The Effect of Audit Fees on Auditors Negligence

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Abstract: The research work examined the effect of audit fees on auditors' negligence. Failure to report certain weaknesses because of the auditors' negligence in his reports to management often affect the performance of corporate organizations negatively. The specific objective is to ascertain whether audit fees influences auditors' negligence. Business analysts, Investors and Academia were used to determine the effect of audit fees on auditors' negligence. Survey design was adopted for this study. Copies of questionnaires were administered to 115 sample respondents. Analysis of variance (ANOVA) was used to analyze data collected statistically at 5% or 0.05 level of significance. Regression analysis was used, with the aid of statistical package for social sciences (SPSS) 20.0 soft ware. The test showed that audit fees lead to auditors' negligence. The researcher recommends that the auditing profession should make significant regulatory pronouncement in this regard. Consequently, there is a need to strengthen the capacity of the regulatory bodies and reviewthe adequacy of statutory enforcement provisions.

Keywords: audit fees; auditor's negligence; professional ethics; competence

JEL Classification: M42

1. Introduction

The auditor, by virtue of his appointment and in course of executing his assignment, should demonstrate some professional skills and competencies as well as upholding requisite professional ethics, competence, fairness, due care, objectivity and independence are some of the requirements. Cullinan, L. (2004) said if the auditor fails to meet the standard of care required and consequently a loss is suffered by any of the affected parties due to auditor negligence, remedy can be obtained against the auditor in a constituted court of law. According to Webster's New College Dictionary (2005), negligence is to exhibit a lack of due care or concern, or to fail to care for or give proper attention. Therefore, audit negligence means some act or omissions which occur because the auditor failed to exercise that degree of reasonable skill and care which is reasonable to be expected in the circumstances of the case. What is reasonable is not what a super careful and

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expert auditor would do but what an ordinary skill man (or woman) would do in the circumstances.

Arens (2002) said, this auditor negligent may lead to audit failure due to a serious distortion of the financial statements that is not reflected in the audit report, and the auditor has made a serious error in the conduct of the audit. Odum, (2010) opines that where a company suffers loss or damages as a result of the failure of its auditor to discharge the fiduciary duty imposed on him by section 368(1) of CAMA 2004, The bankruptcy of Enron in 2001 and the resulting collapse of its auditor, Arthur Andersen, in 2002, Cadbury Nigeria Plc in 2006 have called into question the integrity of audit profession.

1.1. Statement of Problem

There have been series of enormous corporate failures, such as Enron, WorldCom, Hollinger, Nortel, Cadbury Nigeria Plc, Intercontinental Bank Plc in Nigeria, etc. involving fraudulent audited financial statements. Despite the measures taken by the professional accounting bodies in Nigeria to minimize audit failure, the problem still remains. The cry of the users of audit report has invariably been "why are auditors negligent over their duties?" The researcher examines the extent in which audit fees affect auditors' negligence.

The specific objective for the study is to ascertain whether audit fees influences auditors' negligence. The research work is guided by this hypothesis:

Ho: There is no significant relationship between audit fees and auditors' negligence.

1.2. Justification for the Study

The outcome of the study will lead to the formulation of a policy that strengthens the profession position on how auditors are expected to go about their professional duty. It would encourage the professional bodies, such as ICAN, ANAN who gave license to their members to practice as an accounting firm to make a pronouncement about fees to be collected by audit firms in order minimize auditors' negligence.

1.3. Review of Related Literature

According to Webster's New College Dictionary (2005), negligence is to exhibit a lack of due care or concern, or to fail to care for or give proper attention. Therefore, audit negligence means some act or omissions which occur because the auditor failed to exercise that degree of reasonable skill and care which is reasonable to be expected in the circumstances of the case. Palmrose, (1988) said If the auditor fails to meet the standard of care required and consequently a loss is suffered by any of the affected parties due to auditor negligence, remedy can be obtained against the auditor in a constituted court of law.

Audit failure occurs when there is a serious distortion of the financial statements that is not reflected in the audit report, and the auditor has made a serious error in the conduct of the audit (Arens, 2002). De Angelo (1981) and Simunic (1984) posit that there is an understanding that auditors face substantial economic cost when there is an occurrence of audit failure.

The audit report is the end product of every audit assignment that the auditor issues to the members of a client company expressing his opinion on the truth and fairness view regarding an enterprise's financial statements. In Nigeria, this statutory duty is provided for in Section 359(1) of the Companies and Allied Matters Act (CAMA), 1990. The auditor has a statutory responsibility by virtue of Section 359(3) of the Company and Allied Matter Act (CAMA), 2004, to issue a report to the members of the audit committee which must be statutorily set up by such a client.

According to Dictionary of accounting (2007), auditors' fees are fees paid to a company's auditors, which are approved by the shareholders at an annual general meeting. Audit fee is a fee or compensation paid by the client to the public accountant as payment for services that have been done. Audit fees are divided into two categories namely the audit fee of the total audit fees paid by the client while the non-audit fee is the cost of other services that are paid out of a total audit fee. Coate, and Loeb (1997), Elitzur and Falk (1996) said, measure the amount of audit fees can be seen from the characteristics of the client (given the complexity of the audit services, audit risk and effort to get the client) and the magnitude of Public Accounting Firm (PAF) (cost structure and size of PAF).

Firth (1997) observed that Knowledge of determinants of audit fees should be of interest and importance to suppliers and users of the audit services as well as the regulators, because, this would assist the auditors to examine their cost structure, predicting future fees and measure audit efficiency. The first studies on auditing fees were performed in the 1980s. Francis (1984) argues that a large auditing firm will charge higher fees to deliver high-quality services in a competitive market in which there is a demand for service differentiation. Thus, auditing fees can be used to analyze auditors' negligence. Dickins, Higgs, and Skantz (2008) note that there are several studies using different models and variables to find the drivers of audit negligence based on audit fees but that there is no consensus in their results.

2. Methodology

Survey design was used to address the problem of this study. The participants are the Business Analysts, investors' and Academia. Audit firms were excluded from the study to avoid conformity bias, which may results when members of a profession are included as participants in the study. Audit fees were measured by the following features; client size, audit risk (leverage), audit firm size and complexity of audit services render to the client. Test items were developed to obtain audit negligent behaviour score.

2.1. Data Collection

Questionnaire was the instrument used for data collection. The structured questionnaire was administered by hand to the respondents. A four point Likert scale was employed to extract the data. The respondents were made to indicate in the questionnaire the extent they agree or disagree to the stated problems.

2.2. Procedure for Data Analysis

The statistical model chosen for the analysis of data is linear regression analysis and analysis of variance [ANOVA], with the aid of SPSS 20.0 software.

The model in its functional form was specified as follows:

AudNeg = f (, F_k)

The null hypothesis is;

There is no significance relationship between audit fees and auditors' negligence.

Audit fees were measured by the following features; client size, audit risk (leverage), audit firm size and complexity of audit services render to the client.

The model to be used to confirm this proposition is presented below:

AudNegj = B0 + B1 F_k + ej -- eqi

Bi > 0; R^2N > 0

Bi measures the impact of audit fees on audit negligence

Where:

AudNeg = Auditors Negligence

F_k = Audit fees

e = Error term

B0 …….. B3 = Coefficient

2.3. Data Presentation and Analysis

The researcher administered one hundred and sixty – two copies of questionnaires randomly to business analysts, academia and investors out of which one hundred and fifteen copies were successfully retrieved representing 71% of the number of questionnaire administered. The test concerning the parameter was carried out using Analysis of Variance and correlation coefficient.

Administration of Questionnaire

DETAILS	NUMBER OF COPIES	PERCENTAGE (%)
COPIES ADMINISTERD	162	100 %
COPIES RETURNED	115	71 %
WRONGLY FILED / UNRETURNED COPIES	47	29 %

Source: field survey 2015.

Categories of the respondents

S/N	**Respondents**	**Total**
01	Business Analysts	47
02	Investors	40
03	Academia	28
	Total	**115**

Source: field survey 2014.

The table above shows that 47 respondents are Business analysts, 40 respondents are investors while, 28 respondents are academia. This shows that the respondents understand the concept been researched. This will help to guarantee effective response of respondents to the questionnaire.

Testing of hypothesis

Ho: There is no significance relationship between audit fees and auditors' negligence.

Table 1. Model Summary: Regression coefficient for Auditors Negligence on audit fees.

	B	Beta	T=test
Constant	97.23		T=2.81,p=.048
audit fees	20.82	.96	T=-6.95,p=.002

Note, r^2 .92, F (1,4)=48.35, p= .002

Table 2. ANOVA RESULT: Audit negligence on Audit fees.

Model	Sum of square	Df	Mean square	F
Regression	69907.46	1	69907.46	48.35
Residual	5783.88	4	1445.97	
Total	75691	5		

a:dependent variable; audneg

b: predictor(constant), audit fees

Audit fees explains 92 per cent of variation experienced in auditors negligence, and this result is significant F (1, 4) = 48.35, P < 0.05.

Audit fees make a positive impact on audit negligence and this is significant, t(6.95), $P < 0.05$. Therefore, as audit fees increases, auditors' negligence increases.

Decision

Based on the analysis above, the null hypothesis (H0) is rejected while alternative hypothesis (H1) is accepted; which state that there is significant relationship between audit tenure and audit negligence.

3. Summary of Findings

Based on analyzed data, the findings in this study include the followings:

1. It was discovered that audit fees explain 92 percent of variation in auditors' negligence, and this result is significant. Big audit firm do protect their big client, because of fees derived from them, during their audit assignment.

2. We discovered that the auditing firm will be more reluctant to indicate errors in financial statements if it knows that this will significantly jeopardize its future profits.

4. Conclusion and Recommendation

Auditors tend to be negligent in performing their audit assignment when they derived higher percentage of their income from a client. Therefore, audit fees do induce auditors to be negligent in performing audit assignment. The recommendation is that the professional bodies, such as ICAN and ANAN, should make a pronouncement about fees to be collected by audit firms in order minimize auditors negligence.

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