

Application of Auditing Standards and Financial Reporting Among Selected Organizations in Central Region, Uganda

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Abstract

The study investigated the level of compliance with auditing standards in selected organizations in Kampala, Uganda. The specific objective of the study was to determine the level of compliance with auditing standards. The study used a quantitative, ex-post facto, descriptive, comparative, cross-sectional and correlational survey design. Using a self made questionnaire, data was collected answering specific questions on a four point Likert scale. Data analysis by means of frequencies, percentages and means was done, using SPSS. It was revealed that majority of auditors and accountants are University graduates, in the 20 to 39 years age bracket and most of them are men. There is a high level of compliance with auditing standards (general average mean = 3.54) in the selected organizations in Kampala. It was recommended that auditors evaluate team members' competence before deployment of teams for audit, conduct audits from clients' premises and issue timely audit reports. There is also need to emphasize follow up of audit findings and recommendations from previous audits by auditors or Audit Committees.

Introduction

Large organizations like listed companies on stock exchange markets, Government Ministries, Departments and corporations, and all businesses that pay taxes to Governments or where there are stakeholders that are not involved in the day-to-day management are required to have audits. These mandatory audits are usually external in nature and they are intended to provide assurance to organizational stakeholders that the managers are adding value to the organization. In addition to external audits, well established organizations have internal audit functions that are required to appraise internal control systems and advise management on any areas of improvement. In the process, properly conducted audits, in compliance with auditing standards are expected to cause improvements in the organizational accounting environment (Hedger & Blick, 2008; Young & Choi, 2008; Burns & Forgarty, 2010). Auditing standards, procedures and manuals have to be followed by auditors when conducting audits to be effective and cause improvements in systems of audited entities (Revesz, et al, 2004). Standards and control procedures over audits further foster shareholders and other stakeholders trust in the audit process and financial information generated (Zaidi, 2006).

Collapses of large corporate organizations such as Enron, WorldCom and many banking institutions on the local and international scene however have led to questions whether those responsible for auditing these organizations comply with the requirements of auditing standards, and whether the audits are of value to organizational operations, accounting systems and reporting procedures. The business world and the accounting profession have experienced several high profile scandals during recent years where "responsible" accountants and their executives could have saved many investors and others much personal and financial loss (Reinstein, Moehrle & Moehrle, 2004).

On the World scene, collapses of large corporation like Enron in October 2001 in the USA (Wikipedia, 2011), HIH Insurance in Australia (Westfield, 2003) have been witnessed. On the local scene in Uganda, the private sector has seen the collapse and/or disposal of entities in the banking sector like; Uganda Cooperative Bank closed in 1998, Greenland Bank closed in 1999 and the sale of Nile Bank in 2008. All these institutions were subjected to internal and external audits on a regular basis. According to the Office of the Auditor General (2011), inadequate or low quality accounting has continued to be exhibited in various Public organizations such as; inadequate maintenance of accounting records, unauthorized expenditure and inadequate reporting, which subsequently lead to huge financial losses. This study intended to establish the level of compliance with auditing standards in the audit process in the selected organizations and its significance on the quality of accounting.

Literature Review

Compliance with Auditing Standards Auditing

Auditing is examination of books, accounts, vouchers and documents of the entity as to enable the auditor express an opinion whether the state of affairs and the results of operations of the entity are properly disclosed according to the information and explanations provided, and if not to indicate to what respects he is not satisfied with the information (Gupta, 2009; IFAC 2009). The audit process has three main phases; audit planning, field work /execution and reporting (Hayes, Dassen, Schilder & Wallage, 1999). These phases cover various areas including; understanding client business, observation of client business processes, raising a management letter and an audit report to stakeholders, and follow up of implementation of audit recommendations (Gupta, 2009; Tandon, Sudharsanam).

Auditing Standards

Auditing standards give guidance on the conduct of audit. Auditing standards used currently worldwide as issued by IFAC (2010) comprise of; International Standard on Quality Control (ISQC) 1 which pertains to quality controls for firms that perform audits and reviews of financial statements, and other assurance and related services engagements, Standards on audits of Historical Financial Information for private sector audits referred to as International Standards on Auditing (ISAs), issued by the International Federation of Accountants and, International Standards of Supreme Audit Institutions (ISSAIs) used for audit of Public Sector Organizations, issued by the International Organization of Supreme Audit Institutions (INTOSAI). There are about one hundred International standards pronounced in all three respects covering aspects such as; agreeing terms of audit engagement, planning an audit of financial statements, audit evidence, forming an audit opinion and reporting on the financial statements and modifications to the opinion in the independent auditor's report. In addition to these standards and ethical codes of practice, Supreme Audit Institutions and audit firms have manuals which further guide them internally on the audit process and help in incorporating audit standards into audit plans and programmes. These manuals may also be Internal Audit Manuals, used by Internal Auditors in the organization. Internal Auditors may also have further guidance on audits as provided by the Institute of Internal Auditors, this guidance may vary in content from ISAs only in regard to some extra procedures that the Internal Auditors may be required to carry out as internal advisors on the organizational accounting and general internal control systems.

Compliance

Revesz et al (2004) asserted that compliance with auditing standards is important for a quality audit. They defined "Audit quality" as the degree to which a set of inherent characteristics of an audit fulfills requirements. In discussing the work of a Supreme Audit Institution or an Audit Firm, they asserted that those characteristics include among others: Significance; How important is the matter that was examined in the audit? Reliability; Are the audit findings and conclusions an accurate reflection of actual conditions with respect to the matter being examined? Objectivity; was the audit carried out in an impartial and fair manner without favour or prejudice? Scope Did the audit task plan properly address all elements needed for a successful audit? Timeliness; were the audit results delivered at an appropriate time as required by stakeholders? Clarity; was the audit report clear and concise in presenting the results of the audit? an appropriate response from the auditee, shareholders, the Government and/or Parliament?

The development and existence of appropriate, high quality auditing standards is an important step in the road to quality audits (Revesz, 2004). Effective audit standards take account of the complex environment that influences auditor behavior and are designed to promote the sound exercise of professional judgment (Burns & Fogarty, 2010). Landwehr et al (2006) assert that the measure of audit quality is whether the auditor has given an appropriate audit opinion, as evidenced, perhaps, by the absence of audit failures.

Lucy et al (2009) on the other hand, contend that audit quality involves a wide range of inter-related factors which may not be specifically auditing standards, such as management's ethical behavior, the culture within the audit firm and the firm's audit processes, including the experience and technical expertise of the audit team and the audit methodology adopted by the firm. However, Cooper & Grose (2010) assert that failure to comply with auditing standards can lead to unethical audit behavior compromising audit quality and the resultant failure to disclose management weaknesses in accounting and financial reporting.

Calvert, Kurji & Kurji (2010) assert that public pressure for increased transparency in all aspects of accounting reporting, and auditing process has heightened the awareness by public accounting professional associations of the need for greater self-monitoring and the articulation of the expectation of ethical behavior by practitioners. In their study, Woolf and Hindson (2011) point to a number of cases where non-compliance with auditing standards led to several audit failures in detection of management accounting and financial malpractices and subsequent law suits

which resulted in audit firms paying colossal sums of money to companies' stakeholders. Compliance with auditing standards is important for a quality audit.

METHODOLOGY

The study used a quantitative, ex-post facto, descriptive, comparative, cross-sectional snapshot) survey design. The study population was 1,417 accounting and auditing staff from ten selected organizations in Central Region in Uganda, of which 252 were auditing staff and 1,165 accounting staff. Using the Sloven's formula, a sample of 453 respondents was determined, comprised of 155 auditing and 298 accounting staff. The sample size was proportionately allocated to the respondents in the selected organizations. The purposive, stratified, systematic random sampling methods were used in this study. The research tools that were utilized in this study included; the face sheet and researcher devised questionnaires to Cronbach's Alpha coefficient test indicated that the questionnaires were acceptable at above 0.7. Data was edited, coded and entered into SPSS and summarized using simple frequency tables and percentage distributions. Means were applied for the levels of compliance with auditing standards.

Findings

Level of Compliance with Auditing Standards

Compliance with auditing standards was conceptualized in terms of audit planning, audit execution /fieldwork, audit reporting and audit follow up. The level of compliance with auditing standards perceived by auditing staff for each of the four components of compliance is presented in this section. Using closed ended questionnaires, the respondents in the selected organizations in Kampala were asked to rate themselves on the extent to which they comply with auditing standards respect of the dimensions in four components of compliance with auditing standards. All questions were rated using a four point Likert scale where; 1 Strongly disagree; 2 Disagree; 3 Agree and 4 Strongly agree.

Level of Compliance with Auditing Standards in respect of Planning Results revealed that there is a very high level of compliance with auditing standards at the planning stage of the audit for all the fifteen planning dimensions (average mean 3.56). However of all the fifteen aspects of audit planning, carrying out and documenting audit procedures to understand client business is the most complied with (mean 3.78). The results indicate that the auditors take quite a substantial time understanding the nature of their client's business and identifying areas on which to focus the audit. The finding on understanding client business is supported by Hayes et al (1999), Gupta (2009) and Tandon et al (2009) who indicated that it is one of the vital aspects of the planning phase. Having a clear documented procedure of evaluating team members' competence was the least complied with (mean 3.37). This is most likely because the team members closely work together in most organizations and the competence aspect is not given adequate attention; however, this creates risks of having incompetent staff on teams.

Level of Compliance with Auditing Standards in respect of Audit Execution / Field Work

Results indicated that there is a high level of compliance with auditing standards at the audit execution/field work phase of the audit in all the fifteen field work dimensions (average mean =3.54). For all the fifteen aspects of audit field work. Being familiar with accounting processes and terminology is the most complied with aspect of audit field work. Results show the importance auditors attach on

understanding client accounting processes, procedures and terminology in order to have an audit that adds value to the client. Tandon et al (2009), Landwehr et al (2006) and Revesz, et al (2004) assert that at the field work or execution stage, the auditor has to understand client processes and carry out his work with professional care to note areas of material weaknesses. Woolf & Hindson (2011) in their study showed failure to understand client business processes as a cause for low quality audits and subsequent audit failures.

Level of Compliance with Auditing Standards in respect of Audit Reporting

Results showed a very high level of compliance with auditing standards at the reporting phase of the audit, in all the thirteen dimensions (average mean 3.58). For all the aspects of audit reporting, having final audit reports issued to the entity is the most complied with.

The results show that all auditors take issuance of an audit report to entity stakeholders as the most important aspect in the audit reporting phase. It is worth noting that without issuing an audit report to the entity, the audit exercise would be incomplete and all audit efforts in the planning and field work phases futile. The findings are supported by Hayes et al (1999), Gupta (2009), Tandon et al (2009) and Landwehr et al (2006) who indicated that the reporting stage is a key audit phase where audit results are disseminated to all organizational stakeholders. Having timely reports to entity stakeholders was the least complied with, this is attributed to the fact that audits usually start at the end of the accounting period to be reported on and the delays by accounting staff to provide required information.

Level of Compliance with Auditing Standards in respect of Audit Follow Up

Results indicated that there is a very high level of compliance with auditing standards at the follow up stage of the audit (average mean= 3.49). The aspect of raising audit issues in the current year in respect of outstanding audit findings from previous period(s) is the most complied with in the dimensions of audit follow-up. This is significant given the fact that where there is no follow-up on audit findings, there may be management laxity in implementation of findings and recommendations, subsequently failing to realize value addition from audits performed. The results are supported by Armstrong, Jia and Totikidis (2009) and Gupta (2009) who indicated that audit follow up is important to the audit process. Marx (2009) and Knechel and Vanstraelen (2007), stressed that the existence of audit committees will improve audit quality by discussing audit reports and following up implementation of audit recommendations. Reviewing previous year audit reports to ascertain matters raised was the least complied with. The risk with this is the likely failure to identify matters that require follow up and raising in the current period reports.

Summary of Level of Compliance with Auditing Standards

The overall level of compliance with auditing standards from the four phases is in table 1. The table provides the average mean from each of the constructs and the general average.

Table 1

Summary Table on Level of Compliance with Auditing Standards

Constructs	Average Mean	Interpretation	Rank
Audit reporting	3.58	Very High	1
Audit Planning	3.56	Very High	2
Audit execution / field work	3.54	Very High	3
Audit follow up	3.49	Very High	4
General Average	3.54	Very High	

Source: Primary data, 2012

Results in Table 1 indicated that on the overall, there is a very high level of compliance with auditing standards in the selected Public and Private sector organizations in Central Uganda, in respect of all the four constructs (general average mean 3.54). The very high level of compliance is attributed to the high caliber of staff employed by the organizations. For all the four constructs, audit reporting is the most complied with (mean 3.58). The results show that auditors consider the audit reporting phase as the most vital in the auditing process and they ensure highest compliance with auditing standards in this phase. It is vital for the auditors to issue audit reports resulting from their audit efforts to justify their audit effort.

Compliance with auditing standards in respect of follow up is least complied with (mean 3.49). This indicates that the auditors would prefer having an audit carried out and a report issued on the current period to spending time on follow up of previous year audit issues. This tends to leave the aspect of follow up of audit matters with audit committees increasing possibilities of non-implementation of audit findings and recommendations.

CONCLUSIONS

There is a very high level of compliance with auditing standards in the selected organizations, in respect of all the constructs (general average mean 3.54). For all the four constructs, audit reporting is the most complied with (mean 3.58), while audit follow up is least complied with (mean 3.49). The items that were perceived as most complied with were; carrying out and documenting audit procedures to understand client business at the planning stage, being familiar with accounting processes and terminology at the audit field work stage, having final audit reports issued to the entity at the reporting stage and raising audit issues in current year in respect of outstanding audit findings from previous period(s) at the audit follow up phase. The items that were perceived as least complied with were; having a clear documented procedure of evaluating team members' competence and independence from audit clients at the planning stage, conducting audits from the client premises at the execution stage, having timely reports to entity stakeholders at the reporting stage and, reviewing previous year audit at audit follow up. However, generally the level of compliance.

Recommendations

It is important to ensure that audits are conducted from their client premises most of the time. Carrying away audit documentation from client premises should be done under exceptional circumstances such as under investigations by

an authorized Government agency, lack of space at client premises, or such special circumstances that may not warrant conduct of an audit at the client premises.

Auditors should have clear documented procedure of evaluating team members' competence and independence from audit clients before commencement of audit. This enables deployment of staff that have the required skills to accomplish the tasks, it also helps to ensure that staff who are deployed are independent of staff of the audited organization to have an objective audit process.

Audits should be planned in such a way as to enable submission of audit reports to stakeholders in time. Timely submission of audit reports and the related financial statements allows stakeholders to take appropriate action in time.

There is need for auditors need to review previous year audit reports when planning or carrying out field work for a subsequent audit to ascertain matters raised which need follow up in the subsequent audit to bring out matters that have remained outstanding.

It is necessary for Auditors needs to be strengthened to address audit findings and recommendations made. Audit Committees need to be formed in most of the organizations that have large resources and operations to have an independent review of audit reports and follow up implementation.

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