

An Empirical Analysis of the Impact of Auditors Independence on the Credibility of Financial Statement in Nigeria

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Abstract

In this study the independence of auditors was critically evaluated and the importance of auditors' independence in financial statement credibility was analysed. In order to make informed decision it is important for the financial statement to be credible. The auditors are expected to audit the financial statement of companies in order to present a true and fair view or otherwise of the financial statement. The data used for this work were collected from both primary and secondary sources. The relevant data collected were analysed 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. The reason why audit exists is because investors and creditors can make use of financial statement to make their decisions. The study concluded that auditors' independence and the credibility of financial statement are to be significantly impaired when non-audit services are conducted and that there is a positive relationship between independence of an auditor and the credibility of financial statement, therefore the independence of an auditor is fundamental to the credibility of financial statement. Finally, the study recommends that there should be rotation of auditors to improve the auditors' independence, implementation of peer assessment in other to ensure that audit are carried out with outmost professionalism and mutual respect and that auditors should not be allowed to provide audit client with any other advisory services.

Key words: External Auditor, Financial Statement, Auditors Independence

Introduction

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) have all attempted to clarify and strengthen auditor independence. Also in the medieval era financial statements were not necessary and hence financial statements were not prepared neither used 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 organisation so that stakeholders can make decisions.

Securities and exchange commission (SEC) require traded companies to make sure their statements are prepared and audited by certified public accounting firm who assume the responsibility for the fairness of the financial statements. This opinion adds to the credibility of the statements which is agreed by the lender and private investors who voluntarily allow company's statement to be verified by independent body. The user of financial statement which include: shareholders, government, creditors, investors, etc. All rely on the audited financial statement in other to make informed decision. Therefore the credibility and reliability of this statement is necessary.

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 objective of an audit of financial statements is to enable the auditor express an opinion whether the financial statements are prepared in all material respects and also in accordance with auditing standard.

The function of auditing is to lend credibility to the financial statement. The financial statements preparation is the responsibility of the management, while auditor responsibility is to lend credibility of the financial statements. 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 influenced 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.

The auditor independence has long been recognized as the cornerstone of the public accounting profession (Sweeney, 1992; Mednick, 1997) and that it is privileged to govern itself. Society grants power and privilege to the Accounting profession. Auditors are obligated to perform their duties for the public benefit in exchange for exclusive professional privilege. Traditional audit independence view regard as a moral perspective (Preston et al., 1995; Thompson and Jones, 1990). As for a moral perspective, auditors are professionals, with professional obligations to the public. They should not engage in any activity that appears to impair their effectiveness as professionals, regardless of the totality of their incentives (Antle, 1999). Professionals are presumed to do things because of their professional duties, not because of their best interests. Incentives right or wrong is concentrated. 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 and Armstrong, 1995; Libby and Thorne, 2007).

The ideal of auditor independence has been clearly stated for a long time. The second general standard of generally accepted auditing standards states that "in all matters relating to the assignment, independence in mental attitude is to be maintained by the auditor or auditors."

Essentially, an auditor may function as an employee (internal auditor) or an independent professional (external auditor).

Users of these entities' financial information, such as investors, government agencies, and the general public, rely on the external auditor to present an unbiased and independent evaluation on such entities.

In an ideal world this may be the case, but in reality i will argue that these auditors may be less independent than the other auditors.

Therefore safeguarding auditor's independence is a key priority not only for auditors, but also for management and investors. In the global market of today, the government, creditors, institutional investors, lenders, regulator, stakeholder etc rely on the information provided by the auditors on the credibility and reliability of the financial statements.

Statement of the Problem

Financial reports as stated in Igben (1999) are meant to be a formal record of business activities and these reports are meant to provide an overview of the financial position and profitability in both short and long term of companies to the users of these financial statements such as shareholders, managers, employees, tax analyst, banks, etc. But in recent times, the financial manipulations, weak internal control systems, ignorance on the part of the board of directors and audit committee, manipulation on the part of the reporting auditor and other fraudulent activities that occur within companies, creating a negative goodwill to the general public. A typical example of a financial statement malfunction is the popular case of Enron. Enron was one of the largest energy companies in theUS. By fraud and bribery, Enron

executives avoided income taxes, and this led to the downfall of this multi-billion dollar firm. Importantly, this wasn't the first; a similar case appeared in 1973, when equity funding, an insurance firm located in Los Angeles went bankrupt (McLean and Elkin, 2003). In fact every year, a new business fraud is unravelled, often with similar components: corporate instability, uniformed accountants, high-level connections, and broke investors (Swartz and Watkins, 2003).

Enron started in July 1985 when Omaha-based inter-north merged with Houston natural gas. Kenneth Lay, who had originally held positions in academia and the government, became chief executive and chairman. By 2001, Enron had grown to one of the largest energy companies in the world (McLean and Elkin, 2003). However, the company suddenly unravelled and collapsed.

Some other examples of corporate failure on the local scene are Lever plc now Unilever in (1998) and African Petroleum (2000). From the above discussions, there is need to ensure credibility of financial statement of companies in order to increase users confidence and thereby affecting investors behaviour. This study seeks to investigate why corporate organisations fail and how it is occasioned by the independence of auditors.

Objectives of the Study

The study in specific terms intended to:

- i. To know how auditors' independence affects the financial statement of a limited liability company.
- ii. To assess the factors that affect an auditor's independence.
- iii. To know how an auditor's right or wrong judgement will affect the credibility of the financial statement.
- iv. To examine the acts and standards that regulate the attitude of auditors.
- v. To examine reasons for auditor's independence.
- vi. To examine the duties, powers, and functions of an auditor.
- vii. To assess how a wrongly audited financial statement affects a limited liability company.
- viii. To evaluate the variables that influence auditor's decision about the financial statement of the organisation

Research Questions

Answer to the following questions will be sought as a basis for testing the hypotheses:

- i. Does auditors' independence affect the credibility of a financial statement?
- ii. What are the duties, powers, and rights of an auditor?
- iii. Does an auditor's right or wrong judgement affect the credibility of a financial statement?
- iv. Are there factors that affect auditors' independence?
- v. Do auditors always operate within the framework of accounting standard and other regulations?
- vi. Are there variables that influence auditor's decision about the financial statement of the organisation?
- vii. Are there right or wrong judgment which will affect the credibility of the financial statement?

Research Hypothesis

These are of two types:
The null h_0 hypothesis; and
The alternate h_1 hypothesis

Hypothesis 1

Ho: there is no significance relationship between auditor's independence and credibility of the financial statement

H₁: there is significance relationship between auditors independence and credibility of the financial statement

Hypothesis 2

Ho: Improvement in the credibility of financial statement cannot minimize the manipulation of financial statement

H₁: Improvement in the credibility of financial statement can minimize the manipulation of financial stat

Theoretic /literary reflections

Auditors' Independence

Auditor independence has been defined by different people above but there are some concept about an auditor that needs to be emphasized. The concept requires that auditor should carry out his work freely and in an objective manner.

The purpose of an audit is to enhance the credibility of the financial statements by given reasonable assurance from an independent source that they present a true and fair view in accordance with an accounting standard. Independence is fundamental to the credibility and reliability of auditor's report and if the reports are not credible, the investor would have little confidence in them if auditors' are not independent in both fact and appearance.

Audit independence is defined as an auditor's unbiased mental attitude in making decisions throughout the audit and financial reporting (Bartlett, 1993). The attribute of independence is a very specialized concept for auditors. Looking for maintaining the highest ethical standard for the accounting profession, independence refers to the quality of being free from influence, persuasion or bias (Maury, 2000). In addition, independent auditor is expected to be without bias with respect to the client under audit and should appear to be objective to those relying on the results of the audit (Maury, 2000). Similarly, auditor independence refers to the auditors' ability to maintain an objective and impartial mental attitude throughout the audit (Sridharan et al, 2002). In the absence of independence, the value of audit services will be greatly impaired (Sweeney, 1992) and in turn, if an auditor lacks independence, this increases the likelihood that they would be perceived as fewer objectives and therefore less likely to report a discovered breach (Lowe and Pany, 1995). Compromised independence results in a lower level of audit quality being provided on financial statements (Baber et al., 1995). In other words, if the auditor is not independent, the incentive to do a high quality audit is weakened, as misstatements will not be reported even if found (Pike, 2003). Little studies have been done on direct measures perceived auditor independence and audit quality (Raymond, 2005). This research uses direct perceived measures of those. Auditor independence helps to ensure quality audits and contributes to financial statement user reliance on the financial reporting process (Lindberg and Beck, 2004). Moreover, audit credibility can be achieved through various mechanisms of assurance, i.e. Assuring the public and other users that the information in a report is true and fair (Dando and Swift, 2003). It hasn't an emergence, if auditors lack of objectivity and professional scepticism. That is level of assurance provided by auditor independence links to the audit credibility. The higher level of audited financial statement assurance reliance based on higher auditor independence that its relation to the auditor credibility. At the result, strength of auditor independence also enhances auditor credibility (Dopuch et al., 2003). This is an important factor in the credibility of financial reporting. An auditor as a member of the accountancy profession maintains a professional attitude characterised with its objectivity and integrity. He must not only be independent but to be so at all times. I.e. He or she should not be involved in relationships, financial or otherwise which may cast doubt on his integrity.

In 1932, AICPA council considered prohibitions against auditors serving as officers or directors of clients, and rejected them as unnecessary. However, the proposal indicated the first concerns over a need to preserve the appearance of maintaining objectivity, as well as being independent in fact. After the securities act of 1933 was enacted, the federal trade commission issued regulations stating that it would not consider auditors to be independent if they served as officers or directors or had any direct or indirect interest in public audit of clients.

Types of independence

There are three main ways an auditor's independence can manifest itself

Programming independence

Investigative independence

Reporting independence

Programming independence essentially protects the auditor's ability to select the most appropriate strategy when conducting an audit. Auditors must be free to approach a piece of work in whatever manner they consider best. As a client company grows and conduct new activities, the auditor's approach will likely have to adapt to account for these. In addition, the auditing profession is a dynamic one, with new techniques constantly being developed and upgraded which the auditor must decide to use. The strategy/proposed methods, which the auditors intend to implement, cannot be inhibited in any way.

While programming independence protects auditors' ability to select appropriate strategies, investigative independence protects the auditor's ability to implement the strategies in whatever manner they consider necessary. Basically, auditors must have unlimited access to all company information. Company must answer any queries regarding a company's business and accounting treatment. The collection of audit evidence is an essential process, and cannot be restricted in any way by the client company.

Reporting independence protects the auditors' ability to choose to reveal to the public any information they believe should be disclosed. If company directors have been

misleading shareholders by falsifying accounting information, they will strive to prevent the auditors from reporting this. It is in situations like this when auditor independence is most likely to be compromised.

Real Independence and Perceived Independence

There are two important aspects to independence which must be distinguished from each other: independence in fact (real independence) and independence in appearance (perceived independence). Together, both forms are essential to achieve the goals of independence. Real independence refers to the actual independence of the auditor, also known as independence of mind. Real independence is concerned with the state of mind the auditor is in and how the auditors deal with a specific situation. An auditor who is really independent has the ability to make independent decision even when there is no independence present or if he is placed in a compromising condition by the director of the company. Similarly, an auditor's objectivity must be beyond question and this can be guaranteed by perceived independence which is very important. (Lindberg, D.L and Beck, F.D, 2004).

It is also important that the auditor should not only act independently, but appears independent. If some facts suggest that an auditor is not really independent this could lead to the public concluding that the audit report does not represent a true and fair view. Independent in appearances also reduces the opportunity for an auditor to act otherwise than independently, which subsequently adds credibility to the audit report.

Restrictions on Independence

When auditors of a company are in conflict with the directors it is important this conflict can be resolved without the auditors losing any of their independence. This can prove to be difficult as an auditor earns a fee from providing a service, which is how he earns a living. This fee is paid by the board of directors leaving them with the power in the relationship. Therein lies the dilemma, how can the audit team please the directors without losing any of their independence but keep the directors happy to ensure maintain repeat business? The problem regarding independence stems from two main sources the auditors' relationship with the company and the nature of the accountancy profession. An auditor earns a living from the fee he is paid it is therefore automatic that does not want to do anything to jeopardize this income. This reliance on clients' fees may affect the independence of an auditor. If the auditor feels this client income is more important than their responsibilities to shareholders he may not perform the audit with the shareholder's interest in mind. The larger the fee income the more likely the auditor is to shirk his responsibilities and perform the audit without independence. This could lead to the manipulation of figures and exploitation of accounting standards. By performing the audit without independence the shareholders' may get misled, as the auditor is now reliant on the directors. To encourage auditors to maintain their independence they must be protected from the director's board. If they were able to challenge statements and figures without the risk of losing their job they would be more likely to work with complete independence. Ultimately, as long as the client determines audit appointments and fees an auditor will never be able to have complete economic independence. In most cases it is the directors that negotiate an audit contract with the auditors. This may cause problems. Audit firms on occasions quote low prices to directors to ensure repeat business, or to get new clients. By doing so the firm may not be able to perform the audit fully as they do not have enough income to pay for a thorough investigation. Cutting corners could mean the audit team would be reporting without all the evidence required which will affect the quality of the report. This would bring into question their independence. It is common for the audit firm of a company to provide extra services as well as performing the audit. Helping a company reduce its tax charges or acting as a consultant for the implementation of a new computer system, are common examples. Having this additional working relationship with the client would result in questions being asked of the independence of the audit firm. If non-audit fees are substantial in retaliation to audit fees suspicions will arise that auditing standards may be compromised. The firm would no longer be unbiased, as it would want the company to perform well so it can continue to earn the addition fee for their consultancy.

This would mean the audit firm would be dependent on the directors and they would no longer be working with independence.

Audit and its Legal Implication

Laws differ from country to country so also an audit of the financial statement of a public company is usually required for investment, financing and tax purposes which are usually done by independent accountant or an auditing firm. The audit opinion on the financial statement is usually included in the annual report. There has been a legal debate over who an auditor is liable to either to shareholders or investors. But in Canada, auditors are liable to investors who use prospectus to buy shares in the primary market. In the united kingdom, they have been held liable to potential investors when they are aware of how the potential investor would use the information in the financial statements

In the united state, especially in the post-Enron era there has been substantial concern about the accuracy of financial statements. The chief executive officer (CEO) and chief financial officer (cfo) are liable for attesting that financial statements do not contain untrue statement of material fact necessary to make the statement under any circumstances must not be misleading with respect to the period covered by the report. For example, former CEO of WorldCom Bernie Ebbers was been sentenced to 25 years imprisonment for allowing WorldCom's revenue to be overstated by \$11 billion dollars over five years

Future Developments

Audit quality is defined as the probability that an auditor will both discover and truthfully report material errors, misrepresentation, or omissions in the client's material financial statement (Deangelo, 1981). Audit quality has been defined in numerous means. Some of the more frequently definitions of audit quality include (1) the probability that an auditor will both discover and truthfully report material errors, misrepresentation, or omissions in material financial statement (Deangelo, 1981), (2) probability that an auditor will not issue an unqualified report for statements containing material errors (lee et al., 1999), (3) the accuracy of auditor's information reporting (Davidson and neu, 1993), and (4) measure of the audit's ability to reduce noise and bias and improve meticulous in accounting data (Wallace, 1980). The audit service is the provision of independent verification of the credibility of financial statements to users. In order to ensure that the audit enhances the credibility of financial statements, it must be of a sufficient audit quality (Sucher et al., 1998) and, in turn, audit credibility (Gaynor, 2000). Financial statement users will change assessments of audit quality based on new publicly available information about an auditor (Dopuch and Simunic, 1982). New information, such as audit independence as auditor's ethical behaviour, lower perceived auditor independence, may be lower perceived financial statement reliability and, thus, the perceived quality of audit services provided (palm rose, 1988). In other words, high-quality auditors give greater credibility and better quality to financial statements than low-quality auditors (Wong, 2005). The higher audit quality generates the higher the information credibility and information quality that has impact on the higher quality of financial statements and that means auditors with high-quality and high--credibility (Watkins et al., 2004). In accounting context, higher audit fees are reflected by higher costs that have to infer that these higher costs result in greater audit quality. Hence, the auditor should have a higher reputation as a result (Moizer, 1997). The link of the relationship between the reputation and the audit quality is provided by economic theorists such as Klein and Leffler (1981) and Shapiro (1982). The essence of their arguments is that individual has an economic incentive to incur above average costs in order to produce a service...

Service limitations: many have advocate that in order for an auditor to remain independent they should not be allowed to provide audit clients with any other advisory services. Both auditors and their clients have argued that the knowledge acquired during the audit process allow other services to be provided less expensive.

Audit committees: the motion to form audit committee was first made in the cadbury report (1992). A group of three to five non-executive directors from within the company are chosen to provide what is supposed to be an objective view on all aspects of the audit from the

evaluation of internal control systems to recommendations on audit fee. Through the cadbury report this practice has been implemented and many are still not convinced of the neutrality of non executive directors

Peer review or assessment: this is a new audit approach and it is not common in nigeria. It involves a review of an audit firm system, procedures and strategies by another audit firm of comparable size reputation and standard. This is a requirement in the us that must be satisfied once every three years. This implemented to ensure external audits are carried out with the utmost professionalism and independence at all times. Such a system has not been accepted by uk auditors, however, it is expected that many large firms already

Rotating external auditors: it is widely believed that rotation of an audit firm will improve auditor's independence. Firstly, auditors will have no incentive to work together with their clients if the contract is due to expire in the foreseeable future. (dunn j, 1996). Auditors will likely forge relationships with directors and staff, thus will less concern about upsetting them through an unfavourable audit report. In rotating an auditor, the auditor will try to prepare his account properly in order to produce audit report so as to avoid any shortcomings from the incoming or the new audit team.

Powers, Duties and Functions of an Auditor

Duties

According to section 237 of the company act 1985 the following are the duties of an auditor:
A company's auditor shall, in preparing their report, carry out such investigation as will enable them to form an opinion as to;

Whether proper accounting records have been kept by the company and proper returns adequate for their audit have been received from branches not visited by them, and

Whether the company's individual accounts are in agreement with the accounting records and returns.

If the auditors are of opinion that proper accounting records have not been kept, or that proper returns adequate for their audit have not been received from branches not visited by them, or if the company's individual account are not in agreement with the accounting records and returns, the auditors shall state that fact in their report.

If the auditors fail to obtain all the information and explanations which, to the best of their knowledge and belief, are necessary for the purposes of their audit, they shall state that fact in their report.

If the requirements of schedule 6 (disclosure of information: emoluments and other benefits of directors and others) are not complied within the annual accounts, the auditors shall include in their reports, so far as they are reasonably able to do so, a statement giving the required particulars.

Subsection 1 requires the auditor to carry out investigation to determine if proper accounting records have been kept and proper returns from branches (at least branches not visited by the auditor) have been received. The subsection also requires the auditor to carry out investigations to determine whether the accounts are in agreement with the accounting records and with returns from branches.

Subsection 2 requires that if the investigations required by subsection 1 lead the auditor to form a negative opinion on proper accounting records or agreement of accounts and records then the auditor are given a duty. The duty is to state the fact of his negative opinion in his report. If he forms a positive opinion he need say nothing in the matter in his report.

Subsection 3 is another duty. If the auditor fails to get all the information and explanations which are necessary for the purposes of the audit he has to say so in his report.

Subsection 4 gives the auditor some more duties the requirement mentioned are concerned with disclosure in the accounts of dealing with directors (remuneration, loans e.t.c.)

Powers

An auditor of a limited company is given burdensome duties by the companies act. he is required to make a report on, amongst other things, the truth and fairness of the annual accounts. if he is negligent in any way and fails to discover that the accounts contain an untruth or do not fairly present the position then he may be legally required to compensate from his own pocket any persons who lose money as a result of actions taken as a result of the false accounts.

Non Audit Services

The effect of non audit services on auditors' objectivity has long been an area of concern. That concern has been compounded in recent years by significant increases in the scope of non audit services provided by audit firms.

Audit Fees and Independence Threat

external auditor plays a crucial role in improving and promoting financial reporting quality because auditors give credibility to accounting information system by providing verify independent of manager to prepared the financial statements (Simunic and Stein 1987). Therefore an outsider cannot trust a company's financial statement without having confidence in the independence of an auditor. in order to issue a qualified opinion, an auditor must be able to objectively evaluate firms' performance and also to withstand client pressure to issue an opinion (Hillson and Morecroft 2004). thus based on this, it is not surprising that the research on whether auditors compromise their independence through fee provide mixed evidence.

Self Interest Threat

This is a threat to auditors' objectivity stems from a financial or other self interest conflict which could result from a direct interest or indirect interest in a client for losing the audit assignment. Which might make them being reluctant to take actions that would be adverse to the interest of the audit firm?

Self Review Threat

This arises when the result of non audit service is performed by the auditors or by others within the audit firm are included in the figures disclose in the financial statements. The apparent difficulty of maintaining objectivity and conducting what is effectively a self review if any product or judgment of a previous audit assignment or non audit assignment needs to be challenged or re-evaluated in reaching audit conclusion.

We have many other threat that can question the independence of an audit which include (Whitaker A.M, 2006): familiarity threat, advocacy threat, intimidation threat and management threat

Evolution of 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. Hence, the need for proper book-keeping and an independent assessment of the accountability of management to owners.

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 etc(Olagunju: 2008).

Balance sheet: 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.

Purpose of Financial Statements

The objective of financial statements is to provide information about the financial position, performance and changes in financial position of an enterprise that is useful to a wide range of users in making economic decisions. Financial statements should be understandable, relevant, reliable and comparable. Reported assets, liabilities and equity are directly related to an organization's financial position. Reported income and expenses are directly related to an organization's financial performance.

Financial statements are intended to be understandable by readers who have "a reasonable knowledge of business and economic activities and Accounting and who are willing to study the information diligently. Users may use financial statements for different purposes:

Owners and managers require financial statements to make important business decisions that affect its continued operations. Financial analysis is then performed on these statements to provide management with a more detailed understanding of the figures. These statements are also used as part of management's annual report to the stockholders.

Employees also need these reports in making collective bargaining agreements (CAB) with the management, in the case of labour unions or for individuals in discussing their compensation, promotion and rankings.

Prospective investors make use of financial statements to assess the viability of investing in a business. Financial analyses are often used by investors and are prepared by professionals (financial analysts), thus providing them with the basis for making investment decisions.

Financial institutions (banks and other lending companies) use them to decide whether to grant a company with fresh working capital or extend debt securities (such as a long-term bank loan or debentures) to finance expansion and other significant expenditures.

Government entities (tax authorities) need financial statements to ascertain the propriety and accuracy of taxes and other duties declared and paid by a company.

Vendors who extend credit to a business require financial statements to assess the credit worthiness of the business.

Media and the general public are also interested in financial statements for a variety of reasons.

Quality of Financial Statements

Understandable: it is very important that any information produced must be understandable. Financial statement is intended to be understood by readers who have economic and business knowledge. As business owner, you have to think of the different accounting backgrounds of different types of people who will be reading your reports.

Relevant & material: it is important to disclosed and report information that is relevant for anyone to make a decision. Accounting information must also deals with those things that are significant to impact decision that are made by those who use financial reports

Reliable: the figures and facts printed on your financial statement must be true and fair. Your financial statement must be verifiable and free from error.

Comparable: comparability relates to the ability of information to be compared with those of other similar companies so that decision-makers can compare which of the choices or decision they should take. Generally accepted accounting principles (GAAP) allow for certain choices of different accounting methods for depreciation and inventory management.

Method

Population, Sample and Sampling Procedure of the Study

The study covers 100 respondents purposively selected from the population. The basic research design used in this study was survey. The population of the study consisted of banks and telecommunication companies in Nigeria. The sampling method used to select ten organizations out of the population was simple random sampling technique. With this sampling procedure, every bank had an equal chance of being selected out of the population of the study. Table 1 shows the number of companies involved and the number of questionnaires distributed and returns of questionnaires. The two hypothesized statements were tested using chi-square in analysing and interpreting responses connected with the main variables of the hypotheses

Research Instruments

The study made use of primary and secondary data. Concerning the primary source, questionnaire was used to gather the data. The questionnaire was a five-point rating scale (Likert scale), starting from strongly agreed (SA), agreed (A), and undecided (UN), disagreed (d), and strongly disagreed (SD). The questionnaire was designed in such a way that every question in the questionnaire was related to the research questions and hypothesis of the study. Also the result was used to answer the research questions and test the relevant hypotheses.

Data Summary

Based on the questionnaire prepared and administered on 100 respondents that made up the sample of the study, the following data in table 1 bellow is the sample generated from the population of the study.

table 1. Distribution and return of questionnaire

Respondents	Number administered	% of number administered	Number returned	% of number returned
A	25	25	19	23.75%
B	25	25	22	27.5%
C	25	25	20	25%
D	25	25	19	23.75%
Total	100	100%	80	100%

Source: field survey, April 2011

Test of Hypotheses

Chi-square of independence test with 5% level of significance was employed in testing the hypothesis. The decision rule is to accept the alternative hypothesis if the calculated value is greater than the critical value and reject if otherwise.

Chi-square is calculated with the help of the following formula.

$$X^2 = \sum \frac{(o_{ij} - e_{ij})^2}{E_{ij}}$$

Where o_{ij} = represents observed frequency

E_{ij} = represents expected frequency

$E = \frac{\text{number of questionnaire}}{\text{Number of response}}$

Level of significant = 0.05

Formula for degree of freedom = $n-1$

Therefore the degree of freedom $df = 5-1 = 4$

Thus, the value of x^2 from that 4 degree of freedom at 5% significance is 9.488

The hypothesis to be tested is:

Hypothesis One

H_0 : There is no significant relationship between auditors' independence and credibility of the financial statement

H_1 : There is significant relationship between auditors' independence and the credibility of the financial statement. This hypothesis is representing question 15

Table 2

Question: Does auditor independence affect the credibility of the financial statement?

s/no.	Responses	No. of respondent	% of respondents
1	strongly agree	30	38
2	agree	38	47
3	undecided	3	4
4	disagree	9	11
5	strongly disagree	0	0
Total		80	100

Source: Field survey, April 2011

Table 3

Degree of freedom= 5-1=4

observed	expected	o-e	(o-e) ²	(o-e) ² /e
30	16	14	196	12.25
38	16	22	484	30.25
3	16	-13	169	10.56
9	16	-7	49	3.06
0	16	-16	256	16
80			$\chi^2 =$	72.12

Source: Field survey, April 2011

At 5% it is 9.488

Decision rule

If the calculated χ^2 is less than the critical value (i.e. The value of χ^2 from the table) accept the null hypothesis and reject the alternative and if the calculated χ^2 is greater than the critical value the alternative hypothesis will be accepted and the null hypothesis rejected.

Decision

Since from computation χ^2 is 72.12 which is greater than χ^2 critical at 9.488, therefore the null hypothesis (h_0) is rejected while the alternative that hypothesis h_1 is accepted. This means that the independence of an auditor affects the credibility of the financial statement

Hypothesis Two:

H_0 : Improvement in the credibility of the financial statement cannot minimized the manipulation of financial statement

H_1 : Improvement in the credibility of the financial statement can minimized the manipulation of financial statement.

This hypothesis is representing question 16

Table 4

s/no.	responses	no. of respondent	% no of respondent
1	strongly agree	30	37
2	agree	33	41
3	undecided	11	13
4	disagree	6	8
5	strongly disagree	0	0
total		80	100

Source: Field Survey, April 2011

Table 4.3.2- Analysis of Questionnaire based on Hypothesis 1

Observed	Expected	O-E	(O-E) ²	(O-E) ² /E
----------	----------	-----	--------------------	-----------------------

30	16	14	196	12.25
33	16	17	289	18.06
11	16	-5	25	1.56
6	16	-10	100	6.25
0	16	-16	256	16
80			$\chi^2 =$	54.12

Decision Rule

If the calculated χ^2 is less than the critical value (i.e. The value of χ^2 from the table) accept the null hypothesis and reject the alternative and if the calculated χ^2 is greater than the critical value the alternative hypothesis will be accepted and the null hypothesis rejected.

Decision

Since from computation, χ^2 is 54.12 which is greater than χ^2 critical at 9.488, therefore the null hypothesis (H_0) is rejected while the alternative that hypothesis h_1 is accepted. This means that improvement in the credibility of the financial statement can minimize the manipulation of financial statement

Discussion of Findings

The result of the hypothesis tested show that the independence of an auditor affects the credibility of financial statement. The purpose of an audit is to enhance the credibility of the financial statements by given reasonable assurance from an independent source that they present a true and fair view in accordance with an accounting standard. Independence is fundamental to the credibility and reliability of auditor's report and if the reports are not credible, the investor would have little confidence in them if auditors are not independent in both fact and appearance. This means that when an auditor is independent, he will be able to present true and fair result for the management and which will make its financial statement credible and reliable. Auditing which involves an independent examination of the financial statement of an enterprise that is prepared by the management of that enterprise by an appointed person called the auditor in order to express a professional opinion whether or not those financial statement show a true and fair view position of the enterprise as at the end of the financial period in accordance with the auditors terms of engagement as well as other relevant statutory and professional regulation. Users of audited report also believe that an auditors opinion on the financial statement of a company can be relied upon which makes it credible.

Furthermore, result on hypothesis two tested also showed that the improvement in the credibility of the financial statement can minimize the manipulation of financial statement. This means that credible financial statement prepared can reduce the manipulation of financial statement by the management. From the ancient period up to the middle of 19th century, the main objective of auditing was for detection of fraud. When fraud are detected it will minimized the level of manipulation done by the management since they know that the external auditor will detect it and their determination is of truth and fairness of reported financial statement. This type of report is issued by an auditor when the financial statements presented are free from material misstatements and are represented fairly in accordance with the generally accepted accounting principles (GAAP), which in other words means that the company's financial condition, position, and operations are fairly presented in the financial statements. It is the best type of report an audit may receive from an external auditor.

Conclusion

From the discussion presented in the preceding section of this study, the following conclusions were made:

1. It is clear that auditors' independence is fundamental to the credibility of the financial statement. The opinion of the auditor is what the users of financial statement use in making their decisions.
2. For appropriate decision to be made the auditor's report has to be one that is void of bias or manipulation. In order to be able to do this efficiently the auditor should be discouraged from providing non audit services.
3. Auditors fee are influenced by various economic determinants including the size and complexity of the audit work. For example, Kinney and Libby (2002) argue that unexpected fee are a better measure of the auditors economic bond because they reflect the excess profit derived from an audit client
4. According to the standard (IAS 24), an auditor does not have primary responsibility for the prevention of fraud, but provides an approach that an auditor should follow when conducting an audit. It state that when planning and performing an audit procedures, reporting and evaluating the procedure thereon, the auditor must consider the risk of material misstatement in the financial statement resulting from error and fraud.

Recommendations

This study has investigated many issues, both empirically and in literature and based on the findings, certain conclusion have been drawn. This section further extends frontiers of the study by putting up some recommendations generally intended towards improving the independence of an auditor that will enhance the credibility of the financial statement. The following specific recommendations are deemed appropriate at this juncture.

1. For auditors to remain strictly independent, they should not be allowed to provide audit clients with any other advisory services.
2. There should be rotation of auditors to improve the auditors' independence.
3. There should be an implementation of peer assessment in order to ensure that audits are carried out with utmost professionalism and mutual respect.
4. An audit committee should be set up by every limited liability company to evaluate the audit work done.
5. The aspect of auditors providing consulting services to the client company should be properly examined

It is anticipated that when all these are done it help the auditor to be independent and also be able to present a true and fair view of the financial statements.

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