

Auditor's Independence and Internal Control System in Damaturu Local Government Area

Mohammed Gana Ibrahim, Mohammed Abbas Ardo and Abdulmalik Ahmed

Department Accountancy

The Federal Polytechnic Damaturu

Corresponding author: mganaibrahim@gmail.com, 08060354890

ABSTRACT

This study examines auditor's independence and internal control in Damaturu local government area, it's a known fact that local government administration in Nigeria is vulnerable to lot of problems, Damaturu local government, is not an exception. The objective of this study is to examined auditor's Independence and Internal control in Damaturu local government the population of the study are the entire staff of treasury and account department of Damaturu local government as at 2023. A sample size of 24 staff was drawn using simple random technique. Both primary and secondary data were employed. Data obtained was analysed and hypotheses tested using chi-square which revealed however as follows that, Internal control system has no significant effect on resources mismanagement in Damaturu local government, Auditors independence has no effect on duplicate of function and duties in Damaturu local government, Auditors independence has no effect on weak internal control system in Damaturu local government,. Therefore, the study recommends that authorities at the local government level especially in Damaturu local government should allowed auditor's to exercise their independence as well as ensure internal control system adequately operational to curb resources mismanagement and wastages in the local government.

Key words: Auditors, independence, internal control, local government

INTRODUCTION

The efficiency and effectiveness of a good internal control system as well as auditor's independence in any establishment cannot be overemphasized as the duo served as a consolidated (building blocks capable of standing test off time) it is the building block and for ensuring effective control, and judicious use of resources for effective local government administrative performance. In the Nigeria's local government settings, the responsibility for the preparation of accounts is with the Treasurer of Local Government and the effective controls of accounts according to legal and regulatory framework is a major managerial responsibility placed on competent public accounting officers who reports or prepares accounts and present such to the Chairman for endorsement. To enhance credibility and transparency of financial system and stakeholders' reliance on the statements of accounts prepared by them, Auditor's independence becomes imperative as this will enable the Auditor give objective audit opinion on the financial statement placed before him. Auditor independence is a situation where the auditor is in position to take an unbiased viewpoint in performing an audit test, analyzing the result and reporting it objectively. It is this act of meaningful audit exercise that gives credibility to the activities of public officers through a mechanism for checkmating their activities to ensure that government funds entrusted are properly appropriated, and accounts prepared according to stipulations and lay down principles. These lay down principles of operation within the Local government also is to ensure proper administration and adherence to financial regulations provisions.

A well-established internal control system reveals how the government efficiently manages its finances and its use of public resources, hence there is need to pay special attention to the

improvement of local government whole system of administration, to ensure the public resources with public office holders are properly managed and utilized for the growth and development of the society. Hence, all local government and ministries ought to enhance and ensure the adequacy of internal control systems, auditor's independence because they promote good governance. Such successful internal control framework can give information to the Council's Management about the advancement, or otherwise towards the accomplishment of their objectives. Local government is said to be run effectively if they are able to stick to established policies, setup a framework that would stop and eradicate manipulation of accounting information.

However, this study's objective is to evaluate the auditor's independence and internal control in Damaturu local government area of Yobe State. The paper sought to test the following hypotheses, stated in null form:

H₀₁: Internal control system has no significant effect on resources mismanagement in Damaturu local government".

H₀₂: Auditors independence has no significant effect on duplication of function and duties in Damaturu local government.

H₀₃: Auditors independence has no significant effect on internal control in Damaturu Local government

Thus, the finding of the study would help administrators in the Nigerian local government through formulating strategies and decisions that will have bearing on the life of a common man at the grassroots.

Concept of Auditor's Independence

Auditor's independence has been defined by different people all stressing that auditor be allowed to carry out his work freely without interference. The purpose of an audit is to

Auditor's Independence and Internal Control System in Damaturu Local Government Area

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.

The concepts that underpin this study are auditors' independence and internal control system. Different authors have different views on the meaning and usage of these concepts.

Mautz and Sharaf (1961) proposed that practitioner's independence is based on professional independence consisted of objectivity, integrity of auditor professional. Whereas, professional independence refers to apparent independence of auditors to the public as a professional group. This view is similar to the lines of thought of American Institute of Certified Public Accountants' (2017) Code of Professional Conduct which defines independence as "the capacity of auditor to remain impartial and objective during the process". AICPA stated further that "it requires that the relationship between auditors and their clients must be such that the auditors will appear independent to third parties". These key definitions appear to be in agreement as to basic essentials of auditors' independence, summary of which is that, if their opinions on the financial statements must be credible, the external auditors' position should be such that would enable them to be objective and impartial.

On this note, Okolie (2007) equates auditors' independence, objectivity, impartiality, fairness, unbiasedness, and honesty". The definitions of auditor's independence above lend credence to one position which is, that auditor's independence implies objectivity and integrity, and that auditor's judgment is not subordinate to the wishes or directives of other parties such as directors or top management or his own self-interest.

According to Wiki Accounting (2023), Auditor's independence means the ability of the auditor to adopt an approach with integrity and objectivity within the audit process. This mainly requires the auditor to have the liberty to execute his work in a free and objective manner. It gives him the ability to base his opinions without any biases or external pressures. Hence, when the auditor cannot adopt an independent approach towards the audit process, the statement issued might not be valid and cannot be relied upon.

Maury (2020) sees audit independence as an auditor' unbiased mental attitude in making decisions throughout the audit and financial reporting. The attribute of audit 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. 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.

Sridharan, Animasaun and Adegbite (2002) similarly states that auditor's independence refers to auditor's ability to maintain an objective and impartial mental attitude throughout the audit. In the absence of independence, the value of audit services will be greatly impaired and in turn, if an auditor lacks independence, this increases the likelihood that they would be perceived as less likely to report an objectives discovered breaches. Compromised audit independence results in a lower level of audit quality being provided on financial statements. 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.

Samphina (2022) stated that 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 independence, including independent in fact. After the securities act of 1993 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.

Concept of Internal Control

According to Isah (2021), The auditing standards Guidelines define an internal control system as “the whole system of controls both financial and otherwise established by management in order to carry on the business of the enterprise in an orderly and efficient manner, ensure adherence to management policies, safeguard the assets and secure as far as possible the completeness and accuracy of the records”. It is also defined as a systematic measures (such as reviews, checks and balances, methods and procedures) instituted by an organization to conduct its business in an orderly and efficient manner, safeguard its assets and resources, deter and detect errors, fraud, and theft, ensure accuracy and completeness of its accounting data, produce reliable and timely financial and management information, and ensure adherence to its policies and plans.

William, (2020) also defined internal controls as the process affected by an entity’s Board of Directors, Management and other personnel designed to provide reasonable assurance regarding the achievement of objective in the following categories. Operation’s control - relating to the effective and efficient use of the entity’s resource. Financial reporting controls- relating to the preparation or reliable published financial statement. Compliance controls - relating to the entity compliance with applicable

laws and regulations. Internal controls work best when they are applied to multiple divisions and deal with the interactions between the various business departments. No two systems of internal controls are identical, but many core philosophies regarding financial integrity and accounting practices have become standard management practices. According to the University of Delaware HULLIHEN hall, internal control is broadly defined as a process, designed by entity’s board of trustees, management, and other personnels, to provide reasonable assurances regarding the achievement of objectives in the following categories: Effectiveness and efficiency of operations Reliability of financial reporting Compliance with applicable laws and regulations Safeguarding assets.

Restrictions on Auditors Independence

Samphina (2022), states that when auditors of a company are in conflict with the directors it is important that this conflict be resolved without the auditors losing any of their independence. This can prove to be difficult as auditor earns a fee by rendering services to the former a means of livelihood. 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 and maintain repeat business? He opines that 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 automatically he does not want anything jeopardizing his income. This reliance on clients’ fees may affect the independence of an auditor. If the auditor feels his 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

Auditor’s Independence and Internal Control System in Damaturu Local Government Area

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, Okezie & Egeolu. (2019) opined that 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 their 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.

Limitations of Internal Control System

Internal control system, no matter how sophisticated or strong, it cannot by itself guarantee efficient administration and accuracy of records, nor can it be full proofed against part of those holding position of authority or trust.

According to Kenyon (2006) the following are some of the limitations of effective internal control system.

Staff collusion: This means the control system which depends on segregation of duties, can be rendered ineffective by the collusion of staff performing complementing functions.

Abuse of authority: This occurs when staff vested with authority of exercising authorization decides to convert such controls to satisfy selfish ends or engage in transactions that are deemed fraudulent.

Management overriding established control: For control to work, members of the organization whether in management or operational cadre must submit themselves to control procedures put in place. For example, if management refuses to be subjected to security checks by gatekeepers, such actions are imitated by officers immediately below the management and before you know it, control is jeopardized and rendered ineffective.

Incompetence and human factors: This occurs when unqualified or inexperienced staff assigned a position of authority that is greater than their capabilities. Therefore, whenever a mistake is done in course of carrying out personnel control, the consequence may be fatal to other controls put in place.

THEORETICAL FRAMEWORK

The Policeman Theory

This theory claims that auditor is responsible for searching, discovering and preventing fraud. In the early 20th century this was certainly the case. However, more recently the main concern of auditors has been to provide reasonable assurance and verify the truth and fairness of the financial statements. However, the detection of fraud is still a hot topic in the debate on the auditor's responsibilities. Typically after the events where financial statement frauds have been revealed, the pressure increases on increasing the responsibilities of auditors in detecting fraud.

Signaling Theory: Originally developed by Michael Spence in 1973, the signaling theory refers to a situation where one party (termed the agent) credibly conveys information to another party (the principal). It was initially based on observed knowledge gaps between organizations and prospective employees but later extended to other domains. Signaling theory posits that firms with good performance are inclined to making voluntary disclosures more readily because doing so is regarded as an easy means of distinguishing themselves from others in the marketplace. Hence this study assumes that auditors' independence is positively related to reliability of financial reports. It is suggested by Scott (2009) that manipulative accounting may be used for signaling since managers will endeavor to window-dress the report in such a manner that it will transmit their desired information to users.

Systems Theory: Harvey and Brown, (2018) sees system as a set of interrelated and related segments that cooperate in a manner to accomplish a set objective. These components or sub-systems are between ward and the disappointment of one component prompts the disappointment of the entire system. An association is a perplexing system which is isolated in different subsystem (units, divisions and offices) and henceforth requires an arrangement of powers over units, divisions,

offices, for its adequacy and survival. A successful internal control system is a coordinated framework with interrelated parts, supporting standards and characteristics. As indicated by Grieves (2015), an internal control system accessible to a firm comprises of: the board oversight and the control culture; chance acknowledgment and evaluation; control of exercises and isolation of obligations; data and correspondence and checking exercises and adjusting deficiencies. Internal control system is an integrated system, integrated with management processes to attain overall organizational goals. For an organization to achieve its organizational objectives, then the five control components of control environment, risk assessment, control environment, information and communication and monitoring must be integrated into management processes over the entire organization (Subsidiaries, divisions, units). Like the body system, the internal control components and other processes must interact ceaselessly for a healthy, effective internal control system. Control objectives and measures that are derived from the monitoring and assessment of risks must be integrated into operational business units' business practices. The justification of utilizing system theory in this paper is that, system is included with a few segments which work together in order to guarantee the objective and goals of the organization are accomplished. An organization can have different internal control system which work together to guarantee responsibility. For example, as an internal control system, money related administration system cannot work alone without other control systems, for example, lawful structure. However the, system is aimed to work together to accomplish objectives and targets of the association. In that specific case, it guarantees responsibility.

Auditor's Independence and Internal Control System in Damaturu Local Government Area

For the purpose of this paper, since the main objective of this study is to examine the auditor's independence and internal control system in Damaturu Local Government area of Yobe State. This work is anchored on both the signaling and system theory because these theories contribution bring a lot in assessing the relationship between Auditor's Independence and Internal control on improving the value of local government financial credibility.

Methodology

The study uses a descriptive survey research design, the purpose of using survey research design to describe the state of affairs as it exists at the present time. The population of the research consists of all the staff of Damaturu Local Government Area as at 2023. The sample is Twenty Four (24) respondents from the account and treasury department of Damaturu Local Government consisting of the senior, junior and other staff, which are categorized as following; Senior staff 6, Junior 10 and other staff 8. The simple random sampling was used to give each member of the population equal chance of being selected as every member has vital information to share which is required by the study. Two

methods of data collection which are primary source and secondary source were used to collect data related to the topic either past, present, prevailing and anticipated conditions as they affects the research problems The primary sources was the use of questionnaires, while the secondary sources include textbooks, internet, journals, published and unpublished articles and government publications. The responses were analyzed using the simple percentage which provided answers to the research questions, while the hypotheses stated were tested using Chi-square. This gives a compelling reason to reduce bias and assist the study to make fair analytical judgment that rules out misinterpretations.

Each chi-square were tested as follows
Chi-square formula = $X^2 = \sum (fo-fe)^2$

Where:-
 \sum = Summation
 fo = Observed Frequency
 Fe = Expected Frequency

The ninety five (95%) confidence level was used, where computed value is greater than critical value at 0.05 level of significance, the null hypotheses is rejected and alternative accepted and vice versa.

Table 1: Question 1: Does internal control system have any significant effect on recourses mismanagement in Damaturu local government.

Respondent	Yes	No	Total
Senior	6	-	6
Junior	9	1	10
Others	6	2	8
Total	21	3	24
Percentage	87.5%	12.5%	100%

Source: Field Survey 2023.

Table 1 shows that 87.5% agrees that internal control has significant effect on resources mismanagement, while 12.5% representing 3 of the entire sample did not agree to the question raised. This plies that internal control has significant effect on resources mismanagement in Damaturu local government.

Question 2: Does auditor's independence have significant effect on duplicate of functions and duties in Damaturu local government.

Auditor's Independence and Internal Control System in Damaturu Local Government Area

Respondents	Yes	No	Total
Senior	4	2	6
Junior	6	4	10
Others	5	3	8
Total	15	9	24
Percentage	62.5%	37.5%	100%

Source: Field Survey 2023.

From table 2, 62.5% respondents are of the opinion that auditors independence has significant effect on duplicate of function and duties, while 37.5% affirmed that auditors independence does not have effect of duplicate of function and duties in Damaturu local government. This clearly depicts that auditor's independence has significant effect on duplicate of function and duties in Damaturu local government.

Question 3: Does auditor's independence has any effect on internal control system in the Damaturu Local government.

Respondent	Yes	No	Total
Senior	5	1	6
Junior	7	3	10
Others	6	2	8
Total	18	6	24
Percentage	75%	25%	100%

Source: Field Survey 2023.

From the table above, 75% agreed that auditor's independence has effects on weak internal control in Damaturu local government, while 25% did not agree that auditor's independence has effects on internal control. This shows that auditor's independence has effects on internal control in Damaturu local government.

Question 4: Does embezzlement of funds affect internal control system in Damaturu local government?

Respondent	Yes	No	Total
Senior	1	5	6
Junior	4	6	10
Others	3	5	8
Total	8	16	24
Percentage	33.3%	66.7%	100%

Source: Field Survey 2023.

Table 4 shows that 33.3% agrees that embezzlement of funds affect internal control system in Damaturu local government, while (16) respondents representing 66.7% says that it does not. This depicts that embezzlement of funds does not affect internal control system in Damaturu local government.

Table 5: Question 5: Do auditors depend on internal control system when carrying out their work?

Respondents	Yes	No	Total
Senior	2	4	6
Junior	2	8	10
Others	4	4	8
Total	8	16	24
Percentage	33.3%	66.7%	100%

Source: Field Survey 2023

Table 5 above, 33.3% of the total respondents agree that auditors depend on internal control system when carrying out their work in Damaturu local, while 66.7% of the total respondents did not agree that auditors depends on internal control system when carrying out their work in Damaturu local. This shows that auditors do not depend on internal control system when carrying out their work in Damaturu local government.

Table 6: Are there factors that hinder effective implementation of sound internal control system in Damaturu local government.

Respondents	Yes	No	Total
Senior	6	0	6
Junior	8	2	10
Others	5	3	8
Total	19	5	24
Percentage	79.2%	20.8%	100%

Source: Field Survey 2023.

Table 6 show that 79.2% of the total respondents agree that there factors that hinders effective implementation of sound internal control system in Damaturu local government, while 20.8% of the total respondents did not agree that there are factors that hinders effective implementation of sound internal control system in Damaturu local government. This depicts that there are factors that hinders effective implementation of sound internal control system in Damaturu local.

Table 7 Are there measures in place to improve the internal control system in Damaturu local government.

Respondents	Yes	No	Total
Senior	2	4	6
Junior	5	5	10
Others	3	5	8
Total	10	14	24
Percentage	41.7%	58.33%	100%

Source: Field Survey 2023

Table 7 shows that 41.7% agree that there are measures in place to improve the internal control system in Damaturu local government, 58.33% of the total respondents did not agree. This implies that there are no measures in place to improve the internal control system in Damaturu local government.

Hypothesis I

H₀₁: Internal control system has no significant effect on resources mismanagement in Damaturu local government".

Auditor's Independence and Internal Control System in Damaturu Local Government Area

Contingency table

Observed	Expected	(O - E) ²	(O - E) ² /E
6	5.25	0.56	0.11
9	8.75	0.06	0.007
6	7.00	1	0.14
0	0.75	0.56	0.75
1	1.25	0.06	0.048
2	1	1	1

$X^2 = 2.06$

Base on the above, the decision rule is to accept the null hypotheses (H_{01}) and reject the alternative hypotheses since the calculated X^2 (2.06) is less than the tabulated value of (5.99). The table X^2 was arrived at by determining the degree of freedom

The degree of freedom (df) = (C - 1) (R - 1)

R= row total

$(3-1)(2-1) = 2 \times 1 = 2$

(Df) at special level of significance at 0.05 = 5.99

Therefore we accept the alternative hypotheses at 95% confidence level and critical value of 0.05 level of significance.

Hypothesis 2

H_{02} : Auditors independence has no significant effect on duplication of function and duties in Damaturu local government.

Table 9: Contingency Table

Observed	Expected	(O - E) ²	(O - E) ² / E
4	3.75	0.06	0.016
6	6.25	0.06	0.0096
5	5	0	0
2	2.25	0.06	0.027
4	3.75	0.06	0.016
3	3	0	0

$X^2 = 0.07$

The table above shows the computation of chi-square of 0.07 which is lower than the critical value at 5% level of significant is 5.99, the research failed to reject the null hypothesis (H_{02}) which state that "": Auditors

independence has no significant effect on duplication of function and duties in Damaturu local government".

Hypothesis Three

H₀₃: Auditor’s independence has no significant effect on internal control system in Damaturu local government.

Contingency table

Table 10: response for Hypothesis Three

Observed	Expected	(O - E) ²	(O - E) ² / E
5	4.5	0.25	0.056
7	7.5	0.25	0.033
6	6	0	0
1	1.5	0.25	0.167
3	2.5	0.25	0.1
2	2	0	0

$X^2 = 0.356$

Table 10 shows the computation of chi-square of 0.356 which is lower than the critical value at 5% level of significant is 5.99, the research failed to reject the null hypothesis (H₀₃) which state that "Auditors independence has no significant effect on weak internal control system in Damaturu local government.

Based on the chi-square results, it is concluded that the study failed to reject the five, Null Hypotheses (H₀) as a result of critical value (5.99) greater than the calculated values.

This implies that, internal control system has no significant effect on resources mismanagement in Damaturu local government; Auditor’s independence has no significant effect on duplication of function and duties in Damaturu local government. Auditor’s independence has no effect on internal control system in Damaturu local government.

Conclusion and Recommendations

This study examines Auditor’s Independence and Internal Control in Damaturu local Government.

Auditor’s Independence and Internal Control System in Damaturu Local Government Area

Results from the Chi square analysis revealed that internal control system has no significant effect on recourse mismanagement in Damaturu local government, that auditor’s independence has no significant effect on duplication of functions and duties in Damaturu local government, while the last hypotheses also revealed that auditor’s independence has no effect on internal control system in the Damaturu Local government. This mean in order to ensure adequate discharge of duties and responsibilities in the affairs of Damaturu local government auditors as a matter fact auditors have to be accorded their legitimate recognition as well as ensure a fully operational internal control on ground by so doing resources and records will be adequately safeguarded.

The study recommended as follows:

- i. Internal control system should be strengthened and improved greatly to curb resources mismanagement and wastages in Damaturu local government.

- ii. Auditor's independence should be paramount at all times so as to avoid unbiased review resulting into poor and inefficient use of resources.
- iii. Auditors should demonstrate professionalism while discharging their duties by adhering strictly to the profession's code of ethics.

References

Adebayo, A., (2011). Financial reporting: An aid to efficient economic management in the public sector. *Niger. Accountant*, 38(1): 33-38.

American Institute of Certified Public Accountants, 2017

Damagum. I. M. (2021). *Basic auditing theory*, Jos: University of Jos Press Limited

Grives, (2015). *Role of company's internal control system in Fraud Prevention*

Harvey and Brown (2018). *Internal control system implementation and fraud detection*

Kenyon (2006). *Implementing audit guide*. USA.

Mautz, R. K. and Sahraf, H. A. (1961). *The philosophy of auditing*, Florida: American Accounting Association.

Okolie, A. O. (2014). Auditor tenure, auditor independence and accrual – based earnings management of quoted companies in Nigeria. *European Journal of Accounting Auditing and Finance Research*, 2(2), 63–90.

Siegel. Authur (2002) *Threats and safeguards in the determination of auditor independence* William T. Allen New

York University Independence Standards Board

Stewart, J. and Subramaniam, N. (2010). "Internal audit independence and objectivity: Emerging Research Opportunities" January 2010

Ultimate, Okozie and Egeolu (2019). *Relationship between auditor's independence and the credibility of the financial statement in Nigeria*. Enugu, Enugu State - Nigeria

Wiki Accounting 2023

William, R. S. (2009). *Financial accounting theory* (5th edit). Pearson Prentice hall: Toronto – Canada.