

DETERMINANTS OF EXTERNAL AUDIT FEES: AN EMPIRICAL ANALYSIS OF DEPOSIT MONEY BANKS IN NIGERIA

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ABSTRACT

The study determined the determinants of external audit fees of Nigerian deposit money banks. Specifically, the study ascertains the extent client complexity, and audit committee independence significantly affects audit fees of Nigerian deposit money banks. Ex-post facto research design will be adopted for the study. Using a sample of 15 banks quoted on the Nigeria Stock Exchange, data for the study was obtained from annual published financial reports of the banks covering a period of eight years from 2009-2018. Ordinary least square regression was used to test the two formulated hypotheses. Findings show that audit size, client complexity and audit committee independence have positive influence on sampled quoted Nigerian deposit money banks audit fees but these influences are not statistically significant on audit fees. It therefore recommended that regulators of auditing practice should embrace a strategy to direct and monitor the audit fees process in order to strike a balance and reduce over-charging and under-charging which could be used to impair the independence of the auditor.

Keywords: External audit fees, client complexity, and audit committee independence

INTRODUCTION

There is a growing trend in accounting in recent years about the issue of audit fees on how auditors determine the amount of fees charged for audit services. This is a fundamental issue that needs to be evaluated for clarity. The full separation between shareholders and management led to the issue of appointment of an auditor to assume the responsibility of examining the financial statements prepared by client's management. The fee to be charged by the auditor for service or engagement within a given duration is very fundamental in auditing service. The auditing profession has come under increased scrutiny over the years about the growing amount of fees paid by audit client and the contributing impact of such fees on auditor independence (Geiger, & Papanatasiou, 2006; Geiger & Rama, 2003). The necessity for this study arises from the fact that very few studies have considered the audit fees determinants from the perspective of auditees, corporate governance and auditing firm attributes.

Consequently, the development of audit fee models should assist in providing benchmarks for assessing audit fees, which, in turn, should assist clients both in reviewing current fee levels as well as in better informing their choice of auditors (Alhassan, 2017). When external audit is put out for tender, identifying those variables that are significantly associated with audit fees should help refine the tender specification, and thus improve comparison of the tenders received: over time this could increase the competitiveness of the audit market, and consequently reduce prices.

Additionally, this process may well also indicate certain financial areas within the organization where closer attention to accounting and management issues could be beneficial. Also clients need to have confidence in their audited accounts if they are to discharge their duties effectively (Francis, 2004). Using the models could enhance directors' accountability for, and control of, the resources expended on audit of the financial statements (Paino & Tahir, 2012; Sundgren & Svanstrom, 2013).

While the determinants of audit fees are not new in literature, the significance of the determinants in pricing audit fees within a developing country context is limited. While the determinants of audit fees are not new in literature, the significance of the determinants in pricing audit fees within a developing country context like Nigeria is limited. Many studies have been focused on the market for audit profession and services in developed and developing countries, but few research works have been conducted on Nigerian deposit money banks in particular. Agbaje and Sokunle (2016) focused on the role of external auditor in fraud prevention and Soyemi and Olowookere (2013) studied on client attribute on external audit fees charged by banks. Thus, the current study extends previous studies by presenting new evidence about the external audit fees determinants in Nigerian deposit money banks. This study determines the effect of external audit fees determinants on audit fees of Nigerian deposit money banks. Specifically, the study intends to achieve the followings;

1. *To ascertain the extent client complexity significantly affect audit fees of Nigerian deposit money banks.*
2. *To evaluate the extent audit committee independence significantly affect audit fees of Nigerian deposit money banks.*

REVIEW OF RELATED LITERATURE

Conceptual Framework

External Audit Fees

Audit fee is a fee that a company pays an external auditor in exchange for performing an audit. The audit fee charged is influenced by auditor dependent factors: the reputation of the auditor, auditor experience, competition in the audit market (Hentati & Jilani, 2013; Ask & Holm, 2013; Castro, Peleias & Silva, 2015).

In point of fact, both US and UK are the original countries to investigate the matters related to external audit fees. Consequently, in researches on pricing of audit service determinants, both of the countries have been focused on: US (Bedard & Johnstone, 2010) and the UK (Pong, 2004). In addition, scholars have also taken companies of Australia (Carson, Fargher, Simon & Taylor, 2004; Carson & Fargher, 2006), France (Gonthier-Besacier & Schatt, 2007), India Bangladeshi, and Pakistan (Ahmed and Goyal, 2005), Danmark (Thinggaard and Kiertzner, 2008), Bahrain (Joshi and Bastaki, 2000), Kuwait (Meshari, 2008) into consideration.

In most of the mentioned studies, relationships between external audit fees and some factors are usually found. Gonthier-Besacier and Schatt (2007) indicated that external audit fees paid by listed French companies have an important and significant association with audit size, audit risk and auditor size. Meanwhile, Joshi and Bastaki (2000) conclude that audit fees paid by Bahrain listed companies rely on size of the reporting entity, profitability, company risk, company complexity and providing non-audit services. Furthermore, Bedard and Johnstone (2010) pointed out that audit tenure is positively associated with the level of external audit fee.

Moreover, they suggest that the closer association between external auditors and their clients can generate a financial dependence of auditors on their clients which threatens audit independence. The study of Ahmed and Goyal (2005) examines the determinants of audit fees charged to listed companies in South Asia including Bangladesh, India and Pakistan. They show that auditor size and auditee size are the most important determinants of audit fees, but the results indicated that audit fees and auditee complexity are not associated. To sum up the above, audit fee structure has been displayed as complex by the empirical research of audit fee determinants in different countries. Nearly all research has shown connections between auditee size, auditee risk, and auditor size and audit fees. Research indicates that, in specific situations, investors may even trust companies that pay high audit fees. Furthermore, these results also show that the concern about audit independence impairment derived from high external audit fees is reasonable. Consequently, it is important to regulate audit rotation. Furthermore, this finding can be an indication for other countries that audit tenure may cause audit independence impairment.

Client complexity

Auditee complexity has been of interest in researching into determinants of audit fees. Audit fees are dependent on how long auditors have to spend for a particular audit engagement and this may therefore imply that companies with complexity will be charged higher audit fees.

Results of Joshi & Bastaki (2000); Gonthier-Besacrier & Schatt, 2007; Ahmed & Goyal (2005) seem to be consistent with the view that auditee complexity has a significant relation with audit fees.

Complexity of the auditees can be measured by the number of branches and subsidiaries of the firm locally and internationally. Sandra and Patrick (1996) assert that, the more complex the client firm is, the greater the number and the more diversified the subsidiaries and operations are; which necessitate more audit work leading to a higher audit fees. Auditors of high complex firms often charge high audit fees in examining and evaluating the firm's financial statements. According to Sandra and Patrick (1996), foreign subsidiaries have to abide by a variety of legislative and proficient requirements for disclosure, which necessitate further audit testing, requiring more time and additional manpower to complete the audit process. This implies that, the companies have to bear additional charges for audit work.

Therefore, client's complexity has a positive correlation with the audit fees (Carson, Fargher, Simon & Taylor, 2004). Complexity of audited firm is commonly examined in two aspects; that is complexity of operations and complexity of the financial statements composition. Consequently, the complexity of operations of the enterprise may lead to Complex transactions which will invariably require an auditor spending longer time and other resources in carrying out an audit task, and the consequence of this is high audit fees. In particular, Joshi and Al-Bastaki (2000) have shown that audit fees are positively associated with the number of subsidiaries in foreign countries. To buttress this assertion further, Gonthier-Besacrier and Schatt (2007) and Semiu and Olayinka, (2010) found considerable evidences that suggest a positive association of firms' complexity and audit fees.

Audit committee Independence

Boo and Sharma (2008) observe a negative association between audit committee independence and audit fees indicating that auditors will minimize their effort in the presence of independent audit committee. Vafeas and Waagelein (2007) also, examined the association between audit committee characteristics and audit fees shows that independent audit committee is positively associated with audit fees and further suggest that audit committee serves as a complement to external auditor in monitoring mechanism and financial reporting quality.

Based on the role of audit committee, Collier and Gregory (1996) argued that audit committees independence may have effect on audit fees in two opposite ways. The first is to enhance audit quality, audit committee may require more work done by external auditors and hence, may put pressure on the company to pay higher audit fees. The second is since audit committee independence can strengthen internal control systems, audit procedures may increase and thus audit fees will decrease (Ohidoa & Okun, 2018). The auditors discovered that in the UK, the existence of audit committee independence has a positive and significant effect on audit fees; in contrast, Ho and Hutchinson (2010) find that in Hongkong, auditors expect that the presence of audit committee independence lower audit risk, thereby leading to lower audit fee charged.

Nevertheless, Goddard and Masters (2000) investigate that the existence of audit committee independence in the UK's companies has no relationship with the amount of audit fees. Also, to the above assertions, Steward and Munro (2007) state that Australian external auditor relies on an effective internal control but does not reduce their audit testing. Moreover, time and effort saved due to the presence of effective internal control balance with time spend for more meetings with client managers and partners and so, it has no significant relationship with audit committee independence (Steward and Munron, 2007).

Finally, it can be argued that each industry has its own peculiar characteristics and this might dictate the audit style and audit approach which could invariably impinge on the annual fee charge by the auditor. Auditors take different audit procedures for different industries. In this sense, audit fees charged will be different. For instance, Gonthier-Besacier and Schatt (2007) subdivided French listed firms into firms in information technology (IT) sector and others to test the impact of industrial sector on audit fees. The result indicates that audit fees paid by companies in IT sector were much higher than that paid by the others.

Review of Empirical Studies

Ohidoa and Okun, (2018) examined the firms' characteristics and audit fees in Nigeria. The study employed a time series and cross-session data (panel data) of firms listed at the Nigeria Stock Exchange. A sample size of eighty-nine (89) firms was used through the aid of Yaro (1964) formula for sample size determination. And the statistical tool used in the study was Panel Least Square Regression with the aid of Eview 7.0 and SPSS 20. The study found that, auditor type, client's firm size, client's complexity, client's firm risk and audit committee independence have significant effect on audit fees, while firm's profitability has no effect on audit fees. Alhassan (2017) examined the determinant of audit fee with empirical evidence from the Ghana stock exchange. Specifically, the study examined audit fee determinant which included the client size, profitability measured by ROA, LOSS, client risk measured by debt ratio, YEAR (season) and MNC. Using the Simunic (1980) model, this study reveals that client's size of business, international recognition, affiliation of audit firms (Big four firms) and profitability are significant determinants of audit fee in Ghana. Results in study indicate that ignorance of risk factor by the auditors may pose serious threat to fame and reputation of audit firm along with indication of feeble legal regime in Ghana. Bogale (2016) analyzed the external audit quality and the various determinant factors those influence it. Specifically, the study used documentary analysis of companies' audited financial statements and personal inquiry with audit directors/officials of audit firms and company managers. Consequently, the study selected a sample of eighteen (18) companies for the period of five years (2011-2015) with the total of 90 observations. The results of panel least square regression analysis show that certified audit professionals and joint provision of audit and non-audit services have statistically significant and positive relationship with manufacturing share companies' external audit quality. Belen et al. (2014) studied the auditor tenure association with audit quality by using a sample of 254 audits carried out on Spanish state-owned foundations between 2003 and 2010. The results revealed that audit quality, measured as the likelihood that an auditor will submit a qualified opinion, increases over the first five years of the relationship and then decreases. Soyemi and Olowookere (2013) empirical

examination of client attributes which significantly explain variations in the amount of external audit fees charged by bank auditors in Nigeria; a standard audit fee model, modified accordingly, is used to investigate the specific effect of bank size, risks and complexities on audit fees for top ten (10) publicly quoted commercial banks, which constitute over 70% of the total assets of the industry. Multiple OLS regression was adopted as the estimation technique on the panel data gathered through content analysis of annual reports and accounts of these banks over a 4-year post consolidation periods covering 2009-2012. The findings from this study reveal that bank size is also an important factor that is priced by bank auditors having shown a positive and significant influence accounting for 63% variations. Augustine et al. (2013) examined determinants of audit quality in Nigerian business environment. The objective of this study was to analyze the determinants of audit quality in the Nigerian business environment. The study used primary data. Data collection instrument was questionnaires that were constructed using the likert scale. A regression model was used to analyze the existence of significant relationships between audit quality and the audit firm related characteristics. The study found significant relationships between audit quality and the audit firm related characteristics.

Siregar, Amarullah, Wibowo, & Anggraita (2012) investigated the effects of auditor rotation and audit tenure of the public accountant and the public accounting firm, on audit quality (before and after the implementation of the mandatory auditor regulation) in the Indonesian. Their results showed that mandatory auditor rotation did not increase audit quality, and that shorter audit tenure (both partner and firm level) did not also increase audit quality. Walid (2012) concluded that the size of the audit firm is important factor in affecting the amount of external audit fees in Lebanon. Presently, the Big 4 audit firms dominate the audit services market, and consequently, smaller firms face huge obstacles to enter the market of big companies. Moreover, the fee charged by big audit firms may be higher than that of non-big ones, due to the reputation impact and advantage of the former.

Sharma (2011) researched on the relationship between joint provision of audit and non-audit services and loss of auditors' independence for publicly listed New Zealand companies in 2011. Using discretionary accruals as an indicator of audit quality, the regression analysis discovered a significant positive relationship between lower abnormal accruals indicate that earnings quality is higher, which is a proxy of audit quality and the practice whereby external auditors providing non-audit service to its audit client. Dehkordi and Makarem (2011) ascertained the influence of audit firm size (Big auditors vs. non-Big auditors) and auditor type (governmental vs. private auditors) on audit quality. A sample of 224 firms was observed from the Tehran Stock Exchange (TSE) companies during the period 2002 to 2007. Their results indicated that the size of non-governmental audit firms does not affect their audit quality. Ahmed and Goyal (2005) examined the determinants of audit fees charged to listed companies in South Asia including Bangladesh, India and Pakistan. They show that auditor size and auditee size are the most important determinants of audit fees, but the results indicated that audit fees and auditee complexity are not associated. To sum up the above, audit fee structure has been displayed as complex by the empirical research of audit fee determinants in different countries. Nearly all research has shown connections between

auditee size, auditee risk, and auditor size and audit fees. Research indicates that, in specific situations, investors may even trust companies that pay high audit fees.

From the existing studies, most of studies revealed that client's size of business, international recognition; affiliation of audit firms (Big four firms) and profitability are significant determinants of audit fee. On the other hand, some researchers found negative significant effect between audit fees and its determinants. While the determinants of audit fees are not new in literature, the significance of the determinants in pricing audit fees within a developing country context is limited. Thus, the current study extends previous studies by presenting new evidence about the external audit fees in Nigeria.

METHODOLOGY

Research Design

Ex-post facto research design was employed for the study. This is appropriate because the study aims at measuring the relationship between one variable and another, in which the variables involved are not manipulated by the researcher.

Population of the Study

This study used 15 deposit money banks quoted on the Nigerian Stock Exchange. The study covered ten years annual reports and accounts of these banks from 2009 to 2018.

Method of Data Analysis

The data for the study was collected from annual reports and accounts of deposit money banks quoted on the Nigerian Stock Exchange (NSE). The dependent variable is proxied using audit fees, while the independent variables are Client Complexity and audit committee independence.

Audit fees comprise the natural log of the audit fees paid by the company. This operationalization follows the approach used in Kane and Velury (2011) where big audit firms are assumed to have quality audit services than other smaller audit firms.

Model Specification

The specified simple regression estimated model takes the following form:

$$AUDFE_{it} = a_0 + \mu_i + \beta_1 CLTCOMP_{it} \sum_{it} \dots \dots \dots (i)$$

$$AUDFE_{it} = a_0 + \mu_i + \beta_2 AUDCIND_{it} \sum_{it} \dots \dots \dots (ii)$$

Where:

The dependent variable: Audit fees measured as the amount of fees charged by the auditor for an audit service and the independent variables:

CLTCOMP= In this study we measured firm complexity by the number of branches a company operates.

AUDCIND= It is measured by the ratio of non-executive directors to the total number of the board.

a_0 = slope of the model

$\beta_1, \beta_2, \beta_3$, = coefficient of parameter.

DATA ANALYSIS

Hypothesis One

Ho: Client complexity has no significant effect on audit fees of Nigerian deposit money banks.

Table 1: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.148 ^a	.022	.014	277345.11720

a. Predictors: (Constant), CLTCOMP

Table 1 above shows that the Model revealed the value of $R^2 = 0.022$ and Adjusted R^2 value is 0.014. This suggests that the model explains about 1.4% of the systematic variations in the dependent variable. This means that the regression explains 1.4% of the variance in the data.

Table 2: ANOVA^a

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	226305920146.729	1	226305920146.729	2.942	.089 ^b
	Residual	10076561138262.096	131	76920314032.535		
	Total	10302867058408.824	132			

a. Dependent Variable: AUDFEES

b. Predictors: (Constant), CLTCOMP

Table 3: Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	80355.041	64949.308		1.237	.218
	CLTCOMP	483.648	281.969	.148	1.715	.089

a. Dependent Variable: AUDFEES

In table 2, it reveals that the F-stat (2.942) and p-value (0.089) indicates that the hypothesis is not statistically significant; hence its p-value is greater than 0.01%.

In table 3, the regressed coefficient correlation result shows that an evaluation of the external audit fees of the explanatory variable (Beta Column) shows that client complexity is not significant (Sig.= 0.148). Therefore, we reject alternative hypothesis and uphold null hypothesis which states that client complexity has no significant effect on audit fees of Nigerian deposit money banks.

Hypothesis Two

Ho: Audit committee independence has no significant effect on audit fees of Nigerian deposit money banks.

Table 4: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.051 ^a	.003	-.005	134144.57549

a. Predictors: (Constant), AUDCIND

Table 4 above shows that the Model revealed the value of $R^2 = 0.003$ and Adjusted R^2 value is -0.005 . This suggests that the model explains about 0.5% of the systematic variations in the dependent variable. This means that the regression explains 0.5% of the variance in the data.

Table 5: ANOVA^a

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	6070587021.565	1	6070587021.565	.337	.562 ^b
	Residual	2321324960135.824	129	17994767132.836		
	Total	2327395547157.389	130			

a. Dependent Variable: AUDFEES

b. Predictors: (Constant), AUDCIND

Table 6: Coefficients^a

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	176144.454	25732.573		6.845	.000
AUDCIND	-2299.543	3959.126	-.051	-.581	.562

a. Dependent Variable: AUDFEES

In table 5, it reveals that the F-stat (0.337) and p-value (0.562) indicate that the hypothesis is not statistically significant; hence p-value is greater than 0.001%.

In table 6, the regressed coefficient correlation result shows that an evaluation of the external audit fees of the explanatory variable (Beta Column) shows that audit size is not significant (Sig.= -0.051). Therefore, we reject alternative hypothesis and uphold null hypothesis which states that audit committee independence has no significant effect on audit fees of Nigerian deposit money banks.

Discussion of Findings

The results obtained from the analysis revealed that client complexity and audit committee independence has no significant effect on audit fees of Nigerian deposit money banks. This result was in line with that of Alhassan (2017). Bogale (2016) study reveals that client's size of business, international recognition; affiliation of audit firms (Big four firms) and profitability are significant determinants of audit fee. Also, according to Urhoghide and Izedonmi (2015), the results for audit client characteristics revealed that audit client size and complexity have a positive and significant impact on audit fee while profitability, fiscal year end and industry have a negative and significant influence on audit fee.

CONCLUSION AND RECOMMENDATIONS

Based on this study, it is found that audit fees in Nigerian banks is positively and statistically significant related to the client size, and client profitability of our sampled banks in Nigeria. Meanwhile audit size, client complexity has a positive influence on our sampled quoted banks audit fees and this influence is not statistically significant. However, audit committee independence was found to have a negative influence on our sampled quoted banks audit fees and this influence is also not statistically significant on audit fees of Nigerian deposit money banks.

This outcome is similar to that obtained by numerous audit fee research performed in several countries. Moreover, the results revealed that the amount of audit fees is positively related to the profitability and client size. This finding leads to the assumption that better-off audit clients might be viewed to have a "deeper pocket," and so are charged higher amounts of external audit fees.

A rationale for this could be that, in Nigeria, rules and regulations are not strict and hard like developed countries where mostly auditors are held liable and punished for manipulation of accounting figures. Furthermore, these results also show that the concern about audit independence impairment derived from high external audit fees is reasonable.

Based on this, the study recommended that regulators of auditing practice should embrace a strategy to direct and monitor the audit fees process in order to strike a balance and reduce over-charging and under-charging which could be used to impair the independence of the auditor.

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