: Egypt is indebted to a lot of countries. The fourth type of obstacles is the administrative limitations where, the immensely poor performance in Egypt's public sectors shows the weaknesses in the administrations of the Egyptian public sectors. And last and most important type of obstacles the faced the researcher in his studies is the cultural issues where, it was found that The Egyptian culture also can be considered from the limitation of this study.

As it is being concluded by this and other studies, Egypt has no any successful independent internal auditing system, and will not have any successful internal audit system, unless, the administration methodology is changed radically, once most of the focal issues have been resolved, Egypt will be able to hold a successful independent internal audit system.

5.2. Recommendations

In order to design a plan for enhancing the internal audit system in the Egyptian public sector, this research identified the real causes of the prevalence of an ineffective one.

This study indicates that Egypt have an internal audit system in most of all its public sector entities, but evidently this system suffers inefficiency and inconsistency in

some of its factors. This is primarily due to the non-existence of an independent professional internal audit body that is concerned with the interests of the Egyptian internal audit function (El-Kheir, 1997).

From the extensive research in the public sector institutions it was found that not all of these institutions has a separate internal audit department. Therefore, it was proven important to have a separate one in each public entity. As illustrated by El-Keir, the existence of an internal audit department is not an aim in itself, but it will eventually help in enhancing the internal audit function (1997). This can be done by:

- Having organizational restructure, in order to establish a new internal audit department without having it to be costly by recruiting more staff.
- Setting up policies and rules that plainly states the importance and the responsibilities of internal audit departments in the public sector as a whole.

Meanwhile, as assured by the interviewees, the internal audit work in Egypt does not have a structured workflow, and the internal auditors are not aware by the standards of internal audit. Moreover, their role is strictly limited to the financial audit. Thus, it is highly recommended to:

- Have a clearly stated guidelines that organize the work of internal auditors.
- Widen the perception of internal auditing to have the modern definition and role of internal auditing within its scope
- Offer the required transparency in order for the internal auditors to obtain all the needed information to perform the new context of internal auditing.

Besides, it is apparent from the results of the interviews that internal audit departments in Egypt have underqualified internal auditors in terms of training and educational skills, therefore, it is recommended to:

- Allocate more budget for the *Training and Development Department*, in order to implement its yearly plan that helps in increasing the technical and educational skills of the internal auditors working in these departments.
- Avail an opportunity for internal auditors to be trainees under the observation of private audit firms.
- Offer regular training programs that cover all the aspects of the modern internal auditing system to the internal audit department staff.
- Develop the salaries system, in order to attract more qualified staff to work for them.

As it was proven many times in many studies, Egypt lack the independence of internal audit system, this independence is the main key to having a successful internal audit body, so as to lessen the severity of the independence problem it was recommended to execute a successful independent internal audit system, but that was proven inconvenient because of the previously mentioned obstacles that Egypt might face, but fortunately there are some other ways, that may help with the case:

- We might solve the issue of independent internal auditing by handling the authority of executing an independent body to the private sector, which is a newborn concept in Egypt and a well-respected solution, which also hasn't been yet applied in Egypt, although it has been running in other countries for years and has proven its efficiency. This private sector will be hired by the public sector to hold the responsibility and the efficiency of internal audit in

Egypt, and will also be responsible for the out-sourcing of every single internal auditor to every entity under the public sector's command.

- If hiring the private sector to execute an independent internal auditing body is proven to be inefficient, luckily there is another respective solution. Setting up an independent department in the external audit bodies that are responsible for external public audit, the role of this independent department will be to review the functions and activities of public sector organizations, and also this department will make recommendations for improvement and add value to public sector. Another important thing that this independent body will be responsible for, is the assigning of internal auditors to review all governmental organizations.

Finally, if Egypt was to apply all the previously mentioned recommendations, this will lead to a more motivated staff who will perform the audit in its wider scope.

Accordingly, the internal audit function in the Egyptian public sector will be enhanced to a level that is vitally needed to combat corruption, increase public savings, enhance institutional efficiency and promote public services.

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Appendices

Appendix 1: Interview Guide:

In countries that have a solid internal audit system there are two complementary separate bodies: External audit bodies and internal audit bodies. The latter works as a preventive body for the frauds and violations and the external audit bodies complements the work of the internal auditing in terms of assurance that maintaining control.

Contemporary Practice: Adoption of Internal Auditing

- If you were to use an illustrative diagram, how would you describe or draw the ‘auditing cycle’ concerning the public sector in Egypt?
- Does Egypt have an Internal and an External audit system?
- If Egypt only has external auditing institutions, is there an independent body with an intermediary role facilitating the work flow between external auditors and public sector institutions?
- Does the existing auditing system in Egypt meet international best practices? Which ones are the most ensured?

Policy-oriented Research

- Do the “Administrative control authority” (ACA) and “Accountability state authority” have a department that can potentially fulfil the role of internal auditing?
- Does the “Administrative control authority” only intervene when there is a potential problem/complaint pointing to certain violations? What are the exact steps preceding the interference of the ACA? Does the ACA have periodical patrols that can detect a problem before it really happens?

- How the preventive role of internal auditing is fulfilled in Egypt, if at all?

Prospects

- Does ACA have any plans for institutional reform to empower the idea of preventive auditing? If yes, what are the main highlights of this plan and when is it going to be ratified?
- Several countries use internal audit bodies from the private sector in order to ensure the independent/unbiased auditing mechanism. Do you think this can be considered in Egypt?
- What are the obstacles preventing the development of a structured and efficient internal auditing mechanism in Egypt?
- Do you have any personal recommendations or ideas on how to develop a structured internal audit system in Egypt?

Appendix 2: The IRB Approval

CASE #2015-2016-146



To: Samar El-Tahan
Cc: Mariez Wasfi
From: Atta Gebril, Chair of the IRB
Date: April 20, 2016
Re: Approval of study

This is to inform you that I reviewed your research proposal entitled "Adoption of internal auditing" and determined that it required consultation with the IRB under the "expedited" heading. The proposal used appropriate procedures to minimize risks to human subjects and that adequate provision was made for confidentiality and data anonymity of participants in any published record. I believe you will also make adequate provision for obtaining informed consent of the participants.

This approval letter was issued under the assumption that you have not started data collection for your research project. Any data collected before receiving this letter could not be used since this is a violation of the IRB policy.

Please note that IRB approval does not automatically ensure approval by CAPMAS, an Egyptian government agency responsible for approving some types of off-campus research. CAPMAS issues are handled at AUC by the office of the University Counsellor, Dr. Amr Salama. The IRB is not in a position to offer any opinion on CAPMAS issues, and takes no responsibility for obtaining CAPMAS approval.

This approval is valid for only one year. In case you have not finished data collection within a year, you need to apply for an extension.

Thank you and good luck.

A handwritten signature in black ink that reads "Atta Gebril".

Dr. Atta Gebril
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