Impact of Auditor Independence on Accountability and Transparency in Corporate Organizations in Nigeria

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Abstract

The study seeks to examine the impact of auditor independence on accountability and transparency of corporate organization in Nigeria. There are factors that constitute threats to the independence of an auditor. The literature development was guided by the credibility theory, Theory of inspired confidence, Agency theory and the Quasi-judicial theory. The exploratory assessment method was adopted in this study. The study used the secondary method of data collection basically sourced from journals, internet and other relevant publications; which includes a survey of published research. The study had the following research questions: Are there threats to auditor independence that affect accountability and transparency in corporate organizations in Nigeria, How crucial is auditor independence as regards the reliability of financial information reported to the public(stakeholders) and if auditor independence affect audit quality in corporate organizations in Nigeria. The study found out that there are threats or impediments to auditor independence. The independent auditor performs a key function in ensuring that the public (stakeholders) rely on financial report. The study also revealed that audit quality is affected by the auditor independence; increasing the independence of auditor is to contribute to improving the quality of the audit. The study concludes that auditor independence has an impact on accountability and transparency of corporate organization in Nigeria. The study therefore recommends that there should be more framework on auditor independence, study should be carried out on the factors that lead to the threat of auditor independence and how to mitigate them and study should also be carried out on accountability and transparency as it affects audit.

Keywords: Auditor Independence, Accountability, Transparency, Corporate Organizations

INTRODUCTION

Independence is one of the most important attributes of the accounting profession. Investors rely on information from management regarding the financial position of the company. Managers have an obligation to uphold the continuity of the company's profits and growth. Managers thus have their own goals and interest in mind apart from the investors- that is to make the company appear to be in good standing at all times. The investors are interested in knowing the correct position of the company, so they can decide whether or not they will continue to invest in the corporation. Therefore an intermediary is involved (the auditor) to protect the investors from the self-interests of managers. The investors' confidence in the auditor depends on the auditor's credibility on how well the intermediary has been correctly verifying managers' assertions of the financial statements. As a result, auditors have to maintain and appear to maintain their independence at all times. This becomes difficult, because managers are responsible for hiring and firing the auditors under their own authority. This allows the auditors to be influenced because of conflict of interest, and perhaps lose his independence.

Auditing ensures the effectiveness, proper, and economic use of resources in the organization through the objective examination, evaluation and reporting on the adequacy of internal control. The effectiveness of the auditing function lies on its independence. The independence in terms of organizational status and personal objectivity of the internal auditors facilitates the proper and effective performance of his duties. Also, there are changes in globalization in general which carries significant influence on the development of the world's economy. This change is a change in the external business environment that is pressing the company to be able to produce strong competitiveness so as to receive the benefit of globalization. Investors from various countries can invest in other countries that provide better returns by studying and analyzing the relevant information before making an investment decision. And one of the relevant information is the financial statement. For the financial statement to be trusted, an audit is very necessary, so also is the independence of the auditor and also the accountability and the transparency of the corporate organization. According to Saputra (2015), auditing is the accumulation and evaluation of evidence about information to determine and report on the degree of correspondence between those assertions and established criteria. As cited by Okafor, C. N. (2012), auditing is the systematic process by which a competent, independent person objectively obtains and evaluates evidence regarding assertions about an entity or event, for the purpose of forming an opinion about and reporting the degree to which assertion conforms to an identified set or standards. Also, Izedonmi(2000) defined auditing as an independent examination of the financial statement of an enterprise by an appointed person called auditor, in order to express as professional opinion whether or not those financial statement show true and fair view of the financial period in accordance with the auditor's term of engagement as well as other relevant statutory and professional regulations.

Audit refers to an examination of the financial report of a firm by an independent entity. The separation of business ownership and management in modern society has created a need for accountability; causing the role of audit to change as the needs of stakeholders' change. Audit in itself caters to the relationship of accountability, independent from other parts of the firm to provide a true and fair view of the financial report of an organization. Whereas the 'value relevance' refers to the auditors' ability and responsibility to provide reasonable assurance that financial statements are free of material misstatement, either due to fraud or error; or both. Auditing was also seen and defined by many "as a review of a statement of account prepared by the appointed officer of an organization or by some other persons"(Okolo,2001). In other words, an auditor's objectivity must be beyond questions when conducting an audit. Hence the approach of an audit work must be with integrity and objectivity and spirit of independence of mind. According to Arens, A. A. &Loebbecke, J. K.(1997), audit is the process by which a competent, independent person accumulates evidence about quantifiable information related to a specific economic entity for the purpose of determining and reporting on the degree of correspondence between quantifiable information and established criteria. Audits are categorized by purpose, including financial statements audit, compliance audit, and performance audit. According to the International Federation of Accountants (2007), audit is about auditors examining and expressing their opinions on financial statements. Consequently, the main aim of this study will be to examine the impact of auditor independence on accountability and transparency in corporate organization in Nigeria. In order to achieve the objective, the following hypotheses are formulated thus:

Ho 1: There is no significant relationship between threats and auditor independence as it affects accountability and transparency.
Ho 2: There is no significant relationship between auditor independence and reliability of financial information reported to the public (stakeholders).
Ho 3: There is no significant relationship between auditor independence and audit quality in corporate organizations in Nigeria.

LITERATURE REVIEW

Conceptual Framework

Auditor Independence

Independence has traditionally been defined as the ability to act with integrity and objectivity. According to the American Institute of Certified Public Accountants (AICPA 1948) independence, both historically and philosophically, is the foundation of the public accounting profession and upon its maintenance depends the profession's strength and its stature. International Auditing Practices Committee of the International Federation of Accountants (1980), in its International Auditing Guidelines (AG-3), defines the auditor independence in these words. The auditor should be straight forward, honest and sincere in his approach to his professional work. He must be fair and must not allow prejudice or bias to override his objectivity. He should maintain an impartial attitude and both be and appear to be free of any interest which might be regarded, whatever its actual effect, as being incompatible with integrity and objectivity".

Arens (2012) explains that independence requires an attitude of responsibility separate from the client's interest. The auditor must maintain an attitude of healthy professional skepticism.According to BahramSoltani (2007) as cited by Saputra, W.(2015), auditor independence refers to the auditor's ability to maintain an objective and impartial mental attitude throughout the audit. Independence is described as having a position to take an unbiased viewpoint in the performance of audit tests, analysis of results, and attestation in the audit report. Based on the above understanding can be concluded that the independence of the auditor is the auditor's ability to maintain mental attitude objectively and impartially in the interests of the client in conducting the audit, analyzing the results, and attestation in the audit report. Independence Standard Board (ISB) (2000) defines auditor independence as freedom from those factors that compromise, or can reasonably be expected to compromise an auditor's ability to make unbiased audit decisions. ISB does not specify independence questions, but it supplies a structure and methodology for analyzing issues. The need for a framework arises from the jumble of confusing independence rules and regulations. The framework is the product of an open process. A task force of academics, lawyers, audit committee members regulators, auditors and others helped to identify the issues and reviewed for clarity and completeness.

Dimensions of Independence of Auditor

According to Le-Doan (2019), independence is the cornerstone of auditing and is essential for the reliable corporate financial statement. In common with the International Federation of Accountants in Vietnam, independence is defined in the professional ethics of accounting and auditing issued in accordance with Circular 70/2015/TT-BTC dating 8 May2015(VMF, 2015), the Vietnam's Ministry of Finance has classified independence into two parts: independence in fact (real independence) and independence in appearance (perceived independence). Arens et.al (2012), explains that the independence of the auditor is divided into two parts as follows: "independence as consisting of two components: independence in mind and independence in appearance. He also cited that Mautz and Sharaf (1993), stated that the independence of auditors is composed of three dimensions: the independence of the audit program, the investigative independence, and the independence of the audit reporting.

Threats to Auditors Independence

Threats to auditor independence represent pressures or other factors impairing an auditor's objectivity. To be independent, an auditor must be able to overcome the threats that compromise objectivity. Identifying sources of threats help to illuminate their nature and impact on the auditor's independence. Conceptual Framework for Auditor Independence (CFAI) illustrates five potential threats; self- interest threats relating to auditors acting in their own self-interest (such as emotional, financial or personal). Self-review threats arising from auditors reviewing their own work or that of other firm members, as auditors must not audit their own work. Next is advocacy threats which relates to auditors advocating for or against an auditee or its position rather than serving as unbiased attesters of the financial information. Familiarity (or trust) threats is from auditors influenced by a close relationship with an auditee, while intimidation threats are threats from auditors overtly or covertly coerced by auditees or other interested parties. Both the probability and materiality of each threat should be evaluated. The foregoing threats encompass two familiar concepts: "acting in the capacity of management and having a mutuality of interests with the client ". Auditors must not act as managerial decision makers. Auditors must not favor their clients' interests or goals. Instead, they must be watchdogs for the public.

The Vietnam's Ministry of Finance Circular also mentioned some threats affecting the independence of auditors as: self-interest, self-review, familiarity, advocacy and intimidation. While independence of mind is key factor to forming a judgment about the contents of the financial statements, there are threats to auditor's independence that affect their judgment. Impediments to independence are often viewed in terms of financial considerations or personal relationships.In Vietnam, Dang(2011) has found four main factors affecting the quality of services of auditing companies in Vietnam: (1) the auditing firm and client relationship; (2) the process of training and capacity building of auditors; (3) the audit cycle; (4) the effectiveness of the audit process. Other studies have also found the cause of impairment of the values of auditing services in the auditor client relationship. Researches carried out by Nguyen and Ha (2015) have reviewed the views and opinions on the subjects related to financial reports and independence of not only the auditors in Vietnam (but also the accountants, bank creditors and investors) and factors that affect this independence. The authors found that eight factors: (1) non-audit services, (2) audit fees; (3) audit's tenure; rotation of auditor's/audit firms, (5) the auditing committee appointed, (6) the competition in auditing market (7) the size of the auditing companies, (8) the risks of disclosure of financial relationships have different levels of impact that increase or threaten the independence. Recent research by Vo (2016) shows that there are four factors that have the opposite effect (non-audit services, auditing costs, tenure and rotation of auditors) to the independence of the auditor.

Accountability and Transparency

Accountability is all about being answerable to those who invested their trust, faith, and resources to you. Arena (2010) defined accountability as the obligation to demonstrate that work has been conducted in accordance with agreed rules and standard and that officer reports fairly and accurately on performance results vis-à-vis mandate roles and plans. It means doing things transparently in line with due process and provision of feedback. Badara (2012) posits that public accountability is an essential component for the functioning of our political system, as accountability means that those who are charged with drafting and / or carrying out policy should be obliged to give an explanation of their actions to their electorate. Theofanis (2011) observed that the capacity to achieve full accountability has been and continuous to be inadequate, partly because of the design of accountability itself and partly because of the widening rage of objectives and associated expectations attached to accountability. He further argues that if accountability is to be achieved in full, including its constructive aspects, then it must be designed with care. According to Shrivastara (2015), transparency is a process or a mechanism of knowing. Transparency in its literal meaning refers to the state of being easily visible throughout.

Accountability is a concept of varied interpretations. In literal meaning it deciphers to be responsible. Accountability is a channel to reach better amount of transparency. Transparency and accountability are mutually beneficial to each other. Transparency encourages accountability and accountability demands transparency. Transparency is also a necessary precondition for the exercise of accountability since without access to clear, accurate and up-to-date information, it is impossible to judge whether the standard promised has been met. According to MacGee&Gaventa (2010), both transparency and accountability have emerged over the past few decades as being appropriate way to tackle democratic deficits and developmental failures. Based on the developmental framework, multiple arguments have emerged postulating that the " leaky pipes" of inefficiency and corruption could be mended, aid channeled in a more transparent and effective way, and developmental initiatives could lead to the generation of better results through greater accountability from the concerned individuals. MacGee and Gaventa (2010) claim that accountability is the path to empowerment and enhanced effectiveness in the operations of many organizations based on their responses to the needs of the people that they serve.

Concept of Audit Quality

Arenset (2011) as cited by Saputra (2015) defines the quality of the audit to mean how well an audit detects and reports material misstatements in financial statements, the detection aspects are a reflection of auditor competence, while reporting is a reflection of ethics or auditor integrity, particularly independence. Furthermore, The US Government Accountability Office (GAO) (2015) explains the notion of audit quality as an audit conducted in accordance with Generally Accepted Auditing Standards (GAAS) to provide reasonable assurance that the audited financial statements and related disclosures are (1) presented in conformity with GAAP and (2) are not materially misstated whether due to errors or fraud. Public Company Accounting Oversight Board (PCAOB) (2015) defines audit quality as meeting investors' needs for independent and reliable audits and robust audit committee communications. Australian Public Policy Committee (2014) defines audit quality as meeting investors' needs for independent and reliable audits and robust audit committee communications on: Financial statements, including related disclosures; Assurance aboutinternal control; and going concern warnings. Based on the above understanding can be concluded that the quality of the audit conducted in accordance with auditing standards generally acceptable that can detect and report material misstatements in the financial statements include disclosure relating either caused by an error / fault or fraud, is able to provide assurance of internal controls, and capable to provide going concern warnings. IFAC (2015) in the statement of a "a framework for audit quality indicator" describes the dimensions and indicators to assess the quality of audit as follows; Values, Ethics and Attitudes.

Empirical Review

The study carried out by Austin, et al (2014), in a research paper, 'Auditor independence': a review of literature in which they surveyed 16 auditor independence – related research articles, which were published during the time frame of 1992-2010. According to them, selecting this time period proved beneficial and provided astounding insight into the emerging concerns about auditor independence, amidst an increase in scandals which ultimately has led to the economy being forced into recession. Their submission is that, in these times of worldwide recessions and rebuilding of the economy, auditor independence will continue to remain at the forefront of importance to the accounting profession. Auditor independence is crucial to the key information investors and corporations rely for the sustaining of capital market's profit and growth. They added that one factor alone is not the reason itself but just part of the reason; therefore, one factor should not be deemed as the primary cause. They recommended that auditor independent-related research be centered on all factors such as: audit fees, low balling, audit firms hiring clients, non-audit services, and litigation and risks. Findings of Saputra (2015) titled, " The Impact of Auditor's Independence on Audit Quality" : A Theoretical Approach; the study discloses that to carry out an audit in a manner that meets the reasonable expectations of users of audited financial statements, it is essential that work is performed with due regard for audit quality. The quality of auditing is an audit conducted in accordance with auditing standards generally acceptable that can detect and report material misstatements in the financial statements include disclosure relating either caused by an error / fault or fraud, is able to provide assurance of internal controls and capable to provide going concern warnings. The independence of the auditor is the auditor's independence. The independence of the auditor is the auditor's ability to maintain mental attitude objectively and impartially in the interests of the client in conducting the audit, analyzing the results, and attestation in the audit report. It is composed of three dimensions namely programming independence, investigative independence, and reporting independence. Based on theoretical approaches, it can be concluded that audit quality is affected by the auditor's independence, thus the more independent an auditor then increasing audit quality.

Furthermore, Saputra (2015) cited that various theories were put forward by the experts stated that the independence of the auditor affect the quality of the audit include: Ross L. Watts, et al (1986) states that to create a demand for audit services, auditors have to convince the market that they have some competence and they will have some independence from the client. The same thing was also confirmed by Arens, et al (2014) that the value of auditing depends heavily on the public's perception of the independence of auditors. Similarly, David N. Ricchiute (2006) states that in practice, independence is powerfully important to the profession's reputation as a trusted player in the market for audit services. The financial community values the reports of certified public accountants precisely because CPAs are perceived as having no vested financial or personal interest in the outcome of the engagement. Some recent research also said similar thingsabout the impact of auditor independence on audit quality, among others: Enofe, et. al (2013) stated that as auditor independence increase, the quality of the audit also improves. That the same thing was also confirmed by EkoSuyono (2012) stated that independence of auditor and accountability affect audit quality. Similarly, NovieSusantiSuseno (2013) asserts that auditor independence significantly influences the audit quality.

Several researches have come to the conclusion that one of the major factors which affect the auditor independence is the non-audit services, especially MAS. To reduce the effect of the audit independence, one should reduce the restrictions of the audit and non-audit engagements between the accounting firms and their clients as per the proposed regulatory framework which in turn reduces the auditors' incentives leading to the involvement of the audit-client in fraudulent activities. The premise is that auditors need to operate in the framework that discourages immoral behaviors (Gavious, 2007). Furthermore, there are additional regulatory frameworks for the auditors and to establish higher standards for the corporate governance (Rezuee, 2005). Myers (2005) perceived that audit independence was fundamental to the credibility of the profession. The audit independence can be viewed from two angles: (i) Actual independence is the achievement of actual freedom from bias, personal interests, prior commitment to an interest, or susceptibility to undue influence or pressure, and (ii) the perceived independence is the belief of financial report users that actual independence has been achieved. Briloff (1990) observes that the client hires the auditor and pays the fees but the auditor is supposed to conduct the audit in an independent fashion adhering to profession's "covenant with society". The auditor is required to express an opinion on the financial statements as to whether they are presented fairly or not. It is assumed that he or she is independent and acts honestly. Independence is a function of the auditor's mental attitude, and one must look at the various factors which influence the auditor's behavior to determine whether his psychological makeup allows him to be objective, honest and independent. Thus it is necessary to consider the position advanced by behaviorists (Alleyn et al, 2006). The literature has shown that the key factors to be considered include consequentialism and deontology (Moizer, 1997), cognition (Dillard and Yuthas, 1997; Moore et al, 2003) and structurization (Giddens: 1984). The concept of independence envisions both real independence and apparent independence. It is observed that an auditor will be lost if the auditor owns a stock, participates in managerial decision making, is a relative of the member of the board, takes up an executive position or is an employee.

Theoretical Framework

The Lending Credibility Theory

This theory suggests that adding credibility to financial statements is an integral part of auditing, making it a fundamental service auditors provide to clients. Audited financial statements boost users' confidence in an organization's financial records and management's stewardship; in turn, improving their decision quality such as, investment or new contracts, based on reliable information. This is because stakeholders need to have faith in the financial statements would affect decisions by stakeholders (example credit limits provided by suppliers) and also helps shareholders put trust in management, reducing the 'information asymmetry' between stakeholders and management. The credibility theory provides the primary function of auditing to increase the reliability of financial statement, Ittonen (2010), in which the auditor independence provides public trust Beatti, Brandt, &Fearnley (1999). It is fundamental to the existence of auditing (Bakar& Ahmad, 2009) to act in accordance with social expectations (Suchman, 1995). Based on the theoretical view of legality, many studies have shown that when attitudes and social expectations change audit independence should be appropriately adapted within the framework of standards (Deegan, 2006; Lindblom, 1994).

Theory of Inspired Confidence

This theory was developed in the late 1920s by the Dutch Professor Theodore Limperg (Hayes et al; 1999). Limperg's theory addresses both the demand for and the supply of audit services. According to Limperg, the demand for audit services is the direct consequence of the participation of outside stakeholders in the company. These stakeholders demand accountability from the management, in return for their contribution to the company. The auditor's job should be executed in such a way that the expectations of a rational outsider are not thwarted. So given the possibilities of audit technology, the auditor should do everything to meet reasonable public expectations. The relationship of accountability is realized with financial statements; however, as outside parties cannot monitor any material misstatement or bias in financial reports, the demand for an independent reliable audit arises. The supply of audit services should satisfy the public confidence that arises from the audit and fulfil community expectations, as the general function of audit is derived from the need for independent examination and an expert opinion based on findings; due to the confidence society places in an independent auditor's opinion. It can be assumed that if society lost confidence in audit opinion, the social usefulness of audit would cease; as audit delivers benefits to the users of financial statements. The auditor should maintain appropriate business practices to maintain his independence from the firm being audited, in order to satisfy his obligation to examine business practices and provide a credible opinion on the financial statements.

Agency Theory

According to Jensen and Meckling (1976), agency theory analyzes the relationship between two parties: Investors and managers. The agent (i.e manager) undertakes to perform certain duties for the principal (i.e investors) and the principal undertakes to reward the agent. According to this theory, Anderson and Emander (2005) assert that the role of the auditor is to supervise the relationship between the manager and the owners. A gab expectation occurs when the distribution of the responsibility is not well defined. The responsibility of every part is well defined in the regulation. The manager and the owners have to realize that the auditor does not have responsibility of the accounting, but only sees that the auditing is done properly. Donaldson and Davis (1991) argued that in a corporation in which ownership is widely spread, managerial behavior does not always maximize the returns of the shareholders. The degree of uncertainty about whether the will pursue self-interest rather than comply with the requirements of the contract represents an agent risk for an investor. According to Hermanson et al (1993), there are four conditions in the business environment which create a demand for an independent audit – conflict of interest, consequence, complexity and remoteness.

Quasi – Judicial Theory

In this theory, the auditor is regarded as a judge in the financial distribution process (Hayes et al, 1999). However, Porter concludes that (i) an auditor's decisions and decision process are not publicly available; (ii) the doctrine of precedence/consistency is not guaranteed in auditing; and (iii) an auditor's independence differs from a judge's independence because of the different reward system involved.

METHODOLOGY

This study adopted exploratory assessment method by reviewing research work done by other writers in related field. The data for this research study were adequately sourced using the secondary method of data collection basically sourced from journals, internet and other relevant publications.

RESULTS AND DISCUSSION

In conducting this research, data were sourced from relevant publications, internet and from journals. Among others, the work of Austen and Herath (2014) 'Auditor independence: a review of literature', Int. J. Economics and Accounting, Vol. 5, No. 1. It suggests that a wide range of topic areas has been discussed and this learning can be incorporated in revising auditor independence related curricula. Findings from the study revealed that there are threats to auditor independence. This aligns with the study conducted by Austen, et al (2014) that auditor independence is crucial to the key information investors and corporations rely for the sustaining of capital market's profit and growth. The study also revealed that depending on the circumstance and individual, independence can be impaired. Researchers have searched for an explanation as to why an auditor might lose his/her independence. The public's concern for auditor independence became heightened as companies wanted to ensure a company's adherence to professional accounting standards and principles. Summarizing the findings of auditor independence studies conductedin developed countries, such as the United States (Bamber&Iyer, 2007; Blay& Geiger, 2013; Carcello& Nagy (2004), UK (Beattie et al, 1999), and in developing countries such as China (Wu & Ying, 2016); Malaysia (Bakar& Ahmad, 2009,) Taiwan (Chi et al., 2009), Thailand (Boatham & Ussahawanitchakit, 2009), Vietnam (Dang, 2009, 2011; Giang, 2010; Nguyen & Ha, 2015; Vo, 2016), a combination of factors impacting on auditors independence and audit quality such as non-audit services, the audit fee, the relationship between the auditor and the client, the size of the auditing companies and the audit term has been established. Many studies have not been published extensively on the impact of corporate governance on the independence of audit.

These studies have not fully investigated the factors that affect independence through the threat of compromising audit independence: the threat of self- interest, the threat of self-review, and the risk of self-defence, friendly risk, threats and safeguards. These risks and safeguards constitute audit independence. Each risk has many factors. Therefore, it is important to study the factors that lead to the threat of auditor independence. The stakeholders or the public will rely on reported financial information if they believe the auditor is independent of other parties, more specifically company directors. Furthermore, the finding from the study also revealed that auditor independence affect audit quality. This aligns with Saputra (2015), based on his theoretical approaches; revealed that audit quality is affected by the auditor independence. The more independent an auditor then increasing audit quality.NovieSusantiSuseno (2013) asserts that auditor independence significantly influences the audit quality.Duc et al (2015), increasing the independence of auditors is to contribute to improving the quality of the audit.

CONCLUSION AND RECOMMENDATION

In the light of the above, the study concludes that auditor independence has impact on accountability and transparency in corporate organizations in Nigeria. EkoSuyono (2012) states that independence and accountability affect audit quality. The auditor carries out his work freely and in an objective manner and that work is conducted in accordance with agreed rules and standards and the auditor reports fairly and accurately on performance results vis-à-vis mandate roles and plans. The value of auditing depends heavily on the public's perception of the independence of auditors and independence is of utmost importance to the reputation and credibility of the profession. Based on the findings and conclusion drawn from the study, the following recommendations are made:

i. There should be more frameworks on auditor independence so as to ensure more accountability and transparency.
ii. The researcher also recommends that more studies should be carried out on the factors that lead to the threat of auditor independence and how to mitigate them.
iii. Also, study should be carried out on accountability and transparency as it affects audit quality.

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