

**EFFECT OF ENFORCEMENT CAPACITY OF EXTERNAL AUDIT  
RECOMMENDATIONS ON FINANCIAL PERFORMANCE OF COUNTY  
GOVERNMENT OF NAKURU, KENYA**

**John Gathii Kamau**

School of Business and Economics, Kabarak University, Kenya  
jgathii@kabarak.ac.ke

**Abstract**

The expectation after an audit is that the audit client will address the concerns raised by the external auditor. In many instances this is not so due to reasons beyond the control of the audit client due to lack of capacity. This study sought to examine the effect of enforcement capacity of external audit recommendations on financial performance of county government of Nakuru, Kenya. Data was collected using structured questionnaires. The hypothesis stated that there is no statistically significant influence of enforcement capacity of external audit recommendations on financial performance of County Government of Nakuru, Kenya. This study employed a multiple study design. Correlational, causal and cross sectional study design were used. The proposed hypothesis that enforcement capacity of external audit recommendations have no statistically significant influence on financial performance of County Government of Nakuru was rejected on the basis that -statistical value of (4.853) was greater than the critical value and that the p-value was less than 0.05. It was therefore concluded that there is statistically significant influence of enforcement capacity of external audit recommendations on financial performance of County Government of Nakuru, Kenya. It was further concluded that the independent and dependent variables of this study are functionally linearly related.

**Keywords:** *enforcement capacity, external audit recommendations, financial performance*

**Introduction**

The capacity to enforce audit recommendations is critical in determining the performance of both auditing and financial performance at large. The audit exercise, expensive, time consuming and tedious as it is could be rendered ineffective if the audit client has no capacity to implement the recommendations by the external auditor. The failure to implement the auditor's recommendation could have a negative some impact on the financial performance of the audit client. This study sort to establish the relationship between enforcement capacity of external audit recommendations and financial performance of County Government of Nakuru Kenya.

**Objective of the Study**

To examine the effect of enforcement capacity of external audit recommendations on financial performance of county government of Nakuru, Kenya.

### **Literature review**

Kwaza (2017) examined the utilization and implementation of the auditor general's reports within selected municipalities of Amathole district in South Africa. The study used descriptive research design. The study collected data using a study questionnaire and interview guide. The study revealed that; 10.9%, 26.2%, 53.4%, and 9.5% of the respondents indicated that they strongly disagreed, disagreed, agreed and strongly agreed that audit recommendations is monitored until they are fully implemented. The study found that the monitoring of implementation of audit queries was done quarterly as cited by 35.3% and 41.3% of respondents who agreed and strongly agreed respectively.

Utumi (2016) carried out a study to evaluate the efficiency of internal auditing practice in enterprises owed by the government of Indonesia. The study used a case study research design whereby one state-owned enterprise was studied. The sample size for the study comprised on internal auditors and head of internal audit department in the state-owned corporation. In the study, data was collected using interviews and unstructured questionnaires. The study found out that internal auditors have the capacity to monitor and follow up with internal and external audit recommendations. The study further found out that the head of internal audit had a direct access to audit reports from audit committee.

Based in Zimbabwe, Shumba (2015) investigated the impacts of failure by the organization management to implement audit recommendations in national social security authority(NSSA). The study targeted directors, accounts clerks, accountants, bookkeepers and administration staffs of the national social security authority. The study used questionnaires as well as interview guides to collect data. The study found out that 72% and 19% of the respondents strongly agreed and agreed respectively that the authority was not implementing the audit reports. Through the interviews, it was revealed that lack of capacity to enforce the recommendation was the main reason for failure to implement audit recommendations.

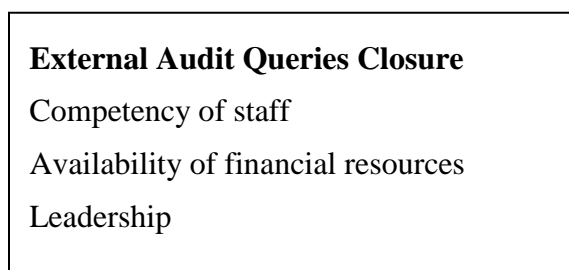
On Ethiopian context, Korje (2016) carried out a study in Public Sector organizations that sought to assess the implementation of Audit Recommendations in Government Public Institutions at Oromia Region of the country. This study adopted descriptive research design. Cluster sampling was done and a sample size of 435 respondents was obtained. The study used there sets of research instruments, namely; questionnaires, interviews and documents obtained from various sources. Using frequency distributions, the study found out that 32.4% of the respondents agreed that only few audit recommendations were implemented, with 21.7% citing that all audit recommendations were implemented and yet 14.55 of the respondents indicating that no action was taken on the audit recommendations. The study sought to find out the reason for failure to implement audit recommendation. In this regard, the study found out that the management structure of the organization does not have the capacity to implement audit recommendations. Other reasons given include; lack of competency of human resources, poor supervision and control aspects of public institutions, poor quality of services in the institutions,

inadequate internal control measures and lack insufficient budget to implement the audit recommendations.

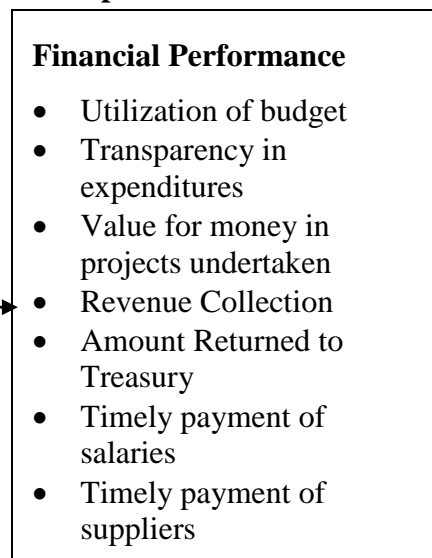
### **Conceptual Framework**

The enforcement capacity of audit recommendations was examined using county government leadership structure having capacity to implement audit recommendations, county government employees having required competency to implement external unit queries, proper supervision in audit queries implementation, adequacy of funds to implement audit recommendations at county government, and sufficiency of time on county government for the implementation of audit recommendations.

#### **Independent Variables**



#### **Dependent Variable**



### **Research Methodology**

This study adopted descriptive research design as the blueprint that guided all the methodological aspects of the study. Descriptive research design involves investigating a certain phenomenon on its natural setting without imposing control measures upon the phenomenon(Keller, 2014). In so doing, the study examined the effect of external auditing on financial performance of the county government of Nakuru. Using descriptive study, a researcher is able to obtain more information about a phenomenon under investigation and in an accurate manner (Saunders et al., 2009). This study desired to obtain more accurate information on external auditing and financial performance and hence the choice of the model. The study targeted all employees in the County Government of Nakuru who were involved in financial roles. These employees were targeted for they were knowledgeable on auditing aspects and financial performance in the county government. According to the County Government of Nakuru (2018), there are employees from finance and accounting department in the County government. Therefore the target population for this study was 80 people. This was composed of eight senior finance management staff, thirteen junior finance management staff, forty nine

finance clerks and ten departmental heads from the ten departments in the county government of Nakuru. This study used the census approach where members of the entire population were used for data collection (Sekaran & Bougie, 2011). The target population is as shown on Table 1.

**Table 1: Target Population**

<b>Employee Category</b>	<b>Frequency</b>
Senior Finance Management Staff	8
Junior Finance Management Staff	13
Finance Clerks	49
Departmental heads	10
<b>Total</b>	<b>80</b>

Data collection instruments refer to the study tools that are used to collect data for the study (Jankowicz, 2005). This study used a data collection instrument that provides privacy in responding to the study questions. It was also the interest of this study to use a research tool that could facilitate fast collection of data without necessarily having the researcher present at the time of data collection. In view of the outlined qualities, the study used structured questionnaires. Structured question provides a quick way of data collection since it contains possible answers to the closed ended questions in the questionnaire (Kombo & Tromp, 2009). A respondents can choose to respond to research questions at own time without the supervision of the researcher and this results in high response rate (Orodho & Kombo, 2002).

The filled questionnaires were checked to confirm whether or not they have been filled to completion. Only questionnaires filed to completion were used for analysis. The data from the questionnaire was coded and entered in Statistical Package for Social Sciences (SPSS) version. The study used descriptive statistics and inferential statistics to analyse the data.

Descriptive statistics refers to the use of measures of central tendencies and dispersion to describe basic characteristics of data.. For inferential statistics, the Fisher's exact test, Pearson Correlation, and a multiple linear regression were used to examine the relationship between external audits aspects and financial performance of County Government of Nakuru. A Fisher's exact test is a statistical test that assists researchers to determine whether there are non-random associations between two categorical variables (Jankowicz, 2005). The null hypothesis of the Fishers exact test states that there is no association between two classifications (Saunder et al., 2009). At a level of significance of 0.05, a p-value less than 0.05 leads to the rejection of the null hypotheses and the acceptance of the alternative hypothesis. The implication of this is that the two categorical variables in the test are not associated or related.

### **Results and Discussion**

The effect of enforcement capacity of external audit recommendations on financial performance of county government of Nakuru, Kenya was examined based on the aspects of competency of staff, availability of financial resources, and leadership. The results of the attitudes of respondents towards various statements related to these aspects are shown in Table 2.

In the context of leadership, a majority of the respondents (38.0%) tended to agree to a large extent that the County Government of Nakuru leadership structure has the capacity to implement audit recommendations. Other respondents who tended to agree with the statement were 25.4% to a moderate extent, 16.9% to a very large extent, and 14.1% to a small extent. A few respondents (5.6%) disagreed with the statement and indicated that the County Government of Nakuru structure has no capacity to implement audit recommendations. These findings differ from those made by Shumba (2015) in Zimbabwe. The study found out that 72% and 19% of the respondents strongly agreed and agreed respectively that the authority was not implementing the audit reports. Through the interviews, it was revealed that lack of capacity to enforce the recommendation was the main reason for failure to implement audit recommendations.

***Table 2: Frequencies, chi-square, and p-value for Enforcement Capacity of External Audit Recommendations***

	NE	SE	ME	LE	VLE	Chi-Square	P
	%	%	%	%	%	Value	
The county government leadership structure has the capacity to implement audit recommendations	5.6	14.1	25.4	38.0	16.9	23.998	0.000
The county government employees have the required competency to implement external audit queries	2.8	7.0	35.2	43.7	11.3	25.311	0.000
There is proper supervision in the implementation of audit queries	4.2	16.9	39.4	33.8	5.6	25.871	0.000
There are enough funds to implement the audit recommendations at the county government	7.0	15.5	36.6	31.0	9.9	20.788	0.007
The county government has enough time for the implementation of audit recommendations	11.3	12.7	29.6	38.0	8.5	24.319	0.000

Korje (2016) carried out a study in Public Sector organizations and also made findings that are contradicted by those of the current study. The study found out that 32.4% of the respondents

agreed that only few audit recommendations were implemented. The study sought to find out the reason for failure to implement audit recommendation. In this regard, the study found out that the management structure of the organization does not have the capacity to implement audit recommendations. The current study carried generated a chi-square value of 23.998 and p-value of 0.000 ( $p < 0.05$ ) which revealed that a relationship exists between leadership structure's capacity to implement audit recommendations and financial performance of the County Government of Nakuru, Kenya.

In regards to competency of staff, most of the respondents (43.7%) tended to agree to a large extent that the County Government of Nakuru employees have the required competency to implement external audit queries. Other respondents who also tended to agree with the statement were 35.2% to a moderate extent, 11.3% to a very large extent, and 7.0% to a small extent. On the other hand, County Government of Nakuru employees were perceived not to have the required competency to implement external audit queries by 2.8% of the respondents (chose "No Extent" prompt). The study found that the competency of employees to implement external audit queries is related to financial performance of the County Government of Nakuru, Kenya (chi-square value=25.311;  $p < 0.05$ ).

A majority of the respondents (39.4%) tended to agree to a moderate extent that there is proper supervision in the implementation of audit queries in the County Government of Nakuru. Further, 33.8% of the respondents tended to agree with the statement to a large extent, 16.9% to a small extent, and 9.9% to a very large extent. Respondents who tended to disagree (4.2%) indicated that to no extent is there proper supervision in the implementation of audit queries. A Fisher's exact value of 25.871 and p-value less than 0.05 (0.000) revealed that supervision in the implementation of audit queries and financial performance of the County Government of Nakuru, Kenya are related.

In the context of availability of financial resources, 36.6% and 31.0% of the respondents tended to agree to a moderate extent and large extent, respectively, that there are enough funds to implement the audit recommendations at the County Government of Nakuru. Other respondents who tended to agree with the statement were 15.5% to a small extent and 9.9% to a very large extent. However, 7.0% of the respondents chose the "No Extent" prompt which indicated they tended to disagreed with the statement. The availability of funds to implement the audit recommendations and the financial performance of the County Government of Nakuru, Kenya were found to be related (chi-square value=20.788;  $p < 0.05$ ).

A majority of respondents tended to agree to a large extent (38.0%) that the County Government of Nakuru has enough time for the implementation of audit recommendations followed by 29.6% of respondents who tended to agree with the statement to a moderate extent. Some respondents tended to agree to a small extent (12.7%) and very large extent (8.5%) that the County Government of Nakuru has enough time for the implementation of audit recommendations. Respondents who tended disagree with the statement were 11.3%. The chi-square results

revealed the existence of a relationship between adequacy of time for the implementation of audit recommendations and the financial performance of the County Government of Nakuru, Kenya. This is due to a chi-square value of 24.319 and a p-value of 0.000 which was less than 0.05.

### **Correlation Analysis**

To establish whether there was a significant relationship between the study variables, the study used Pearson Correlation.

**Table 3: Pearson Correlation**

		<b>Enforcement Capacity</b>
Financial	Pearson Correlation	0.806**
Performance	Sig. (2-tailed)	.000
	N	71

The study found that the enforcement capacity had a positive and statistically significant influence on the financial performance at correlation coefficient of 0.806.

### **Regression Analysis**

The study used multiple linear regressions to establish the effect of staff attitude towards external audit, external Audit Outcomes, Audit Queries Closure and Enforcement Capacity external audit recommendations on the financial performance of County Government of Nakuru. Table 4 shows the model summary of the regression model.

**Table 4: Model Summary**

<b>Model</b>	<b>R</b>	<b>R Square</b>	<b>Adjusted R Square</b>	<b>Std. Error of the Estimate</b>
1	0.916 <sup>a</sup>	0.839	0.829	0.22250

a. Predictors: (Constant), Staff Attitude, Audit Outcomes, Audit Queries Closure, Enforcement Capacity

The model summary gives an R value of 0.916 and R-square value of 0.839. An adjusted R Square value of 0.829 and standard error of estimate of 0.22250 were also obtained. The R is the correction coefficient between the observed and predicted values of the dependent variable and it indicates the goodness of fit of the regression model to the data (Saunders, Lewis, & Thornhill, 2009). Therefore, there was a strong relationship between the observed and predicted values of

the financial performance of County Government of Nakuru. This implies that the model provides a good fit for the data. R-Square is called the coefficient of determination and shows the proportion of variation in dependent variable that is attributable to the independent variables in the study (Keller, 2014). This therefore implies that 83.9% of the variation in the financial performance of County Government of Nakuru is cumulatively attributable to staff attitude towards external audit, external Audit Outcomes, Audit Queries Closure and Enforcement Capacity external audit recommendations. In this regard, 16.1% of the variation in the financial performance of County Government of Nakuru is attributable to other factors that were not studied by the current study.

Adjusted R-Squared shows the effect of adding more predictor variable into the regression equation. It gives the portion of variability in the dependent variable as explained by significant predictors only (Jankowicz, 2005). In this regression model, 82.9% of the variability in financial performance of County Government of Nakuru is attributable to staff attitude towards external audit, external Audit Outcomes, Audit Queries Closure and Enforcement Capacity external audit recommendations without the constant value which was found to be statistically insignificant ( $p > 0.05$ ). Standard error of estimate shows the accuracy of the prediction model (Sekaran & Bougie, 2011). A low standard estimate of error of 0.22250 obtained in this regression model indicates that the multiple regression model is accurate in its prediction of financial performance of County Government of Nakuru. The study further sought to establish whether the regression model is significant predictor of the dependent variable as shown in Table 5.

**Table 5: ANOVA<sup>a</sup>**

<b>Model</b>		<b>Sum of Squares</b>	<b>Df</b>	<b>Mean Square</b>	<b>F</b>	<b>Sig.</b>
1	Regression	17.055	4	4.264	86.128	.000 <sup>b</sup>
	Residual	3.267	66	.050		
	Total	20.322	70			

a. Dependent Variable: Financial Performance

b. Predictors: (Constant), Staff Attitude, Audit Outcomes, Audit Queries Closure, Enforcement Capacity

The F-value in the analysis of variance indicates that significance of the regression model as a whole. The null hypothesis of the F-test in the regression model states that the multiple linear regression model has no predictive capacity better than a regression model that consists of zero predictor variables (Saunders et al., 2009). The regression model in this study obtained an F-statistic value of 86.128 with 4 degrees of freedom for the regression and 66 degrees of freedom for residual. This test was found to be statistically significant at 5% significant level ( $p < 0.05$ ). This implies that the regression model had a statistically significant predictive capacity more than a regression model that contains zero predictor variables. Therefore the regression model can significantly predict financial performance of County Government of Nakuru using staff

attitude towards external audit, external audit outcomes, audit queries closure and enforcement capacity external audit recommendations as predictor variables. The study further sought to establish the effect of each of the predictor variable on the financial performance of County Government of Nakuru as shown in Table 6.

**Table 6: Model Coefficients**

<b>Model</b>	<b>Unstandardized Coefficients</b>		<b>Standardized Coefficients</b>		
	<b>B</b>	<b>Std. Error</b>	<b>Beta</b>	<b>t</b>	<b>Sig.</b>
(Constant)	0.168	0.202		0.830	0.409
Staff Attitude	0.253	0.063	0.262	3.994	0.000
Audit Outcomes	0.199	0.059	0.102	3.684	0.007
Audit Queries Closure	0.361	0.062	0.410	5.826	0.000
Enforcement Capacity	0.252	0.052	0.332	4.853	0.000

a. Dependent Variable: Financial Performance

The study hypothesis stated that there is no statistically significant influence of enforcement capacity of external audit recommendations on financial performance of County Government of Nakuru, Kenya. This hypothesis was rejected on basis of -statistic value (4.853) greater than the critical value and p-value less than 0.05.

### **Conclusion**

The study concluded that enforcement capacity of external audit recommendations influences financial performance of County Government of Nakuru, Kenya.

### **Recommendations**

It is recommended that the County Government of Nakuru address the aspect of capacity to implement auditor general's recommendations in order to enhance financial performance. It is further recommended that a study be done to establish the factors that determine capacity to implement auditor general's recommendations so that they can be addressed.

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