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GOING CONCERN AND AUDIT OPINION OF NIGERIAN BANKING INDUSTRY

Rafiu Oyesola Salawu, Obafemi Awolowo University
Titilayo Moromoke Oladejo, Obafemi Awolowo University
Eghosa Godwin Inneh, Obafemi Awolowo University

ABSTRACT

This paper investigates the relationship between going concern and audit opinion of banks in Nigeria using financial ratio between 2007 and 2012. The study employed secondary source data collection obtained from published financial statements of selected banks and the Factbooks of Nigerian Stock Exchange. Multivariate regressions were employed to determine the effect of financial ratios used as going concern indices such as deposit to total asset (proxy for liquidity), return on capital employed (profitability measure) solvency, operating cashflow to total liabilities and growth on audit opinion. The result reveal that solvency, liquidity (DPA) and profitability (ROCE) have significant relationships with audit opinion. Furthermore, the study showed that going concern could be a signal of financial distress as it reveals the status and capability of banks to continue in operation. Finally, the study recommends the Central Bank of Nigeria should put in place policies that can enhance financial strength and stability of banks. The Nigerian Financial Reporting Council and other regulatory bodies, in line with best practices, should try to organize training and workshops to improve financial skills and expertise of auditors for quality reporting in Nigeria banking industry.

JEL: M4

KEYWORDS: Audit, Going Concern, Solvency, Money Deposit Bank

INTRODUCTION

The financial crisis and demise of some banks in Nigeria between 2007 and 2012 was a serious issue that questioned the integrity and competence of auditors because most of these banks were issued unqualified opinion prior to the year of their extinction. This financial turbulence played a significant role in the downturn of economic activities, damage the reputation of some renowned auditors in Nigeria associated with this unholy practices, damage the confidence of investors and other users of financial statement who lost their fortune in the incidence. The crisis was blamed on auditors who were expected to certify the credibility of financial statements that it gives the true and fair view of the financial position of an organization but failed in their responsibilities, these auditors were caught in the web of unethical practices that made their safeguard to be considered worthless since it neither corrected the anomaly in the financial statement nor improve the quality of audit but worsened the situation of things in the country. The issue of banks going to extinction after being certified to be financially worthy raises question concerning the accuracy of auditors going concern opinion and this need to be address before the situation gets out of hand. There is gap in the literature as regards assessing the accuracy of going concern's ability of financial institution in Nigeria and this work is carried out to bridge the gap. This study analyzed the factors that influence auditors' decision to issue qualified opinion to banks that shows the signal of distress in order to improve the quality of audit. Chen et-al (2005) argued that the extent at which the auditor is willing to issue qualified opinion often provides some indication of audit quality. Auditors by the International Standard on Auditing are saddled with the responsibilities of considering the appropriateness of management assertion of going concern assumption in financial statement prepared by them.

This assurance adds credibility to financial statements, lowers information risk, and facilitates capital formation, adding value to the entire capital market system (Elliot and Jacobson 1998; Carmichael 1999). In lieu of these responsibilities, auditor when carrying out their work are expected to gather enough information from their client, look for some conditions or event that may cast significant doubt on the ability of a firm to continue as a going concern, then auditor should obtain information about the plans and consider whether it is likely that the adverse effects be mitigated for a reasonable period of time and that such plan can be effectively implemented. But if the auditor still has substantial doubt about the entity's ability to continue as a going-concern, the auditor should consider the adequacy of management's disclosures in the financial statements and the auditor must modify his/her opinion to include an explanatory paragraph outlining the reasons for concern.

Bank failure started 1930, but became worse in 2004 when the numbers of banks reduced drastically from 89 to 24, the liquidity problem witnessed by banks forced Central Bank of Nigeria (CBN) to raise the minimum balance to 25billion ($167million) some banks were taken off by others while other merged together to form new banks. Nigeria lost huge amount of money to banking sector fraud which was estimated to be a total of N6billion ($42.9m) Bakre, 2007. (This Day Paper, 16th October 2008) reported that CBN audited the activities of the remaining 24 banks quoted on Nigerian Stock Exchange and discovered that they were also insolvent and already showing symptoms of distressed so CBN considered bailout option for them as was practiced by other advanced countries like UK, US to save them out of financial mess. But in 2009 the activities of these banks showed that they were still not financially stable and because of this CBN released N420 billion ($2.8billion) to five banks that failed their audit test. These banks include Afribank, Intercontinental, Oceanic, Finland and Union bank. CBN further released the sum of N200billion ($1.33billion) to four other banks which are Spring, Equitorial, Trust and Wema bank to remain going concern and sacked their former managers for poor managing of the banks (Sahara reporter, Oct 8, 2010, This Day, 12 Dec, 2009, Nigeria Tribune, Dec 8, 2009).

Many studies have been carried out on going concern using financial ratios as determinant, most especially in foreign countries. Erly S. And Elok T. P. (2012) Puji (2007) assessed going concern opinion using financial and non-financial information and concluded that financial information has no significance with going concern but non- financial measured with prior opinion and auditor reputation have significant effect on going concern. In the work of Davoudi (2007) Marteen etal (2008) Hao etal (2011) Oni and Desi (2006) their results indicated that financial ratios are important measure of going concern opinion. Research done in Nigeria did not actually address the factors that influence auditors decision to issue going concern but addressed the role of auditor in banks financial distress, (Jibrin and Blessing [2014], Otusanya and Lauwo [2010]) they concluded that auditor lacked their claimed expertise to conduct an independent audit and objective reporting of corporate affairs and also that audit model is fundamentally flawed and cannot deliver independent or searching audit. Oladipupo and Izendomi [2011] work on propensity of qualified audit reports and auditors' independence reported that there is positive insignificant relationship between auditor's independence and nature of report issued. Onwuchekwa, Erah and Izendomi [2012] argued that mandatory audit rotation do not in any way improve the quality of audit. Because of the dearth of work on going concern and in a bid to bridge this gap and add to existing literature, it may therefore be pertinent to investigate factors that influence the auditors' issuance of qualified going concern opinion in Nigerian Banking industry. Apart from the above introductory section, the rest of this study has been divided into three sections. In section two, we discuss the literature review of the study. Section three explains the data, methodology and results. The study is concluded in section four.

LITERATURE REVIEW ON GOING CONCERN AND AUDIT OPINION

The literature is replete with studies on going concern and types of opinion issued by the auditor after examining the financial statement prepared by management of an organization. Sugiono Poulus (2015), in his work on the comparative analysis of precision prediction of liquidity static, dynamic liquidity and altman Z-score related to the provision of audit opinion going concern carried out on 373 manufacturing companies publicly listed on the Indonesia Stock Exchange in 2010-2012, using explanatory research by cross sectional and discriminant analysis concluded that the most influential financial ratios are Quick Assets to Total Assets, Total Liabilities to Total Assets, and Net Worth to Total Liabilities. The results of this study proved that the model of liquidity, especially static liquidity could be used as a valuable tool in assessing the company's going concern status. Erly S. And Elok T. P. (2012) carried out research on the effect of financial ratios, prior audit opinion and growth on the auditor's going concern, the result of their work indicates that the variable ratio of corporate finance (liquidity ratios, profitability ratios and solvency ratios and growth) do not have a significant effect on the provision of audit opinion by the auditor going concern. Hao, Zhang, Wang, Yang, and Zhao (2011) in their work affirmed that financial ratios like current ratios, casflow, return on capital employed and high leverage have significant effect on going concern opinion and concluded that auditors are likely to issue going concern opinion to firms with low liquidity, poor performance, less cash inflows and high leverage. Martens, Bruynseels, Baesens, Willekens and Vanthienes (2008) in their work predicting going concern opinion with data mining on United States listed companies concluded that profitability ratios are an important determinant of going concern decision making. Their decision model furthermore indicates that a company is more likely to receive a going concern modified audit report if it has lower total assets, lower current ratio, decreasing working capital to total assets, and increasing total liabilities to total assets.

Davoudi (2007) Reviewed Effectiveness of Cash Flows from Operating Activities for Evaluating the Going Concern of the Listed Companies in Tehran Stock Exchange. He concluded that the most important financial ratio of significant relationship with going concern of the firms is the cash flows from operating activities to average assets ratio.

Alireza Safari (2002) reviews the financial ratios and going concern of entities. Results of the research suggest that there is a significant relationship between financial ratios and going concern. (Faghani N. M 2002) empirically examined "The Relationship between Financial Ratios and Bankruptcy Prediction of Listed Companies in the Stock Exchange" and come to the conclusion that there is a significant relationship between key financial ratios and bankruptcy prediction.

Puji Rahiyu (2007) investigates the usefulness of financial and non-financial information's for assessing going-concern to predict the issuance of going-concern opinion on private commercial banks listed in JSX (Jakarta Stock Exchanges) and SSX (Surabaya Stock Exchanges) for the year 2000 to 2005. They used Binary Logistic Regression as a tool for analyzing financial information proxied by financial ratios of Liquidity, Profitability, and Solvency. Liquidity measured by Quick Ratio (QR) and Banking Ratio (BR), Profitability measured by Return on Assets (ROA), Solvency measured by Capital Adequacy Ratio (CAR). The results show that financial variables (Liquidity, Profitability, and Solvency) are not effective for assessing going-concern to predict the issuances of going-concern opinion. Both of Descriptive Statistics and Logistic Regression show that all the financial variables are not significant.

Oni and Desi (2006) conducted study in Indonesia on Analysis of determinants of going concern and audit report of manufacturing company; he tested its relationship with financial ratios and two new variables, the audit committee and size of audit firm. The financial ratios used in this study as an indicator are current ratio, net income before tax/net sales ratio, total debt to total equity ratio, cash flow to total debt ratio, which each of them are represent liquidity ratio, profitability ratio, solvency ratio, and cash flow ratio. They concluded based on analysis result and discussion that Liquidity, Profitability, Operational cash flow, and the existence of audit committee of a company has no significant effect against the issuance of going concern audit opinion by the auditor. Whereas solvency has a significant effect and size of audit firm has sufficiently significant effect against the issuance of going concern audit opinion by the auditor.

DATA AND METHODOLOGY

Panel data gathered from annual reports of selected quoted banks in Nigeria was used for this study. The data were obtained from audited financial statements and Factbooks of Nigerian Stock Exchange of the sampled fifteen (15) banks out of the 22 listed banks in Nigeria with 90 observations taken from 2007-2012. This study used data collected from secondary sources on relevant variables such as AO, DPA, SOL, ROCE, OCFA and GRT. This study employed the use of Binary Logistic regression since the dependent variable (AO) is dichotomous in nature. The functional relationship of going concern and audit opinion is given below

$$AO_{it} = \beta_0 + \beta_1 DPA_t + \beta_2\, ROCE_{it} + \beta_3\, OCFA_{it} + \beta_4\, GRA_{it} + \beta_5 SOL + \mu_{it} \dots\dots\dots..eqn\ (1)$$

Where:

AO = Audit Opinions will be equal to 1 if a company receives audit opinion and 0 otherwise. The audit opinions in this study are all types of audit opinions that address the going concern problem faced by the company, either qualified with explanatory paragraph, disclaimer or adverse opinion.
The independent variables are:

DPA = Deposit to Total Asset (Customer deposit / Total Asset)

ROCE = Return on capital employed (Net profit / Total Assets – Current Liabilities)

GR = Growth = (Current year total asset - prior year total asset) / Prior year total asset

SO = Solvency = Total liabilities / Total assets

OCF = Operating Cash flow = Cashflow from operations / Total Liabilities

DISCUSSION OF RESULTS

This section reveals the analysis of effect of going concern on audit opinion of Nigerian banks. The results of the analysis of the regression estimated to evaluate the influence of the going concern on audit opinion are shown in Table 1, 2 and 3 The data in Table 1 present the average indicators. The mean value of DPA, ROCE, SOL, OCFA and GRT are 0.5378, 0.1373, 0.7988, 0.0401 and 0.2664 respectively.

This indicates that banks liquidity is not bad during the period of analysis; this is expected in the banking industry. Banks profitability is good but the rate of variability is high as shown by the standard deviation of 1.660. The result indicate that average of growth, operating cashflow and solvency is low and also the rate of their variability.

Table 1: Descriptive Statistics of Going Concern and Audit Opinion

	DPA	SOL	ROCE	OCFA	GRT_2	AUD_O
Mean	0.5378	0.1373	0.7988	0.0401	0.2664	0.3111
Median	0.6894	0.1483	0.0739	0.0348	0.2130	0.0000
Maximum	0.8793	0.2916	7.819	0.3661	2.175	1.000
Minimum	-0.1782	-0.3187	-0.3585	-0.2779	-0.9991	0.0000
Std. Dev.	0.3006	0.0963	1.660	0.0990	0.5415	0.4655
Skewness	-0.9983	-2.0909	2.380	0.0529	0.3906	0.8160
Kurtosis	2.448	10.395	8.281	5.491	4.956	1.666
Jarque-Bera	16.091	270.65	189.54	23.306	16.632	16.663
Probability	0.0003	0.0000	0.0000	0.0000	0.0002	0.0002
Sum	48.402	12.361	71.895	3.607	23.977	28.000
Sum Sq. Dev.	8.041	0.8252	245.32	0.8722	26.091	19.289
Observations	90	90	90	90	90	90

This table shows the descriptive statistics of independent variables used for this study, row 2 shows the mean of all the variables, row three their median, row four their maximum value, row six the standard deviation of each variables and the last row shows the total number of observations. Source: Authors computation 2015

The five regressors were subjected to pairwise correlation to ascertain if any of the stimulus variables explains another. The result reported in table 2 showed that there is no multicollinearity among the regressors. Hence, the five regressors can be included in the model.

Table 2: Correlation

	DPA	SOL	ROCE	OCFA	GRT_2
DPA	1.000				
	(0.0000)				
SOL	0.0650	1.000			
	(0.5426)	(0.0000)			
ROCE	0.1816	-0.3631	1.000		
	(0.0867)	(0.0004)	(0.0000)		
OCFA	0.0984	-0.1117	0.0793	1.000	
	(0.3563)	(0.2944)	(0.4577)	(0.0000)	
GRT_2	0.1102	-0.0912	-0.0657	0.2032	1.000
	(0.3011)	(0.3925)	(0.5386)	(0.0547)	(0.0000)

This table shows the result of pairwise correlation of stimulus variables. From the results the upper figure in each cell represent the pairwise correlation of the regressors and the figure in the bracket is the corresponding probability of the correlation, the result indicates that there is no problem of multicollinearity among the variables. Source: Authors Computation 2015

Table 3 presents the results of logistic regression of going concern and audit opinion of Nigerian banks. The result shows that DPA, ROCE and SOL are determinants of going concern. These regressors are negatively significant at 95% level of confidence. The decision model furthermore indicates that a company is more likely to receive a going concern modified audit report if it has lower deposit to total asset, decreasing return on capital employed and less solvent. This result supported the work of Nina Sormunen (2012), Oni and Desi (2003), Hao, Zhang, Wang, Yang and Zhao (2011) that a company with low liquidity, poor performance and high leverage will be issued going concern opinion.

Table 3: Logistic Regression Estimates of Equation Audit Opinion = $\beta_0 + \beta_1$ (Deposit to Total Asset) +β_2 (Return on Capital Employed) +β_3 (Operating Cashflow + β_4 (Growth) +β_5 (Solvency)

Variables	Coefficient	z-Statistic	P-value
Constant	2.046	2.490	0.0128
DPA	-1.7432	-2.1341	0.0328**
ROCE	-0.7024	-2.5668	0.0103***
SOL	-10.7586	-2.7148	0.0066***
OCFA	3.088	1.078	0.2808
GRT	-0.9245	-1.7543	0.0794
R2 =0.2026			
LR= 22.61			
Prob LR = 0.004			

*This table shows the regression statistics of going concern and audit opinion of sampled banks, column two indicate the coefficient of dependent and independent variables, column three shows the kind of relationship that exit between the dependent and independent variables while the last column shows the level of significance of the variables. *** and ** reveals that variable is significant at 1%, and 5% respectively*
Source: Authors Computation 2015

CONCLUSION

The study investigates the relationship between going concern and audit opinion of quoted banks in Nigeria during a six years period. The results reveal that there is a significant relationship between going concern and audit opinion. The results suggest that banks in Nigeria have good liquidity and profitability level but their level of solvency, growth and cashflow is very low. Thus, the results from the study indicate that the relationship between going concern and audit opinion was observed to be highly positively significant meaning that most accounting improprieties and collapse in Nigeria in the past few years have all had a link with going concern related problems.

This could mean that going concern can actually offer a solution to the problem that financial statements pose. This study has its own limitation because it is only carried out on financial institutions and the result cannot be used to generalize what happened in other sectors like manufacturing and service oriented firms.

Also, it only makes use of financial ratios while non-financial ratios that may explain the situations better were not included. The result indicated that going concern had a positive significant effect on audit opinion and that banks that have good liquidity, profitability level, solvent, have good growth level and cashflow are less likely to receive going concern, But banks that accumulated debt, incurred losses repeatedly, have liquidity problem are more likely to receive qualified going concern opinion or wind up. Finally, the study recommends that the Central Bank of Nigeria should put in place policy that can enhance financial strength and stability of banks.

The Nigerian Financial reporting Council and other regulatory bodies in line with best practices should try to organize training and workshop to improve financial skills and expertise of auditor for quality reporting in Nigeria banking industry. More work are still needed to be carry out on this topic but researchers may look at other sectors as different from financial institutions and also make use of both financial and non-financial variables.

APPENDIX

List of Banks Used for the Study

NAME	YEAR
Fidelity Bank	2007-2012
Union Bank	2007-2012
Ecobank	2007-2012
Zenith Bank	2007-2012
Ibtc Stanbic Bank	2007-2012
Skye Bank	2007-2012
First Bank	2007-2012
Guaranty Trust Bank	2007-2012
Diamond Bank	2007-2012
Unity Bank	2007-2012
Access Bank	2007-2012
Sterling Bank	2007-2012
First City Monument Bank	2007-2012
Wema Bank	2007-2012
United Bank for Africa	2007-2012

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BIOGRAPHY

Rafiu Oyesola Salawu, an economist and Fellow Chartered Accountant holds Doctor of Philosophy degree in Management and Accounting from Obafemi Awolowo University, Nigeria. He is a Professor of Accounting and Finance at Obafemi Awolowo University. He teaches and conducts research in the area of accounting and finance. He can be contacted at Phone:0803 3795 887 Email: osalawu02@yahoo.co.uk, Titilayo Moromoke Oladejo is a Ph.D Students of Obafemi Awolowo University. Her research interest includes auditing, public sector and accounting. She can be contacted at: Phone no 0815,0740,728. Email: oladejotitilayo2011@gmail.com

Eghosa Godwin Inneh is a Lecturer at Obafemi Awolowo University. He can be contacted at Phone :0803 5421 052 Email: macinneh2@yahoo.com