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The Moderating Effect of Organizational Changes on the Influence of Ethical Decision Making on Public Sector Internal Auditor Performance

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ABSTRACT

This study investigates the role of organizational change in moderating the effect of ethical decision making on internal auditor performance. The study population comprises internal auditors who work in the public sector (a government-owned company in Indonesia). Smart Partial Least Square statistic software is used to test the hypotheses. This study has led to three findings. First, this study finds that ethical decision making provides support for auditor performance. Second, this study finds that organizational change does not provide support for auditor performance. Third, the analysis shows that the role of organizational change does not succeed in helping to strengthen or weaken ethical decision making in auditor performance.

KEY WORDS:

Organizational changes, ethical decision making, internal auditor performance, public sector

JEL Classification: M420, M480, H830, L2

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1. Introduction

Reinventing the public sector is difficult work (Osborne, 2007) that requires great persistence. Facts show that many planned changes fail or take a long time to succeed. There are several causes of failure; for example, the lack of public sector employee competence in financial management mentioned in some studies (Priono, Yuhertiana, Sundari, & Pus-

pitasari, 2019; Yuhertiana Andre Purwanugraha, Andayani, Andhaniwati, & Denhas, 2019). Further, conditions are often inappropriate and unpredictable due to differences in organizational characteristics and environments. New Public Management, as an issue of change, which was introduced decades ago, also experienced a change in orientation. Although, it still has the same vision, namely, to make the organization of the public sector less bureaucratic and more oriented toward public service. Citizens pay more attention to public sector performance related to this new paradigm (Priono et al., 2019).

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This study examines one of the functions of public sector organizations, namely, the audit function. The audit function is essential because it is tasked with overseeing and ensuring that state assets are not corrupted and are used efficiently and effectively. Some studies have examined organizational change in the audit function. There has been a change in the audit mindset from traditional audits to performance audits (Kidron, Ofek, & Cohen, 2016). This shift implies that internal auditors in the public sector function as change agents who underpin the fundamental change process (Sutherland, 1993). Change in the audit process means that internal audits must be more focused on risk-based auditing (Cao, Li, & Zhang, 2015; Johnsen, Meklin, Oulasvirta, & Vakkuri, 2001).

The changes in organizations have impacted the psychology of auditors. As professionals, auditors face ethical dilemmas in decision making related to psychological issues. There is a need to be more aware of the psychological factors related to audit work (Chambers, 1986). Psychology is related to interpersonal skills. The various elements of interpersonal aspects that impact internal auditing have been summarized (Dittenhofer, 1988). As agents of change, auditors face many challenges (Pearson, 2014). Not only must auditors deal with organizational changes due to the demands of good governance related to the implementation of bureaucratic reform, but also, they are faced with a change in mindset from traditional to risk-based audits. This change requires auditors to be ready to face challenges in dealing with time and budget pressures as well as with ethical dilemmas. For government auditors, the political environment puts added pressure on them, which, of course, has a psychological effect on them. Additionally, company politics and lack of training and development opportunities are other significant sources of stress (Lee Larson, 2004); hence, the present research. Auditing in the public sector is an area in which more research would be valuable (Hay & Cordery, 2018).

Many studies have examined the relationship between the personality of the auditor and ethical dilemmas in decision making (Afifah, Sari, Anugerah, & Sanusi, 2015; Espinosa-Pike & Barrainkua, 2016; Keim & Grant, 2008; Nikmatuniyah, 2015; Reynolds, 2000; Sweeney & Roberts, 1997; Yendrawati &

Witono, 2017; Yuhertiana, Priono, Setyaningrum, & Hastuti, 2016). There is evidence that individual ethical decisions affect personality (Saadullah & Bailey, 2014). The conflict in the auditor's dilemma leads to the challenge of developing a set of ethical standards that would improve the ethical judgment and behavior of accounting professionals (Espinosa-Pike & Barrainkua, 2016)

Auditors face ethical dilemmas in a number of circumstances (Sweeney & Roberts, 1997; Yuhertiana, & Soeparlan, & Priono, 2016), and the internal auditor continually faces ethical dilemmas involving choices among conflicting values. Internal auditors use their code of ethics to help resolve professional and ethical dilemmas (Reynolds, 2000). Internal auditors also face public demand to provide an accurate report that adheres to the ethics of the profession.

Dilemmas trigger internal self-conflict. Audit conflicts appear when auditors perform internal auditing activities. As workers in the organization, internal auditors will discover problems related to the findings of an audit that should be reported and that may not be beneficial to the management of performance assessments or audit objects. This audit conflict develops into an ethical dilemma when auditors are required to make decisions that are contrary to the independence and integrity of the economic rewards that may ensue or to put pressure on others (Keim & Grant, 2008). Ethical dilemmas also occur when auditors and auditees do not agree with some aspects of the function and purpose of the inspection (Espinosa-Pike & Barrainkua, 2016). In these circumstances, auditees may affect the process of an audit conducted by an auditor by preventing the auditor from performing a given action, which violates the standards of the review. To that end, the auditor is faced with matters related to making ethical and unethical decisions. When the auditor meets the demands of the auditees, this means that the auditor has violated the code of ethics and standards of examination and may have been potentially rewarded by the auditees. However, if the auditor decides to not meet the demands of the auditees, then he or she will be under pressure from the auditees. In such a situation, the auditor is expected to take ethical considerations into account which, in the end, will affect the decisions made.

Ethical dilemmas, especially in the public sector, appear in all budgeting processes, beginning with the planning process, proceeding through the ratification process and implementation process, and ending with controlling the budget (Yuhertiana et al., 2016; Yuhertiana, 2015). Public sector reform that focuses on increasing transparency and accountability requires a structural change in public sector organization. Commitment and support from all stakeholders, the government, individuals, political parties, and the private sector is required. Change means going against something. Managing organizational change takes time primarily because it combines the capabilities of human resources with the conditions of the new organization. As scholars have indicated, all too often, the introduction of a change in an organization elicits negative responses, frequently quite justifiably so. These negative responses often include live demonstrations of resistance, to the extent that the organization ends up no better off after the change than it was before (Oreg, Michel, & By, 2009).

2. Literature Review and Hypothesis Development

2.1 Ethical Decision Making and Auditor Performance

Ethics play a role as a predictor of performance (Meriac, 2012). The relationship between workplace ethics and work outcomes has been studied by many researchers (Meriac & Gorman, 2017; Porter, 2010; Rokhman, 2010; Selart & Johansen, 2011). In the workplace, employees always face an environment involving ethical issues. Sometimes an employee finds it personally difficult to decide on the right way to behave in some circumstances. An ethical decision is one that is both morally and legally acceptable to the broader community. Ethical decision making is defined as making decisions that consider the ethical aspects of a situation, the good or bad sides of an issue. To tell or not to tell becomes a dilemma when a person faces circumstances that are illegal (Keim & Grant, 2008).

Auditors are a controller profession and often face ethical dilemmas (Arnold, Dorminey, Neidermeyer, & Neidermeyer, 2013; Keim & Grant, 2008; Sweeney & Roberts, 1997). Auditors with a strong ethical orientation of relativism, compared to idealism, demonstrate undesirable ethical decision-making processes

(Johari, Mohd-Sanusi, & Chong, 2017). On the other hand, in the public sector context, research has shown how auditors, using their performance audit devices in various ways, make efficiency auditable (Skærbæk, 2009). Auditor performance in the public sector is determined by its audit quality, which is related to time and budget pressures (Deis & Giroux, 1992). In the case of an ethical dilemma, an auditor who can manage time and budget pressures performs very well. It is clear that good ethics will result in an increase in excellent performance.

H1: The higher the ethical decision making, the better the auditor performance

2.2 Organizational Changes and Auditor Performance

The organizational change literature continues to be responsive to the dynamics of contemporary workplace demands (Armenakis & Bedeian, 1999). There are four themes in organizational change studies. First are content issues, which primarily focus on the substance of contemporary organizational changes. Second are contextual issues, which principally focus on the forces or conditions in an organization's external and internal environments. Third is the concern with process issues, which address actions undertaken during the enactment of an intended change. Finally, criterion issues, deal with outcomes commonly assessed in organizational change efforts (Armenakis & Bedeian, 1999).

The current study observed organizational change and auditor performance in the public sector. This type of change and performance (Burke & Litwin, 1992; Pettigrew, Woodman, & Cameron, 2001) have a causal relationship. In public sector auditor circumstances, the new public management wave is pressing for organizational change throughout the world. One example of a change in public sector auditing is the use of the performance audit. Performance audits, as practiced by national audit offices, are a relatively new and rapidly developing set of activities. Auditors claim to have moved beyond issues of compliance and regularity and to be able to directly investigate the efficiency and effectiveness of public programs, projects, and institutions (Pollitt & Summa, 1998). In Indonesia, in situations in which the Indonesian government

requires immediate reform, the BPK (general government auditor) has been trying to improve its audit performance to provide a better auditing scope to monitor the quality of public administration (Dwiputrianti, 2011).

H2: The higher the organizational change support, the higher the auditor performance.

2.3 Role of Organizational Change as a Moderator Variable to Influence Ethical Decision Making in Auditor Performance

The current study shows that proper and effective work relationships are significant in organizational change. Managing conflicts, building supportive work relationships, and communicating effectively all contribute to the formulation of positive attitudes to change and, therefore, to the success of a given change program (Vakola & Nikolaou, 2005). In addition, an old, unproductive habit is that people are comfortable with the idea of behaving in some unethical manners. The commitment to change could reduce this negative attitude and, ultimately, increase the auditor's performance. Organizational change is related to ethical culture and mindfulness. Mindfulness can prove a valuable tool in enabling individuals and organizations to challenge and change their unethical behavior (By, Armenakis, & Burnes, 2015).

On the other hand, an organization with a high commitment to change plans a detailed program that involves all organization members staying the course with their commitment to change. The support for organizational change will increase their motivation to adopt good habits and ethical practices and, in turn, will increase the performance of organization members.

H3: Support for organizational change can moderate the influence of ethical decision making on auditor performance.

3. Data Collection and Research Methodology

3.1. Sample Composition and Data Collection

The current study investigated the role of organizational change as a moderating variable in ethical decision making and internal auditor performance.

The research involved 146 auditors working at an Indonesian government-owned enterprise (part of public sector entities). The number of samples was calculated using Slovin's formula, which obtained a total of 59 samples.

$$n = \frac{N}{1 + Ne^2} \quad (1)$$

n: sample size,

N: Population size,

e: Percentage of inaccuracy due to sampling errors that can be tolerated (10%).

This study used a survey method. We distributed written questionnaires to auditors, who were given a return period of one week from the time they received the questionnaire.

3.2 Definition and Variable Measurement

3.2.1. Dependent Variable: Internal Auditor Performance

The internal auditor performance measurement used the indicator of audit quality variable. This variable is defined as the probability that the auditor will find and report violations in the government accounting system based on established accounting and audit standards. Audit quality variables are measured using 12 items (Carcello, Hermanson, & McGrath, 1992), namely:

1. Experience in conducting financial statement audits.
2. Deep understanding of the client's business characteristics.
3. Responsiveness to client needs.
4. Competence of audit team members in accounting principles and audit norms.
5. Independence in everything.
6. Audit team members having a cautious attitude.
7. A strong commitment to quality.
8. Involvement of internal auditor leaders in conducting audits.
9. Implementation of field audits.
10. Engagement of the audit committee before, during, and after the audit.
11. High ethical standards from the audit team.
12. Team members have a skeptical attitude.

Table 1. Population and sample

Auditor Rank	Population	Sample
Chief Audit Executive	3	1
VP Corporate Internal Audit	27	11
VP Investigation Audit & WBS	14	5
VP Upstream, Gas & NRE Internal Audit	12	5
VP Downstream Internal Audit	19	8
Audit Planning & Quality Assurance Mgr.	71	30
Total auditors	146	59
Usable questionnaires		37

3.2.2. Independent Variable: Ethical Decision Making

Ethical decision making is the act of making decisions by considering the ethical, or good or bad, sides of an issue. These measurements use Modarres & Rafiee (2011) as a basis. The following is a list of personal indicators of ethical decision making:

1. I use religious values to decide ethical issues related to my audit work.
2. To decide an ethical dilemma in audit work, I am guided by religious rules.
3. I make decisions for mutual interests and for those that many people like.
4. I think something that is considered correct by many people is ethical.
5. Complying with audit standards will reduce my dilemma when faced with ethical or unethical decisions.
6. I always obey the law, including the professional standards of auditors.
7. What is best for me is the basis for my decision making.
8. I always choose the best alternative.
9. There is no relationship between accounting and ethics.
10. As an auditor, I do not want to be faced with an ethical dilemma.

3.2.3. Control Variable: Organizational Change

Organizational change is a situation in which an organization experiences a change that will maintain or develop the organization and enhance its capability and role, and that will require adjustments both internally and externally. Organizational changes of attitude variables are measured using instruments (Gardner, Dunham, Cummings, & Pierce, 1987).

3.3 Analysis Tool

The analysis tool used was the Partial Least Squares (PLS). The PLS method has its advantages, including that data do not have to be multivariate normally distributed and the sample size does not have to be large. Thus, we applied the PLS method to the sample in our study, which included 37 respondents, as it can be used in a small sample (see Goodhue, Lewis, & Thompson, 2006; Hair, Sarstedt, Hopkins, & Kuppelwieser, 2014; Shackman, 2013).

4. Empirical Results

4.1. Demographics of Respondents

The majority of respondents were male with a bachelor's degree and were still young, from 20 to 30 years old, but had enough experience to be senior auditors

Table 2. Organizational change indicator

Indicators	Items of statement
Cognitive attitude	1. Change always reduces my ability to control what happens in the workplace. 2. I usually resist new ideas. 3. I did not like the change. 4. The change made me frustrated. 5. Most of the changes in the workplace felt intrusive. 6. I am usually reluctant to try new ideas.
Affective attitude	1. The changes are usually profitable for the organization (company). 2. Most employees benefit from the changes. 3. I tend to do whatever is possible to support the changes. 4. I am usually supportive of new ideas. 5. I found that most of the changes are subtle. 6. I usually receive the benefit of the change.
Behavioral attitude	1. I expect changes in the workplace. 2. I was compelled to try new ideas. 3. The changes tend to be uplifting to me. 4. I often suggest new approaches to various things. 5. Changes often help me to do well. 6. Everyone else thinks that I support the change in the Audit.

4.2. Evaluation of the Partial Least Squares Models

4.2.1. Measurement Model (Outer Model)

a. Test the validity of the construct

For the validity test, the measurement results were obtained following the theory used to identify a construct. The following results were obtained after the final test (after each indicator is above 0.5):

After retesting, each construct had a value above 0.7, so that the next test could be performed to observe the construct validity and reliability of this model.

In this study, the construct validity test used the convergent validity test and discriminant validity test described as follows:

Convergent validity. Convergent validity was fulfilled because the AVE and communality values were over 0.5. The convergent validity test parameters used can be determined from the AVE scores and communality, and each must be above 0.5. Based on the results of the tests carried

out, these results, as presented in the table that includes ethical decision making, organizational change and auditor performance, all had values above 0.5. Thus, the indicators in this study converged and entered into a construct with a value of more than 50%.

Discriminant validity. To test discriminant validity, the parameters to be used involve examining the AVE root compared to the correlation between variables, and the value of the AVE root must be higher than the correlation between the latent variables. The test results show that the AVE root value of each variable was more significant than each correlation of latent variables.

b. Reliability test

A construct can be said to be reliable if its composite reliability is > 0.7 and Cronbach's α is > 0.6 . In this study, the composite reliability for each variable was above 0.7 and Cronbach's α for each variable was also above 0.6. Thus, the model used in this study is reliable.

Table 3. Demographic statistics

Demographic variable	Percentage
Gender	
Male	72%
Female	28%
Highest Level of Education	
High school	0%
Bachelor	88%
Master's	12%
Doctoral	0%
Age Group	
20 - 30 yo	58%
31 40 yo	33%
41 – 50	3%
51 – 60	6%
Auditor's rank	
Junior Team	32%
Senior Team	42%
Junior Team Leader	26%
Senior Team Leader	0%
Technical Controller	0%
Quality Controller	0%
Auditor Experience	
under five years	32%
5 – 10	51%
11 – 15	8%
16 – 20	4%
over 20 years	5%

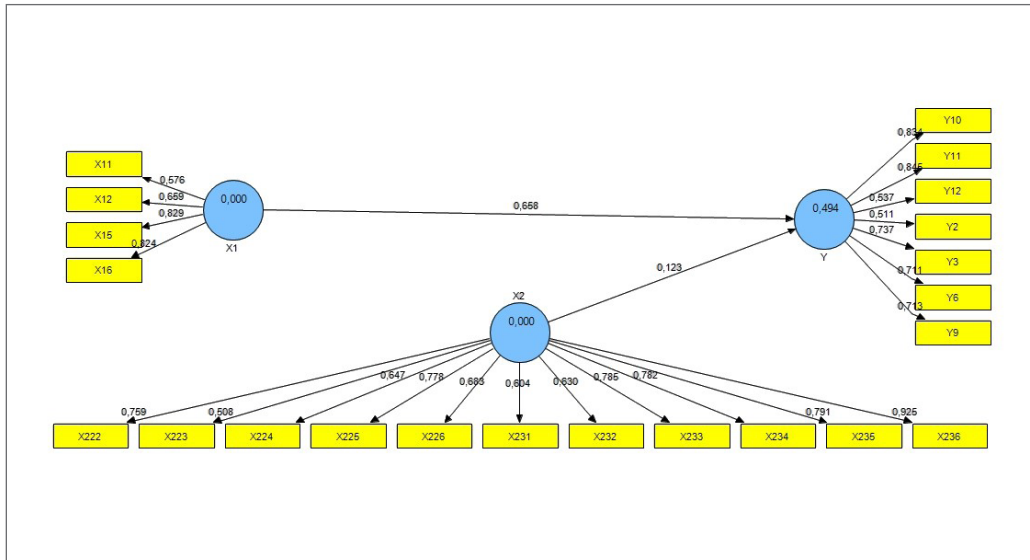


Figure 1. PLS test results after removing constructions < 0.5

Table 4. AVE test results and commonality

	AVE	Communality
Ethical decision making (X1)	0,53	0,53
Organizational changes (X2)	0,53	0,53
Auditor performance (Y)	0,50	0,50

Table 5. Correlation of latent variables

	Ethical decision making	Organizational change	Auditor performance
Ethical decision making	1,00		
Organizational changes	0,28	1,00	
Auditor performance	0,69	0,31	1,00

Table 6. AVE and AVE root

	AVE	AVE root
Ethical decision making (X1)	0,53	0,73
Organizational changes (X2)	0,53	0,73
Auditor performance (Y)	0,50	0,71

Table 7. Reliability test results

	Composite reliability	Cronbach's alpha
Ethical decision making (X1)	0,82	0,73
Organizational changes (X2)	0,92	0,91
Auditor performance (Y)	0,87	0,83

Table 8. R square test results

	Overview algorithm	R Square
Ethical decision making (X1)		
Organizational changes (X2)		
Auditor performance (Y)		0.49

4.2.2. Structural Model (Inner Model)

To assess the structural model (inner model) using PLS, this study used the value of R². The level of variance in the change is in the independent variable with the dependent variable. The test results are presented in Table 8:

Based on the results, the auditor performance variable is explained by ethical decision making variables and organizational change by 49%, while the remaining 51% is explained by other variables not used in this study.

4.2.3. Discussion

The structural model (inner model) predicts the causality relationship between latent variables. The value of the path coefficient or inner model reached the level of significance in testing the hypothesis. Using the bootstrapping process, the t-test parameter was obtained to prove the hypothesis.

First Hypothesis Test Result. This result shows that X1 (ethical decision making) supports Y (auditor performance) because it has a t value of 11.92 which is higher than t table 1.96.

Table 9. Regression result

	Original sample (O)	Sample mean (M)	Standard deviation (STDEV)	Standard error (STERR)	t statistics (O/STERR)
X1 ->Y	0,65	0,67	0,06	0,06	11,92
X2 ->Y	0,12	0,15	0,08	0,08	1,56

Table 10. Moderating test results

	Original sample (O)	Sample mean (M)	Standard deviation (STDEV)	Standard error (STERR)	t statistics (O/STERR)
X1 ->Y	0,27	0,56	0,68	0,68	0,39
X1 * X2 ->Y	0,59	0,18	1,04	1,04	0,57
X2 ->Y	-0,23	0,04	0,69	0,69	0,36

Second Hypothesis Test Result. This result shows that X2 (organizational change) does not support Y (auditor performance) because it has a t value of 1.56, which is smaller than t table 1.96.

Third Hypothesis Test Result. Hypothesis 3 tested moderation, following the results of the test by first making X2 a moderating variable, as in the table below.

This result shows that X2 (organizational change) is not able to moderate the relationship between X1 (ethical decision making) and Y (auditor performance) because it has a t value of 0.57, which is smaller than t table 1.96.

Effect of Ethical Decision Making on Auditor Performance. The results of the statistical tests show that X1 (ethical decision making) supports Y (auditor performance) because it has a t value of 11.92, which is higher than t table 1.96. This result is in line with research by (M Nizarul Alim, Trisni Hapsari, 2007). The results indicate that independence and competence as ethical indicators significantly influence audit quality. However, the current study found evidence that the interaction between auditor ethics and competence did not significantly influence audit quality.

The results of the questionnaire analysis support the hypothesis that the majority of respondents tend to use ethics in decision making, strengthening audit quality. Respondents have religious values in their career and work lives. Thus, auditors relate workplace problems related to ethical dilemmas or morals to the religious values (as shown by the high average size for questions one and two).

Regarding the statement about ethics and audit work, respondents stated that there was a strong relationship between ethics and auditing, even though the value of this question was the lowest, which means that many respondents did not believe in this relationship.

Effects of Organizational Change on Auditor Performance. The statistical test results show that X2 (organizational change) does not support Y (auditor performance) because it has a t value of 1.56, which is smaller than t table 1.96. This result is not in line with the findings of (Heldalina, 2013), which show that organizational change has a significant positive effect on auditor performance. Heldalina (2013) examined government auditors in the Indonesia Development Finance Supervisory Agency (BPKP), and the influence

has a positive relationship with performance, meaning that an organizational change improves employee performance because employees are required to adjust to the organizational change. According to Heldalina (2013), the chief representative should have the courage to implement items that are on the agenda of organizational change. Applying organizational change in the new role of the BPKP is in consulting and assurance, which can be done by increasing collaboration with stakeholders.

The current research shows different results: Organizational change was not shown to affect audit quality (audit quality measures an auditor's performance but, more specifically, only in measuring the achievement of audit work results, whereas auditing performance measures not only the results of audit work but more generally includes another respondent's work).

Role of Organizational Change in moderating the effect of Ethical Decision Making on Auditor Performance. This result shows that X2 (organizational change) cannot moderate the relationship of X1 (ethical decision making) toward Y (auditor performance) because it has a t value of 0.57, which is smaller than t table 1.96. The failure of organizational change as a moderating variable means that it does not play a role in strengthening or weakening the acquisition of ethical decisions in improving auditor performance in terms of audit quality work. The failure of this organizational change is explained by the obstacles that cause the change process to fail: organizational constraints, functional constraints, and individual constraints:

1. Organizational obstacles. Organizational structure and culture can be barriers to change. When an organization establishes its organizational structure, a stable pattern of task relationships is formed that influences the relationships among employees. Over time, when there is a shift in employees, the task relationship remains unchanged, which is why organizational structures are resistant to change. The norms and values of organizational culture are also resistant to change.

2. Functional obstacles. The organizational structure and culture at the functional level can also be barriers to change. At the managerial level, functional managers will try to lobby according to their interests and try to influence the change process so that the

changes can benefit them. The level of task dependency among existing functions also causes difficulties in achieving change because changes to one function will affect all other functions. The higher the dependency among functions, the more difficult it will be to achieve change.

3. Individual obstacles. The presence of a deep-seated prejudice toward change can affect managers' individual perceptions of a situation and can cause them to interpret changes according to their wishes to benefit themselves. Another reason why employees are resistant to change is the presence of stress and discomfort at work, both for managers and employees. Employees develop regular habits that can make it easier for them to control the situation and make routine decisions. When their routine is interrupted, employees experience stress, and to reduce stress, they tend to return to their old habits.

4.2.4. Suggestions

Based on the above discussion, we provide the following suggestions:

- a. To improve audit quality, the ethical sensitivity of auditors must be improved by means of a variety of formal and informal approaches to increase auditor performance.
- b. The results of questionnaires indicate that respondents have a serious desire to change and to explore new ideas. The respondents must thus be continuously encouraged through example and leadership support to reduce the obstacles that arise organizationally, functionally, and individually.
- c. The limitations in measuring audit performance through audit quality must attract the attention of researchers by adding personal performance to team performance.
- d. It is necessary to apply the results of this research to broader government auditor organization entities, both internal auditors and external auditors.

5. Conclusion

This study presents three findings. First, ethical decision making provides support for auditor performance. Second, organizational change does not provide support for auditor performance. Third, organizational change does not succeed in providing support to strengthen or weaken ethical decision making in auditor performance.

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