



A Strategy for Developing an Internal Audit Charter: A Case of State-owned Enterprise in Indonesia

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Abstract

We employ institutional theory to examine the types of isomorphism experienced by the internal audit function (IAF) of an SOE in Indonesia and how the SOE responds to gain legitimacy from its stakeholders. We also examine what strategies and tactics the SOE uses in response to the pressures. The study finds coercive isomorphism arises from five government institutions and four professional bodies. Normative isomorphism arises from the stem change from professional and sustainable education, and mimetic isomorphism arises from complex working experience, including how to develop a proper internal control system, as well as how to implement the ICoFR. The study finds that the IAF uses different strategies and tactics across those isomorphisms. The study contributes to the domain of internal auditing by developing an audit charter. It confirms the validity of institutional theory as a lens to identify the source of pressures and how they are responded to. The study also has potential implications in practice for policymakers and professional bodies in IAF.

Keywords: Internal audit, time budget pressure, moral reasoning, integrity, objectivity

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1. Introduction

The internal audit function (IAF) plays an important role in maintaining internal control and delivering efficiency and the quality of work done. The firms with a weaker IAF are susceptible to financial consequences, as evidenced by corporate collapses such as the WorldCom scandal, which IAF highlighted the improper recording of large profits from 1999 to 2002 (Arena and Azzone, 2007, p.92). The scandal led to increasing public demand for better corporate governance (Burnaby et al., 2009, p. 837). According to Boulton (2022, p. 42), IAF needs to reform to resolve companies' failures that typically occur in one of three areas: fraud, resilience, or internal control.

According to Humphrey and Moizer (1990, p. 219), internal audit is a socially constructed function, a contextually dependent phenomenon, serving a variety of roles and functions that consist of values and beliefs in which it operates. Legitimation of the internal audit units is affected by its values and beliefs that are reflected in the audit charter that defines the purpose, authority, and responsibility of the function (Vinten, 1999). In developing an audit charter, the IAF may experience various pressures from internal and external entities. Therefore, there is a need to study how the internal audit charter was developed and what pressures may influence the process.

State-owned enterprises (SOEs) in Indonesia experienced many cases of corruption, fraud, and inefficiency for a long time. Although the government has issued some regulations to improve the role of internal audits, corruption and fraud still occur (Wibisana, A.W., 2023). According to Christensen (2022, p.12), the IAF has a significant impact on internal controls and delivers work at a high quality, in which the audit charter will facilitate the effectiveness of the IAF (Vinten, 1999; Archambeault et al., 2008).

The study investigates how the audit charter of a SOE (State Owned Enterprise) in Indonesia is developed. It uses the institutional theory of DiMaggio and Powell (1983) as a lens to identify the source of pressure of three isomorphisms: coercive, normative, and mimetic. The study also uses Oliver's (1991) strategic responses to identify how and what strategies and tactics the IAF uses to respond to the isomorphism. The finding indicated that various internal and external entities create isomorphism, and it was also found that the IAF uses different strategies and tactics to respond across the three types of isomorphism.

The rest of the paper is organised as follows. Section two presents a background and research questions used by the study. Section three comprises the research method used by the study, and section four describes a review of the literature on internal audit charters. Section five contains a discussion of organisational theory on isomorphism as well as the possible strategy and tactics used to respond. Section six provides a discussion about the case of the IAF under study and its existing audit charter. Section seven provides data analysis and discussion. Section eight presents the findings and contributions of the study, and finally, it concludes the study.

2. Background and research questions

The internal audit function (IAF) plays an important role in organisations by adding value and improving their efforts to achieve set objectives through a systematic and disciplined approach to control and evaluate operations. However, with corporate governance and accounting scandals in the US and UK in recent years, the effectiveness of the audit functions has been questioned (Allegrini et al., 2009; Schneider, 2003). Christensen (2022) undertook a single case study of the Internal Audit Function (IAF) of a large Danish financial institution that is under EU regulation. The study explored the impact of IAF on Internal Control, and it found that internal audit functions *...have a significant impact on internal controls and deliver work at a high quality* (Christensen, 2022, p.12). Similarly, Boulton (2022, p.42) mentioned the

recent corporate failures “...failings typically occur in one of three areas: fraud, resilience, or internal control”.

The effectiveness of IAF in Indonesian SOEs has come under scrutiny due to an ever-increasing number of corruption and fraud cases. Prior studies (Diansyah et al., 2012; Umar, 2011; Wicaksono, 2009) identified that ineffective internal audit functions have contributed to the increase in fraud and corruption in government institutions as well as in SOEs. During the years 2001-2004, over 6,000 suspected corruption cases were reported by BPK (the Supreme Financial Audit of the Indonesian Government), and more than 700 cases involving corruption were reported by BPKP (the Financial and Development Supervisory Agency, which is a government internal audit department). In addition, many Chief Executive Officers (CEOs) of the SOEs were convicted by KPK (the Corruption Eradication Commission) on corruption scandals (Umar, 2011).

Accordingly, in 2011, the government issued Regulation No. PER-01/MBU/2011 requires the SOEs to improve the effectiveness of the internal audit functions. Although various regulations have been issued, corruption within the SOEs is still rampant. Wibisana A.W. (2023, pp.31-32) describes various recent corruptions and frauds that occurred in SOEs in Indonesia, such as PT Istaka Karya (Persero), PT Merpati Nusantara Airlines (Persero), PT Industri Sandang Nusantara (Persero), PT Iglas (Persero), and PT Kertas Kraft Aceh (Persero). Some cases are mega corruptions, such as PT Garuda Indonesia (Persero), PT. ASABRI (Persero), and PT. Jiwasraya (Persero) as well as PT Asabri (Persero). In addition, the corruption perception index in 2022 showed an unimpressive figure of 110/180 (Transparency, 2023). Ojha (2012, p. 3) suggested the changing role of IAF by saying,

As organisations work towards reducing the losses due to fraud, their anti-fraud programmes are increasingly looking towards the internal audit function for support in light of the fact that, over time, as internal auditors review systems in the organisation, they develop an overall knowledge of the organisation's processes, risks, control systems and personnel which can contribute to an effective fraud risk management.

Subsequently, the IAF has lost its credibility and should be able to gain legitimacy from its stakeholders (Power, 2003). The IAF must have the authority to conduct its job effectively, and it should be stated in a document called the audit charter, which is described by McKinley (2013):

...the charter is a formal document outlining the function's purpose, authority, and responsibility. It establishes the internal audit department's position within the organisation and provides a formal, written agreement with management and the board about the department, should any questions arise.

The charter will gain the IAF's legitimacy in its existence. However, there is no prior study investigating the practice of how the internal audit charter is designed by the IAF of SOEs in Indonesia. The SOEs have two types of shareholders, government and private, which makes their institutional environment complex in terms of the requirements of their stakeholders. Consequently, the IAF may experience great pressure in creating its audit charter to accommodate the stakeholders' needs. The study attempts to identify the detailed experiences of the IAF of an SOE to create its audit charter in three research questions: First, what are the sources and kinds of pressures that are experienced by the IAF when creating the audit charter? Secondly, how does the IAF attempt to gain legitimacy from its stakeholders? Thirdly, what kind of strategies and tactics are used by the IAF to deal with the pressures to gain its legitimacy?

3. Research method

Qualitative investigation is used by this study on a case study research design to gain a deep understanding of the response of the internal audit unit in a public SOE toward institutional pressures. This design is chosen because it allows the researcher to obtain a comprehensive and meaningful picture of phenomena found in real-life events such as organisational and managerial processes, daily-life activities, and a community's social system (Yin, 2014). According to Yin (2014), a case study approach is an appropriate strategy when the research meets three conditions. Firstly, the form of the research question consists of 'how' or 'why' questions. Secondly, the researcher is not required to control the behavioural events. Thirdly, the research focuses on contemporary events. Based on these arguments, a case study design is an appropriate research strategy for this research. Data collection was done by visiting the company over three months to undertake interviews, observation, and documentation of archival documents.

The study investigates the pressure from the stakeholders of the SOE, which may include government units and professional bodies. The source of pressure from the government units arises from the laws and regulations that are issued by relevant government units such as Bapepam-LK (Capital Market Regulator), Ministry of SOE, BPK, BPKP, and IDX (Indonesia Stock Exchange). The pressure from professional bodies may arise from the demand on auditors to qualify in technical and professional skills. The relevant professional bodies used by the study are the IIA/SPAI (Institute of Internal Auditors/Professional Standards of Internal Audit), SOX 2002 (Sarbanes-Oxley Act 2002), COSO (Committee of Sponsoring Organisations), and International Organisation for Standardisation (ISO 26000).

The company's audit charter, SOPs, and evaluation report are important sources used by the study to see the reflection on IAF's response to the pressure. Interviews with the key informants in the company and observation results are used to interpret the practice and to indicate the strategies and tactics used by the unit in response to the isomorphism. The data collected either from documentation or interviews was converted into written text, including the translation process from Indonesian to English. The written interview data were then coded into themes and sub-themes concerning the research question. The study executes two levels of examination on how and what actions are taken by the unit in response to the pressures. Firstly, it uses content analysis on documents and traces them to the audit charter to identify its responses on three isomorphisms of institutional theory of DiMaggio and Powell (1983). Secondly, the study takes three months of fieldwork at the site to collect relevant documents and conduct interviews and observations to explore how the items of the charter are practised. From the interviews, observation, and documentation, the study identifies the strategies and tactics of Oliver (1991) that are used by the IAF in response to the isomorphisms.

4. Internal Audit and Audit Charter

According to IIA (2023), internal auditing is:

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

The definition indicates that IAF has important roles for the organisation. According to Humphrey and Moizer (1990, p. 219), internal audit functions were *socially constructed, contextually dependent phenomena, capable of serving a variety of roles and functions*. Whittington and Pany (2008) also indicated that the socially constructed IAF has occurred to meet the needs of business, governmental, and non-profit organisations. This argument is strengthened by Flint (1988, p.14), who declares that:

...audit is a social phenomenon. It has no purpose or value except in its practical usefulness. It is wholly utilitarian. The function has evolved in response to a perceived need of individuals or groups in society who seek information or reassurance about the conduct or performance of others in which they have an acknowledged or legitimate interest.

Historically, the role of the IAF has evolved from time to time. For example, a public swindling scandal by Ivar Kreuger in 1932 drove the Securities and Exchange Commission (SEC) in the US to issue the Securities Act in 1933 and 1934 that required listed companies to provide audited financial statements. It encourages public companies to strengthen their internal control, which is generally part of the IAF (Whittington and Pany, 2008). Since then, the role of IAF has been perceived as a shadow of independent auditing (Gupta and Ray, 1992) as defined by the IIA:

...an independent appraisal activity within an organisation for the review of accounting, financial, and other operations as a basic service to management. It is a managerial control, which functions by measuring and evaluating the effectiveness of other controls (Mousa, 2005, p.40)

Many failures of IAF in many countries (Verschoor, 1991) and increasing business and audit failures in the 1980s led to the establishment of a commission called the National Commission on Fraudulent Financial Reporting (Treadway Commission). The Commission considers the investor to have the right to know the responsibilities of management on the financial statements and internal control of the company. Therefore, in 1987, the Commission recommended (Treadway et al., 1987, p. 11) that top management of public companies must *maintain internal controls that provide reasonable assurance that fraudulent financial reporting will be prevented or subject to early detection*. Treadway et al. (1987, p.37) mentioned that,

...public companies should maintain an effective internal audit function staffed with an adequate number of qualified personnel appropriate to the size and the nature of the company ... The internal audit function ... is an important element in preventing and detecting fraudulent financial reporting.

The criteria of effectiveness and objectivity of IAF are elaborated as follows:

...the internal auditor's qualifications, staff, status within the company, reporting lines, and relationship with the audit committee of the board of directors must be adequate to ensure the internal audit function's effectiveness and objectivity. The internal auditor should consider his audit findings in the context of the company's financial statements and should, to the extent appropriate, coordinate his activities with the activities of the independent public accountant (Treadway et al., 1987, p.11-12).

In 1992, COSO established a Framework as a system to create integrated internal control into the business process. The framework focused the internal control report on the control environment, risk assessment, control activities, information and communication, and monitoring. Another trigger for IAF to develop was during the collapse of several corporations, such as Enron Corporation and MCI Inc. (formerly WorldCom), which was primarily due to accounting fraud that demolished public confidence. The scandal indicated the weakness of the IAF in having control mechanisms to detect fraud or misuse of corporate assets (Arena and Azzone, 2007). The scandal led to increasing public demand for better corporate governance,

which ultimately affected the development of IAF within the organisation (Burnaby *et al.*, 2009).

In line with the recommendation of the Treadway Commission (1987) to strengthen the internal control of public companies, investors should have certain statements to ensure that their investment is in the safe hands of IAF. The statement on the role and function of the IAF is facilitated by the Internal Audit Charter as described by the Audit Committee of PwC (2023),

The internal audit charter provides the functional and organisational framework within which internal audit operates. This document sets out the nature, role, status, authority, and responsibility of the internal audit.

Accordingly, to gain legitimacy, the IAF needs to be aware of the demands of stakeholders on the role of the IAF. The information on the role of the IAF should be available in the audit charter. Flint (1988) indicated that the operations of the IAF are affected by diverse aspects of its institutional environments. Considering the complex institutional environment faced by an IAF, this study uses institutional theory to investigate the case. The institutional theory describes the pressure from the institutional environment, which is called isomorphism. This study investigates the source of the isomorphism that influences the IAF in developing its audit charter.

The IIA (2013, p. 42) described the internal audit charter as,
...a formal document that defines the internal audit activity's purpose, authority, and responsibility. The internal audit charter establishes the internal audit activity's position within the organisation; authorises access to records, personnel, and physical properties relevant to the performance of engagements; and defines the scope of internal audit activities.

The IIA Position Paper, January 2019, stated the condition of a design charter as,

For an internal audit to operate at the highest levels, it must have clearly defined and articulated marching orders from the governing body and management. This is most easily achieved with a well-designed internal audit charter.

PwC (2003) also indicates the importance of the charter by stating:

An internal audit charter sets out the roles, responsibilities, authority, and reporting requirements of the internal audit function. The charter will vary from company to company.

The audit charter is an essential foundation to achieve its objectives as well as a basis for external stakeholders to evaluate the effectiveness of the internal audit function (Vinten, 1999). Since the Audit Charter is an important element in guiding the internal audit function effectively, it should be regularly reviewed by the audit committee and approved by top management before implementation (ECIIA, 2005; Vinten, 1999).

There are some studies on the practice of the audit charter (Burnaby *et al.*, 1994; Allegrini *et al.*, 2006; and Al-Twaijry *et al.*, 2003). Burnaby *et al.* (1994) conducted a study on eleven countries on the use of the charter in practice. They found that 39 out of 123 companies that participated in the study did not have a formal charter. They also found that Japan and the UK placed little importance on the charter in practice. Allegrini *et al.* (2006) undertook a study in France and Belgium. The survey in France was sent to 508 chief internal auditors (CAEs), with a response rate of 37 per cent, and in Belgium to 260 private companies with a response rate of 30 per cent. The survey in France found that *a large majority (82 per cent) of the internal audit departments have an internal audit charter, formally approved by top management and the audit committee* (Allegrini *et al.* 2006, p 846). The study in Belgium found that *...internal audit charter is used in more than 90 per cent of the cases* (Allegrini *et al.* 2006, p 848). Al-

Twaijry *et al.* (2003) conducted a study in Saudi Arabia and found that the IIA did not have a strong influence on the role of the internal audit function.

Mihret *et al.* (2012) conducted a study in Ethiopia on three forms of institutions: state-owned enterprises, government ministries, and private companies. Since 1992, the government of Ethiopia has required all state-owned enterprises to establish internal audit departments and specify the roles of internal audit, its authority, responsibilities, as well as its relationship with the board of directors. Mihret *et al.* (2012, p.159) found that all units operating under the government used a uniform internal audit manual, which is similar to the audit charter of the Ministry of Finance and Economic Development. In private companies, the Commercial Code of Ethiopia only required the formation of an internal audit unit limited to the Banking and Insurance industries. Mihret *et al.* (2012) used two companies and found that the audit charter was at the stage of drafting and had not yet been implemented.

The internal audit charter becomes more important and is in line with the developments of the IAF. It is indicated that some studies have found some changes in the appraisal function of IAF to be more related to the consulting function (Mihret *et al.*, 2010; Yee *et al.*, 2008; Mihret and Woldeyohannis, 2008; Hass *et al.*, 2006; Zain, 2005; Ahlawat and Lowe, 2004). The changes brought effects on the quality of the internal audit function, including the changes in the services of internal auditing (Anderson, 2003; Nagy and Cenker, 2002), the scope of work (Cohen *et al.*, 2004; Gramling *et al.*, 2004); the level of competence requirements (Arena and Azzone, 2009; Sarens, 2009; Hass *et al.*, 2006), and the approach to conducting the audit (Hass *et al.*, 2006). In addition, there are deliberations about the reliability and independence of the internal audit function as well as the objectivity of the auditor in conducting the work (Christopher *et al.*, 2009; Brody and Lowe, 2000). These changes put the audit charter as an important document to ensure the quality of the internal audit function is in place and supported by the IIA. It is mentioned that,

... without legal requirements to adhere to IIA Standards, the need for formalisation through a charter of the internal audit department's responsibilities is not determined to be important (Burnaby *et al.*, 1994, p. 253).

Some authors specified that the alteration of the practice of IAF was constructed by the regulations and professional bodies (Burnaby *et al.*, 2009; Cohen *et al.*, 2008; Allegrini *et al.*, 2006; Cooper *et al.*, 2006; Hass *et al.*, 2006; Stewart and Kent, 2006; Cohen *et al.*, 2004; and Vanasco *et al.*, 1995). Those studies indicate that the IAF should change and respond to the requirement of institutional pressure in which it operates. Therefore, this study investigates how the internal audit unit of an SOE in Indonesia responds to its institutional pressure to be legitimate.

5. Isomorphism and response

The transparency of the IAF unit is demanded by its stakeholders and will lead to legitimacy. The BAPPEPAM-LK (Indonesian Securities and Investment Commission) required the IAF to be transparent by issuing a regulation number Kep-643/BL/2012. Clause number 2 of the regulation states that every company listed in the Indonesian Stock Market must have an internal audit charter. The charter will define its existence, purpose, authority, and responsibility so it can be seen and assessed by its stakeholders and lead to legitimacy. The regulation can be seen as an effort to impose an organisation to practice in the same way or quality, which is considered as uniformity of practice across the field of IAF. DiMaggio and Powell (1983) considered this situation as institutional isomorphism. Institutional theory has been considered a useful lens to investigate the responses of an organisation to its environmental demand to be legitimate (DiMaggio and Powell, 1983; Meyer and Rowan, 1977; Meyer and Scott, 1983; Zucker, 1988). DiMaggio and Powell (1983, p. 149) defined isomorphism as

...a constraining process that forces one unit in the population to resemble other units that face the same set of environmental conditions.

DiMaggio and Powell (1983) developed a framework of isomorphism that takes three forms: Coercive, Mimetic, and Normative. *Coercive* isomorphism occurs when organisations seek legitimacy from regulatory pressure or other expectations that may come formally or informally (DiMaggio and Powell, 1983). The formal source of pressure stems from legal sources, which may include government mandates, laws, legitimised rules and structures, and Standard Operating Procedures (SOPs). Informal pressure may come from outside organisations that the institution relies upon administratively and culturally (DiMaggio and Powell, 1983).

The *Mimetic* isomorphism arises from uncertainty that led to the institution's attempts to overcome uncertainty by imitating practices of successful organisations (DiMaggio and Powell, 1983). The *Normative* isomorphism is based on the premise that changes in organisational structures and practices take place through the process of professionalism (DiMaggio and Powell, 1983). This process occurs through formal education and research-based products from authoritative experts, professional networks that share science and technology (DiMaggio and Powell, 1983), as well as professional standards (DiMaggio and Powell, 1991).

The response of the IAF to the pressure may differ strategically. Oliver (1991) divides responses toward institutional pressures into five strategies: *Acquiescence*, *Compromise*, *Avoidance*, *Defiance*, and *Manipulation*. Each strategy has several different tactics. *Acquiescence* strategy means compliance with institutional pressures using three kinds of tactics: *Comply*, *Imitation*, and *Habit*. *Comply* tactics means obeying regulations and rules consciously, whilst *Imitation* means copying successful institutional models, and *Habit* means unconsciously following invisible, taken-for-granted norms. *Compromise* is a strategic response that is undertaken when there is a conflict between internal and external institutional pressures concerning efficiency. This response may be performed in three different tactics: *Balance*, *Pacify*, and *Bargain*. The *Balance* tactic is used to balance the expectations of multiple constituents. The *Pacify* tactic is used to please and accommodate a variety of institutional elements. The *Bargain* tactic is used to negotiate with the institutional stakeholders (Oliver, 1991).

Avoidance strategy is related to ...the organisational attempt to preclude the necessity of conformity (Oliver, 1991, p.154). This strategy consists of three means: *Conceal*, *Buffer*, and *Escape* tactics. Oliver (1991, p.154) defined the *conceal tactic* as

...involve disguising nonconformity behind a façade of acquiescence. An organisation, for example, may establish elaborate rational plans and procedures in response to institutional requirements in order to disguise the fact that it does not intend to implement them.

(Oliver, 1991, p.155) mentioned that the *Buffering* tactic refers to, ...attempt to reduce the extent to which it is externally inspected, scrutinised, or evaluated by partially detaching or decoupling its technical activities from external contacts.

Moreover, Oliver (1991, p. 155) described the *Escape* tactic as, ...an organisation may exit the domain within which pressure is exerted...or significantly alter its own goals, activities, or domain to avoid the necessity of conformity altogether.

The *Defiance* strategy is related to ...a more reactive resistance to institutional processes (Oliver, 1991, p.156). This strategy comprises three forms of tactics: *Dismiss*, *Challenge*, and

Attack. The *Dismiss* tactic is characterised by ...*ignoring institutional rules and values* (Oliver, 1991, p.156). The *Challenge* is described as ...*offensive in defiance of these pressures and may indeed make a virtue of their insurrection* (Oliver, 1991, p. 156). The *Attack* is indicated by ...*the intensity and aggressiveness of the organisation's active departure from institutional pressures and expectations*" (Oliver, 1991, p.156).

The *Manipulation* strategy refers to the way organisations redefine the organisational reality perceived by others. Oliver (1991, p. 157) contends that manipulation is used to, ...actively change or exert power over the content of the expectations themselves or the sources that seek to express or enforce them.

Manipulation strategy covers three tactics: *Co-opt*, *Influence*, and *Control* (Oliver, 1991). *Co-opt* tactic could be conducted by someone who decides to, ...persuade an institutional constituent to join the organisation or its board of *directors* to neutralise institutional opposition and enhance legitimacy (Oliver, 1991, p.157).

Oliver (1991, p. 158) described the *Influence* tactic as, ...more generally directed toward institutionalised values and beliefs or definitions and criteria of acceptable practices or performance.

In addition, Oliver (1991, p. 158) said that the *Control* tactic refers to, ...specific efforts to establish power and dominance over the external constituents that are applying pressure on the organisation.

This study uses the contents of the audit charter to investigate its responses to isomorphism and the use of the strategies and tactics developed by Oliver (1991).

6. The Case and its audit charter.

The study was done on the internal audit unit of a state-owned enterprise (SOE) in Indonesia. The company was established in 1953, and at this stage, it is listed in the IDX with 51% owned by the government and 49% by the private sector. The SOE was naturalised after the independence of Indonesia in 1945, after which the company's IAF experienced many changes.

The internal audit unit was established at the end of 1960. However, in 1967, the Indonesian government collaborated with the Inter-Governmental Group in Indonesia (IGGI) as a financing institution, which required the improvement of the IAF of SOEs. In response, the government of Indonesia differentiated the SOEs into three types: Bureau enterprise (Perdjan), Public enterprise (Perum), and Public Company (Persero). The Perdjan and Perum were the government's enterprises as an extension of the government's hand to provide services to its citizens, while Persero was a company that is a for-profit operation in which the SOE understudy is one of them. The operation of SOE is under the control of the Ministry of Finance. In the early 1980s, the name of the auditing unit was changed to the Internal Supervisory Unit (SPI). The change also changed its position to be under the CEO instead of under the commercial unit. In 1983, the government failed to improve the SOEs' performance as the management was unprofessional and non-transparent, as indicated by corruption, collusion, and nepotism, which led to financial losses. In 1991, the government undertook a privatisation programme by selling some of the SOEs' shares to the public.

In 1997, the Asian crisis hit Indonesia, which ended up following the request of the IMF to extensively liberalise the economy. In 1998, the government established the Ministry of SOE and took the authorities from the Ministry of Finance to oversee the SOEs. In 2003, the Ministry of SOEs issued a regulation that required all SOEs to put internal audit units into proper operation. The regulation gave special attention to the establishment of internal audit units within the SOEs as well as the appointment of BPK as the external auditor of the SOEs. In

2008, the Bapepam-LK made a compulsory requirement for all public companies to release a guideline to compose the Internal Audit Charter, which was similar to the requirements of the IIA Standards. In a similar vein, Bapepam-LK's regulation also required the internal audit unit in the public SOE to comply with the IIA Standards. In 2011, the Ministry of SOE implemented Good Corporate Governance (GCG), which required the internal audit unit to use the standard of the Institute of Internal Audit (IIA) requirements, followed by issuing a guideline of assessment indicators in 2012 for the implementation of GCG in SOEs. Currently, the regulations that are imposed on the internal audit practice in a public SOE arise from many institutions, including Bapepam-LK, the Ministry of SOE, BPK, and BPKP. The IDX also required SOE to be annually audited by an accounting firm that has an affiliation with an international accounting firm that follows the SOX 2002 and COSO.

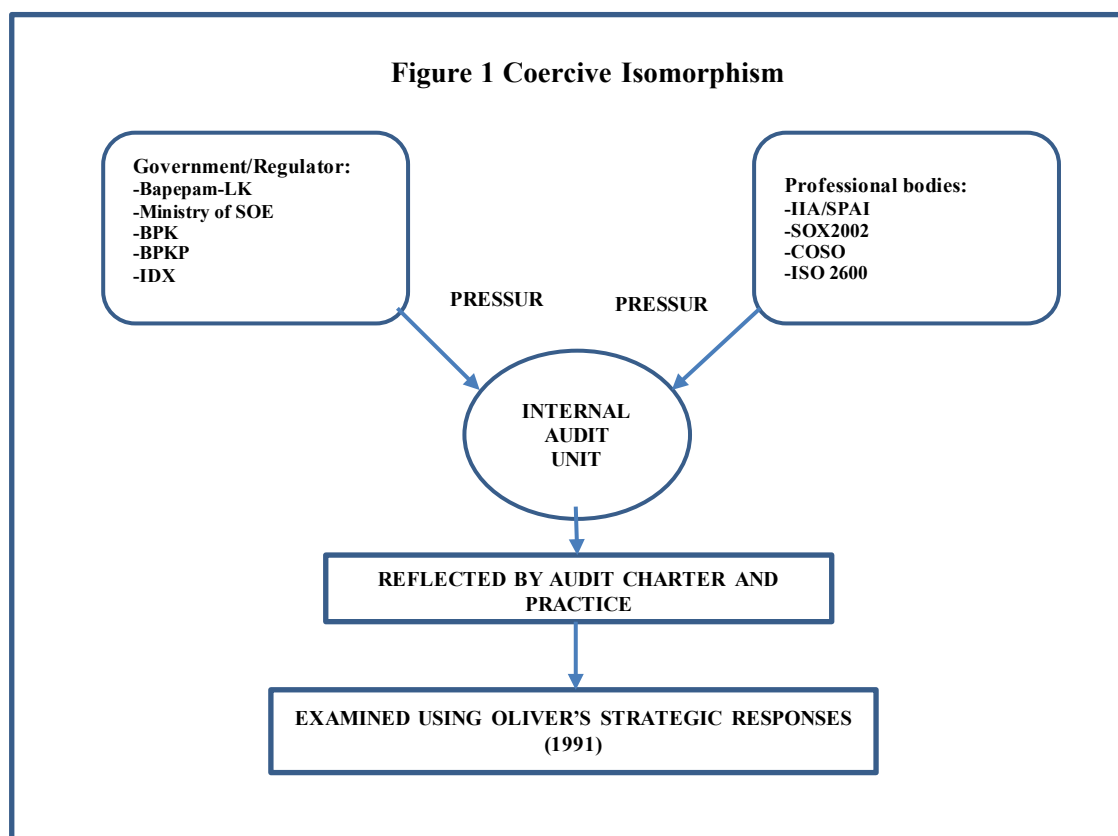
Despite the regulations that have been imposed, the increasing number of corruption and fraud cases within Indonesian companies is still high (Umar, 2011; Diansyah *et al.*, 2012; Wicaksono, 2009). During 2001-2004, over 6,000 suspected corruption cases were reported by the BPK, and more than 700 cases involving corruption were reported by the BPKP. Many Chief Executive Officers (CEOs) of the SOEs were convicted by the KPK on corruption scandals (Umar, 2011). In response to that, the SOE understudy restructured its internal audit unit into several functions: auditing, consulting, and catalyst functions. In February 2014, the Ministry of SOE and OJK required the SOE to establish another bureau, namely ICT (Information and Communication Technology). However, until the field study was undertaken, the internal audit charter used by the company was still the one that was established in 2012, as confirmed by the telephone conversation with the agent on 3 September 2023.

The internal audit charter of the company under study consists of five chapters: Introduction, Internal Audit, Standard Operating Procedures, Code of Conduct, and Concluding. Chapter one, Introduction, consists of three sections: Background, Purpose, and Vision and Mission. The second chapter, Internal Audit, contains seven sections: the first is Definition and Purpose, the second is Scope of IAF, the third is Authority of the IAF, the fourth is Position of IAF, the fifth is Organisational Structure, the sixth is Communication, and the seventh is Responsibilities of IAF. Chapter three, Standard Operating Procedures, covers six sections: first is General, second is Professionalism, Independence and Objectivity, third is Competency, fourth is Control, fifth is Managing Internal Audit, and lastly is Execution of activities and monitoring the recommended action. Chapter four, Code of Conduct, covers two sections, firstly General and secondly Standards of Behaviour. Lastly, chapter five is concluding.

Having the details of the Audit Charter, then by using content analysis, all regulations and demands that create isomorphism will be traced to the charter. Finally, the data from interviews and observation will be analysed to identify the strategies and tactics used by the IAF.

7. Data Analysis and Discussion

The SOE has two types of owners, government and private, which make the IAF deal with a complex institutional environment. The IAF needs to respond appropriately to the demands of its stakeholders to gain legitimacy. The detail of both stakeholders is presented in Figure 1.



Coercive isomorphism

The source of coercive isomorphism may arise from two sources formal and informal sources (DiMaggio and Powell, 1983). The study identified formal sources that may come from five government bodies that control SOEs in Indonesia they are Bapepam-LK, the Ministry of SOE, BPK, BPKP, and IDX. Another pressure may come from four professional bodies: IIA/SPAI, SOX2002, COSO, and ISO 26000. Details of each source will be discussed below.

Bapepam-LK

Bapepam-LK is an Indonesian Capital Market Regulatory Body and Financial Institution that issued Rule No: KEP-496/BL/2008, which contains ten listed requirements to standardise the role and the practice of the internal audit unit of SOEs. In response, the IAF under study created its Audit Charter in 2012. Although in 2011 the government of Indonesia created a new institution, namely OJK (Indonesia Financial Services Authority), to replace two existing institutions, Bapepam-LK and PPATK, the rule of 2008 is still valid. In response to the requirement of Bapepam-LK, the IAF created its Audit Charter in 2012. It should be noted that the content of the audit charter is still being used by the company until now, with some changes of expression from the word “company” to the word “parent company” because the company is now becoming a parent company⁴.

When those ten requirements are traced to the audit charter, it was found that all those requirements are spread into 12 items in the charter. Further investigation was done through an interview with participants in managerial positions on how the audit charter was developed. One of the participants described that the audit charter was developed by the internal audit unit, saying⁵;

⁴ Confirmed by one the auditors on 3 September 2023 through a telephone contact.

⁵ Interview with E, a senior-level auditor

The preparation of the Internal Audit Charter was done by involving several parties, the Chief of the Planning and Development of Internal Audit Bureau, the Chief of the Accounting and Finance Audit Bureau, the Chief of the Commercial Audit Bureau, the Chief of the Information and Communication Technology (ICT) Audit Bureau, Chief of the Engineering Audit Bureau, Chief of the Internal Audit Unit and Audit Committee.

It was mentioned that eight of the items in the charter were created consciously by the IAF (see Table 1). Furthermore, another participant said that⁶ *We propose an Internal Audit Charter to the CEO and Audit Committee, signed by both parties.*

Table 1: Items appear in the Audit Charter in response to the Bapepam-LK Regulation using the Acquiescence strategy and Comply tactic	
1.	The public company is required to have an internal audit unit
2.	The public company must own the Internal Audit Charter set by top management and approved by the board of directors.
3.	The Charter must state the definition of internal auditing and describe the functions of internal audit, the assurance provider, and the consulting functions.
4.	Code of Ethics of internal audit refers to the national or international Code of Ethics of Internal Audit.
5.	The structure and position of the internal audit unit in a public company: <ol style="list-style-type: none"> The internal audit unit is led by the head of internal audit. The head of internal audit is appointed and dismissed by the CEO and approved by the board of directors. The head of internal audit is responsible to the CEO.
6.	The duties and responsibilities of the internal audit unit: <ol style="list-style-type: none"> Set an annual internal audit plan. Examine and assess the efficiency and effectiveness of financial, accounting, operational, human resources, marketing, information technology and other activities. Recommend improvement and objective information on the activities being audited to all levels of management. Cooperate with the audit committee. Perform special audits if necessary. Set the program to evaluate the quality of internal audit activities. Test and evaluate the implementation of internal control, and risk management in accordance with the company's policy. Compose the audit report and deliver it to the CEO and the board of directors. Monitor, analyse, and report on the follow-up to audit recommendations.
7.	The authority of the internal audit unit consists of: <ol style="list-style-type: none"> Access to all relevant information of the company. Regular and incidental meetings with the company.
8.	Qualifications of the internal auditor: <ol style="list-style-type: none"> To have communication skills. To keep confidential information and company data related to the internal audit duties, except as required by legislation or court. Must have integrity, professional behaviour, independence, and be honest and objective in performing their duties. Has knowledge and experience in the audit with both technical and other relevant knowledge. Understands the capital market regulations and other legislation. Obeys professional Standards issued by the Internal Audit Association. Understand the GCG principles and risk management. Is willing to increase their professional knowledge, skills, and capabilities continuously.

⁶ Interview with J, a manager-level auditor

Acquiescence strategy with Comply tactic.

Through a further interview, the study found some testimonies on how they are practised by auditors. Item 6-point f) mentioned that the regulation does not clearly describe who and how to evaluate the internal audit activities, and therefore, it was mentioned to be done by an external entity, such as a public accounting firm. Furthermore, in item 8-point c) on Independence, it was mentioned that it is difficult to apply because the IAF is still under management. Nevertheless, the independence of the internal auditor is still presented in the charter, and it was mentioned that the auditor will maintain independence as much as possible. Other than item 6-point f and item 8-point c, all other parts of the eight items were mentioned to be practised by the unit. The practice includes attaining the required knowledge and experience in audit techniques, understanding GCG principles and risk management, and assessing the internal controls over financial reporting (ICoFR). The findings of this study fulfill the gap of previous studies that did not investigate GCG and ICoFR on internal auditors (Mihret et al., 2012; Al-Twaijry et al., 2003) and did not reveal the practice of the requirement of the GCG principle (Arena et al., 2006).

The independence of IAF is important and recommended by some authors (Chun, 1997; Hughes, 2004; Messier and Schneider, 1988; Rittenberg and Purdy, 1978), such as independence from management interference (Chun, 1997; Courtemanche, 1986), and being objective (Bailey et al., 2003; Courtemanche, 1986). However, violation of the independence of internal auditors has been discovered by some studies (Al-Twaijry et al., 2003; Brody and Lowe, 2000; Mihret et al., 2012; Arena et al., 2006). Nevertheless, as per Oliver's (1991) definition, it could be said that the response to eight items is using the Acquiescence strategy and Comply tactic.

Avoidance strategy with Conceal tactic.

The remaining four of the twelve items need to be further investigated. Table 2 presents items 9 and 10 out of the twelve items below.

Table 2: Items appear in the Audit Charter in response to Bapepam-LK Regulation using the Avoidance strategy and Conceal tactic	
9.	The number of internal auditors should be appropriate to the size and complexity of the company.
10.	The internal audit unit has the authority to communicate directly with top management, the board of directors, the audit committee, and their members.

The organisational structure of the IAF under study contains three audit bureaus: Engineering, Accounting and Finance, and Commercial and Management Systems. From the documentation, there is no information regarding the number of staff positioned in each bureau. Regarding item 9, the IAF should possess an appropriate number of auditors in those three audit bureaus. From the observation and interview, it is revealed that the IAF experiences staff shortage. This finding leads the study to trace the practice to the possible strategy and tactic that was staged by the IAF. According to Oliver (1991), the Avoidance strategy may be relevant to this practice, which is defined as "...the organisational attempt to preclude the necessity of conformity" (Oliver, 1991, p. 154). Concerning the tactic, it seems that the IAF uses the conceal tactic, which is defined to be associated with the response to disguise the fact that it does not intend to implement the requirement using a rational plan (Oliver, 1991, p. 154). This finding contributes another example to the literature of institutional theory on how the avoidance strategy and concealment tactic are used in practice.

Regarding item 10, the regulation stated that the internal audit unit has the authority to communicate directly with top management, the board of directors, the audit committee, and their members. Accordingly, the Internal Audit Standard number 1111 (IIA, 2013, p. 17) also ruled the internal audit unit to have direct interaction with the board as part of the independence and objectivity of the internal auditor. From an interview, it is revealed that communication

with the board must be done through meetings that are scheduled by management. It means that management may control the topic to be discussed with the board. It is also indicated by the SOPs that the meeting should be scheduled by the management. This finding indicates that the response to this requirement uses the avoidance strategy with the conceal tactic, which may be able to lessen the independence of internal auditors as well as widen the communication distance between the internal auditor and the board.

Defiance Strategy with Dismiss tactic.

Table 3: Items appear in the Audit Charter in response to the Bapepam-LK Regulation using the Defiance strategy and Dismiss tactic
11. It is forbidden for internal auditors to work as operational staff in holding and/or subsidiary companies.
12. The internal audit unit has the authority to coordinate its activity with the external auditor's activity.

As presented in Table 3, item eleven is in line with the Internal Audit Standard No. 1120 (IIA, 2013, p.18), which states that "Internal auditors must have an impartial, unbiased attitude and avoid conflict of interest". Surprisingly, from an interview, it was revealed that some auditors possess positions as treasurers for CSR programs. It indicates that the IAF presented it in the charter but did not put it into practice.

Item twelve is in line with Internal Audit Standard number 2050, which states that:

The chief audit executive should share information and coordinate activities with other internal and external providers of assurance and consulting services to ensure proper coverage and minimise duplication of efforts (IIA, 2013, p. 28).

In an interview, it was mentioned that the external auditors can be from a public accounting firm that audits the company, BPKP, which is the internal auditor of the government that assesses the implementation of good corporate governance, and BPK, which is an independent assessor who undertakes the Quality Auditing Review (QAR). In an interview, one of the auditors mentioned that in practice, they keep portions of the information confidential. This practice indicates that the IAF uses a defiance strategy, which is defined by Oliver (1991, p. 156) as "...a more active resistance to institutional processes and the use of a dismissive tactic which is characterised by ignoring institutional rules and values " (Oliver, 1991, p. 156).

In summary, it can be said that the coercive isomorphism from the ten items required by Bapepam-LK has been responded to by the IAF by containing them in twelve items in the audit charter. The finding indicated that eight items of the requirement were approached using the acquiescence strategy and compliance tactic. Two items were approached using avoidance strategy and conceal tactic, while the last two items used defiance strategy and dismiss tactic.

The Ministry of SOE

Acquiescence strategy with Comply tactic.

The decree of the Ministry of SOEs No SK-16/S.MBU/2012 contains thirty requirements, which have been condensed into seventeen items. The study presents those seventeen items in three tables: tables 4, 5, and 6. Although some items are like the requirement of Bapepam-LK, they need to be investigated. The study tracks those seventeen items in the charter and found that fourteen items are listed in the charter and are presented in Table 4.

Table 4: Items appear in the Audit Charter in response to the Decree of the Ministry of SOE using the Acquiescence Strategy and Comply tactic	
1.	The SOE is required to have an internal audit unit.
2.	The Charter is stipulated by the top management and approved by the board of directors.
3.	The content of the Internal Audit Charter must be in line with Baepam-LK/OJK Regulation and Company Law.
4.	The Charter must be reviewed and updated if necessary.
5.	The Internal Audit Charter must contain: <ul style="list-style-type: none"> a. Consideration of using the Professional Standards of Internal Audit issued by the Indonesian Consortium of Internal Auditors or the International Professional Practices Framework of the IIA. b. Explanation of the position of the internal audit unit in an organisation, the authorities of the internal audit function, which includes having access to all recordings, people, and assets of the company, and also the scope of the internal audit function.
6.	The head of the internal audit unit is appointed by the CEO and approved by the board of directors.
7.	The position of the internal audit unit is directly under the CEO in the organisational structure.
8.	The internal audit unit must make a plan for the necessity of its auditor staff.
9.	The qualities of internal auditors are appropriate to undertake internal audit activities. <ul style="list-style-type: none"> a. The internal auditor staff possesses knowledge, and skills, and are required to have appropriate professional certificates. b. Having the proper quality of internal auditor professionalism. c. There is a continual professional development program for internal auditors, which aims to maintain their professional certification and provide education support for them
10.	The internal audit unit has a quality assurance program in which the program is assessed by an independent assessor every five years, who evaluates the compliance with the Charter, standards, and code of ethics, efficiency, and effectiveness of internal audit functions to fulfil stakeholders' needs.
11.	The internal audit department sets annual internal audit plans and undertakes the audit activities as planned. <ul style="list-style-type: none"> a. The annual internal audit plan takes a risk-based approach. b. The annual internal audit plan is communicated to the audit committee to obtain recommendations. c. The audit plan must be approved by the CEO and communicated to top management. d. The accomplishment of the targets is in the annual audit plan.
10.	The internal auditors report to the CEO and the audit committee. <ul style="list-style-type: none"> a. The head of internal audit has direct access to report to the audit committee. b. The QAR's report also has to be delivered to the audit committee.
11.	The internal auditors give recommendations on the business strategy of the company. <ul style="list-style-type: none"> a. The internal auditors evaluate whether the goals of the programs and their operational activities are in accordance with the organisation's goals. b. The internal audit recommendations can be applied to improve the operational activity.
12.	The internal auditors monitor the follow-up of internal and external audit recommendations. <ul style="list-style-type: none"> a. The internal audit unit has guidelines for monitoring the follow-up of the internal and external audit recommendations. b. The internal auditors record the results of monitoring activities. c. The internal auditors report the monitoring results to the CEO and the audit committee.
13.	The internal audit unit must have audit guidelines, SOP, and supervisory roles in the internal audit unit, and undertake a quality assurance program. <ul style="list-style-type: none"> a. The head of the internal audit unit sets the policy and procedures as an activity's guidelines for the internal auditor. Such policies and procedures should fit with the structure of the internal audit unit, its size, and the complexity of the business activities of the company. b. The head of internal audit carries out a quality assurance program which covers all aspects of internal audit activities.
14.	The internal audit functions contribute to the corporate governance process, risk management, and internal control improvement.

It was mentioned that twelve of the items were practised, which can be said to be responded to by using the acquiescence strategy with the comply tactic. A further investigation on item 13th part a) was done by tracing it to SOPs, and it was found to be presented in the SOPs and practised by the IAF. Item 13th part b) is the same as the requirement of Bapepam-LK item 6 (f) ed in Table 1. This item was found in an interview in the unit that undertook a quality assurance program in three Quality Assurance Reviews (QAR)⁷. The review starts with an evaluation of the supervision from the stage of audit planning to monitor the audit recommendations, followed by a review of audit activities conducted by a unit external to the internal audit unit, and finally, a review is made by parties external to the company, such as a public audit firm or BPKP. This finding also indicated a response to item 13 is using the acquiescence strategy with the compliance tactic.

Item 14 is presented in the charter and was mentioned to be practised by the IAF to assess the Internal Control over Financial Reporting (ICoFR), risk-based audits, and audits on ICoFR. However, since the position of the internal audit unit is directly under the CEO, management intervention may reduce the quality of the assessment. Nevertheless, it could be said that it responded by using the acquiescence strategy with the comply tactic.

Compromise strategy with the Pacify tactic.

Item 15 of the regulation of the Ministry of SOE requires the head of internal audit to be qualified as an internal auditor and certified by the professional association (see Table 5).

Table 5: The requirement of the Decree of the Ministry of SOE using the Compromise strategy and Pacify tactic
15. The qualities of internal auditors are appropriate to perform internal audit activities by means: a. The head of internal audit has capabilities that are qualified as an internal auditor that are certified by the professional association (Certified Internal Auditor / Qualified Internal Auditor).

When this item was traced into the audit charter, it was not found in the charter, and therefore, it needs further investigation. From an investigation, it was found that the head of the unit was not qualified as a Certified Internal Auditor (CIA). From a tracing to the Good Corporate Governance (GCG) report 2012, issued by the BPKP, it was mentioned that the head of the unit was undertaking a course for the preparation of the Certified Internal Auditor (CIA) examination. Through an interview, it was mentioned that the head of the unit had attempted the examination but had not yet passed the exam. Although the unit has not fulfilled the requirement of this regulation, it has nevertheless made an effort to do so and did not present it in the audit charter. This finding indicated that the audit unit has responded partly in line with the legislative expectation, which can be categorised as a compromise strategy and a pacifying tactic. Oliver (1991) defined the compromise strategy as a strategic response when there is a conflict between internal and external institutional pressures concerning efficiency. The pacify tactic is defined as "...constitute partial conformity with the expectations of one or more constituents" (Oliver, 1991, pp. 153-154).

Avoidance strategy with Conceal tactic.

Further investigations were done on the last two items of the decree of the Ministry of SOEs, which are items 16 and 17, as presented in Table 6.

Table 6: Items appear in the Audit Charter in response to the Decree of the Ministry of SOE using the Avoidance strategy and Conceal tactic
16. The number of internal auditors is appropriate for conducting the internal audit activities.
17. The head of internal audit has direct access to report to the audit committee.

⁷ Interview with E, a senior-level auditor

Regarding item 16, in the audit charter, it was mentioned that the IAF has three audit bureaus, namely the engineering audit bureau, the accounting and finance audit bureau, and the commercial and management system audit bureau. An investigation was done to find out whether the number of auditors available is appropriate for the task of the IAF. When this matter was asked in an interview⁸, it was mentioned that the IAF is using the matrix structure as the solution due to the lack of a sufficient number of auditors. This response indicates that the unit uses avoidance strategy and conceal tactic, in which Oliver (1991, p.154) defines avoidance strategy as ...*the organisational attempt to preclude the necessity of conformity*, and the conceal tactic as,

...establish elaborate rational plans and procedures in response to institutional requirements in order to disguise the fact that it does not intend to implement them.

Item 17 requires the auditors to have direct access to the audit committee, and this requirement is presented in the audit charter. When this matter was further investigated, it was found in the policy that the communication with the audit committee is arranged by the management in a schedule of three months. This policy may facilitate management to control the listed topics to be discussed in the meeting. This situation again indicates the usage of a conceal tactic to respond to the pressure. It can be summarised that the seventeen items of coercive isomorphism from the Ministry of SOEs had been responded to by the IAF using the acquiescence strategy and compliance tactic for fourteen items, compromise strategy and pacify tactic on one item, and avoidance and conceal tactic on two items.

BPK (the Supreme Financial Audit)

The Indonesian Constitution 1945 specifies the Supreme Financial Audit (BPK) as an external auditor of financial matters of all government units, including SOEs. This institution is accountable to the House of Representatives of the Republic of Indonesia. Law No. 15 of 2006 gives authority to BPK to audit SOEs, and in verse 20, it requires the auditees (SOEs) to respond to the audit recommendations issued by BPK. Therefore, any audit recommendation issued by BPK puts pressure on the SOE to comply with it. Concerning the response of the audit unit to this requirement, the study investigates the practice of internal audit in dealing with the role of BPK in auditing the SOE.

The audit charter item 2.2.14 stated that IAF has to become a counterpart of external auditors and other relevant audit institutions. The Charter item 2.2.6 also stated that the IAF must comply with rules and regulations, standards, and business ethics. Regarding this counterpart role, the study searched the Audit Report of BPK 2012 on its website, which shows that BPK conducted a special audit on the SOE under study, including the holding company and all its subsidiaries. The audit report of BPK presented the following concerns: 11 cases of internal control system irregularities and 15 cases of other irregularities. For these findings, BPK issued 24 audit recommendations. BPK then monitored the follow-up actions to the recommendations, which were recorded in the BPK's report in 2013. The report stated that 17 recommendations were followed up by the company, and seven recommendations were still in progress. The practice of only partially complying with the regulation to follow up the recommendation can be categorised as the use of a pacifying tactic, in which Oliver (1991, p.153) mentioned: ...*pacifying tactics also constitute partial conformity with the expectations of one or more constituents*. Regarding the strategy used, it can be categorised as a compromise strategy, which Oliver (1991, p.153) described by saying,

⁸ Interview with a manager unit level auditor.

Although acquiescence may be instrumental to organisations, by virtue of the enhanced legitimacy and social support that acquiescence provides, organisations may consider unqualified conformity unpalatable or unworkable.

BPKP (the Financial and Development Supervisory Agency)

The Presidential Decree No. 192 of 2014 specifies the duties of the BPKP to assist the government with internal oversight on national financial accountability in government institutions, including at the SOEs. The BPKP is responsible to the President, as a coordinator of all internal audits of government units, including SOEs. The Decree further describes the scope of audit activities comprising the setting of national policies on financial accountability, undertaking an audit over financial accountability, and providing consulting services on risk management, internal control, and good corporate governance. The Minister of SOE, through an official letter, SE-14/MBU/2010, instructed the boards of directors and the CEOs of SOEs to assess the GCG implementation every two years using BPKP as independent assessors.

In response, the IAF accommodates the requirement in the charter by stating BPKP as a counterpart to assess the GCG implementation. In the GCG implementation report, BPKP did not mention any objection to the role of the IAF. This finding indicated that the IAF used an acquiescence strategy with a comply tactic to respond, which is *conscious obedience to or incorporation of values, norms, or institutional requirements* (Oliver, 1991).

IDX (the Indonesian Stock Exchange)

The IDX is an institution that is responsible for carrying out securities trading in Indonesia. It was a merger of two stock exchanges: the Jakarta and Surabaya Stock Exchanges. One of the regulations of the IDX that is related to internal auditors is Regulation No. Kep-306/BEJ/07-2004, which requires companies to provide an audited annual and interim report to the public. In response to this requirement, the unit incorporated this requirement in the charter by stating that the internal auditor should periodically conduct analytical reviews on the financial statements of the company, which was set in the planning to undertake the review in April, July, and October. This indicates that the audit unit uses the acquiescence strategy with the comply tactic to this requirement.

Coercive Isomorphism from Informal Sources

The isomorphism may arise from non-regulator organisations on which the institution relies administratively and culturally as expected by society (DiMaggio and Powell, 1983). This study uses four informal sources: IIA, SOX2002, COSO, and ISO 26000.

The Institute of Internal Auditors (IIA)/Indonesian Professional Bodies

The IIA issues the International Professional Practices Framework (IPPF) that recommends guidance that contains three components: Position Papers, Practice Advisories and Practice Guides. The requirement is supported by the Consortium of Internal Audit Profession Organisations in Indonesia, which has members from various associations, including the IIA Indonesian Chapter, FKSPI, an association of internal auditors of SOEs, the Foundation of Internal Audit Education (YPIA), the Certification Boards of Qualified Internal Auditors (DSQIA), and the Association of Indonesian Internal Auditors (PAII). All these bodies collaborated to issue an internal audit professional standard called SPAI that covers the Internal Audit Definition, the Code of Ethics, the Professional Standards of Internal Audit, and the Practice Advisories. This standard is adopted from the IIA to be followed by internal

auditors. However, as a professional body, it does not have a formal rule or regulation to oblige the implementation of the standards.

The response of the IAF toward this pressure was traced to the Internal Audit Charter. It is found that the charter accommodated this requirement by using SPAI and the IPPF as references to carry out internal audit practice. However, since the IAF is under the CEO, it may affect the ability to partly comply with the independence, which makes the response to use a compromise strategy with a pacifying tactic as characterised by *...partial conformity with the expectations of one or more constituents* (Oliver, 1991, p. 153).

The Sarbanes-Oxley Act (SOX Act) 2002

The SOX 2002 sets several requirements for corporate responsibilities, particularly for financial reports (section 302) and management assessment of internal controls (section 404). The SOX 2002 requires a more effective system of internal controls over financial reporting (ICoFR) (Hass *et al.*, 2006). The implementation and assessment of the ICoFR is one of the key aspects of good corporate governance (GCG), spread globally through the requirement of the NYSE for all companies listed on the NYSE to implement GCG principles. The legislation also indirectly affects internal audit activities by extending its scope of work, especially in ensuring the effectiveness of ICoFR in Indonesia. The Ministry of SOE issued a GCG handbook for all SOEs that operate in Indonesia. Another independent institution called the National Committee of Governance Policy (KNKG) issued a GCG handbook for all sectors, including non-SOEs. Since the KNKG is an independent institution, the requirements in the handbook will be complied with voluntarily. The requirement of the KNKG handbook reflects the expectations of Indonesian society towards the public and private sectors in having ethical awareness in conducting business. The guidance also recommends that companies establish an internal audit unit to assist top management in maintaining the effectiveness of the risk control process.

The IAF under study is only listed on the Indonesian Stock Exchange (IDX). Although it is not listed on the US stock market, the IAF considers the GCG requirement as pressure from public expectations, both domestically and internationally. In response to this pressure, the IAF has adapted the requirement in the charter that states the internal audit should ensure the implementation of the GCG. The charter also mentioned the role of IAF to ensure the effectiveness of internal control as a whole, in which the ICoFR is a part of the internal control systems.

Since the Ministry of SOEs is involved in this requirement, it is considered as coercive isomorphism, in which this situation demonstrates that the internal audit unit used the acquiescence strategy with an imitate tactic toward the SOX 2002 expectation. DiMaggio and Powell (1983, cited in Oliver, 1991, p.152) gave an example of the imitate tactic as *...imitation of successful organisations and the acceptance of advice from consulting firms or professional associations*.

The Committee of Sponsoring Organisations (COSO)

COSO recommends that public companies maintain appropriate internal controls and effective internal audit functions to prevent and detect fraudulent financial reporting. In 1992, COSO issued a framework named Internal Control-Integrated Framework that comprises five components: Control environment, Risk assessment, Control activities, Information and communication, and Monitoring. The critical role of the IAF is in the monitoring component to ensure the objectives are achieved effectively, efficiently, and reliably financial reports and compliance with laws and regulations. When this requirement is traced to the Audit Charter, it was found that there is no adoption of the COSO requirement in the charter. Although there is

no mention of COSO in the charter, from an interview, it was found that the internal audit unit used the COSO framework as a guide in their audit activities. In addition, the audit plan also indicated that a consultant provided a training course on the COSO framework for the internal auditors. Therefore, it could be said that the IAF used an acquiescence strategy with an imitate tactic.

The ISO 26000

The International Organisation for Standardisation (ISO) 26000 guides organisations to carry out their business activities in a socially responsible way. The companies are recommended to perform their actions ethically and transparently and contribute to the health and welfare of society. In this case, society means people or groups who are affected by the actions of organisations and vice versa. ISO 26000 provides several indicators for ethical behaviour. One of these is stated in clause 2.7, which mentions, “...ask yourself: would you be comfortable if your actions were to become public knowledge? (ISO 26000, 2010, clause 2.7)”. Undertaking CSR programs is a critical approach to maintaining a beneficial relationship between the companies and society as well as the environment in which they operate. Therefore, it could be said that society's expectations are represented by ISO 26000.

Since Indonesia is a member of ISO, the ISO 26000 is adopted by the National Standardisation Agency (BSN) of Indonesia, which is called SNI ISO 26000. Both international and domestic standards of ISO 26000 are used as guidance in conducting CSR programs by the SOE under study. According to the company policy, the implementation of CSR programs covers the area surrounding the factories of the entity. The CSR programs comprise diverse programs such as the Partnership Program (PK) and the Environment Development Program (BL).

In terms of pressure from public expectations that are represented by ISO standards, the response of the IAF to this pressure is stated in the audit charter, verse 2.2.6, to require the internal auditors to ensure the company comply with regulations, laws, standards, and business ethics. In an interview regarding the audit of the PK (partnership program)⁹, it was mentioned that they found fraud and irregularities in running the program, and this was mentioned in the audit report. The response to this public pressure demonstrates that the auditors implemented the requirement of the charter, which indicates the response to the use of the acquiescence strategy and compliance tactic to respond to the expectation of ISO standards.

Normative Isomorphism

Normative isomorphism is based on the idea that organisational change stems primarily from professionalism and sustainable education (DiMaggio & Powell 1983), which comprises two important aspects of isomorphism sources, formal education and professional networks that share knowledge and technologies. Regarding this matter, the study takes the position of the pressure that arises from the professional bodies on the qualification of the auditors. Several professional bodies may be relevant to create pressure, such as the IIA and the Indonesian Consortium of Internal Audit Professional Organisations. Both the IIA, as an international body, and the Consortium issued Internal Audit Standards. The standard issued by the Indonesian Professional bodies is an adoption of the international standard issued by the IIA. Therefore, the study will investigate the requirements of the IIA as the source of the pressure. The requirements essentially aim to promote internal audit guidance and professional standards to foster global adoption of internal audit best practices, as indicated by 3 items as presented in Table 7 below.

⁹ Interview with D and L, middle-level auditor

Table 7: Main Source of Normative Isomorphism	
1.	Education and training system
–	The IIA suggests that internal auditors possess sufficient knowledge, skills, and other competencies
–	The IIA encourages the internal auditor to possess appropriate certifications
2.	The IIA recommends that auditors undertake their duties with due professional care
3.	The IIA encourages the internal auditors to enhance their competence through continuing professional development

Using content analysis by tracing the response to the audit charter, it is found that the IAF responded to the normative pressures by presenting its requirements in the Internal Audit Charter. This means that the IAF complies officially with all items suggested by the professional bodies. Regarding item one, the charter presents the competencies as including capabilities in internal auditing, information technology, accounting (limited to auditors on financial aspects), good business practices, and knowledge to identify fraud. The IAF was found to fully comply with the pressure. An interview with a middle-level auditor¹⁰ mentioned that many of the auditors undertook training domestically and internationally, but it was mentioned that currently, many of them are still unqualified¹¹. It can be said, therefore, that the response made by the audit unit was the acquiescence strategy with the comply tactic.

Regarding item two, the IIA (2013, p.20) requires that *...Internal Auditors must apply the care and skill expected of a reasonably prudent and competent internal auditor*. This requirement is adopted in the charter number 3.3.2-point h) and in more detail in i), which mentions that the execution of the internal audit function must comply with regulations and standards, including carrying out the task with due professional care. From interviews¹² with the auditors, it was found that they practised the requirement in conducting the audit using their knowledge, skills, and competencies. It could be said, therefore, that the unit used the acquiescence strategy with the comply tactic.

Regarding item three, continuous development is practised in various activities such as attending training, seminars, and other events to gain an understanding of the latest developments of standards, procedures, audit techniques and business environment. However, the charter did not mention the membership of professional bodies as part of continuous professional development. From an interview, it was found that not all auditors¹³ attended even the domestic training. This finding indicated that the IAF did not fully respond positively to the IIA's encouragement, which indicated the use of a compromise strategy with the pacify tactic.

Mimetic Isomorphism

Mimetic isomorphism arises from uncertainty (DiMaggio and Powell, 1983), from poor understanding of organisational technologies, goal ambiguity and uncertainty on environmental expectations. The mimetic efforts may be followed intentionally or unintentionally. The intentional effort may be based on observation of a successful organisation or suggestions from a consulting firm or professional association (DiMaggio and Powell, 1983). In turn, the unintentional desire to copy may arise through employees who bring their previous knowledge or practice (DiMaggio and Powell, 1983).

¹⁰ Interview with L, J and E, middle-level auditors.

¹¹ Interview with E, middle-level auditors

¹² Interview with R middle-level auditor, and P junior-level auditor

¹³ Interview with L, a middle-level auditor

An interview with senior auditors¹⁴ mentioned that, ...the IAF perceived that the activities of the company are complex and need a strong technological base and internal control systems. At this stage, the internal auditor was unsure how to develop proper internal control systems.

From the interview, it was revealed that a team of auditors went to visit a successful SOE in Jakarta that is listed on the NYSE, and another team went to visit a successful company overseas. In addition, it was also mentioned that the company used a public accounting firm to assess the implementation of ICoFR and a consultant firm to assess the implementation of the guidance of COSO. These findings show the mimetic isomorphism in three items as presented in Table 8.

Table 8: Mimetic Isomorphism indicated by three items	
1.	The mention of a formal visitation to other SOEs and overseas corporations, which are perceived to be more successful, to learn their technology-based internal control system.
2.	The use of a public accounting firm to assess the implementation of audit on the Internal Control over Financial Reporting (ICoFR) as one of the core of SOX 2002
3.	The use of a consultant to assess the implementation framework issued by the COSO on the effectiveness of internal control.

Concerning the first pressure listed above, an interview was found to support that possibility. A further investigation was done by the head of the unit, who confirmed that the visit was followed up by developing a technology-based internal control system assisted by a consulting firm and involving information technology personnel of the company. The head of the unit also mentioned his intention to visit a similar SOE soon. Therefore, it could be said that the internal audit unit uses the acquiescence strategy with an imitate tactic to respond to the mimetic isomorphism by consciously adopting a technology-based internal control system.

Regarding the second item, the interviews revealed that this pressure stemmed from the recommendation of the international affiliation of public accounting firms. Although the charter does not state that the IAF has to follow a recommendation, however, it was described in the charter that the internal auditors are the counterparty of external auditors in conducting the audit activities and may exchange their management letters of the audit report. The management letter contains all deficiencies found in the audit process, including the weaknesses of internal control systems, which need to be improved. In interviews¹⁵, it was mentioned that the internal audit unit responded to the recommendation by implementing ICoFR and creating accompanying guidelines. The analysis on this matter demonstrates that the internal audit unit used the acquiescence strategy and imitate tactic. This tactic is clearly described by DiMaggio and Powell (1983, cited in Oliver, 1991, p.152) as *...the acceptance of advice from consulting firms or professional organisations*.

Regarding the third item on the use of a consultant firm, it is described in the audit charter that the IAF may use a consulting firm if necessary. Further investigation through an interview revealed that the IAF hired a consulting firm to assess COSO implementation and propose recommendations. In addition, it was also found that the IAF hired a consulting firm for training and seminars, which may influence the IAF to implement COSO requirements as indicated in the annual report 2014. These findings, therefore, may be said to indicate that the IAF responded to mimetic pressure by implementing an Internal Control-Integrated Framework issued by COSO as recommended by the consulting firm. Therefore, it can be said that the response used by the unit is the acquiescence strategy with the imitate tactic.

¹⁴ Interview with N and E, senior-level auditors and D, a middle-level auditor.

¹⁵ Interview with K, a middle-level auditor

8. The findings and contribution

The study has demonstrated the use of institutional theory to identify three isomorphisms dealt with by the IAF of an SOE in Indonesia. The Coercive, Mimetic and Normative isomorphism (DiMaggio and Powell, 1983). Five government institutions and four professional bodies are identified to create coercive isomorphism. The government bodies are Bapepam-LK, Ministry of SOEs, BPK, BPKP, and IDX, and the professional bodies are IIA/SPAI, SOX2002, COSO, and ISO 2600. The Institute of Internal Auditors (IIA/SPAI) is considered the source of normative isomorphism regarding professionalism and sustainable education. The mimetic isomorphism arises from the uncertainty perceived by the IAF on the complexity of the job concerning the technological base and internal control systems. These findings can be said to answer the question of the source and type of isomorphism from each source. The sources of the isomorphism are considered key stakeholders of the IAF, and therefore, to gain its legitimacy, the IAF attempted to satisfy their requirements by placing the requirements in the audit charter. The findings should answer the second question of how the IAF gained its legitimacy from its stakeholders.

Regarding the third question on the use of strategies and tactics, this is responded to differently in isomorphisms. The Bapepam-LK creates coercive isomorphism by issuing ten items of requirements. The IAF accommodates the requirements by adapting them into twelve items in the charter (see Tables 1, 2 and 3). Eight items were approached by using the acquiescence strategy and compliance tactic, two with the avoidance strategy and conceal tactic, and two were approached by using the defiance strategy and dismiss tactic. The regulation of the Ministry of SOEs requires seventeen items to be practised by SOEs (see Tables 4, 5 and 6). All items required are presented in the charter, but fourteen items are responded to by acquiescence strategy and compliance tactic, one item is approached by compromise strategy and pacify tactic, and two items are responded to by avoidance strategy and conceal tactic. The requirements of BPK are responded to using a compromise strategy and a pacifying tactic. The requirement of the IDX is handled by using the acquiescence strategy and compliance tactic.

The four sources of coercive isomorphism from professional bodies as IIA/SPAI, SOX2002, COSO, and ISO 2600. The requirements of IIA/SPAI are about internal audit standards. This requirement is found in the audit charter using the compromise strategy and pacify tactic. Although the IAF is only listed on the Indonesian stock market, the IAF put in the charter the requirement of SOX2002 on the implementation of GCG using acquiescence and imitate tactics. The requirement of COSO on the implementation of the Internal Control-Integrated Framework was not present in the charter, but they are it was used as guidance. Therefore, it can be said that the IAF uses an acquiescence strategy and an imitation tactic. Since Indonesia is a member of ISO 26000, the IAF was found to put the requirements of the ISO on the audit charter using the acquiescence strategy and compliance tactic.

The source of Normative isomorphism was found in the requirement for organisational change around professionalism and sustainable education. This requirement is presented in three items in the charter (see Table 7). Accordingly, the first and the second items are approached using the acquiescence strategy and compliance tactic, and the third item is responded to by using the compromise strategy and pacify tactic. There are three items (see Table 8) of mimetic isomorphism that were responded to by the IAF using an acquiescence strategy and tactic. Three items as the sources of Mimetic isomorphism are found to arise from the IAF's perceived complex organisational environment and the advanced technological base and internal control. These three sources of mimetic isomorphism are approached using the acquiescence strategy and imitate tactic.

The study may generate some research contributions to the domain of internal auditing and confirm the validity of the application of institutional theory as a lens to examine organisational responses toward various institutional pressures. This study also broadened the level of examination into two two-level examinations as suggested by Fogarty (1996), which contrasts with previous studies in this area that undertook one level of examination (for example, Al-Twajry et al., 2003; Arena et al., 2006; Arena and Azzone, 2007; Mihret et al., 2012). One of the major strengths of this study is that it has attempted to answer 'how' questions through an interpretative case study, which fills the gap in the literature highlighted by Humphrey (2008), who argues that there is a lack of qualitative research in examining internal audit issues. The study also has potential implications for policymakers and professional bodies, especially in IAF.

9. Conclusion and Suggestions for Further Research

The study uses institutional theory to investigate how an SOE in Indonesia responded to three forms of Isomorphism, namely Coercive, Mimetic and Normative, to be legitimate. In response to those pressures, the study attempted to identify strategies and tactics that were used to indicate how it responded to the pressure. Four government bodies and four professional bodies are considered to create coercive isomorphism as a formal and informal source of pressure on the SOE understudy. Data collection was done by visiting the site over three months to collect documentation and undertake interviews and observations. The study uses content analysis to identify the strategies and tactics of Oliver (1991) that were used by the unit to respond to the pressure. The first level of investigation is to trace the adoption of the requirements to the audit charter of the company; the second level is to use interviews, observation, and documentation to confirm that the requirements were implemented in practice.

The study found that internal audit units responded differently to coercive isomorphism from formal sources of government regulators. The responses were varied in a combination of acquiescence strategy with comply tactic, avoidance strategy with conceal tactic, defiance strategy with dismiss tactic, and compromise strategy with pacify tactic. The informal sources, in turn, were found to use the pacify tactic, the acquiescence strategy with the imitate tactic, and the acquiescence strategy with the comply tactic. The normative isomorphism responded as using the acquiescence strategy with the comply tactic, the compromise strategy with the pacify tactic, and the mimetic isomorphism using the acquiescence strategy with the imitate tactic.

The findings of this study are subject to several limitations. The study focuses on a public SOE in Indonesia as a single case study. The common criticisms of the single case study method draw concerns about methodological rigour, researcher subjectivity, and external validity and interpretation based on the findings of a single case. In addition, the findings of the study may not be relevant to another internal audit unit that operates in a different context and institutional environment. Therefore, it is suggested to undertake further study using multiple case studies, either in SOEs or non-SOEs in Indonesia or other countries with different contexts and institutional attributes. So, further studies may contribute to the collection of cases using institutional theory and content analysis as part of the research.

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