



Auditing as a Tool for Effective Control of Fraud and Financial Irregularities: A Case of Oshimili South Local Government, Delta State, Nigeria

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ABSTRACT

The study was designed to examine auditing as a tool for effective control of fraud and financial irregularities in Oshimili South Local government of Delta state. Two research questions and hypotheses were adopted for the study. The study adopted survey research design. The target population of the study was 35 respondents. No sampling technique was employed due to the manageable size of the population. Data was collected from respondents using structured questionnaire and analysed using mean and standard deviation. Simple Regression Statistic was used to test the hypotheses. The results of the analysis revealed that ensuring that decision makers comply with regulations guiding the Local Government Council; monitoring the effectiveness of the management; reviewing contracts in potential conflict of interest; check abuse of power; amongst others were techniques employed by auditors to check and control fraud and financial irregularities in the study area. The public sector's constitution guiding auditor's activities, powers and duties, does not provide auditor with complete and unrestricted access to employees. Lack of property and other information needed to execute their work; insufficient facilities funding; poor qualifications and incompetence to conduct the full range of audits amongst others were factors inhibiting effectiveness of auditors in the control of fraud and financial irregularities in the study area. The study recommended that the Council Management should support the activities of the auditors by providing them with adequate finance and logistics to effectively carry out their duty. The internal audit at the local government should be independent of political interference so that they can carry out their duties effectively. Qualified and competent staff need to be recruited into the audit department of local government in order for the unit to function effectively.

Keywords: Auditing, Effective Control, Fraud, Financial Irregularities

INTRODUCTION

Local government is the third tier of government in Nigeria that is nearest to people at grassroots. It is a structure which provides for the social services needed by the people and also brings development and good governance to the grassroots. The major objective of establishing local government is for the development to thrive at the grassroots level.

At all levels of government, controls have to be exercised over all aspects of the government resources. All organizations whether profit oriented or not-profit making operates within resource constraints. As a result, various forms of control are taken and procedures established to ensure that the use of the resource

is maximized in achieving the organizations goals. Therefore, local government as an organization also incorporates into its accounting system all methods and forms of controls which enable her to operate effectively and efficiently to achieve her targeted objectives.

Apart from the problems of scarce resources, local governments are vulnerable to run a high rate of fraud, errors, misappropriation, and inefficient and effective operations. Steps are required therefore, to minimize, if not eliminate completely, these risk by establishing rules and regulations. For every local government, there are risks that the local government goals and objectives may not be achieved. All efforts aimed at preventing such risks, and/or identifying and controlling such risk and irregularities, are viewed as internal audit function.

Internal audit being a unit in any establishment set up by the management of an organization for the review of internal control system as a service to the organization. The objective is to assist members of the organization including those in management and the board in the effective discharge of their responsibilities. To this end, internal auditing furnishes management of local governments with analysis, appraisals, recommendations, counsel and information concerning the activities reviewed. Diamond (2002) opined that auditing objectively examines, evaluates and reports on the adequacy of internal control as a contribution to the proper, economic, efficient and effective use of resources. Internal audit a component of government financial management and a tool for improving the performance of the government sector. In other words, auditing ensures judicious use of funds and check irregularities in the usage of funds in any organization.

Internal audit in local government and other public and private sectors serves as a control mechanism (Badara & Saidin, 2013). There seems to be impediments infringing on local government's functions and performance in recent times. These impediments range from political undue interference from the higher levels of government, that is, State and Federal government.

As stated earlier, the local government is the closest tier of government to the people in Nigeria was established as a means for providing socio-economic development at the grassroot level. To this, resources have always been allocated but no commensurable achievement have been seen. This is what members of the general public alleged as fraud, corruption and failure of the internal audit unit to install control mechanism that would minimize misuse of resources in the local government (Kwanbo & Dabo, 2009).

A constant complaint in the sector by the general public especially the residents of the Oshimili South LGA who are closer to local authority is that, the unit which is established to check the financial dealings of the local government (internal audit unit) is too weak in its functions either as a result of inadequate staffing, weak internal control, poor administration, lack of required personnel, inadequate documentation, and application of appropriate internal audit techniques in the local governments, among others, to prevent fraud.

Irregularities in spending public fund have been highlighted by Buang (2008) in his study. Some of these weaknesses and irregularities involve serious violation of established financial management guidelines and procedures such as poor planning of procurement, equipments supplied, work done and services rendered not in accordance with the original specification, cost overrun due to delays in project completion, improper payment made for equipments not supplied, work not done and services not rendered, equipment and goods procured at a much higher cost than market value, procurement not done according to established regulations. Thus the role of internal audit (IA) unit is to determine that effective control is in place by reviewing policies and practices in the organization in order to avoid loss of financial resources, noncompliance and also to provide reasonable assurance that public fund has been spent in an efficient and effective manner. Audit services could help the local government for the success of better financial management in public service by playing the effective and efficient roles to promote better governance in managing public money. Therefore, the study intents to look at effective ways, auditing can be used in controlling fraud and financial irregularities in Oshimili South Local Government.

Objectives of the Study

The main purpose of this study is to examine auditing as a tool for effective control of fraud and financial irregularities in Oshimili South Local government. The sub objectives are the following:

1. To determine techniques employed by auditors to control fraud and financial irregularities in Oshimili South Local government area of Delta State
2. To examine factors affecting effectiveness of auditors in the control of fraud and financial irregularities in Oshimili South LGA of Delta State

Research Questions

The research questions for the research work are:

1. What are the techniques to be employed by auditors to control fraud and financial irregularities in Oshimili South Local government area of Delta State?
2. What are the factors affecting the effectiveness of auditors in the control of fraud and financial irregularities in Oshimili South Local Government Area of Delta State?

Research Hypotheses

The following hypotheses were formulated for this study:

HO₁: There are no specific techniques to be employed by Auditors to control fraud and financial irregularities in Oshimili South local Government Area of Delta State.

HO₂: There are no specific factors that will enhance the effectiveness of Auditors in the control of fraud and financial irregularities in Oshimili South Local Government area of Delta State

LITERATURE REVIEW

In this study, explanation will be given to the terminologies that are used in a special way for the purpose of the study. The concepts include auditing, financial control and effectiveness, Fraud and financial irregularities. These concepts will be explained one after the other in order to substantiate and give meaning to the study.

Audit

Auditing is originally a financial management concerned with assessing practice for the internal financial status of the organization and the evaluations of the financial performance of the organization (Manal, 1999). Auditing practices have evolved over the years and developed into the broader aspects to become a field of fraud detection and financial accountability. It also provides feedback on organization financial information and reporting. It also becomes a tool for an analysis of any fraudulent activity, potential and actual within the organization.

Audit is one of the mechanisms to the fight corruption. Most of the standard setting in the auditing profession has taken place in the private sector and corruption has not been a serious issue in the private sector because the auditing profession, as it has evolved, has its roots in the private sector where audit against corruption is not a serious concern of the stakeholders who are more interested in fraud or theft of their assets (Okafor & Ibadin, 2009). This, no doubt is responsible for the very little discussion in the literature on corruption auditing and probably the lack of standards for auditing corruption. Almost all professional bodies of auditors across the globe have published standards and techniques about fraud auditing.

Effectiveness

The word “effectiveness” has been defined by different researchers, for instance, Arena and Azzone (2009) defined effectiveness “as the capacity to obtain results that are consistent with targets objective,” while, Dittenhofer (2001) views effectiveness as the ability toward the achievement of the objectives and goals. In the same context, a program can be seen as effective if its outcome goes along with its objectives (Ahmad, Gloeck, Ahmi & Sahdan, 2009; Mihret *et al*, 2010). In this situation, audit effectiveness means the ability of the auditor to achieve the established objective within the local government. This goes along that the objectives of an internal audit for every organization are depending on the goals set out by the management of the organization (Pungas, 2003) as such, the objective of internal audit in local government should also go along with the set goals by the management of the particular councils, even though the degree of internal audit effectiveness tends to vary within organizational level as well as country (Al-Twaijry, Brierley & Gwilliam, 2003).

Fraud and Financial Irregularities:

Fraud is an intentional misrepresentation, concealment, or omission of the truth for the purpose of deception/manipulation to the financial detriment of an individual or an organization which also includes embezzlement, theft or any attempt to steal or unlawfully obtain, misuse or harm the asset of the organization.

Aderibigbe and Dada (2007) see fraud as a deliberate deceit, planned and executed with the intent to deprive another person of his property or rights directly or indirectly, regardless of whether the perpetrator benefits from his/her actions. Bostley and Dover (1972) and Adeduro (1998) noted that fraud has increased considerably over the recent years and professionals believe this trend is likely to continue. On the other hand, financial irregularities refer to intentional mistake or distortions of financial statement such as misrepresentation or misappropriation of assets. In simple term it refers to forgery or alteration of cheques, drafts, promissory notes and securities. This can be curtailed in any organization through the provision of an internal audit which is a part of the internal control system.

Financial Control:

Glance (2006) provided that internal control system refers to “the local government process and procedure that is been established with the aim of objective achievement.” The internal control system also serves as a process that guides an organization towards achieving its established objectives (Amudo & Inanga, 2009; Baltaci & Yilmaz, 2006; Jokipii, 2010). From the above definition of internal control system, we can understand clearly that it is all about the provision that will assist in achievement of the objectives. Therefore, financial control implies the effective control measures established by an organization with the aim of safeguarding their assets to ensure the reliability of financial records is in compliance with relevant policies and procedure that will ensure the achievement of the local government authority. Figure 1 shows the conceptual framework of the study.

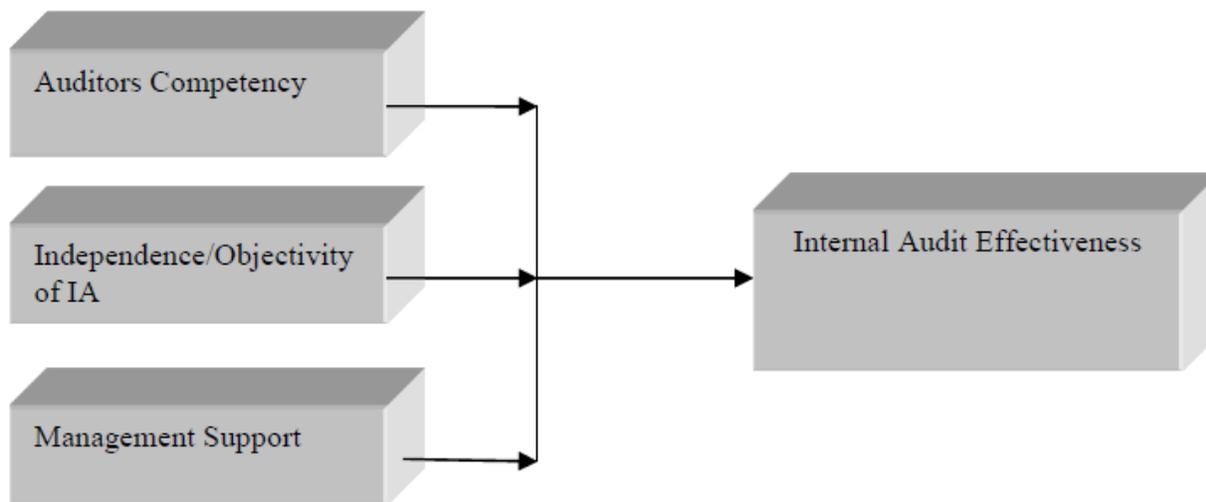


Fig 1: Conceptual framework of the study
Source: Adopted from Zulkifli, Alagan & Mohd (2014).

THEORETICAL FRAMEWORK

Policeman Theory

The policeman theory claims that the auditor is responsible for searching, discovering and preventing fraud (Hayes, Knechel & Wong, 2005). In the early 20th century this was certainly the case. However, more recently the main focus of auditors has been to provide reasonable assurance and verify the truth and fairness of the financial statements. The detection of fraud is, however, still a hot topic in the debate on the auditor's responsibilities, and typically after events where financial statement frauds have been revealed, the pressure increases on increasing the responsibilities of auditors in detecting fraud.

In relevance to the study, the auditor ensures truth and fairness with the utilization of resources to provide governance in the public sector. The local government authority provides dividends of the governance to the rural settings. The way resources provided by the state and federal government are being utilized are inspected by the auditors in compliance with the law (Act) guiding the local government authority. An auditor's job is to focus on arithmetical accuracy and on the prevention and detection of frauds. The auditor ensures that good governance is provided by local government authority to rural people.

Agency Theory

This theory is associated with conflicting interests of shareholders and management of organizations, suggesting that the less informed party will have to demand for information that monitors the behaviour of better informed manager (Akinbuli, 2010). According to Hayes *et al.* (1999), agency theory can be used to explain the supply side of the audit market. The contribution of an audit to third parties is basically determined by the probability that the auditor will detect errors in the financial statements and the auditor's willingness to report these errors.

In relation to the study, the shareholders who could be referred to as the populace of the local government area that complains of not benefitting from the politicians and public office holders (Management) of dividend of democracy at the grassroots. The suggestion of this theory is that auditors should be a third party to monitor and ensure that monies and or dividends of governance at the grassroots are being inspected by the auditors in compliance with the law guiding the local government authority act. This will ensure that good governance is provided by local government authority to rural people.

EMPIRICAL REVIEW

Ima (2005) examined the internal audit activities in some Nigerian firms. Generally internal control being an integral part of corporate governance has faced a lot of regulatory reforms due to the corporate scandals and financial crisis in the economic environment. Regulators have been faced with increased disclosure requirement. Nigeria has continually been faced with high level of financial loss due to fraudulent practices. Specifically, the study looks at internal audit, as an important aspect of internal control to examine if there is a positive and significant relationship between its effectiveness and fraud prevention. The study adopted the analytical survey method to gather information on internal audit activities from our sample. The population comprised of senior management and staff of internal control department of firms listed on the Nigerian stock exchange. Using judgement, 2 senior management staff and 4 staff of internal control department of firms listed on the stock exchange that are been audited by the big four audit firms were chosen for the sample. Data collection was by means of the questionnaire with response options graduated into 5-point Likert scale designed to capture information on internal audit processes in the organization. Logistic regression analysis was used to test the hypothesis and the result showed that a positive and significant relationship existed between the internal audit practices and fraud deterrence. The study provides an insight into internal audit activities in Nigerian firms. The internal audit practice in most Nigerian organizations is not commendable. Therefore we recommend a more vibrant internal audit through establishment of a vibrant internal audit department, ensuring independence of the internal audit unit, attention paid to internal auditors report and recommendation and regular evaluation of the effectiveness of the internal audit unit.

Coram, Ferguson and Moroney (2016) assessed organizations with an internal audit function are more likely to detect fraud than those without. In this study we use a unique self-reported measure of fraud, primarily relating to the misappropriation of assets, for the first time. The fraud data are from the 2004

KPMG Fraud Survey. The internal audit data are from a separate mail survey sent to the respondents of the KPMG Fraud Survey. They found that organizations with an internal audit function are more likely than those without such a function to detect fraud within their organizations. Further, organizations that rely solely on outsourcing for their internal audit function are less likely to detect fraud than those that undertake at least part of their internal audit function themselves. These findings suggest that internal audit adds value through improving the control and monitoring environment within organizations to detect fraud. These results also suggest that keeping the internal audit function within the organization is more effective than completely outsourcing that function.

Agu (2015) examined the extent to which the internal control measures installed in the system were adhered to and the role they played in fraud reduction. 524 respondents comprising 255 males (48.79) and 269 females (51.39) from six local governments in Enugu State answered the questionnaires. The mean age of the respondent is 2.06 SD = .58. The result revealed that the important control measures were not adhered to and this led to fraud.

RESEARCH METHODOLOGY

The research design for this study is survey research design. Data was collected using the primary and secondary source. Questionnaire was the primary source of eliciting information or data. Newspaper, internet, journals and books were used to source for secondary data. In designing the questionnaire the likert scale was used. Each response would be rated using a scale of 1-5. Strongly Agree (5), Agree (4), Undecided (3), Disagree (2), Strongly Disagree (1).

The questionnaires were validated by experts. The reliability of the instrument was established using the Cronbach Alpha and the split-half technique. Trial testing of the instrument was carried out in Oshimili North LGA using 10 staff in finance and audit department of the Local Government Council. This population is different from the sample of the study. A coefficient value of 0.797 was obtained. The high coefficient suggests that the instrument was reliable for the study.

The population of the study comprised of thirty five (35) staff in finance and audit department of Oshimili South Local Government. All the subjects in the population were used for the study due to its manageable size. So, sampling technique was not employed. Data collected from the field were analyzed using frequencies, percentages, mean and standard deviation. Simple regression statistic was used to test the hypotheses. Where the computed value of the R-square (R^2) method is greater than the critical value the null hypothesis (H_0) will be rejected. Otherwise, it will be accepted

PRESENTATION OF RESULTS

Table 1: Demographic information of respondents (N=35)

Variables	Frequency	Percentage
Gender		
Male	21	60.00
Female	14	40.00
Educational Qualification		
Ph.D	02	5.71
MSc	06	17.14
BSc/HND	15	42.86
NCE/OND	12	34.29
Years of Experience		
0-3 years	9	25.71
4-6 years	07	20.00
7-10 years	05	14.29
10 years and above	14	40.00

Source: Field Work, 2017

The results in Table 1 showed that most of the respondents were male (60%), while 40% of the respondents were female. Response on educational qualification showed that 5.71% of the respondents

had Ph.D; 17.14% of the respondents had M.Sc, 42.86 % had B.Sc/HND, and 34.29% had NCE/OND. Response on years of experience indicated that 54.29% of the staff have experience of 7years and above while 45.71% have work experience below 6years.

Research Question 1: *What are the techniques to be employed by auditors to control fraud and financial irregularities in Oshimili South Local government area of Delta State?*

Table 2: Mean responses of respondents on techniques to be employed by auditors to control fraud and financial irregularities in Oshimili South Local government area [N=35]

S/N	Statement items	Mean	S.D	Remark
1	Auditors assist decision-makers in the LGA in exercising oversight to ensure that funds were spent for the intended purpose	2.03	0.72	Disagreed
2	Auditors assist decision-makers to complying with laws and regulations guiding the council	3.09	0.74	Agreed
3	Auditors contribute to public accountability by providing access to the performance information of the management to stakeholders	2.17	0.77	Disagreed
4	Auditors monitor the effectiveness of management's internal control structure to identify and reduce the conditions that breed corruption	2.68	0.68	Agreed
5	Auditors review contracts for potential conflicts of interest	2.63	0.81	Agreed
6	Audit activity feedback to enable council to adjust policies	3.31	0.86	Agreed
7	Auditors help the council to look forward by identifying trends and bringing attention to emerging challenges before they become crises	3.01	0.83	Agreed
8	Auditors play a key role in helping managers understand and initiate risk assessments	2.51	0.87	Agreed
9	Auditors serve as a check on abuse of power and privilege	2.88	0.91	Agreed
10	Auditors may sometimes abuse their own power and privilege	2.91	0.82	Agreed
11	Auditors conduct their work with integrity and in full compliance with the laws and regulations	3.13	0.76	Agreed
12	Auditors periodically provide statement showing progress in the collection of revenue under the various heads to compare it with the budgeted	2.98	0.71	Agreed

Source: Field Work, 2017

The data presented in Table 2 showed that the statement items had a mean range of 2.03 to 3.31. Most of the mean items were above the cut-off point of 2.50, while items 1 and 3 were below the cut-off. This indicates that the respondents agreed that most of the identified items were current practices of auditors in the study area. The standard deviation of the items ranged from 0.68 to 0.91. This indicated that respondents were unanimous in their responses as the range of score was not from each other.

Research Question 2: *What are the factors affecting the effectiveness of auditors in the control of fraud and financial irregularities in Oshimili South Local Government Area of Delta State?*

Table 3: Mean responses of respondents on factors affecting the effectiveness of auditors in the control of fraud and financial irregularities in Oshimili South Local Government Area

S/N	Statement items	Mean	S.D	Remark
1	Auditors conduct their work without interference by the council management	1.51	0.63	Disagreed
2	Auditor's activities, powers and duties are established by the public sector's constitution guiding the council	3.31	0.72	Agreed
3	Auditor are not provided with complete and unrestricted access to employees, property and other information needed to execute their work	3.56	0.74	Agreed
4	The audit activity lacks sufficient funding relative to the size of its audit responsibilities	2.51	0.78	Agreed
5	Auditors must be competent to oversee and manage an audit function	2.61	0.68	Agreed
6	Some audit staff have impartial attitudes and entertain conflict of interest	2.03	0.54	Disagreed
7	Audit activity needs a professional staff that collectively has the necessary qualifications and competence to conduct the full range of audits required by its mandate	3.45	0.67	Agreed

Source: Field Work, 2017

Table 3 showed that the respondents agreed to most the items on factors affecting effectiveness of auditors. However, items 1 and 6 were rejected because their mean values were below the cut-off point of 2.50. This implies that most of the identified items were factors affecting auditors in the study area from performing the duty effectively. The standard deviation of the items ranged from 0.54 to 0.78. This indicated that respondents were unanimous in their responses as they were not from each other.

Hypothesis 1

HO₁: There are no specific techniques to be employed by Auditors to control fraud and financial irregularities in Oshimili South local Government Area of Delta State.

Table 4: Regression analysis on techniques employed by Auditors to control fraud and financial irregularities

Variables	R	R-square	Adjusted R-square	P-value	Remark
Techniques	0.893	0.887	0.807	0.05	Rejected

Source: Field Work, 2017

Table 4 shows the regression analysis on techniques employed by Auditors to control fraud and financial irregularities. The result showed that the R² value (0.88) is higher than the critical value of P at 0.05 level of significance. This indicates that techniques employed by Auditors to controlled fraud and financial irregularities. Therefore, the null hypothesis is rejected.

Hypothesis 2

HO₂: There are no specific factors that will enhance the effectiveness of Auditors in the control of fraud and financial irregularities in Oshimili South Local Government area of Delta State

Table 5: Regression analysis on factors that will enhance the effectiveness of Auditors in the control of fraud and financial irregularities

Variables	R	R-square	Adjusted R-square	P-value	Remark
Factors	0.793	0.71	0.702	0.05	Rejected

Source: Field Work, 2017

Table 6 shows that regression analysis on factor affecting effectiveness of Auditors in the control of fraud and financial irregularities. The result showed that the R^2 value (0.71) is higher than the critical value of P at 0.05 level of significance. This indicates that the identified factors affected effectiveness of Auditors in the control of fraud and financial irregularities. Therefore, the null hypothesis is rejected.

DISCUSSION OF FINDINGS

Techniques employed by auditors to control fraud and financial irregularities

The result in Table 2 indicated that auditors assist decision makers to comply with regulations guiding the Local Government Council; monitor the effectiveness of the management; review contracts in potential conflict of interest; check abuse of power amongst others were techniques employed by auditors in the study area. The findings are in corroboration with the results of Millichamp (2000) and Sani, 2009) who identified the common areas covered by internal auditing which include among others; reviewing the internal control system with a view to determining its adequacy and effectiveness, reviewing compliance with government regulations and account rules and standards, checking compliance with policies and procedures, safeguarding the asset of the organization so as to prevent and detect errors, frauds and theft, appraising the effectiveness and efficiency in the use of resources, ensuring that the goals and objectives of the organization are attained, making recommendations on improvement in the operation of the organization, acting as in-house consultant on control matters. The result also indicated that auditors did not participate in decision-makers in the LGA to ensure that funds were spent for the intended purpose; and public accountability was not provided to access the performance information of the management to stakeholders. This is true as audit activity usually suffers from interference from management staff which negatively affects the way audit conduct its work. According to Ahmi and Shahdan (2010) stated that the effectiveness of the auditors function in State and Local Government appears to be directly related to the management style of organization heads and their links, relationships and position in the social contract. Some auditors function appears to be doing well, the determining factors appear to be the attitude and leadership qualities of the head of an organization and audit reports that are ignored by everyone (Ahmi & Shahdan, 2010).

Factors affecting the effectiveness of auditors in the control of fraud and financial irregularities

The result in Table 3 indicated that auditor's activities, powers and duties are established by the public sector's constitution guiding the council, auditor are not provided with complete and unrestricted access to employees; lack property and other information needed to execute their work; insufficient funding; necessary qualifications and competence to conduct the full range of audits were factors inhibiting effectiveness of auditors in the control of fraud and financial irregularities in the study area. In consonance with findings, Observer Newspaper (December, 2014) stated that volume of work, number of staff, inadequate/lack of staff training, delays in operational procedure, frustration due to irregular payment of salaries amongst others were factor inhibiting effectiveness of auditors in government institutions. The result also indicated that auditors conduct their work with interference by the council management. This implies that audit activity suffers from interference from management staff which negatively affects the way audit conduct its work (IIA, 2001). This is very crucial element in conducting audit because the auditors can't access documents relating to the audit work and conducts the auditing without fear and favour.

Hypotheses

The result in Table 4 indicated that techniques employed by Auditors significantly controlled fraud and financial irregularities in the study. This implied that that effective and efficient audit of accounts ensures the proper reporting of the activities of the council activities. Johnson (2004) also stated that auditing

ensures that funds have been expended in accordance with the terms by which such monies were appropriated and that accounts have been properly prepared. Therefore, the results reveal that auditing of local government accounts ensures the proper accountability and Stewardship reporting of local government officials

The result in Table 5 indicated that the identified factors (interference, restriction of access to employees, property and other information among others) negatively affected effectiveness of Auditors in the control of fraud and financial irregularities.

CONCLUSION

The local government is a key institution in local governance. The primary level of grassroots political mobilization and a major reference point in the distribution by government of certain economic and social services. Local government has been recognized as a critical factor in national development. The motivation for the study is rooted in the fact that local governments as the third tier of government in Delta State and Nigeria in general performs poorly as a result of misappropriation of public funds as well as the need to understand the audit functions of local government councils. The study found that public sector auditing strengthens public governance by providing for accountability and protecting the core values of the Local government auditing in Oshimili South LGA ensures that politicians and public office holders utilize public funds transparently, fairly, and honestly, as well as with equity and integrity. However, lack of property and other information needed to execute their work; insufficient funding; poor qualifications and incompetence to conduct the full range of audits amongst others were factors inhibiting effectiveness of auditors in the control of fraud and financial irregularities in the study area.

RECOMMENDATIONS

1. The council management should support the activities of the auditors by providing them with adequate finance and documents to effectively carry out their duty
2. Qualified and competent staff needs to be recruited into the audit department of local government in order for the unit to function effectively.
3. The internal audit at the local government should be independent of political interference so that they can carry out their duties effectively.
4. There should be training and retraining of internal auditors through seminars, workshop and symposium in order to improve their effectiveness on internal and financial control.

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