

## CHAPTER ONE

### INTRODUCTION

#### 1.0 BACKGROUND TO THE STUDY

As the stakeholders become dissatisfied with the work of the audit profession, their confidence in audited financial statements will erode with time if nothing is done to remedy the situation. Best, Buckby and Tan (2001) claim that society's trust is the 'heart-beat of a profession'. Hence, if such trust disappears or is eroded in any way, the outcome is likely to involve skepticism and the depletion of value attributed to such profession. Although fraud detection has been taking out of the primary objectives of the auditing profession, the 5th Global Economic Crime Survey by PricewaterhouseCoopers (2009) reports that fraud remains a pervasive business risk and almost every firm is subjected to occupational fraud in their daily businesses, leading to huge losses for businesses and society.

There is no gainsaying that the audit profession is a social functions which provides services to associated parties and is based on confidence between the professional auditor and those parties. the importance and responsibilities of auditing has increased in recent years due in part to reliance of other parties on the data included in the financial statement and audit reports produced by the auditor. Despite the importance of the audit profession, it has been subjected to increased criticisms in the performance of its role and function, as a result of the challenges the accounting profession has faced a long time, the issue of Audit Expectation Gap (AEG) :which is the "difference between what the public and users of financial statements perceive the role of an audit to be and what the audit profession claim is expected of them during the conduct of an audit (Ojo, 2006).

The AEG has become a serious issue because of the damage it could potentially bring to the essence of auditing profession, this is why it has been increasing in its significance since it was identified in the mid 1970s.

Pierce and Kilcommins (1996) also defined the audit expectations gap as when external auditors' understanding of their role and duties is compared against the expectations of user groups and the general public. Moreover, Audit as we all know refers to the formal examination, correction, and official endorsing of financial accounts, especially those of a business, undertaken annually by an Accountant., yet the accounting profession in Nigeria has been under intense pressure due to rising public expectations which is as a result of series of financial failures that occurred during the recessionary years of the late 80's and the early 90's (Ekwueme, 2013:14). These financial failures happened too quickly after an 'unqualified' audit report was issued by the external auditors. Koh and Woo (1998), noted that in recent years, some spectacular and well-publicized corporate collapses and the subsequent implication of the reporting auditors have highlighted the audit expectation gap. In reality, the unqualified opinion is wrongly seen as a certification that the firm or enterprise is solvent, liquid and has the capacity to adapt to the dynamics of the environment. Any subsequent failure of business resulting from management misjudgment, fraudulent practice, economic instability, inconsistency in micro and macroeconomic policies etc are viewed as failures of auditors (Adeniji, 2004:510).

Furthermore, Stakeholders too often see the audit as a relatively discrete event when, in fact, the processes and controls that ensure the broader integrity of the audit comprise much more than the audit opinion itself. These processes and controls range from the company's collection and recording of financial information to

the actual audit, through to the issuance of the financial report. As a result, the quality of financial reporting – so critical to investor confidence and transparency – is directly dependent on the quality of the audit. The value of an expert, independent opinion on a company's financial statements simply can't be underestimated. And the simple knowledge that the audit is coming, combined with the requirements and internal controls that exist around it, exerts a preventative, quality-control pressure on financial statement preparation – even before the audit takes place, yet These perceptions draw a line that needs to define the role of the auditor in protecting the interest of shareholders and ensuring that there is good corporate governance. Owners of business need auditors, more than ever, to detect and prevent fraud. Perhaps, this is due to the expanding nature of modern day businesses. Clients need value added and not an auditor that will vouch and does the normal trade test (Nwokolo, 1998:25). Additionally, auditors have been known for high integrity and objectivity as well as their commitment to public interest. In relation to this view, Hillier (2000) stated that diverse clients now expect them to provide more services than just performing statutory audit and attesting to the credibility of financial statements.

## **1.2. STATEMENT OF PROBLEM**

The global search for a solution to the audit expectation gap by auditor has become strident, the credibility of the auditing profession appears to be at its lowest ebb. In the United State of America, the profession has lost its self regulatory status, in these circumstances, the profession is bestirring itself and the result is a welter of fresh suggestion and initiatives aimed at solving the expectation gap problem. Some of the suggestion appears mundane while some appears controversial. However, like a sore thumb, the gap appears to have remained as wide as ever, at the local level, the recent scandal in Cadbury Nigeria Plc whereby profit were overstated by a large sum with the knowledge of auditors, and the subsequent indictment of the accounting firm of Akintola William Deloitte for audit failure, has further aggravated the expectation gap conundrum.

The criticism of auditors in Nigeria by users of audited financial statements has stirred many a response both from the profession and statutes. It seems the users have a different idea of what auditing should be. This is what has led to the audit expectation gap. The existence of this gap has been caused by many factors [communication factors and audit failures]. In this changing world, business environment requires that auditor's responsibilities be increased to include fraud detection/prevention. Also, users want to be able to rely on audited financial statements for investment decision making. They also desire the absolute independence of the auditor because absence of it may reduce performance. Users also may have a different interpretation of the nature and meaning of audit report.

The crucial nature of auditing in ensuring the integrity and reliability of financial information cannot be overemphasized. It is for this reason that the canons of many countries require the attestation of financial statements by external auditors.

Unfortunately, there are criticisms of the auditor from which opinions have emerged over the years as a result of companies that have failed. This criticism of auditors in Nigeria by users of audited financial statements has stirred many a response both from the profession and statutes. It seems the users have a different idea of what auditing should be. This is what has led to the audit expectation gap. The existence of this gap has been caused by many factors. Moreover, the business environment is changing and this requires that the auditor's responsibilities be increased to include fraud detection/prevention. Also, users want to be able to rely on audited financial statements for investment decision making. They also desire the

absolute independence of the auditor because absence of it may reduce performance. Users also may have a different interpretation of the nature and meaning of audit report messages. These are some of the factors that contribute to the audit expectation gap.

Finally, the accounting profession in Nigeria and other climes has been under intense pressure due to rising public expectations, this expectation has been fuelled largely by demise of some financial institution as a result of widespread of financial scandals and false reporting rifle in this collapsed institution which in turn has cast the organizational controls and the professional auditors in very poor light.

It has also tended to undermine the confidence of the public in the profession to detect and prevent corporate abuses, yet audit failures are always blamed partly, on greed of the auditors, this lack of confidence on the auditing profession would in time destroy the fundamental nature of auditing, which is ensuring the integrity and reliability of financial information.

### **1.3. OBJECTIVES OF THE STUDY**

The general objective of this study is to elicit and assess the role of auditor's in audit expectation gap in Nigeria.

From this general objective, the following specific objectives are drawn:

Ascertain the responsibility and reliability factors which contribute to the audit expectation gap problem in Nigeria.

Ascertain the perception of auditors who are ICAN MEMBERS in Nigeria as to the suggestions for bridging the expectation gap.

Identify the opinion of auditors and audit beneficiaries on the statutory role of external auditors in Nigeria.

Investigate the nature of Audit Expectation Gap and users of financial statement in Nigeria.

Understand the perceptions of auditor and users regarding the auditing roles and functions in Nigeria.

Determine the role played by Auditor with respect to audit profession.

Suggest and provides recommendation to improve and enhances auditing professions.

### **1.4. RESEARCH QUESTION**

In order to achieve these objectives, an ethnographic research approach has been used to answer the question of this research. The general research question includes:

What are the responsibility and reliability factors which contribute to the audit expectation gap problem in Nigeria?

Perception of auditors who are ICAN MEMBERS in Nigeria as to the suggestions for bridging the expectation gap?

What are the opinion of auditors and audit beneficiaries on the statutory role of external auditors in Nigeria?

Investigate the nature of Audit Expectation Gap and users of financial statement in Nigeria?

What are the perceptions of auditor and users regarding the auditing roles and functions in Nigeria?

What are the roles played by Auditor with respect to audit profession?

Are there any possible recommendations to improve and enhances auditing professions?

### **1.5. STATEMENT OF HYPOTHESIS**

To achieve the above objectives, the following hypotheses are formulated for the research study, the hypothesis were stated in null forms.

#### **HYPOTHESIS ONE (1):**

Ho: There is no significant relationship between audit expectation gap and auditor responsibility relating to fraud detection and prevention, and soundness of internal control structure of the audited entity.

### **HYPOTHESIS ONE (2):**

Ho: There is no difference between the opinion of auditors and audit beneficiaries on the statutory role of external auditors in Nigeria.

### **1.6 SIGNIFICANCE OF STUDY**

The problem of audit failures globally had tended to exacerbate the problem of audit expectation gap. As a result the search for a solution has become frenetic. ICAN

MEMBERS, especially as auditors, stand at the centre of this effort at a panacea. The motivation for carrying out this study in Nigeria is that auditors are blamed for business failure, perhaps as a result of misunderstanding of the nature of auditing. This study will be beneficial to the following:

1. Audit clients: who form part of the audit beneficiaries will benefit from the results of this study. i.e. the various organization who needs auditing services. They will have a better understanding of the statutory objectives of external audit in order to reduce any unreasonable expectations of the auditor.
2. Auditors: who help to maintain public confidence in financial statements will understand the expectation of the society in view of protecting their interests and remaining relevant.
3. The Accounting Profession: may need to redefine the role of auditors with regards to AEG because of the changing nature of the business environment in Nigeria.
4. Scholars in Auditing, Forensic Accounting and Related Areas: who push the frontiers of knowledge will benefit from this study by developing research interests from the findings of this study. Also, they will have a broader understanding of the audit expectation gap in the Nigerian context.

Academics will also have a field day as this work will open a floodgate for further researches on other aspects of this all important subject matter as it affects Nigeria. Finally, the International community will have the benefit of Nigeria's experience as the global search for solution to the audit expectation gap cankerworm gathers momentum.

### **1.7. SCOPE AND LIMITATION OF STUDY**

The main focus of this study is to assess the role of auditor's in audit expectation gap in Nigeria. Since the determinants of the audit expectation gap are numerous. For the purpose of carrying out a detailed analysis of research study, the research was restricted to the auditors who are mostly ICAN Members selected from the Central Business District of Lagos metropolis, including few stockbrokers selected through list of brokerage companies that trade on the Nigeria Stock Exchange.

In a research work of this nature difficulties are bound to be encountered. The researcher in the course of carrying out the research was faced with the following problems and constraints.

There was paucity of local literature as the researcher was threading on an area that has not been over flogged. Finance constituted another problem limiting the ability of the researcher to travel more extensively in search of relevant data and opinion. Some of the professional auditors and stockbrokers filled the questionnaires in a hurry, because of their busy schedules, thus affecting the quality of their answers. Time was of the essence in this research and this also affected the researcher.

On the whole, however, the researcher was still able to use his wealth of experience to navigate successfully through the difficulties and produce a work that will stand the test of time.

### **1.8 DEFINITION OF TERMS**

1. **Audit Expectation Gap:** The “expectations gap” is the difference between what the public and users of financial statements perceive the role of an audit to be and what the audit profession claim is expected of them during the conduct of an audit (Ojo, 2006).
2. **Auditor:** Auditor is a qualified accountant who also passed a professional examination. Such a person must be of good conduct and have a vast knowledge and able to understand a practical business, endeavor always to grasp the technicalities and business, methods of any concern whose account he undertakes to audit.
3. **External Audit:** This is an audit carried out by an independent person who is not an employee of the enterprise.
5. **Quality audit** is the process of systematic examination of a quality system carried out by an internal or external quality auditor or an audit team.
6. **ICAN MEMBERS:** These are members of the Institute of Chartered Accountants of Nigeria.
7. **Expectation:** This word refers to the purpose of audit as perceived by the users of financial statements.
8. **Gap:** This is the inability of auditors to meet the expectation of the users. In this study, the gap is a result of misunderstanding of the auditor's role and responsibilities, inadequate understanding of the message passed by the audit report and expectations about auditor's independence.
9. **Reliability factor:** it elicits the extent to which Auditors' work or audited statements can be relied on.
10. **Independence factor:** this shows the extent to which independence of auditors affect the Audit Expectation Gap.

## **ASSESSMENT OF AUDIT EXPECTATION GAP IN NIGERIA, AUDITOR'S CONNECTION.**

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