

External Auditors' Reliance on the Internal Auditors in Sudanese Banks

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Abstract

The purpose of this paper is to examine the perceptions of Sudanese external auditors responsible for bank's audits by studying the factors affecting their reliance degree on the work of internal auditors. The paper also investigates variation of judgment between private external auditors and public sector auditors.

A sample of 46 external auditors from private audit firms and the General Auditor's Chamber is employed to examine their perceptions regarding three factors (objectivity, competence and work performance) that may affect their reliance degree on the work performed by internal auditors. For the purpose of analysis t-test and ANOVA were conducted to analyze the data.

The results indicated that external auditors responsible for bank's audits consider objectivity, competence and work performance of internal auditors as important factors affecting their reliance degree. The results revealed that work performance had the highest mean score followed by objectivity and competence. It is found that there were no variations between private and public sector external auditors in their reliance degree on the work of internal auditors.

The results of this paper will be of concerns to internal audit departments in Sudanese banks to develop their relationship with external auditors.



ملخص البحث:

يقوم هذا البحث بدراسة مستوى اعتماد المراجع الخارجي على عمل المراجع الداخلي في البنوك السودانية. ويهدف هذا البحث الى تحديد مستوى إدراك المراجعين الخارجيين لأهمية وتأثير عمل المراجع الداخلي من خلال دراسة تأثير عدد من العوامل. كما تهدف الدراسة لتحديد مستوى التباين في آراء المراجعين الخارجيين طبقاً لتصنيف نوع القطاع الذي يعمل من خلاله المراجع الخارجي (مكاتب خاصة أو ديوان المراجعة القومي).

فقد شملت عينة الدراسة عدد ٤٦ مراجعاً خارجياً من القطاعين، ولتحقيق اهداف البحث تم دراسة ثلاثة متغيرات تعتبر من أهم العوامل التي تؤثر على درجة اعتماد المراجع الخارجي على عمل المراجع الداخلي وهي الموضوعية والكفاءة المهنية ومستوى أداء المراجع الداخلي. ولاختبار فرضيات الدراسة تم استخدام اختبارات إحصائية أهمها اختباراً واختبار التباين ANOVA لتحليل البيانات. فكانت نتائج البحث تتلخص في أن المرجعين الخارجيين في القطاعين (المكاتب الخاصة والتابعين لديوان المراجعة القومي) ينظرون باهتمام كبير لعمل المراجع الداخلي، ويتم تقييم مستوى اعتمادهم على عمل المراجع الخارجي من خلال العوامل الثلاثة مستوى الموضوعية ومستوى الكفاءة المهنية ومستوى أداء المراجع الداخلي، وكان تقييم مستوى التأثير على النحو التالي: مستوى أداء المراجع الداخلي سجل أعلى وسط حسابي تم يليه مستوى الموضوعية وفي المرتبة الثالثة يأتي مستوى الكفاءة المهنية. كما أوضحت النتائج عدم وجود تباين بين آراء المراجعين الخارجيين (في القطاعين) حول درجة اعتمادهم على عمل المراجع الداخلي فب البنوك السودانية.

1.Introduction:

Although the primary purpose of internal audit differs from that of the external audit there are common interests that provide the basis for co-operation between them (Moeller and Witt, 1999). Not only is the internal audit function an important part of the internal control system, but the reliance by external audit on the work of internal audit is likely to result in less external audit work being performed (AICPA, 1997, p. AU 322) and external audit cost savings (Felix et al., 1998; Gramling, 1999 and Wallace, 1984).

Although there are fundamental similarities between external and internal auditing, many differences separate the two professions. The Performance Standard 2050 of the Institute of Internal Auditors stated that “the chief internal audit executive should share information and coordinate activities with other internal and external providers of the relevant assurance and consulting services to ensure proper coverage and minimise duplication of effort” (IAA, 2001).

However, external auditors may utilize the experience of the internal auditors to reduce the duplication of work and, in effect, the cost of the external audit. Internal auditors may benefit from the expertise of external auditors in areas that the internal audit department needs. Internal auditors may also benefit from exposure to different audit techniques employed by the external auditors (Reckers and Lee, 1997; Burnaby and Klein, 2000; Haron et al., 2004; Schneider, 2009).

In recent years, professional accounting bodies that represent both internal and external auditors have expressed interest in increasing the level of coordination between the internal and external audit (Morrill and Morrill 2003). For external auditors, the purpose of this consideration is to ensure adequate coverage and decrease the duplication of the work and develop a more effective strategy for collaboration (Engle 1999). Furthermore, internal auditors can assist external auditors to understand the internal control system and the level of compliance with controls. For internal auditors, working with external auditors can increase their knowledge and expertise to identify their internal audit department’s needs.

Much of the previous research in this area has been conducted in some countries like USA, Saudi Arabia and Jordan and has examined external auditors’ evaluations of the internal audit departments functions and their decision to rely on the work of internal auditors. However, the objective of this research is to examine the relationship between external and internal auditors in banking sector in Sudan. The research uses questionnaires method to obtain information to address the following research objectives:



- (1) To examine the external auditors' perceptions of the internal audit function in Sudanese banks in terms of independence, competence and work performance?
- (2) To examine the factors -independence, competence and work performance - affecting the external auditor's decision about whether or not to rely on internal auditor's work?
- (3) To evaluate the level of co-ordination between the external and internal auditors in Sudanese banks?

This study could be useful for academics and practitioners. For academics, it will improve their understanding of the factors that influence the reliance decision of external auditors on the work of internal auditors. For practitioners, it may help to solve the practical problems facing the internal audit departments in Sudanese banks in terms of its relationship with external auditors. Third, the results of the study can be used as a base for other studies in other sectors in Sudan such as oil and insurance sectors.

2- Literature review:

2-1 Auditing Standards and previous studies in external auditor's reliance on the work performed by internal auditors:

The British Standard Statement of Auditing Standards SAS No.500, issued by the Auditing Practice Board "Considering the Work of Internal Audit". Para 3 of the statement emphasised the role of internal audit function as an appraisal and monitoring activity established by management and directors for the review of accounting and internal control systems as a service to the entity. However, its function amongst other things is to examine, evaluate, and report to management and directors on the adequacy and effectiveness of the components of the accounting and internal control systems.

Similarly, in the USA, the Statement of Auditing Standards SAS No. 65 (AIC-PA,1997), the Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statements, provided guidelines to use the work of internal audit function on a financial statement audit. The statement considers that the internal audit function is a part of the control system and requires the external auditor to understand the internal audit function.

SAS 65 also provides guidance on how external auditors should:

Modify their procedures based on the internal auditor's work.

Assess, evaluate and test the internal auditor's competence objectivity and work performance.

Furthermore, the Canadian Guidelines of the Canadian Institute of Chartered Accountants (CICA), 1997, states that "external auditors can rely on the work of internal auditors when involved in reviewing and testing the system of internal controls".

Moreover, International Standards Auditing section 260 (ISA 260), "Communications of audit matters with those charged governance" (International Federation of Accountants 2004). The standard provides guidelines for external auditors to communicate matters that may be of interest to the governance body of an entity. The communications included in the guidelines permits the external auditor to communicate with the internal auditor.

Many studies have been conducted on the decision to use the work of internal auditors by external auditors. Maletta (1993) for example asserted "Prior research has generally indicated that the three internal audit variables identified in the professional standards- objectivity, competence and work performance- significantly affect auditors' internal audit reliance judgment". Most of these studies have examined external auditors' general evaluations of the internal audit quality and their decisions to rely on the prior work of internal auditor (for example, Brown 1983, Schneider 1984, 1985 b, Margheim 1986, Messier and Schneider 1988, Krishnamoorthy 2002, Haron et al 2004, and Al-Twajjry et al 2004). Few studies have addressed auditor's decisions to use internal auditors as assistants in conducting the internal audit (for example, Ward and Johnson 1980, Wagonor and Ricket 1989 b, Maletta 1993, and Haron 1996).

Gibbs and Schroeder (1980) conducted a study to determine what criteria are important in determining the competence, objectivity and work performance of an internal audit department. The study developed a list of criteria by surveying both external and internal auditors, considering the experience factor of external auditors in the area of internal auditing. The study produced three detailed ranked lists of criteria that measure how external auditors evaluate the competence, objectivity and work performance of internal audit departments.



Brown (1983) performed one of the first studies aimed to examine the three factors –objectivity, competence and work performance- that might be considered important by the external auditor in evaluating the reliability and the reliance to be placed on the internal audit function. He found that all these factors had simple additive effects on the reliance decision that internal auditor objectivity and the previous years' audit work were the main factors influencing the decision. Generally, the results showed that work performance and objectivity of the internal auditors to be the most important factors with competence a distant third. The study did not find significant interaction effects among the three factors.

Abdel-Khalil et al. (1983) investigated the impact of two of internal audit variables, objectivity and work performed on the percentage of external audit work that auditors assigned to the internal audit function. The results indicated that these factors had a significant effect on the auditor's decisions to use internal auditors as assistants. The study found that one of the objectivity variables (internal auditors reporting level) accounted as the most important factor within the factors used in the study. This study did not use the competence factor.

Schneider (1984) conducted an experimental study on how external auditors evaluate the strength of internal audit function by using the three criteria recommended by SAS No. 65- competence, objectivity and work performance as measurements. The results of the study revealed that external auditors viewed work performance as the most important factor when evaluating the internal audit function, followed by competence and objectivity factors.

Berry (1984) examined the coordination efforts between internal and external auditors through the eyes of the internal auditors. The study took a sample of 18 large companies were selected and interviewed. The study identified ranked criteria for the evaluation of internal audit staff competence, objectivity and performance, in addition to how to establish and introduce a co-ordination program.

Schneider (1985a) conducted a research to examine the relationship between external auditors' evaluation of internal audit function and their evaluations of internal audit strength. Included in the investigation was an assessment of the levels of importance auditors attach to the three criteria recommended in SAS No. 65 in forming evaluation judgments and reliance decisions. The results showed that the auditors generally relied on internal auditing to reduce their external audit work. The study found that

auditors perceived competence and work performance factors to be almost equally important, and the objectivity factor to be less important.

Schneider (1985b) examined the degree of consensus among external auditors in evaluating the internal audit function. Using the three variables objectivity, competence and work performance for examining the degree of consensus, the study found that 9 of the 15 auditors considered the work performance as the most significant factor, with 8 of the 9 indicating the following ordering: work performance, competence and objectivity.

Margheim (1986) conducted an experimental study by examining whether external auditors adjusted the nature and extent of audit procedures due to reliance on the internal audit function and whether this reliance was related to internal audit competence, work performance and objectivity. The experimental task for this study included the evaluation of an accounts receivable control system and the appropriateness of account balances. Results indicated that external auditors reduced planned audit hours if internal audit had a high level of competence and work performance but did not alter their tests in response to changes in the degree of internal auditor objectivity. Moreover, for the competence and work performance variables, the results suggested that internal audit had to perform documented work in specific areas before the external auditor subjects would alter the number of planned hours.

Messier and Schneider (1988) examined the external auditor's evaluation of the internal audit function by using Analytical Hierarchical Process with 22 audit supervisors and managers. The results indicated that external auditors are taking competence as an important factor. Objectivity and work performance followed competence in importance.

Peacock and Pelfrey (1989) carried out a survey covered internal audit directors and their staff who have a direct relationship with external auditors. The study used two questionnaires, the directors of the departments completed one and the other targeted the staffs that have direct involvement with the external auditors. The study aimed to evaluate the relationship between the internal and external auditors in different areas; however, one of these areas was to test the internal auditors' contribution to the external audit. The study found that internal auditors who co-operated with external auditors were not satisfied with their relationship with external auditors because external auditors did not use internal auditors to their fullest extent.



Edge and Farley (1991) conducted a study in Australia by examining the relative importance of the factors that used by external auditors when evaluating the internal audit function based on the factors mentioned on the Statement of Auditing Practice AUP 2 “ Using the Work of Internal Auditor”. Results indicated that technical competence which is measured by experience, supervision and training/educational background as the most significant factor. Work performance is considered as a second factor, previous audit work was considered as the third factor. Organizational status (objectivity) was considered as the least important factor.

Tiessen and Colson (1990) studied whether external auditors can accurately self-report variables they consider in determining the reliance placed on a company’s internal audit function and the variables influencing reliance are affected by the nature of the company’s industry. The study found that the form of working relationship between the external and internal auditor was more important in determining the external auditors’ reliance evaluations than was the specific work internal audit performed. Objectivity of internal auditors was a significant variable in reliance evaluations when the status of the director of internal auditing was such that the company’s audit committee consulted the director about the work of external auditors. Competence variables are not significantly affecting the reliance decision.

Maletta (1993) studied the external auditors decisions to use the internal auditors as assistants. The study used the three factors of SAS 65, competence, work performance and objectivity, furthermore, the study expanded to investigate the impact of inherent risk on auditors’ decisions to use the internal auditors as assistants. Results revealed that when inherent risk is high, auditors appear to use more complex configural decision processes to evaluate internal audit objectivity and work performance than when inherent risk is low. The external auditors consider the effect of work performance of internal auditors in case of high objectivity. In case of low inherent risk conditions, there is no interaction between work performance and objectivity. Moreover the results showed that within the inherent risk conditions, competence of internal auditors is the most important factor, followed by objectivity and work performance.

Krishnamoorthy (1994) investigated the external auditor’s evaluation of the three factors recognized by the standards of internal auditing, objectivity, competence and work performance of internal auditors. The results revealed that evidence related to work performance was of little value to the external auditors when they have negative perceptions about either the internal auditor objectivity or competence. However,

when the external auditor maintain positive perceptions about the internal auditor objectivity and competence, the value of evidence about internal auditor work performance was important. The research recommended that these three factors recognized by the professional standards have significant effects on the evaluation of external auditors and whether or not to rely on the internal audit function.

Felix et al (1998) studied the relationship between the internal and external auditors, in terms of, the work performance of the internal auditors as a part of the external audit function and the reasons for the co-ordination of efforts between the internal and external auditors. Two questionnaires were designed for internal and external auditors beside face-to-face interviews. The main findings of the study indicated that there were interactions between the internal and external auditors, the study showed that there was co-operation and co-ordination in terms of planning the audit work and accessing each other working papers and reports. This research indicated that more than 25% of the internal auditor's time was spent on financial audit, while only 6% spent on assisting the external auditors. Both of the groups agreed that 50% of internal audit work was related to the internal controls.

Krishnamoorthy (2002) examined how the three factors – objectivity, work performance and competence – of internal auditors as identified by the auditing standards interact in determining the strength of the internal audit function. The study used an analytical method based on Bayesian probability to model external auditors' evaluation of the internal audit function. Models based on multistage (cascaded) interference theory are developed and analysed using numerical sensitivity analysis. The results indicated that the importance of the three factors varies with the type of the evidence (convergent or conflicting) observed and contingent on the interrelationships among the three factors.

Al-Twajjry et al (2004) examined the extent of co-operation between internal audit departments directors and partners and managers in external auditing firms in Saudi Arabian companies. Questionnaires and interviews were used for data collection. The results showed that external auditors tend not to endorse the current practice of external auditing and expressed particular concerns about the independence, scope of work and the small size of many internal audit departments. However, the internal auditors considered the co-operation between the internal auditors and external auditors to be limited, where the external auditors were more positive as to the extent of co-operation in the case that the internal audit departments maintain professional skills in its

work. The quality of the internal audit department played a big role on the reliance decision of the external auditors on the work of internal audit departments.

Haron, et al (2004) conducted a study based on Malaysian AI 610, Malaysian Institute of Accountants (MIA, 2001) Considering the Work of Internal Auditing. The objective of the study is to determine which of the criteria as mentioned by the standard (AI 610) was used by the external auditors to evaluate the work of internal auditors. The subjects of the study were external auditors- partners, managers and senior staff- from auditing firms in Malaysia. The study found that the technical competence and scope of function are the two most important criteria that external auditors consider in their reliance on internal auditors.

Suwaitan and Qasim (2010) studied the perceptions of Jordanian external auditors for the importance given by them to a number of factors which may influence their reliance on an internal auditor during their external audit. The paper also examines the relationship, if any, between the degree of reliance on the internal and external audit fees.

The study found that external auditors in Jordan consider the objectivity, competence and work performance of internal auditors as very important factors affecting their reliance decisions. It is found that “objectivity” had the highest mean score (4.353), followed by “competence” (4.188) and “work performance” (4.156).

However, some more recent studies examined external auditor’s reliance on the work of internal auditors from different views.

For example, Desai et al. (2010) hypothesized in an analytical approach that external auditors focus on the interaction of the three quality factors (objectivity, competence and work performance) when assessing the strength of the internal audit function. They found an interdependence of the three factors, like assessment of the internal audit function remains high even when external auditors reflect a negative evidence about one of the factors.

Munro and Steward (2011) investigated how the reporting relationship with the board of directors and business risk influence the reliance on the work of internal auditors. The study found that, both factors affect external auditors reliance on work already performed internal auditors and their use as assistants.

Desai et al. (2011) predicted that external auditors' assessments of objectivity and competence will be greater for cosourced and outsourced IA functions compared to in-house IA functions. Results indicated that external auditors place more reliance on cosourced and outsourced internal auditors compared to in-house internal audit function. However, they found that provision of tax service cosourced and outsourced internal auditors decrease the reliance on internal audit function.

2.2 Auditing profession in Sudanese Companies Act:

Section 138 of the Sudanese Companies Act refers to the powers and duties of the auditors, however, Section 138(1) states that auditors have the right to access to the books, records and accounts of a company. The same Section requires auditors to report on the following:

- Whether or not they have obtained all information and explanations they need.
- Whether the balance sheet has been prepared in accordance with the Act.
- Whether the balance sheet shows a true and correct view of the state of the company's position according to the information provided to the auditors.

The statement true and correct in the Sudanese Companies Act is the same concept to true and fair in the UK.

Section 137 of the Act reflected the requirements regarding the qualifications and appointments. The Act does not mention the necessary qualifications for the person carrying out the audit, however, for the purpose of the independence, the Act prevent any company director, partner and any person in the employment of director or officer to act as a company auditor. Furthermore, Section 137(1) explained that every auditor should have a certificate from the Minister of Finance to act as an auditor.

2.3 Bodies exercising external auditing in Sudan:

In Sudan, like other countries, two bodies exercise the external auditing function; private audit firms and the General Auditor's Chambers.



2.3.1 The General Auditor's Chamber:

The General Auditor's Chamber is responsible for the audit of public owned or semi-owned organizations. The General Auditor's Chamber is an independent body supervising external auditing. The General Auditor is responsible to the Head of the State who appoints him, his deputies and his high level auditors. The Auditor General Law 1986, amended 1990, encompasses 11 chapters including the establishing of the institution, appointment and tenure of the General Auditor and his staff, his authorities and power, General Auditor responsibilities, access to auditees, work performance and report on audits, budget and audit fees. Scope of audits conducted by the General Auditor's Chamber includes all government organizations. These audits are conducted according to the principles and methods of the local and international audit profession. According to Auditor General Law 1990, Chapter (3/7/2 C-D) requires auditors to conduct;

- Financial and regularity audit, that the General Auditor's staff should perform the audit efficiently in order to ensure that the financial transactions, expenditures and revenues have been carried out and accounted for. Therefore, the Law demands firstly a financial audit in order to ensure that the financial transactions regarding the processes of revenues and expenditure are properly authorized and accounted for. The second issue was a regularity audit that ensures all of the expenditures incurred were in accordance with the authorized budget and in accordance with the accounting, administrative and financial regulations.
- Performance audit, A.G.L.3/7/D, requires the General Auditor-or his representative-to perform the necessary checks to ensure the optimal use of assets, human and technical resources and the effectiveness of the financial performance to fulfill these goals.

2.3.2 Private audit firms:

For private audit firms, they conduct the external audit function for privately owned enterprises. Furthermore, partners in these firms are members of the Sudanese Council of Certified Accountants and they are under the supervision of the Council. In Sudan, the number of the firms practicing the auditing profession is fourty firms,

the majority of firms are small i.e. the working force of the firm ranges from 5 to 15 employees including 1 to 2 audit partners. The majority of audit partners obtained their qualifications from different recognized bodies in UK such as the Institute of Chartered Accountants in England and Wales and the Association of Chartered Certified Accountants. Very few audit partners hold qualifications from USA (CPA) and the certificate of the Sudanese Council of Certified Accountants Examinations Board.

3. Sudanese banking sector:

Sudan, like many other colonized developing countries, had known the commercial banking activities in the dual-government regime that was known as the Anglo-Egyptian condominium (1899-1955). The first bank established in Sudan was the National Bank of Egypt in 1901; it obtained a privileged position as banker to and for the government, a “semi-official” central bank. Other banks followed, but the National Bank of Egypt and Barclays Bank dominated and stabilized banking in Sudan until after the Second World War.

The period before the independence of Sudan in 1956 had witnessed the establishment of other six branches, they were: Barclays Bank 1913, the Turkish-Osmani Bank 1949, the Branch of the Egyptian Bank 1953, the French Credit Lyonnais 1953, the Arabian Jordanian Bank 1954, and the Ethiopian Bank 1976. The same period had witnessed the establishment of the Sudanese Agricultural Bank as the first specialized financial institution in Sudan, the act of this bank was issued in 1957 and started the work in May 1959, this bank considered as the first bank established by the national government after the independence of Sudan to promote agricultural ventures (Hamid and Kheir 1997).

After independence, the Sudanese banking system passed through four stages, however, the first stage was the stage of pre-nationalization (1960-1970) which consisted of foreign branches and a limited number of national banks. The second stage was the stage of nationalization and economic openness (1970-1980). This stage witnessed the execution of the Banks Nationalization Act, during this period many branches of the foreign banks had been nationalized and merged with national banks. The third stage known as the stage of banking duality (1980-1990), during this period, most of banks that were working in Sudan implemented the Islamic Financial Laws and some few banks were working according to the traditional banking system. The fourth



stage was the stage of activating the Islamic banking method (1990-up to now) that was reflected in the various achievements that were represented in the banking body expansion, further Islami-clisation procedures, the issuance of regulating the banking activities act and the establishment of the Khartoum Exchange Market. In this period the Bank of Sudan reactivated its handbill-issued in 1984- for the commercial banks to give-up working with interest based system in their banking dealings, and to apply the Islamic Financial Modes in all their banking activities and transactions. (Al-Bagir 1999).

Now, Sudan's banking sector consists of the central bank of Sudan (CBOS); 36 commercial banks, 23 of which are completely or mostly privately owned, and seven state-owned commercial banks. The sector also includes four specialized state-owned banks, two investment banks (Bank of Sudan official website).

4- Methodology:

4.1- Profile of sample:

Eighty nine questionnaires were sent to external auditors in private audit firms and the General Auditors' Chamber. Forty six usable responses from received from both after the two mailings, resulting in a response rate of 52%. Table 2 represents the biographical background information about the respondents.

Table 2: Biographical Background Information:

Sector		
Public	20	43%
Private	26	57%
Education		
Bachelor	24	52%
Higher Diploma	2	4%
MSc	3	6.5%
PhD	17	37.5%
Experience		

From 3 to 5 years	3	7%
From 6 to 10 years	8	17%
From 11 to 20 years	16	35%
More than 20 years	19	41%
Age		
From 25 to 35 years	9	19.5%
From 36 to 45 years	19	41.3%
Older than 46 years	18	39.2%

The majority of the respondents are in the seniors level, located in Sudan and having reasonable experience (41% more than 20 years). The age range from 25 to 46 years and also majority of them are holding graduate/ postgraduate certificate in accounting or auditing qualifications.

4-2 Data:

Table1: Questionnaire description

S.N	Variable Name	SPSS name Variable	Coding instructions
1	Auditor's Objectivity	IAO	Questions 14 Disagree =1 Strongly Agree =5
2	Auditor's Competence	IAC	Questions 14 Disagree =1 Strongly Agree =5
3	Auditor's Work Performance	IAWP	Questions 19 Disagree =1 Strongly Agree =5
4	Auditors' Reli- External ance Percentage	EARP	less 30% =1 from 30% to less 50% =2 from 50% to less 70% =3 or more 70% =4



4-3 Survey design:

This research is designed to help understand of Sudanese practice in the area of integration between Internal Audit (IA) and External Audit (EA), as well as the role of auditing standards in an auditing practices context. We used a questionnaire survey to collect the data and designed two sections of questions focusing on issues arising from our review both of the academic research on auditing practices and recent professional developments. The study questionnaire covered three distinct sub-areas in three groups, these groups reflect the internal auditors' function as in the Institution of Internal Auditor (IIA 2009).1) 14 questions about internal auditors' objectivity (IAO), 2) 14 questions about internal auditors' competence (IAC) and 3) 19 questions about internal auditors' work performance (IAWP). In order to encourage a high response rate the questionnaire was designed so that most questions could be answered by rating alternatives on a five-point Likert-type scale (1= strongly disagree.... 5= strongly agree).

Regarding hypotheses, the study tested three hypotheses. The development of these three hypotheses will be in sections 5.1, 5.2 and 5.4 accompanied with results and discussion of each.

5- Results and discussion:

5.1 Reliance extent:

The external auditor's relationship with internal auditors has become increasingly important in the current governance environment (Glover et al., 2008; Gramling et al., 2004; Grant et al., 2009; Schneider, 2009). The need for high-quality auditing in conjunction with increased compliance costs places greater emphasis on the benefits of an effective and efficient integration of the two audit functions.

In spite of the mixed results of prior research, we expect a strong relationship between the internal audit function and external auditors in Sudanese banks. This, in turn, should impact external auditors' decisions to rely on work already undertaken by internal audit and the use of internal auditor as assistants for performing audit tasks. So, the first question must be answered is that: to what extent external auditors are relying on the internal auditors' work in the banking sector of Sudan? This leads to the following hypotheses:

H1: External auditors are more willing to rely on internal auditors' work in banking sector of Sudan.

Empirical evaluation of internal auditors' functions regarding the perceptions of the message communicated by external auditors in Sudan is expected to provide useful information to address this hypotheses test.

Table 3 bellow reports the descriptive statistical– frequencies for the reliance percent- age among external auditors in this study.

Table 3 : descriptive statistical – frequencies \ Reliance Percentage					
Reliance Percentage		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	less than 30%	26	56.5	56.5	56.5
	From 30% to less than 50%	17	37.0	37.0	93.5
	From 50% to less 70%	3	6.5	6.5	
	Total	46	100.0	100.0	100.0

The above table, shows that most of the external auditors responsible for bank's audits in Sudan (93.5%, 43 From 46 EA) were putting reliance less than 50% on the work of internal auditor in the banking sector of Sudan. Also, only 6.5 % of the external auditors were relying on internal auditor's work from 50% to 70% in terms of reliance on the work of internal auditors. Furthermore, there are no auditors among the respondents relying on the work of internal auditors more than 70%.

Further analysis indicates that, One-Sample test result gives the t-statistic of -21.586 with 45 degrees of freedom. The corresponding two-tailed p value is 0.000. If we take the significance level of 5%, we can see that the p value obtained is less than 0.05. Therefore, we can reject the hypothesis at $\alpha = 0.05$, which means that the sample mean (2.8772) is significantly different from the hypothesized value (4.45) and the average level of the reliance in question is not the same as the average of the optimal level of the reliance at the 5% level of significance. Tables 4 and 5 provide the results of one sample tests.

Table 4 : One-Sample Statistics

	N	Mean	Std. Deviation	Std. Error Mean
External Auditors' Reliance Degree	46	2.8772	49419.	07286.



Table 5: One-Sample Test

	Test Value = 4.45					
	T	Df	Sig. (2-tailed)	Mean Difference	95% Confidence Interval of the Difference	
					Lower	Upper
External Auditors' Reliance Degree	-21.586	45	.000	-1.57283	-1.7196	-1.4261

5.2: Factors influencing reliance degree:

According to the literature reported above, professional auditing standards allow reliance on the work of internal audit subject to an assessment of the internal audit function (ASA 610, 2009; ISA 610, 2010). Both Australian and international standards require the external auditor to consider three key factors when assessing the reliance on internal audit work. These three factors are:

- (1) Internal audit objectivity in terms of the status and reporting lines of the internal audit function;
- (2) The technical competence of internal audit staff;
- (3) Their exercise of due professional care

Similarly, US standards require consideration of the competence, objectivity and work performed by IA as the three key components of internal audit quality (AU Section 322 (AICPA, 2010); PCAOB, 2010).

Many previous researches used the three factors when assessing external auditor's reliance on the work of internal auditors, for example (Schneider (1985a), Schneider (1985b), Edge and Farley (1991), Krishnamoorthy (2002), Al-Twajjry et al (2004), Suwaidan and Qasim (2008) and Desai et al. (2010).

From the above discussion, the study hypotheses can be formulated as below:

H2: 'Internal auditors' objectivity, competence, and work performance are significant determinants of the external auditors in Sudan.

This hypothesis will be tested and discussed after presenting the results of each scale individually.

5.2.1- Scale 1: Internal Auditors' Objectivity (IAO):

Table 6 : internal auditors objectivity: One-Sample Test

Factors	Test Value = 3.85				
	t	Df	Mean	Sig. (2-tailed)	Mean Difference
1- Organizational status	-6.221	45	2.93	.000	-.915
2- Management interference in internal auditing work	-12.334	45	2.20	.000	-1.654
3- Freedom to review any area in the bank	-4.268	45	3.11	.000	-.741
4- Board of directors enhancement of internal auditors	-6.478	45	2.74	.000	-1.111
5- Internal auditor revision of previous work.	-14.257	45	2.17	.000	-1.676
6- Conflict of interest	-8.552	45	2.59	.000	-1.263
7- Relationship with executive management	-18.510	45	1.76	.000	-2.089
8- Appointment of internal auditing directors	-16.395	45	1.98	.000	-1.872
9- Removal of internal auditing directors	-17.216	45	1.83	.000	-2.024
10- Reporting times in the year	-12.224	45	2.15	.000	-1.698
11- Position of internal audit department in the organizational structure	-13.827	45	2.09	.000	-1.763
12- Reporting level	-10.561	45	2.26	.000	-1.589
13- Free access to information	-2.193	45	3.48	.034	-.372
14- Free access to employees	-1.114	45	3.70	.271	-.154

Statements 1-3 mean scores (2.93, 2.20 and 3.11 respectively indicated that external auditors accepted the organizational status of internal audit departments in Sudanese banks as adequate for their job. Although the results did not reflect the majority of the respondents accepted these statements, but the fact is that all of the banks investigated have an internal audit department headed by a director. In addition to that the results suggested that the respondents perceive that the internal auditing staff have freedom to carry out their work freely and objectively without any interference of



the management of the bank (statement No.3, mean score 3.11), however, this situation was in line with responses to statements No.13 and 14 which suggests that the internal auditing staff has the free access to information and employees (mean score 3.48 and 3.70 respectively). However, the above statements showed that the internal audit departments in these banks have the organisation status in terms of department existence in the management hierarchy and their ability to conduct their work freely and objectively and the freedom to review any departments of the bank.

External auditors auditing Sudanese banks believe that the internal audit departments are under the authority of executive management, statement no, 7 mean 1.76). This was not surprising when the study found that most of the internal audit directors reported that the reporting level of the internal audit department is the chief executive director of the bank (statement No.9, mean 2.26) not the board of directors, who receives regular reports from the internal audit director.

Questions (No. 8 and 9 mean 1.98 and 1.83 respectively), appointment and removal of internal audit directors. Results indicated the board of directors (audit committee) were not involved in approving the appointment and removal of internal audit department directors. This situation may affect the decisions of the internal audit departments and its objectivity as a whole. Previous studies suggested that this decision should be one of the board of directors and its audit committee decisions, for example (Joseph and Raghunandan 1994 and Scarbrough et al. 1998).

In conclusion, eleven statements of fourteen statements of objectivity scale have mean score less than 3.00 and overall mean of the scale was (2.5096, see table 9). The results of means for objectivity indicated that external auditors of banks were between neutral and dissatisfied for objectivity variables for internal audit departments of Sudanese banks especially with the statements no (7,8 & 9).

5.2.2- Scale 2: Internal Auditors' Competence (IAC):

Table 7: internal Auditors' competence: One-Sample Test

Factors	Test Value = 3.85						
	t	Mean	df	Sig. (2-tailed)	Mean Difference	95% Confidence Interval of the Difference	
						Lower	Upper
1- Knowledge to carry out responsibilities	-4.830	3.09	45	.000	-.763	-1.08	-.44
2- Skills to carry out responsibilities	-5.525	2.93	45	.000	-.915	-1.25	-.58
3- Management encouraging internal audit staff to continually develop	-10.771	2.52	45	.000	-1.328	-1.58	-1.08
4- Internal audit staff holding professional certificate in auditing	-22.062	1.70	45	.000	-2.154	-2.35	-1.96
5- Availability of internal auditors with certificate in internal auditing	-22.186	1.63	45	.000	-2.220	-2.42	-2.02
6- Appointing internal auditors with accounting and auditing qualifications	-12.824	2.13	45	.000	-1.720	-1.99	-1.45
7- Internal auditors training	-11.972	2.52	45	.000	-1.328	-1.55	-1.10
8- Experience in auditing profession	-16.237	2.13	45	.000	-1.720	-1.93	-1.51
9- Experience in internal auditing	-12.800	2.43	45	.000	-1.415	-1.64	-1.19
10- Staff professional competence	-1.449	3.72	45	.154	-.133	-.32	.05
11- Internal audit staff relations with other employees	-8.633	2.54	45	.000	-1.307	-1.61	-1.00
12- Board of directors manage the competence of internal auditors	-10.309	2.50	45	.000	-1.350	-1.61	-1.09
13- Appointment of experienced internal auditors	-11.027	2.41	45	.000	-1.437	-1.70	-1.17
14- Allocating employees from other departments to internal audit department	-11.027	2.41	45	.000	-1.437	-1.70	-1.17

Some previous studies highlighted that the competence of internal audit departments can be measured by qualifications, training, education and experience. (For example, see Messier and Schneider 1988, Tiessen and Colson 1990, Maletta 1992 and Krishnamoorthy 2002).



Regarding the first two statements that the internal audit department possesses the general knowledge, skills and discipline to carry out its responsibilities (means 2.09 and 2.93 respectively), results give impression that respondents were not highly satisfied with knowledge, discipline and skills of internal auditing staff.

Statements 3 to 9 addressed the issues of qualifications, training and education of internal audit department's staff in Sudanese banks. External auditors were disagree with these statements (see table 7, means values from 1.63 to 2.43). Regarding the qualifications of internal auditors, it can be argued that respondents disagree with the statement that implies the bank management only appoints internal auditors with accounting and management qualifications (mean 2.13). From an open question in the questionnaire, external listed the following problems that facing the competence of internal auditors in Sudanese banks. Firstly, management of banks do not hire professional internal auditors. Second, bank's management do not provide a separate job structure for internal audit staff, an internal auditor can be transferred to the internal audit department from any other department in the bank (rotation of employees within the departments of the bank). However, the concept of professional skills and competence in auditing profession must include a wide range of technical skills. As a result, the auditor must be qualified to understand the criteria used and competent to understand the amount and types of evidence used to reach the proper conclusions (Siddiqui and Podder 2002).

One of the strength of internal auditors in Sudanese banks that they maintain satisfactory relationships with other employees in the bank that facilitate their access to employees and bank records (question 10, mean 3.72).

Finally, the overall mean for competence variables (2.5102, see table 9) revealed that external auditors responsible for bank's audits were between neutral and dissatisfied for competence variables for internal audit departments. It seems that the respondents have some concerns about the competence of internal audit departments. Statements No (4, 5, 6) – concerned with the educational qualifications of internal auditors- reported the lowest means in the scale.

5.2.3- Scale 2: Internal Auditors' Work Performance (IAWP):

This scale addressed three main issues, work performance, monitoring of internal controls and risk management. Taking the highest means in this scale, statement no. 1 attempted to test the role of internal audit department directors in supervising their staff, (mean score 3.54). It seems that the internal audit departments in the banks are well supervised and the directors of internal audit departments have the ability su-

perverse and control their staff. Statement no. 19 (mean score 3.67) addressed the role of internal auditors in evaluating the internal control system in Sudanese banks. The respondents believed that the internal audit departments have the ability to evaluate the adequacy of the internal control system and to ensure that the financial controls are in place which strength the financial reporting. However, one of the functions of the internal auditors in the banks is to ensure that the financial controls are implemented properly.

5.2.3- Internal Auditors' work performance (IAWP):

Table8: Internal auditors work performance: One-Sample Test

	Test Value = 4.36						
	T	Mean	df	Sig. (2-tailed)	Mean Differe- nce	95% Confidence Inter- val of the Difference	
						Lower	Upper
1- Supervision of internal auditing staff	-5.638	3.54	45	.000	-.817	-1.11	-.52
2- Number of internal auditors to the number of branches audited	-18.424	2.26	45	.000	-2.099	-2.33	-1.87
3- Existence of audit schedules for branches/departments audits	-9.215	3.22	45	.000	-1.143	-1.39	-.89
4- Existence of appropriate audit plans for established audit objectives	-11.067	2.89	45	.000	-1.469	-1.74	-1.20
5- Examination of reliability and integrity of information	-8.469	3.26	45	.000	-1.099	-1.36	-.84
6- Revision of adequacy of risk management regularly	-10.449	2.83	45	.000	-1.534	-1.83	-1.24
7- Operating system complied with policies and regulations	-9.424	2.96	45	.000	-1.403	-1.70	-1.10
8- Operation results are consistent with the bank objectives	-10.222	2.83	45	.000	-1.534	-1.84	-1.23
9- Corrective actions on the internal auditors finings	-8.737	3.11	45	.000	-1.251	-1.54	-.96
10- Applying the same rules for all levels of banks	-10.549	2.74	45	.000	-1.621	-1.93	-1.31
11- Checking working papers quality	-9.374	2.98	45	.000	-1.382	-1.68	-1.08
12- Checking the adequacy of internal control system.	-9.687	2.93	45	.000	-1.425	-1.72	-1.13
13- Safeguarding the bank assets	-8.141	3.13	45	.000	-1.230	-1.53	-.93
14- Monitoring the financial controls to ensure reliability of financial reporting	-9.429	3.11	45	.000	-1.251	-1.52	-.98



	Test Value = 4.36						
	T	Mean	df	Sig. (2-tailed)	Mean Difference	95% Confidence Interval of the Difference	
						Lower	Upper
15- Checking the financial controls	-9.710	3.07	45	.000	-1.295	-1.56	-1.03
16- Regular evaluation of risk management procedures	-11.513	2.63	45	.000	-1.730	-2.03	-1.43
17- Understanding the nature of operational controls	-10.313	3.00	45	.000	-1.360	-1.63	-1.09
18- Compliance controls are in line with laws and regulations	-10.629	2.98	45	.000	-1.382	-1.64	-1.12
19- Evaluation of internal controls	-5.057	3.67	45	.000	-.686	-.96	-.41

Statement No. 1 attempted to test the role of internal audit department directors in supervising their staff, however, respondents agreed with the statement (3.54). To some extent, it seems that the internal audit departments in banks are well supervised and the directors of internal audit departments have the ability supervise and control their staff, this is supported by the statement No. 3 that external auditors agreed that the internal audit departments are maintaining audit schedules to audit the departments of the bank and other branches (3.22). This was in line with the statement No. 4 which tested the appropriateness of audit plans for established audit objectives, participants agreed with this statement in terms of implementation of internal audit plans.

In the area of internal controls and safeguard of bank's assets, the majority of respondents between (mean 2.93 to 3.67) were not highly satisfied with the statements 12, 13, 14, 15, 17, 18 and 19. However, external auditors believe that the internal audit departments should have the ability to evaluate the adequacy of the internal control system and to ensure that the financial controls are in place which strength the financial reporting.

Finally, the overall mean for work performance variables in Sudanese banks (2.9637 see table 9). This revealed that external auditors responsible for bank's audits are not highly satisfied with the work performance of internal audit departments although work performance scored the highest overall mean of the three variables.

5.3 Overall evaluation and rating of objectivity, competence and work performance:

Table 9, gives statistical results for the variables objectivity, competence and work performance. This table will present the overall mean scores for external auditors regarding their evaluations of objectivity, competence and work performance in Sudanese banks.

Table 9 : Summary of One-Sample Statistics and One-Sample Test

	T	mean	Test Value	Mean difference	(Sig. (2-tailed)
Objectivity	18.452 -	2.5096	3.85	-1.34043	000.
Competence	-22.226	2.5102	3.85	-1.33978	000.
Work performance	-16.230	2.9637	4.36	-1.39630	000.

Regarding the external auditor's evaluation of internal auditor's objectivity, competence and work performance, statistical analysis of the three factors revealed a significant difference between the variables ($p < 0.000$) (see table 9), thus the hypothesis is rejected.

The objective of this part is to examine how external auditors responsible for bank audits in Sudan evaluated objectivity, competence and work performance of internal audit departments. In other words, how external auditors rated the three factors according to the degree of importance. In fact, if the internal audit department staff perform their work objectively, competently and perform their work properly then they are likely to be capable of contributing to an effective internal audit (Al-Twaijry et al 2004).

Many previous researches have been conducted to examine the external auditors' reliance decision on the work of internal auditors. Most of these studies have examined external auditors' general evaluations of the internal audit quality and their decisions to rely on the prior work of internal auditor using the three factors used in this study (for example, Brown 1983; Schneider 1984, 1985, Margheim 1986; Messier and Schneider 1988; Krishnamoorthy 2002; Haron et al 2004; and Al-Twaijry et al 2004). Few studies have addressed auditor's decisions to use internal auditors as assistants in conducting the internal audit (for example, Ward and Johnson 1980; Wagonor and Ricket 1989; Maletta 1993; and Haron 1996).

According to the results in Table (6), work performance was found to have a significant impact on the reliance decision of external auditors to use the work of internal auditors in Sudanese banks. In other words, external auditors evaluated work performance as the most important factor when they rely on the work of internal auditors followed by objectivity and competence. Comparing this result with the results of overall means of the first three scales, it seems to be logical and consistent that the evaluations of both internal and external auditors in the first three scales indicated the same result in terms of their evaluations of objectivity, competence and work performance.



This result is consistent with Brown (1983) study that found that work performance was the most important factor followed by objectivity and competence. Schneider (1984) found work performance as the most important determinant in evaluating internal audit departments, competence rated as second and objectivity as third. Comparing this result with the study result, it seems that the two studies rated work performance as an essential one but with differences regarding competence and objectivity. Schneider (1985b) used an additive, compensatory model for the same variables and found the same rating (work performance, competence and objectivity) which were consistent in a way with the study results.

The study result was not consistent with (Messier and Schneider 1988; Peacock and Pelfrey 1989, Edge and Farley 1991 and Maletta 1993) who took competence and objectivity as the most important factors followed by work performance.

In a recent study conducted in Jordan Suwaidan and Qasim (2010) found objectivity is the most important factor considered by external auditors followed by competence and work performance, which was not in line with the study results.

In Al-Twaijry et al (2004) study in Saudi corporate sector, the study found that external auditors tend not to endorse the current practice of external auditing and expressed particular concerns about the independence, scope of work and the small size of many internal audit departments. In this study external auditors expressed many concerns regarding internal auditor's objectivity and competence.

Comparing these mean results with the results in table 3 which indicated that 93.6% of the external auditors do not rely on the work of internal auditors (reliance degree less than 50%), this comparison seems to be logical and consistent.

5.4 External auditor's type and the reliance degree:

External auditors in Sudan divided into two categories, auditors practicing in private audit firms and General Auditor's Chamber auditors (GAC). Both of them are practicing external audit profession for banking sector in Sudan. However, General Auditor's Chamber auditors are responsible for the audit of banks owned or partially owned by the government.

The third Hypothesis formulated to investigate which sector has more reliance on internal auditors' work in the banking sector in Sudan.

H3: There is a significant difference in the variation of judgment (reliance degree) between private external auditors and public external auditors in bank sector of Sudan.



Table 10: Reliance level * Auditor’s Sector Crosstabulation

Reliance level * Auditor’s Sector Crosstabulation						
less than 30% From 30% to less than 50%			Reliance level			Total
			From 50% to less 70%			
Auditor’s Sector	Private Auditor	Count	14	5	1	20
		within Sector %	70.0%	25.0%	5.0%	100.0%
	Public Auditor	Count	12	12	2	26
		within Sector %	46.2%	46.2%	7.7%	100.0%
Total		Count	26	17	3	46
		within Sector %	56.5%	37.0%	6.5%	100.0%

Table 10 presented external auditors reliance on the work of internal auditors according to auditor’s sector. However, 56.5% of the participants in both sectors expressed very low degree of reliance (less than 30%), while 37% showed reliance degree between (30%-50%), While only 6.5% expressed some degree of reliance on the work of internal auditors.

The statistical test can be used to find out the variances between both types of auditors in Sudan is ANOVA.

Table 11: correlation between sector type and dependence degree

Correlations			
		Sector	Dependence Degree
Sector (Private & GAC auditors)	Pearson Correlation	1	.213
	Sig. (2-tailed)		.155
	N	46	46
Dependence Degree	Pearson Correlation	.213	1
	Sig. (2-tailed)	.155	
	N	46	46

From the above table, it is clear that the relationship between the external auditor’s type (private or public) and the reliance degree on the internal auditor’s work in banking sector of Sudan is positively weak (Correlation Coefficient is 0.213 \ p>0.05). So, these results suggest that the reliance level of external auditor’s on the work of internal auditors in the bank sector of Sudan is not influenced by the external auditor’s type (private or public auditor).

Considering this result, it can be argued that qualified auditors in Sudan are usually



members of professional bodies such as UK, USA bodies and Sudanese Council of Certified Accountants. These bodies have strict Codes of Conduct and Ethics that require their members to comply with

6- Conclusion:

This study aimed at examining the relationship between internal and external auditors in Sudanese banks in terms of relying decisions placed by external auditors on the work of internal auditors. Three factors were used to test the reliance degree, these factors are objectivity, competence and work performance.

Regarding objectivity (independence) of internal auditors, the results revealed that the reporting level of internal audit departments was found to a significant determinant of objectivity, and that the higher reporting level, the higher objectivity. Furthermore, the process of appointing and removing the director of internal auditing was heavily affecting the independence of their departments that the involvement of bank-managing directors was very clear.

Internal and external auditors considered the competence of internal audit departments as the weakest factor. Lack of training, inexperienced staff and quick turnover of internal audit personnel were the main problems affecting the competence of internal audit departments.

In the area of work performance, the study found that the respondents were satisfied to some extent with the work performance and monitoring of internal control procedures, but some banks reported shortages in their staff that may affect the banks' performance.

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