Auditor Independence in Government Parastatal in Nigeria

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ABSTRACT

The objective of this study is to ascertain the determinants of auditor independence in government parastatal in Nigeria. The study employed ordinary least square regression technique to analyse the data gathered from the field. The results show that ethical consideration has negative relationship with auditor independence while rendering of non-audit has positive relationship with auditor independence. This study recommended that statutory bodies should formulate policies that will not forbids an external auditor from rendering audit and non-audit services to the same client. The study also recommended that audit engagement should be base on competence and not on political affiliation of the auditor.

Keywords: Determinants, auditors, independence, perceptions and opinions.

INTRODUCTION

One of the vital aspects of public sector finance in Nigeria is the concern of government financial reports. It is nevertheless gloomy to point out that a lot government parastatal do not maintain proper financial records. This abnormality unlocked the door for the high level of corruption that becomes the order of day in the public sector today. Anecdotal evidence reveals that wealth is unevenly distributed in most emerging economies and they do not have good infrastructural and social amenities due misappropriation of funds by some duplicitous civil servants. The need for accountability and probity in the public sector has attracted the attention of researchers in modern times. These abnormalities can be attributed to weak audit process and slack internal control. Nwaorgu (2003) and Johnson (2004) argue that auditors in the public sector ought to be objective when performing their duties in order to ensure that government funds are properly appropriated and also to ensure that accounts have been properly prepared. Some scholars are of opinion that lack of regular audit exercise coupled with impaired auditor independence in the Nigerian public sector created the loophole through which fraudsters siphon money from public treasury.

Izedonmi (2009) opines the separation of the electorate from those elected into various offices in public sector can be liken to the separation of the shareholders from the board in the private sector. The author further stresses that it is expedient for government parastatal to periodically prepare account of stewardship but this is not being case in real life. Osisima (2013) asserts that audit is one of the mechanisms for checkmating the activities of fraudulent of public office holders. However, event revealed that most government agencies are not audited periodically. A good example of this is the Nigerian National Petroleum Corporation which events revealed to Nigerians that it has not been audited for pass 10 years.

In an attempt to enhance credibility and transparency of the financial system and accounts prepared by management, auditor's independence becomes imperative. This will enable the auditor to give objective audit opinion on the financial statement placed before him. Okoli (2007) opines that auditor independence is the heart of the any meaningful audit exercisebecause it gives credibility to audit report. The quality of any audit report is a function of the independence of the auditor.

Some scholars argue that connection of auditors with politicians has been a major factor that affects auditor independence in the public sector. Kershaw (2006) reports that the recent evolution of audit firm revenue streams has provided auditors with a substantial incentive to compromise their independence and provide management with credible sanctions to mount pressure on them to do so. Kleinman and Palmon (2001) assert that the personal features that affect auditor independence audit judgment include; individualisms, incentives, ethics, phase of life/profession, and extent of ambition. While organisation-ranking features include; traditions of the firm, configuration of the firm and checks and balance mechanisms and the most important factor is the macro-ranking feature which comprises the client's controlling power-broad ecological factors and the duration of client/auditor relationship.

The audit failures that took place across globe have put auditor independence in the accounting spotlight in recent times and have also made it subject for discuss in auditing researcher. (Otusanya & Lauwo, 2010). The confidence placed on audit report depends ultimately on the user's perceptions of the credibility of the auditor. Credibility of the auditor is a function of the auditors' independence.

Previous studies focused mainly on audit in the private sector, while few studies looked at audit and corruption in the public sector. However, nothing was mentioned about factor that effect the credibility of the auditor in the public sector. This study is different from previous because it focuses on the determinants of auditor independence in government parastatal in Nigeria.

Literature Review

The meaning of audit independence is essentially based on theoretical construct. Audit independence is the absence of interests that create an intolerable threat of significance prejudice with respect to the reliability on the financial statements (Shuetze, 1994). Auditor independence is the feature that is concerned with the auditor's readiness to report areas where laid down principles are violated when they are discovered. This suggests that independence of the auditor is synonymous with impartiality and his capacity to refuse to give in to pressure mounted by client on him to report poor quality financial report as quality financial report. Shuetze (1994) argues that independence is an abstract concept, being defined by a state of mind partly synonymous with honesty, integrity, courage and character. This definition has the mark of statistical concepts. In statistical sampling, one is required to be familiar with the assurance level and the accuracy of objects being investigated at intermission because they stand for the bias risks and the materiality bias respectively of the audit exercise. It is importance for the auditor to be acquainted with both the likelihood of an event taking place and the enormity of the effect when it occurs in order to know the risk it represents.

The definition of independence places no limit on the types of concern that can form bias opinion. The concern could be financial or nonfinancial, as in the situation where a family member of the auditor is a director in the auditor's firm. In clear terms biasness could be motivated by monetary or psychological rewards.

De Angelo (1981) defines auditor independence as the unconditional chances of an auditor disclosing any mistake in financial statements knowing that this mistake has previously been spotted out. Soltani (2007) defines auditor independence as the ability of the auditor to uphold an impartial and unprejudiced mind-set throughout the engagement while Hayes, et.al (2004) defines auditor independence of the auditor as a situation whereby the auditor is in a position to take an unbiased viewpoint in the performing an audit tests, analyzing the results, and reporting the analyzed results objectively. Furthermore, Arens, et.al (2012) report that auditor independence requires an attitude of responsibility that is separate from the client's concern. The auditor must uphold an approach of healthy professional scepticism.

Schuetze (1994) defines audit independence as the ability of the audit to refuse to give in to client's pressure. Knapp (1985) reports that auditor's independence is an attitude/state of mind. Magill and Previts, (1991) define auditor independence as the nonexistence of interests which generates an intolerable threat of being influenced. ISB (2000) defines auditor independence as auditor's ability to give an opinion that is influenced by external parties and is aptitude to refuse to submit to pressures that will make him to compromise audit ethics. Moizer (1991) argues that the independence of the auditors depends on his personality and his manner of mind. Only those who uphold deontological outlook to life and consider acting in a particular way as being compulsory undermining the consequences that may arise as a result acting in that way are said to be independence in the mind.

According to Dunmore and Falk (2001) all the definitions given in extant literature reflect the significance of objectivity (ability to restrain oneself from being biased) and integrity (eagerness to give a judgment that truthfully reflects the assessment of what was discovered during the audit) as these two factors are the major components of auditor independence. Extant literature suggests that independence is not in absolute term but rather exists in levels.

Employing Kohlberg's (1969) stage model of moral improvement and ethical cognition, Ponemon and Gabhart (1990) find out the thinking pattern of the auditor when he is resolving a conflict that arises from independence. Their finding unveils the existence of reasonable relationship between hypothetical and ethical cognition (ethical cognition is used as a proxy for auditor independence). Their study further shows that unbiased audit opinion is directly related to features that lead to punishment and partially related to attachment features. The author in addition, elucidates that the auditor's ethical cognition is correlated with the methodical preference of the auditor on rating the variables that affect his unbiased judgment. The authors use the model to validate the four levels of ethical cognition namely: first, pre-conventional level of ethical cognition is categorized by freedom from pressure to retain client and presence of legal liability that is appreciably higher than the subjects at the conventional level. Second, pre-unconventional, a situation whereby the individual sets self-interest well above the general interests of society and is responsive to penalty elements. Third, conventional- a situation whereby the individual conforms to the rules of society and is receptive to affiliation attributes; and fourth, post-conventional. A situation whereby the individual expresses an opinion that is in line with ethical principles and not to society's rules.

Windsor and Ashkanasy (1995) replicate the work Ponemon and Gabhart (1990) works by inculcating both individualism and financial gains into the existing model. This model helps to classify auditor into three groups namely: accommodating auditor – auditor in this category aligns with individualism and respond to both individual beliefs and client management supremacy; autonomous auditors- these category of auditors strictly uphold individualism and align themselves with client management supremacy with caution; and pragmatic auditors- auditors in this category are those who by no mean submit themselves to client management supremacy. The types of auditors aforementioned simply explain the degree at a person is receptive to low, mid and high moral reasoning in that order.

An auditor does not only have to be independent in fact, but independent in appearance also. Woolf (1978) noted that to proffer solution to the issue of audit independence, the auditors should be allowed to discharge their duties without any fear or intimidation or threat in removal attempt from the directors. The auditor will be independent only when he is assured that his job security is beyond the Directors. De Angelo (1981) opined that the ability of the auditor to avoid biases has to do with his integrity and willingness to report a truthful opinion that captures the issues discovered in the course of the audit. Therefore, Ayvaz and Pehlivanli (2010) are comfortable with the fact that objectivity or independence of mind is crucial in order to have a professional judgment. According to Gupta (1999), if an auditor is not independent of management, his opinion would mean nothing to shareholders, prospective investors, bankers, government agencies, and others who are concerned with the financial statement of the company.

Ye Carson and Simnett, (2006) opine that the economic dependence of auditors on non-audit services, lengthy audit tenure and personal relationships built through alumni employees have contributed to the erosion of auditor independence. The work of Hayes, et al. (2005) suggests that there exists a potential for the impairment of auditor independence in appearance when they render non-audit services.

Sharma (2006), and Sharma and Sidhu (2001) are of the opinion that for us to proffer solution to the issues of auditor independence, it is necessary to verify the opinion the auditor ought to have given as compared to the actual opinion eventually given. If it discovers that the auditor ought to have given a qualified audit opinion, but gave a clean opinion; the brain behind the deviation could be traced to independence impairment after controlling for other explanations.

Numerous threats attributed to auditors' independence discovered may include; self - interest, advocacy, familiarity, and intimidation (Erah &Izedonmi, 2012).Blay (2005) finds out that auditors that are exposed to high independence threats (loss of client fear) were more likely to suggest an unmodified audit report which is consistent with client preferences. In contrast, auditors facing high litigation risk evaluated information as more suggestive opinion of a failing client, and were more likely to advocate modified audit report.

The risks of punishments have been shown to enhance audit independence; risk of damage to auditor's reputation, disciplinary action by government, litigation against the auditor, and disciplinary action by the professional associations. While efforts are being made to address the lapses in the audit systems in developed countries, there have been little or no efforts at positively addressing the challenges posed by non-adherence to corporate governance principles and ethical guidelines in developing countries (Adeyemi & Fagbemi, 2011).

Quick and Warming-Rasmussen (2005) found that German investors perceived non-audit services to impair audit independence. Ojo (2009) argues that the provision of non-audit services does not necessarily impairs auditor independence especially when the fees from such services are less than the fees from audit services

In terms of ethics, Gowthorpe and Amat (2005) conclude that the breach of ethical considerations in the practice of corporate financial reporting is not fair to users and such action can jeopardize the main objective of the reports. As an integral part of the corporate financial statements, auditor's report is required to clearly state whether the financial statements are true and fair or not.

Methodology

The study used primary source. The primary source consisted of information we elucidated directly from the sampled auditors through the administration of questionnaires. Questionnaire was administered to 125 civil servants in selected government parastatal in Abuja. The survey instrument utilized in this study was adapted from the one used in many studies of the perceptions of auditor independence in previous studies (Uchenna & Young 2012; Alleyne & Devonish, 2006; Al-Ajmi, 2010). The statements were adapted to suite the unique characteristics of the Nigerian situation. Thirty-five statements were included in the questionnaire, representing the areas of importance of this study. A Likert type scale was used for this study in which respondents were asked to express their personal views about how the statements on the questionnaire affected auditor independence. The response options are: strongly increases independence, agree undecided, disagree and strongly disagree.

Table 1 Presentation and interpretation of results

REGRESSION RESULT				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	16.34987	1.979015	8.261620	0.0000
CT	0.017254	0.056577	0.304964	0.7608
EC	-0.096974	0.046539	-2.083730	0.0387
NAS	0.085737	0.041793	2.051439	0.0418
LR	0.014272	0.046869	0.304516	0.7611
PCA	0.005518	0.045760	0.120593	0.9042
R-squared	0.752165	Mean dependent var		16.78235
Adjusted R-squared	0.744803	S.D. dependent var		1.968610
F-statistic	5.769219	Durbin-Watson stat		2.120245
Prob (F-statistic)	0.000018			

Source: Researcher's computation (2017)

AIND = 6.349 + 0.017CT -0.097EC + 0.086NAS + 0.014LR + 0.006PCA

(8.2616) (0.3049) (-2.084) (2.0514) (0.3045) (0.1205)

The regression result presented in table 1 show that client threat (CT) has no significant relationship with auditor independence (AIND) as depicted by coefficient value of 0.017 and p-value of 0.761. This relationship is not significant at 5%. The result shows that ethical consideration (EC) has a negative relationship with auditor independence as depicted by coefficient of value of -0.097 and p-value of 0.039. This relationship was significant at 5% level of significance.

Furthermore, the result shows that rendering of non-audit services (NAS) has positive relationship auditor independence as depicted coefficient 0.085 and p-value of 0.042. This relationship is significant at 5%. In the same vein ligation risk (LR) shows a positive relationship with auditor independence. This relationship is not significant at 5%.
Finally, the result shows that political affiliation of auditor has a positive relationship with auditor independence. This relationship is not significant at 5%.

Conclusion and Recommendations

This paper seeks to ascertain the determinants of auditor independence in government parastatal in Nigeria. The study shows that first, client threat has no significant relationship with auditor independence. This implies that any form of threat from client employees has no potential of affecting auditor independence.

Secondly, the result shows that when ethical standards set by professional bodies are violated, auditor independence is drastically impaired. Ethical value, rules, conducts; guidelines and provides the foundation that prevents impairment of auditor independence.

Thirdly, the result shows that rendering of non-audit services has positive relationship with auditor independence. This implies that rendering of non-audit services increases the familiarity of auditor with client hence threat from clients reduces.

Finally, it shows that risk of ligation and political affiliation has no significant relationship with auditor independence. This implies that connection of auditor to politicians does affect the auditor independence.

This study recommended that statutory bodies should formulate policies that will not forbids an external auditor from rendering audit and non-audit services to the same client. The study also recommended that audit engagement should base on competence and not on political affiliation of the auditor.

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Table 1: Questionnaire

	Question
	Bio data
1	Gender
2	Age
3	Educational Qualification
4	Years of Auditing
5	Audit of Government business entity
	Statement Questions
6	Auditor exercising credibility in auditing can influence auditor independence
7	Accountability of the auditor enhances independence
8	Transparency and integrity in undertaking of audit function influences auditor independence
9	Objectivity of the auditor has effect in determination of audit independence
10	When auditor is no longer trustworthy and fair in judgement can impair independence
11	Undue independence of the auditor on the client affects auditor independence
12	Auditor or audit team benefiting from the client financial interest has effect on auditor independence
13	The auditor or audit member previously being a top officer of government business to be audited can affect auditor independence
14	An auditor having close relationship in government enterprise to be audited has effect on auditor independence
15	Restriction, safe guides and policies of government enterprises have effect on auditor independence
16	Introduction of auditor section in Companies and Allied Matters Act on businesses was to facilitate auditor independence
17	Nigerian standards on auditing are aimed at ensuring auditor independence
18	Rules on professional conduct were to enhance auditor independence
19	Auditing guidelines and standards can influence auditor independence
20	Application of moral values in auditing in government business entity can influence auditor independence
21	Non-audit services by big 4 auditor government businesses can impair auditor independence
22	Non-audit services by local auditor to government businesses can impair auditor independence
23	Level of audit market competition on non-audit services to government businesses entityimpair auditor independence

24	The type of non-audit services to government entity has effect on auditor independence
25	High level of audit market competition in non-audit service government entity impair auditor independence
26	Auditor personal interest present risks which can impair auditor independence
27	Action of litigation can have influence on auditor independence
28	Adverse publication about auditor can have influence on auditor independence
29	Auditor report choice has influence on auditor independence
30	Bias in audit reporting pattern of the auditor has influence on auditor independence
31	Politically connected auditors are bias in opinion and can affect auditor independence
32	Politically connected auditors are easily manipulated in auditing government business entity
33	Politically connected auditors in government business entity are subjected in their opinion
34	Politically connected auditors in government business entity are objective in their opinion
35	Politically connected auditors can influence auditor report and its independence

APPENDIX 1

AIND	CT	EC	NAS	RLP	PCA
20	23	21	17	15	11
16	22	24	11	12	12
14	23	23	21	23	22
17	22	25	25	23	20
16	22	25	25	23	21
14	20	20	12	16	17
15	25	24	25	20	12
18	24	24	19	19	22
20	23	18	18	17	17
15	23	18	18	17	17

APPENDIX 3

Heteroskedasticity Test: Breusch-Pagan-Godfrey

F-statistic	3.556744	Prob. F(5,119)	0.0029
Obs*R-squared	2.857239	Prob. Chi-Square(5)	0.0030
Scaled explained SS	2.373221	Prob. Chi-Square(5)	0.0072

Dependent Variable: AIND
Method: Least Squares
Date: 05/08/17 Time: 23:27
Sample: 1 172
Included observations: 172

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	15.38145	2.128610	7.226052	0.0000
CT	0.055302	0.061716	0.896070	0.3715
EC	-0.082804	0.055018	-1.505033	0.1342
NAS	0.066898	0.047287	1.414716	0.1590
RLP	0.041986	0.055848	0.751790	0.4532
PCA	-0.008384	0.050076	-0.167424	0.8672

R-squared	0.474014	Mean dependent var	16.79651
Adjusted R-squared	0.458722	S.D. dependent var	1.973328
S.E. of regression	1.954769	Akaike info criterion	4.212682
Sum squared resid	634.3060	Schwarz criterion	4.322478
Log likelihood	-356.2906	Hannan-Quinn criter.	4.257229
F-statistic	1.652494	Durbin-Watson stat	2.074029
Prob(F-statistic)	0.148912		

Dependent Variable: AIND
Method: Least Squares
Date: 05/08/17 Time: 23:27
Sample (adjusted): 3 172
Included observations: 170 after adjustments
Convergence achieved after 7 iterations

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	16.34987	1.979015	8.261620	0.0000
CT	0.017254	0.056577	0.304964	0.7608
EC	-0.096974	0.046539	-2.083730	0.0387
NAS	0.066898	0.047287	1.414716	0.0418
RLP	0.041986	0.055848	0.751790	0.7611
PCA	-0.008384	0.050076	-0.167424	0.9042

R-squared	0.752165	Mean dependent var	16.78235
Adjusted R-squared	0.744803	S.D. dependent var	1.968610
S.E. of regression	1.820509	Akaike info criterion	4.076414
Sum squared resid	540.2232	Schwarz criterion	4.205535
Log likelihood	-339.4952	Hannan-Quinn criter.	4.128810
F-statistic	5.769219	Durbin-Watson stat	2.120245
Prob(F-statistic)	0.000018		