

PUBLIC CONFIDENCE IN AUDITED REPORT: AN EMPIRICAL REVIEW

Obaretin Osasu

Department of Accounting, University of Benin, Benin City

Jonathan A. Okunbor

Department of Accounting, Ambrose Alli University, Ekpoma, Nigeria

E-mail: jonathanokunbor@yahoo.com

Abstract

Audited report is of no doubt a great influence on the users of the report. In the midst of the seemly ill-conducive environment the question arises, is to what extent users of this information can rely on the reported information as a basis for their decision. The primary aim of this research is to determine the level of public confidence on audited report and also know the extent to which users of this information are aware of the nature of the report. In making this possible, information were gather from both the primary as well as the secondary sources and in analyzing the data gathered from the primary source the non-parametric statistical tool (z-test) was employed. The study revealed that audited report does influence users in positive ways, in as much as most of the users are not aware of the functioning or the activities of audit carried out in companies. Also, most users do not have the ability to analyze and interpret these reports. Premised on the above, it was recommended that the auditors should be given freehand in the course of the audit work; relevant regulatory bodies should constantly enlighten the general public and members of the audit/accounting profession.

Keywords: Auditing, decision making, public confidence

Introduction

The evolution of auditing can be traced back to ancient time when landowner allowed tenant to work on their land while the land owners relied upon an overseer who listen to accounts of stewardship given by the tenants. In the view of this, audit is meant to attest to whether the information given shows a true and fair view of the situation on ground. The act of exercising the audit function is referred to as auditing.

Woolf (1979) defines auditing in the modern sense as a process carried out by suitably qualified auditors whereby the account of business entities including limited companies, charters, truer and professional firms are

subjected to scrutiny in such details as will enable the auditors to form an opinion as to the accuracy of the truth and fairness.

However, this exercise by professional accountants, who have gone through the training and obtained the requisite certificate from a recognized professional accounting body and possess a practice license as in the case of Nigeria was describe by Okolo (1989) as conscientious, objective examination and inquiry into a given statement of account relating to money or money's worth. It also entails the examination of the underlying documents and possible physical assets to enable the auditor to form an opinion as to whether or not the statement of account

presents a true and fair view of what it purports to present.

Historically, annual reports and accounts of companies are produced by the directors to the shareholders and other interested users, better refer to as the stakeholders.

However, today a much wider range of people are interested in the annual report and accounts of companies and other organizations Millichamp (2002) further adds that modern companies could be very large with multinational activities. The preparation of the accounts of such groups is a very complex operation involving the compilation and analysis of accounting and control systems. This assumption has led to much public criticism of an auditor especially when cases are instituted against him for perceived negligence in the performance of his duties.

Most importantly audit is planned so that there is a reasonable expectation of detecting material misstatement in the accounts resulting from fraud or error or breach of regulations.

Section 360 (1) of the Companies and Allied Matters Act of 1990 provides that “it shall be the duty of the company’s auditors in preparing their report to carry out such investigations as may enable them to form an opinion as to whether the company has kept proper accounting records and proper returns adequate for their audit have been received from branches not visited by them; the company’s balance sheet and profit and loss account are in agreement with the accounting records and returns. If this is not the case, the auditors must state so in their report.

It shall be the auditors duties to consider whether the information given in the directors report for the year for which the accounts are prepared are consistent with their accounts and if not he must state so in his report. The issue

which has always existed when manager’s report to owners is should the owners believe the report? This report may contain errors, not disclosed, fraud, be inadvertently misleading because it fails to disclose relevant information and fails to conform to regulations. The solution to this problem of credibility in reports and account lies in appointing an independent person called an auditor to investigate the report. After the auditor has examined the organization records and financial statements he produces a report addressed to the owners on the truth and fairness of the statements.

Therefore, public confidence in the quality of audit works is enhanced when the profession encourages high standards of performance and conduct on the part of all practitioners. It can therefore be seen that the issue of public confidence in audit report is a serious matter.

The objectives of this paper therefore are to examine the level of public confidence in audit report and to find out public perception of audit work in the Nigerian economy. This paper is divided into 5 sections: Following the introduction is the review of literature on audit and auditing, section 3 discusses the methodology and research design, section four is data analysis while the last section deals with conclusion and recommendations.

Literature review

In order to have appreciation of public confidence in audited financial statement or report, it is considered necessary to have a proper understanding of the term auditing in modern sense.

It has been universally accepted that audit was derived from a latin word “audire” meaning to hear. This is because in times past, the account of noble men were checked by them being read out to them by their stewards. The stewards had responsibility of looking after the

affairs of the estate during the noble men's absence.

However, modern auditing began in 16th century in Europe during the reign of Queen Elizabeth 1 (Okolo, 1989). The basic aim was increased activities in international exploration and trade. As commerce developed, it became common for the number of participants in enterprise to increase. In the opinion of Oladipopo (2005) he describe audit in modern sense as process where accounts of business entities are subjected to scrutiny. By business entities are limited companies, charitable organization, trust, NGOs and professional firms

However, on the issue of social and environmental context of auditing, Porter (1992) identifies auditors as the watchdogs of the society. This function is not only applicable to Nigeria and developing nations of the world but also to developed societies. This is why members of the board of large corporations in United States of America and other developed nations always debate about the credibility of the auditing profession and the usefulness of auditors in restoring confidence in the capital markets of any economy. For instance the recent collapse of the US giant Enron Corporation, World com amongst others revealed unethical behaviour of members of board of major corporations which caused people to question the credibility of auditing profession (Okike, 2004). The levels of confidence that people have varies from one country to another. In the case of Nigeria the corporate failures witnessed in the financial sector in the early 1990s, the Cadbury case and the recent downturn of stock of quoted companies in the stock exchange made people to doubt the relevance of the profession in the society.

The role of auditors in checking corruption in financial sector or any system cannot be

overemphasized. In Nigeria, corruption is apparently endemic in most individuals as well as institutions. However, the response of the profession is important since it makes a crucial attempt to restore public confidence. This is extended to their members as well as the extent they have re-established the legitimacy of their continued existence. This is necessary in Nigeria because the country is a leading player not only in Africa but also in the international arena (Okike, 2004). The auditing profession in Nigeria has a crucial role to play in restoring the confidence of investors in audited reports issued in Nigeria. Accountability in all aspects of any economy is an essential ingredient to economic growth and development.

Research hypothesis

- (1) Ho: Users of financial report do not have confidence in audit report
HA: Users of financial report have confidence in the audit report.
- (2) Ho: Users of financial report do not have true understanding of the nature of an audit.
HA: Users of financial report have true understanding of the nature of audit.

Research methodology

For primary source data collection was based on the information obtained through questionnaire administered to literate shareholders who have shares in banks, insurance companies all located in Benin City.

A total of 50 questionnaires were administered to these shareholders and a total of thirty-eight (38) questionnaire were successfully retrieved from the respondents. Thereafter, the binomial test (Z test) a non parametric statistics which

test the association between two variables was used to analyze the data generated.

The decision rule for this test statistics is that the null hypothesis was rejected where the calculated value of Z-cal was found to have exceeded the critical value at 5% level of significance.

Empirical results and discussion of findings

The section of the study provides the relevant data for validating or rejecting the null hypothesis:

Test of hypothesis

Users of financial report do not have confidence in auditor/audit report.

Analysis of respondents

Responses	Number	Percentage (%)
SA	10	26.3
A	15	39.5
U	3	7.9
D	7	18.4
SD	3	7.9
Total	38	100

Source: Field Work (2010)

SA = Strongly Agree, A = Agree, U = Undecided, D = Disagree, SD = Strongly Disagree

The above table reveals that 66 percent of the respondents sampled agreed that users of financial report have confidence in the auditor report, 8 percent are undecided and 26 percent of the respondents do have confidence on the audited financial report.

Using Binomial P, the null hypothesis (Ho) as regards the above table is tested using one tail test as follows;

Ho: $P < 0.5$

HA: $P > 0.5$

Z cal is computed using:

$$Z = \frac{X - np_0}{\sqrt{np_0(1-p_0)}}$$

$$Z = \frac{25 - (38 \times 0.5)}{\sqrt{38 \times 0.5(1-0.5)}}$$

$$Z \text{ cal} = 1.95$$

$$Z_{0.05} = 1.645$$

Since Z cal is 1.95 is greater than Z value at 5 percent which is 1.645, we accept the alternative hypothesis which says that users of financial report have confidence in the audited report and reject the null hypothesis

Hypothesis Two

Users of financial report do not have true understanding of the nature of an audit.

Responses	Number	Percentage (%)
SA	5	13.2
A	11	28.9

U	2	5.3
D	14	36.8
SD	6	15.8
Total	38	100

Source: field survey, 2010

The table above shows that 42 percent of the respondents agree that users of financial report have true understanding of the nature of audit, while 5.3 percent of them are undecided and on final note 53 percent of the respondents disagreed that users of the financial report have true understanding of the nature of audit

Using the Binomial P to test the null hypothesis in respect of the above table as show below;

Ho; $P \leq 0.5$

HA; $P > 0.5$

$Z_{cal} = \frac{16 - (38 \times 0.5)}{\sqrt{38 \times 0.5(1 - 0.5)}}$

$Z_{cal} = -0.973$

$Z_{0.05} = 1.645$

From the above computation, we accept the null hypothesis (Ho) that says users of audited reports of companies do not have true understanding of the nature of audit since Z_{cal} which is -0.973 is less than Z at 5 percent of 1.645

Conclusion and discussion

The purpose of this work was to evaluate user's perception on audited financial statement. In order to achieve this objective, relevant data were sourced from relevant literatures, journals, questionnaires and so on. These data were further analysed using the binomial Z test statistic, which is a non-parametric test.

From the analysis, hypothesis one reveals that users of audited report have some level of confidence on audited report. And was base on 5 percent level of significant, while for

hypothesis two; it was concluded that users of audited financial statement do not have true understanding of the nature of companies audit work or procedure.

However, it was also observed that most users of the report are not properly inform about the working of companies, are unable to analyse, understand and interpret the contents of companies accounted. It was also gather that audited reports are the sure way of enhancing effective communication between the public and the companies. It was further concluded, by the researcher that the principal responsibility for enhancing the level of the public confidence in audited report rests with the auditors themselves and it is hoped that they will live up their responsibility.

Recommendation

Every system has its shortcomings and if noticed, they have to be corrected to enhance the effectiveness and continue its relevance.

Based on this, the following are recommended:

- (1) Organizations should give auditors free hand to perform their job
- (2) Before commencing an audit, an auditor should reach a clear agreement with the client as to the objective and scope of the audit
- (3) Professional bodies should review and broaden existing professional, standards, guides and codes of ethics. Also prompt and adequate sanctions should be taken against any auditors who breaches professional statutory rules

- (4) Professional bodies for example Institute of Chartered Accountants of Nigeria (ICAN) should frequently organize public lecture to educate members of public on the nature and scope of audit.

reporting on the accounts of listed companies in Nigeria following the indigenization of equality capital, Research in Accounting in emerging economies.

References

- Okolo, J.U.T. (1989), *The Concept and practice of Auditing*, Lagos Evans Brothers Nigeria Publisher Limited.
- Millicamp, A.H. (2002) *Auditing: An Instructural Manual for Auditing, Accounting Students*, 8th Edition, London, DP Publishers.
- Woolf, E. (1979), *Auditing Today*, New Jersey, USA, Prentice Hall Inc.
- Porter, B. (1992), "Do external auditors have the role of society's corporate watchdog? An empirical investigation" paper presented at the annual conference of British Accounting Association, University of Warwick, Warwick, 13-15 April.
- Oladipopo, A.O. (2005), *Principles and Practice of Auditing*, Benin City, Mindex Publishing Company Ltd.
- Okike, E.N.M. (2004), "A longitudinal analysis of the quality of auditing reporting on the accounts of listed companies in Nigeria following the indigenization of equality capital", Research in Accounting in emerging economies.
- Owayemi, L. (1990), "ICAN in the next decade agenda for timely change," *The Nigerian Accountant*, Vol. 23, No. 4; pp 9-15.
- Kimbro, M.B. (2002), "A cross-country empirical investigation of corruption and its relationship to economic, cultural and monitoring institutions: an examinations of the role of accounting and financial statements quality" *Journal of Accounting, Auditing and Finance*, Vol. 17.
- Nwokolo, I. (1998), president's post-conference press briefing on the *Nigeria Accountant*, Vol. 31, No. 4, 23p.
- Pandy, I.M. (1999) *Financial Management*, 8th Edition, New Delhi, Vikas Publishing House.
- Nigeria Accounting Standard Board (NASB) Exposure Draft (1991) Objective of Financial Statements and the Qualitative characteristics of financial information.