International Journal of Trend in Scientific Research and Development (IJTSRD)
Volume 3 Issue 5, August 2019 Available Online: www.ijtsrd.com e-ISSN: 2456 – 6470

Appraisal of Audit Independence on Reliance of Financial Report of a Selected Hospital in Awka

Dim Chinwe E

Department of Accountancy, Chukwuemeka Odumegwu Ojukwu University, Igbariam Anambra State, Nigeria

How to cite this paper: Dim Chinwe E "Appraisal of Audit Independence on Reliance of Financial Report of a Selected Hospital in Awka" Published in International Journal of Trend in Scientific Research and Development (ijtsrd), ISSN: 2456-6470, Volume-3 | Issue-5, August 2019, pp.1657-1661, **https://doi.org/10.31142/ijtsrd26803**

IJTSRD26803

ABSTRACT

This study thereby determined the auditor's independence on financial statements of Nigerian hospitals. Specifically, the study intended to; determines the effect of tenure of an audit firm on reliability of financial reporting of general hospital, Awka and ascertain the effect of audit fees on reliability of financial reporting of general hospital, Awka. Survey research was adopted for this study. Survey and descriptive research design were adopted. The population of the study consist 127 staff of General hospital, Awka. A sample size of 96 was obtained from a population of 127 Staff using Taro Yamane's formula. From the analysis of data collected, the result revealed that the tenure of an audit firm and audit fees have significant effect on reliability of financial reporting of general hospital. The external auditor's fees should be determined by office of the Auditor-General for the concerned state rather than by the hospital management being audited in order to guarantee independence of the auditor in question, also that the tenure of audit firms should always be regulated to avoid too much familiarity.

KEYWORDS: *Auditor independence, Audit tenure and Audit fees*

INTRODUCTION

Auditors' independence has been termed the cornerstone of the auditing profession, since it is the foundation for the public's trust in the attest function (Abdul Nasser, Mustapha & Hudaib, 2006) the broader goal of auditors' namely "to support user reliance on the financial reporting process and to enhance capital market efficiency," is accomplished.

However, several major instances of misstated funds have been reported over the last several years in federal higher institutions (Adams, 2001). These misstatements have led many to question the effectiveness of various aspects of the audit function, especially auditors' independence.

Public sector audit has experienced considerable expansion throughout the world. The reason for this is closely related to changes in the structure of government and concern for more accountable and transparent governance, which has resulted in a large increase in the number of accounts and sophistication of financial reporting. The expansion has brought with it an added demand for accountability (Dowdall, 2003). Public sector accounting is quite distinct from commercial accounting in terms of objectives, sources of revenue and bases of recording accounts, responsibility and accountability among others.

In recent times there has been much discussion about the independence of Auditors; the Leadership of the auditing standards board, the public oversight board, the independence standards board, and most recently the proposed independence rules promulgated by the Securities and Exchange Commission (SEC) has all attempted to clarify and strengthen auditor independence (Olagunju, 2011). Also in the medieval era financial statements were not necessary and hence financial statements were not prepared to make decisions. But with the recent development every firm are expected to prepare financial statement in order to know the financial position of the organization so that stakeholders can make decisions (Olagunju, 2011).

The basic purpose of financial statements in the view of Meigs and Meigs (1981) is to assist decision makers in evaluating the financial strength, profitability and the future prospects of a business entity. The basic objective for preparing financial statement is to provide information useful for making economic decisions. The financial statements preparation is the responsibility of the management, while auditor responsibility is to lend credibility of the financial statements. According to Olagunju (2011), the auditor also increases the credibility of other non audited information which is released by the management. For an audit to be credible and reliable, it must be performed by someone who is independent and cannot be influence by position, power which will affect its own conclusion. The securities exchange commission approved new auditor independence regulation which requires that traded companies should disclose the level of fees that were paid to their external auditor for non audit services.

Morally, some seem to believe that it is wrong for an auditor if "appear" not to be independent. Intrinsic ethical concentration is an influencing factor to consider on a moral view the nature of the moralistic analysis that support the enhancement of the audit independence and have significant to the auditor's role to play auditors' primary duty to protect the public interest and the necessity to use judgment in fulfilling this duty (Dobson & Armstrong, 1995; Libby & Thorne, 2007).

Hospitals are charitable in nature. However, they generally do not fit the definition of Section 501 (c) (3) of the Internal Revenue Code for a charitable organization. While public hospitals receive direct tax support, most operate independent of the local government. In this position, they must maintain a separate budget and cannot expect continuous bailouts for fiscal incompetence (Armario, 2010). Various studies were carried out on auditor's independence and likes in diverse areas, studies like; DeZoort et al., 2002; Hermalin & Weisbach, 2003; Vermeer et al., 2006, Wen-Wen and Sennetti, 2010; Olagunju, 2011; Animasaun and Adegbite, 2016; **Ngbame, Okunega and Ediae, 2013; Yahn-Shir, Hsu, Mei-Ting and Ping-Sen, 2013; Adeniyi and Mieseigha 2013; Siriyama, 2018).** However, none the study of these studies had been carried out in Nigerian hospital. This study thereby determined the auditor's independence on financial statements of Nigerian hospitals. Specifically, the study intended to;

1. Determines the effect of tenure of an audit firm on reliability of financial reporting of general hospital, Awka.
2. Ascertain the effect of audit fees on reliability of financial reporting of general hospital, Awka.

Review of Related Literature

Audit Independence

According to them, practitioner's independence, on the one hand, is a state of mind and equates the notion of integrity and objectivity of the individual auditor. Professional independence on the other hand, is apparent independence of auditors, as a professional group, to the public (Animasaun &Adegbite, 2016). The American Institute of Certified Public Accountants' (AICPA) Code of Professional Conduct defines independence as "the Certified Public Accountants'(CPA)'s ability to maintain an objective and impartial mental throughout the engagement". In addition, it requires that the relationship between CPAs and their clients must be such that the accountants will appear independent to third parties. The Institute of Chartered Accountants of Nigeria (ICAN) (1999) defines independence from an objectivity point of view. It defines objectivity as "independence of mind" which is "a state of mind which has regard to all considerations relevant to the task at hand but no other". These two positions require external auditors to be objective and impartial if their opinions on the financial statements must be credible. Commenting on the position of Mautz and Sharaf (1961), Okolie (2007) argues that the appearance of independence can be evaluated at two levels – the user's perception of the individual auditors' ability to be independent particularly to unique circumstances and the general public's view towards public accountants as a professional group. He maintains that both levels exist in authoritative literature but accounting standards tend to attach greater importance to professional independence. Thus, according to Okolie (2007), "the official definition of audit independence equates the term with an attitude and approach of objectivity (being unbiased, fair and impartial) and integrity (being intellectually honest)".

The preceding arguments on auditors' independence can only lend credence to one position: auditors' independence implies that the auditors' judgement is not subordinate to the wishes of directives of other parties – directors or top management or his own self-interest (Animasaun &Adegbite, 2016). According to Mcgrath, Siegel, Dunfee, Glazer and Jaenicke (2001) however, the definition of independence does not require the auditor to be completely free of all the factors that affect the ability to make unbiased audit decisions, but only free from those that rise to the level of compromising that ability.

Financial Statement

The earliest attempts to record information date back to 3500bc, when it was thought necessary to record payments made to armies of the Egyptian pharaoh's. Payments were not in terms of money but by means of cattle, sheep, precious stones etc via trade by barter system. Records of this early civilization were erratic in their form, but this was to be expected, given the absence of any adequate system and monetary level of trade. This made it possible for transaction to be recorded not as many pounds of silver, cowries etc, but in terms of a consistent measure of value.

The evolution dramatically changed by the founder of doubled entry book-keeping system Luca Pacioli. In his famous ''de summa'' a treatise on mathematics and book-keeping, the idea of double entry book-keeping was enunciated which allowed concepts such as trial balance and balance sheet to emerge. Due to expansion of trade provided the ground for further development in financial reporting. Business became large and complex, and more attention was focused on the stewardship function. This separation of ownership from management and the increased importance of proper stewardship created the need for detailed reporting to owners on the results of operation of entity.

Financial statements (or financial report) are the formal records of the financial activities of a business, person, or other entity. This is a generic term for profit and loss account, balance sheets, cash flow statement, five year financial summary, value added statement, income and expenditure account, statement of accounting policy and so on (Olagunju: 2008).

Financial position: also referred to as statement of financial position or condition, reports on a company's assets, liabilities, and ownership equity at a given point in time.

Income statement: also referred to as profit and loss statement (or a "p & l"), reports on a company's income, expenses, and profits over a period of time. Profit & loss account provides information on the operation of the enterprise. These include sale and the various expenses incurred during the processing state.

Statement of retained earnings: explains the changes in a company's retained earnings over the reporting period.

Statement of cash flows: reports on a company's cash flow activities, particularly its operating, investing and financing activities.

For large corporations, these statements are often complex and may include an extensive set of notes to the financial statements and management discussion and analysis. The notes typically describe each item on the balance sheet, income statement and cash flow statement in further detail. Notes to financial statements are considered an integral part of the financial statements.

Review of previous studies

Wen-Wen, Roger and Sennetti, J. T (2010) focused on the role of audit committees in the private sector and less in the public sector, especially public hospitals. They find the presence of a committee and the committee's specific quality characteristics of independence, financial expertise, and increased activity, positively correlate with reduced frequencies of internal control problems. Olagunju (2011) critically evaluated the independence of auditors and the importance of auditors' independence in financial statement credibility. The relevant data collected were analyzed using simple percentages and tables and tested using chi-square. The results of the test show that auditor's independence affects the credibility of financial statement and the improvement in the credibility of the financial statement can reduce manipulation in the financial statement.

Animasaun and Adegbite (2016) examined the effect of auditors' independence on the accountability of Federal Higher Institutions in Ogun State. The research instrument was the use of questionnaires which were administered to 150 respondents. Data collected from the primary source was analyzed through the use of inferential and descriptive statistics. Chi-square was employed as the data analysis technique to analyze the questionnaires and the information was also represented by the use of the pie chart. The results showed that the auditors' independence significantly impacted on the accountability of Federal Higher Institutions in Ogun State. The results also revealed that the tenure of audit had significant effect on the accountability. Enofe, Ngbame, Okunega and Ediae (2013) examined the relationship between audit quality and auditors independence in Nigeria. A cross sectional study analysis of companies listed on the Nigerian Stock Exchange was carried out. A sample of twenty (20) audited financial reports of these companies for the period ending 2011 was selected using the simple random sampling technique. The data collected for the variables were subjected to the ordinary least square (OLS) regression analysis. Findings indicated that as auditors‟ independence increases, the quality of audit also improves and as the independence of the board and ownership structure increases, the quality of audit reduces. Yahn-Shir, Hsu, Mei-Ting and Ping-Sen, (2013) ascertained the relations between audit quality, audit firm size, and financial performance. The study employed Regression analysis to test the formulated hypotheses. The positive relationship of national audit firms is higher than that of regional and local audit firms. Adeniyi and Mieseigha (2013) examined the effect of audit tenure on Audit Quality in Nigeria. Their study revealed that the relationship between tenure and audit quality was observed to be inverse and this could stimulate the discourse on the sensibleness of changing auditors after a period of time as it may be effective at increasing the level of audit quality. Their study further revealed that return on assets have also be seen to be in line with prior studies while that of company size is at variance with prior study.

Monroe and Hossain (2013) investigated whether audit partner tenure and audit quality associations remain significant after the implementation of mandatory audit partner rotation in Australia. Ex-post facto study design was employed and logistic regression model was used to analyze the data. Findings revealed that auditors are more likely to issue qualified going –concern opinion for financially distressed companies when there is mandatory audit partner rotation after a fixed period of time. Nam and Ronen (2014) examined the relationship between audit fees as a proxy for auditor independence and audit quality of firms in New Zealand. Employing three multiple regression models for a sample of New Zealand companies. The study discovered that the provision of non-audit services by the auditors of a firm comprises the auditor's independence; abnormal audit fee change rate is negatively associated with audit quality and auditor's independence of the previous year impacts on the audit fee that is negotiated in the current year. Siriyama (2018) examined whether the size of the audit firm, the size audit fees, the auditor's duration with the client, competition among other firms and the availability of non-audit services will compromise auditor independence. Findings shows that the top determinant of auditor independence was not clear; however, other researches ranked them based off importance because of their hypothesis that they chose to test. It is evident that independence remains a going concern when discovering how reliable and credible financial statements are to investors.

However, some studies indicated a positive relationship while others showed contrary due to the type of study design employed, sample size, data collection instruments and analysis techniques used. In addition, most of the studies on auditor independence on financial reporting of hospital were centered on one or two of the threats and mainly conducted in foreign countries, this however for the significant of this study.

METHODOLOGY

Survey and descriptive research design were adopted. Survey design involves the use of sample to obtain the opinion of large number of people. It is a research design that study the information gathered from a fraction or percentage of the population.

The population of the study consist 127 staff of General hospital, Awka. A sample size of 96 was obtained from a population of 127 Staff using Taro Yamane's formula as follows:

This sample size $n = \frac{N}{I + N(e)2}$

Where
N = the population size
e= estimated error of 5%

Applying the formula

$$\text{Sample size} = \frac{127}{1 + 127\,(0.05)^2}$$

$$= \frac{127}{1.318}$$

$$= \mathbf{96}$$

Source of Data Collection

To obtain reliable information that will help the researcher to ensure the effectiveness of the study in question, data was collected from the primary source. The researcher used questionnaire to obtain primary data.

The questionnaire was design in a structured form and made up of general questions of two (3) research questions to be answered hypothetically and was restricted with the responses made of strongly agree (SA) agree (A) undecided (U strongly disagree (SD) and disagreed (D).

Validation of the Instrument

Validation of the instrument was done. The questionnaire was given to two experts. They examined the questionnaires items and made necessary corrections. The corrections were effected in the final draft of the instrument.

Reliability of Instruments

To ascertain the reliability of the instrument, the instrument was administered on the staff/ officials who directly participate in the day to day operations of the hospital. The result of their responses was correlated using Crobach Alpha formula. The Coefficient Value of 0.82 was obtained for internal consistency. Therefore, the instrument was assumed reliable.

Method of Data Analysis

Data collected for the study were analyzed by the researcher using frequency counts, mean score and standard deviation. The four hypotheses were tested using t-test statistical tool with aid of SPSS version 20.0 at 5% level of significance. The t-test was used to assess evidence in favour or some claim about the population from which the sample has been drawn.

DATA PRESENTATION AND ANALYSIS

Data Distribution and Collection

The above table shows that out of 96 copies of questionnaires distributed, 74 were completed and returned. This represents 77%.

Test of Hypotheses (Null)

Hypothesis One

H_0: Tenure of an audit firm has no significant effect on reliability of financial reporting of general hospital, Awka.

Table1: Applying the Mean Score for Testing Hypothesis One

Questions	X	Y
1	3	3.91
2	3	3.62
3	3	3.70
4	3	3.80
5	3	3.80
6	3	3.64
7	3	3.73
8	3	3.80
9	3	3.69
10	3	3.82

Paired Samples Statistics

		Mean	N	Std. Deviation	Std. Error Mean
Pair 1	x	3.0000	10	.00000	.00000
	y	3.7510	10	.09036	.02858

Paired Samples Test

		Paired Differences					t	df	Sig. (2-tailed)
		Mean	Std. Deviation	Std. Error Mean	95% Confidence Interval of the Difference				
					Lower	Upper			
Pair 1	x - y	-.75100	.09036	.02858	-.81564	-.68636	-26.281	9	.000

Decision

From the above table, the mean of y is 3.7510 as against x which is 3.00. In this case the mean of y is higher than that of x (the mean score). Looking at the mean score table 4.3.1, the mean scores of y are not by chance hence scored above the bench mark and indicate positive response. Based on this, the study rejects null hypothesis and accept the alternative hypothesis which state that the tenure of an audit firm has significant effect on reliability of financial reporting of general hospital, Awka.

Hypothesis Two

H_0: Audit fees have no significant effect on reliability of financial reporting of general hospital, Awka.

Table 2: Applying the Mean Score for Testing Hypothesis Two

Questions	X	Y
1	3	3.78
2	3	3.76
3	3	3.68
4	3	3.76
5	3	3.70
6	3	3.82
7	3	3.70
8	3	3.64
9	3	3.73
10	3	3.78

Paired Samples Statistics

		Mean	N	Std. Deviation	Std. Error Mean
Pair 1	X	3.0000	10	.00000	.00000
	Y	3.7350	10	.05482	.01734

Paired Samples Test

		Paired Differences					t	df	Sig. (2-tailed)
		Mean	Std. Deviation	Std. Error Mean	95% Confidence Interval of the Difference				
					Lower	Upper			
Pair 1	x - y	-.73500	.05482	.01734	-.77422	-.69578	-42.396	9	.000

Decision:

From the above table, the mean of y is 3.7350 as against x which is 3.00. In this case the mean of y is higher than that of x (the mean score). Looking at the mean score table 4.3.1, the mean scores of y are not by chance hence scored above the bench mark and indicate positive response. Based on this, the study rejects null hypothesis and accept the alternative hypothesis which state that audit fees have significant effect on reliability of financial reporting of general hospital, Awka.

Discussion of findings and Conclusion

From the analysis of data collected, the following findings were discovered:

The result revealed that the tenure of an audit firm and audit fees have significant effect on reliability of financial reporting of general hospital, Awka. This depends on the extent to which auditors maintain their independence, and such propel reliability on financial reporting and accountability of the hospitals. Therefore, all factors that can impair or erode this independence must be drastically avoided by the auditors and clients. However, it shows that the longer the period of engagement of an auditor, the higher the level of familiarity that can be established which may impair the level of auditor's independence.

Recommendations

Having investigated empirically and based on the findings, the following specific recommendations were drawn:

1. The external auditor's fees should be determined by office of the Auditor-General for the concerned state rather than by the hospital management being audited in order to guarantee independence of the auditor in question.
2. The tenure of audit firms should always be regulated to avoid too much familiarity.
3. Regulatory bodies should ensure that the financial statements and the books of accounts of various establishment.

References

[1] Adeniyi, S. I. & Mieseigba, E. G (2013). Audit tenure: an assessment of its effects on audit quality in Nigeria. *International Journal of Academic Research in Accounting, Finance and Management Sciences, 3*(3), 275-283.

[2] Animasaun, R. O., & Adegbite, A. I.(2016). Auditors' Independence and Accountability of Federal Higher Institutions in Ogun State. *Research Journal of Finance and Accounting*. 7(24). ISSN 2222-1697 (Paper) ISSN 2222-2847 (Online) www.iiste.org

[3] Abdul Naesser, A. T., S. N. Mustapha, & M. Hudaib (2006). Auditor-client relationship: The case of audit tenure and auditor switching in Malaysia. Managerial Auditing Journal, 21 (7), 724-737.

[4] Armario, C. (March 10, 2010). Major Miami hospital system in 'death spiral' as it runs low on cash; reflects woes nationwide. Los Angeles Times. Available at http://www.latimes.com/business/nationworld/wire/sns-ap-us-miami-hospital-insolvency,0,650089.story

[5] Adams, R. A. (2001). Public Sector Accounting and Finance. 3rd Edition: Yaba, Lagos Nigeria Corporate Publishers Venture.

[6] Dowdall, J. (2003). Audit and Accountability in Government. Report of a joint seminar organized by Institute of governance and economic and social research council of Northern Ireland, pp: 1-2

[7] DeZoort, T., Hermanson, D. R., Archambeault, D., & Reed, S. (2002). Audit committee effectiveness: A synthesis of the empirical audit committee literature. *Journal of Accounting Literature 21*, 38-75.

[8] Enofe, A. O., Nbgame, O. E. & Ediae, O. O. (2013). Audit quality and auditors "independence in Nigeria: An Empirical Evaluation. *Research Journal of Finance and Accounting*. 4(11), 131-138.

[9] Mautz, R. K., & H. A. Sharaf, (1961). The philosophy of auditing. USA: American Accounting Association.

[10] Mcgrath, S., A. Siegel, T. W. Dunfee, S. A. Glazer, and Jaencke, H. R. (2001). A framework for auditor's independence. Journal of accountancy Online; AICPA, January

[11] Monroe, G. & Hossain S. (2013). Does audit quality improve after the implementation of mandatory audit partner rotation? *Accounting and Management Information System.* 12(2), 263-279.

[12] Nam, S., & Ronen, J. (2014). The impact of non audit services on capital markets. *Journal of Accounting, Auditing & Finance*. 27,32-60.

[13] Olagunju, A. (2011). An empirical analysis of the impact of auditors independence on the credibility of financial statement in Nigeria. *Research Journal of Finance and Accounting* 2(3). ISSN 2222-1697 (Paper) ISSN 2222-2847 (Online) www.iiste.org

[14] Okollie, A. O. (2006). Fundamentals of audit practice, Agbor, Nigeria: Progress Printing associates.

[15] Okollie, A. O. (2007). Auditor's re-appointment and its impact on audit independence, the Nigerian accountant, (40)4,

[16] Siriyama, K. H. & Tori, P. (2018). A literature review on auditor independence. *The Business and Management Review,* 9(3).

[17] Wen-Wen, C., Roger,W. M. &. Sennetti, J. T. (2010). Audit committee effectiveness in the largest us public hospitals: an empirical study. *Accounting & Taxation,* 2(1).

[18] Yahn S.C, Mei-Ting. H., Ping .S.Y., & Hsu .C.S.(2013). Relationship between audit quality, audit firm size and financial performance. *International Journal of Business and Finance Research*, 89-105.