

**RELATIONSHIP BETWEEN AUDIT TENURE AND EARNINGS
MANAGEMENT OF DEPOSIT TAKING SACCO'S IN NAIROBI
COUNTY**

JUNIOR MWANZA MWAU

**A RESEARCH PROJECT SUBMITTED IN PARTIAL
FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF
THE DEGREE OF MASTER IN BUSINESS ADMINISTRATION
SCHOOL OF BUSINESS, UNIVERSITY OF NAIROBI**

DECEMBER 2017

DECLARATION

Student's Declaration

I declare that this research project is my original work and has not been presented for a degree in any other university. All references made to works of other persons have been duly acknowledged.

Signed..... Date.....

JUNIOR MWANZA MWAU

REG NO: D61/63238/2010

Supervisor

This research project has been submitted for examination with my approval as university supervisor

Signed..... Date.....

DR. MIRIE MWANGI

Senior Lecturer, Department of Finance and Accounting

ACKNOWLEDGEMENT

My scholarly journey would not have been possible without the financial and moral support of my mother Jane Mwanza, who has sacrificed a lot to ensure that all her children get the highest education possible, for keeping that educational journal that ensured her children are in touch current with the scholar world through attending trainings or undertaking current courses and providing that discipline and drive to achieve excellent results.

To the Almighty LORD who gave me the spiritual support and encouragement, surely without your blessings I would not be where I am today, I am proud to be in this world having this world to shape it as it was intended.

To my sons, Kiefer & Kieran whose keeps reminding me '*Baba nataka kusoma kama wewe*', words that have always urged me on as i strive to be a father and human being that he is proud of and can emulate. I can only hope and pray that one day, they will have a far more successful educational journey than I could have.

And certainly, much appreciation goes to the University of Nairobi for providing a conducive environment, the entire fraternity and its eminent scholars and especially Dr. Mirie Mwangi for sharing his pearls of wisdom, encouragement and patience in the guidance of young minds.

It would not be possible to thank everyone that has contributed to my educational journey and with this opportunity, from deep in my heart, I thank each one of you for any and every way that you have contributed to the success of this work. Thank you all.

DEDICATION

This dissertation is dedicated to my sons, Kiefer and Kieran, for whom I strive to be a better man, mentor and role model every day

TABLE OF CONTENTS

DECLARATION	ii
ACKNOWLEDGEMENT	iii
DEDICATION	iv
TABLE OF CONTENTS	v
LIST OF TABLES	ix
LIST OF ABBREVIATIONS	x
ABSTRACT	xi
CHAPTER ONE	1
INTRODUCTION	1
1.1 Background to the Study.....	1
1.1.1 Audit Tenure	2
1.1.2 Earnings Management	4
1.1.3 Audit Tenure and Earnings Management	5
1.1.4 Deposit Taking SACCO's in Nairobi County	7
1.2 Research Problem	8
1.3 Research Objectives.....	10
1.4 Value of the Study	10
CHAPTER TWO	11
LITERRATURE REVIEW	11
2.1 Introduction.....	11
2.2 Theoretical Review	11

2.2.1 Agency Theory.....	11
2.2.2 Stakeholder Theory	13
2.3 Determinants of Earnings Management.....	13
2.4 Empirical Studies	15
2.5 Conceptual Framework.....	18
2.5.1 Audit tenure and earnings management.....	18
2.5.2 Return on Assets and earnings management	19
2.5.3 Firm growth and earnings management.....	20
2.5.4 Firm size and earnings management.....	20
2.5.5 Firm age and earnings management	21
2.5.6 Firm cash flows and earnings management	21
2.6 Summary of Literature Review.....	22
CHAPTER THREE	23
RESEARCH METHODOLOGY	23
3.1 Introduction.....	23
3.2 Research Design.....	23
3.3 Population	23
3.4 Sample Design	24
3.5 Data Collection	24
3.6 Data Validity and Reliability	24

3.7 Data Analysis	25
3.7.1 Specification of the Model.....	25
CHAPTER FOUR.....	27
DATA ANALYSIS, PRESENTATION AND DISCUSSIONS	27
4.2 Introduction.....	27
4.2 Response Rate.....	27
4.3 Data Validity.....	27
4.4 Descriptive Statistics.....	27
4.5 Correlation Analysis	29
4.6 Regression Analysis and Hypothesis Testing	30
4.6.1 Model Summary.....	30
4.6.2 Analysis of Variance.....	31
4.6.3 Regression Coefficients	31
4.7 Discussion of Findings.....	32
CHAPTER FIVE	35
SUMMARY, CONCLUSIONS AND RECOMMENDATIONS	35
5.1 Introduction.....	35
5.2 Summary of Findings.....	35
5.3 Conclusions.....	36
5.4 Recommendations.....	38
5.5 Limitations of the Study.....	39

5.6 Suggestions for Further Research	40
REFERENCES.....	42
APPENDICES	58
APPENDIX I: DEPOSIT TAKING SACCOS IN NAIROBI COUNTY	58

LIST OF TABLES

Table 4.1: Descriptive Statistics Results.....	28
Table 4.2: Correlation Analysis	29
Table 4.3: Model Summary	29
Table 4.4: ANOVA.....	29
Table 4.5: Coefficients.....	29

LIST OF ABBREVIATIONS

AGM	Annual General Meeting
DTS	Deposit Taking SACCO's
EM	Earnings Management
EY	Ernst & Young
FIN ACCESS	Financial Access
ICPAK	Institute of Certified Public Accountants of Kenya
IFRS	International Financial Reporting Standards
MAR	Mandatory Auditor Rotation
NSE	Nairobi Securities Exchange
PWC	Price Waterhouse Cooper
SACCO	Savings and Co-operative
SASRA	Sacco Societies Regulatory Authority

ABSTRACT

The intention of the study was to interrogate the linkage between the auditor tenure and level of earnings management practices of deposit taking Sacco's in Nairobi County during the 5-year period between January 2012 and December 2016. Discretionary accruals were used as proxies and measured using the modified Jones model. The study employed a descriptive research design and used multiple regression analysis. The dependent variable was discretionary accruals and audit tenure, return on assets, growth, firm size, firm age and cashflow from operations as the independent variables in defining the relationship that existed among audit tenure and earnings management of deposit taking Sacco's in Nairobi County. The study used secondary data from proxy financial information for the 5-year period with the statistical population consisting of 41 DTS's operating in Nairobi County as Licensed by SASRA. The study concluded that all DTS's had complied with the Sacco societies regulatory authority term limit of 3 years for which an audit firm may be on record after which DTS's are required to change auditors and showed that audit tenure had no influence on earnings management practices of DTS's however, a significant relationship existed with return on assets, firm growth and cashflows from operating activities. The study recommends DTS's to consider engaging a wide variety of firms within the existing pool, use of the Big-4 audit firms by DTS's with a large asset base and coming up with measures of detecting earnings management by the audit firms.

CHAPTER ONE

INTRODUCTION

1.1 Background to the Study

Failures attributed to audits, accounting, corporate governance as well as human factors fueled by greed and managements opportunism have largely been blamed for the rise in corporate failures and financial scandals witnessed over the last decade across the globe with the more notable cases including Enron (2001) and Worldcom (2002) in the US. According to Mendonça, Costa, Galdi and Funchal (2010), these two scandals have led to a more concerted look at the roles that auditors play in accounting scandals wherein in 2002, the Sarbanes-Oxley Act was passed purposed to accounting firms that undertake audit of corporations, management actions and interactions with auditors to enhance compliance with policies, laws and regulations.

Despite the increased efforts on regulating the accounting profession, further scandals have emerged including; Parmalat, dubbed ‘Europe’s Enron’ (2003) that had used the same auditing firm since the 1990’s and on changing their auditors in 1999 following the implementation of a new Italian law requiring rotation every 8 years, this led to the fraud discovery of a \$14bn black hole in its finances (Ferrarini & Giudici, 2005), Cardbury (Nigeria) in 2006 which had overstated its accounts by between Naira 13B for the period 2002-2006 having engaged the services of 1 auditor for over 40 years the magnitude of which was realized after a change in auditors (Okalie, 2014), Lehman Brothers (2008) where \$50B worth of loans was disguised as sales and the Saytam Scandal (2009) in India which falsified revenues, margins and balances to the tune of 50B Rupees. More recently in 2015 (Pai & Tolleson, 2015), Toshiba was

found to have been involved in accounting fraud where the firm had overstated its earnings by nearly \$2 billion over seven years.

Kenya has also had its fair share of accounting scandals and corporate scandals in the financial sector with Trust Bank (2006), Imperial Bank (2015) which contemplated suing its auditors who had acted since 2003 where the fraud can be initially traced to, Dubai Bank (2015), Haco Tiger Brands (2015) and Chase Bank (2016) that were accused of manipulating earnings. The DTS sub-sector has also been affected with Kitui Teachers SACCO fraudulently loosing Ksh 3 Million in the period 2003–2005, Harambee SACCO (2012) where more than Ksh 350 Million was unaccounted for through falsification of records and Bandari SACCO (2015) where Ksh 5 Million was lost through accounting fraud.

These accounting frauds and corporate failures have brought into question the value and dependability of corporate information and realization to prevent or at the very least, deter future financial scandals, there is need to look more closely at the relationship between companies and their auditors and with legislation and regulations being one of the avenues that has been suggested as a means of restoring confidence in the financial information presented to the different stakeholders ((Mayasangari, 2007).

1.1.1 Audit Tenure

According to Myers, J., Myers, L. and Omert (2003), number of years an organization retains the services of the same auditor is referred to as audit tenure with the Sarbanes-Oxley Act (2002) defining mandatory rotation as imposing of a time limit for which an audit firm may offer services to an organization. Auditor rotation may exist at partner level where the lead partner is or periodic audit firm replacement.

Such change can either be mandatory as required by legislation through change imposition on firms (Arel, Brody & Pany, 2005) or voluntary (Firth, 2010) as determined by management decision and choice with no consideration to the period of time the auditor has served (Davidson, Jiraporn, & DaDalt, 2005).

Mandatory auditor rotation (MAR) enthusiasts offer that a long audit tenure, compromises objectivity and increases auditor bias (Sori & Karbhari, 2005), compromises the auditor's ability to perform at the highest level (Hamilton, Stokes, & Taylor, 2005) and threatens auditors independence as familiarity and self-interest increases (Mautz & Sharaf, 1961), while a shortened audit tenure improves audit quality as audit firms know their work will be reviewed by other firms or partners (Davis, Soo, & Trompeter, 2009), increases independence and objectivity (Gosh & Moon, 2005), enhances auditors perceived reputation (Hussey & Lan, 2001) and increases an audit firms engagement effort due to additional effort to acquire knowledge in the first year of engagement due to more interaction with management (Bedard & Johnstone, 2010). A new auditor is also perceived to provide a fresh look (Chi, Huang, Liao, & Xie, 2009) and is less susceptible to agreeing with managers on financial issues deemed critical (Ryan *et al.*, 2001).

MAR dissenters alternatively pose that a voluntary rotation un-masks accounting issues that are specific to an organization (Johnson & Lys, 1990), increases transaction costs (Shafie, Yusof, & Hussain, 2004), reduces auditor reliance on management through extensive company knowledge gained over a long period of time thereby increasing auditor independence (Solomon, Shields, & Whittington, 1999), can create a disincentive to acquire firm or industry specific expertise as audit firms are unable to create or target a specific niche market (Lu & Sivaramakrishnan, 2010), restricts organizations auditor choice and may force them to settle for firms

with no prior industry expertise (Ernst and Young, 2011), might increase the cost of information as the investor may not be able to distinguish between voluntary and MAR (Bigus & Zimmermann, 2007), long audit tenure increases an auditors understanding of the firms systems and internal controls (Zawawi, 2007), leads to a loss of previously accumulated client-specific knowledge (Firth, 2012) and new auditors require time to acquire sufficient understanding of the business they intend to audit (Fairchild, 2008).

In Kenya, Section 54, on the appointment of external auditors, sub-section (6) the SACCO Societies Act CAP 490b, addresses the issue of audit tenure where it requires that external auditors be rotated every three years except with leave of the authority upon written request in which this requirement may be waived.

1.1.2 Earnings Management

Schipper (1989) expresses Earnings Management (EM) as managerial intentional intervention on an organizations corporate financial reporting process with the purpose of gaining privately. Okolie (2014) indicates that managers with pre-set targets employ this strategy by taking deliberate steps to attain preferred earnings level (Davidson *et al.*, 2005) through a manager's discretion in financial reporting and transactional restructuring with the intention of providing misleading information on organizational performance to shareholders or with the desire of influencing financial information dependent contractual obligations (Healy & Wahlen, 1999).

Earnings management techniques commonly recognized include: (i) Real EM where an organizations economic reality is distorted through the modification of managerial actions which in turn influences information disclosed to external users (Roychowdhury, 2006) and (ii) Accrual manipulation (Schipper, 1989) which

provides an opportunity for accruals with management exercising discretion over discretionary accruals only (Healy, 1985).

According to Xie, Davidson, and DaDalt (2003), the accrual basis of accounting accords managers with greater latitudes of discretion in determining the earnings of organizations with discretionary accruals being the largest and most important accruals for companies (Francis & Dechow, 2008) due to the opportunities to manipulate earnings and flexibilities it provides to managers (Dechow, Sloan, & Sweeney, 1995). The amount of discretion in accruals provides a measure of EM (Mensing, 2013).

1.1.3 Audit Tenure and Earnings Management

Audit provides an effective control over managers resolutions that veer off from interests of shareholders thereby limiting their opportunity to abuse their discretion over earnings (Jiraporn, Miller, Yoon, & Kim, 2008). The audit function is viewed as a mechanism to reduce to reduce risks, develop management's decision making (Wallace, 1980) and increases access to new information considering the limited access to internal information by shareholders and investors by reporting on whether financial information prepared by managers represent a true and fair view (Rohaida, 2011). External audit therefore has been used as monitoring tool with the intention of reducing incentives and available to manipulate reported earnings.

The primary role of the external audit is to form an independent opinion on the management's assertions presented in the annual financial reports (Bamahros, 2015), with the process aimed at determining whether earnings truly reflect the correct position of a firms operations (Chen, Lin, C., & Lin, Y., 2008) leading to a high quality of financial information presented, lowered earnings manipulation activities

by managers (Habbash, 2010) and provides stakeholders with an assurance on the reliability of information provided by managers (Rohaida, 2011).

With the perception of financial statements as a joint work-product involving management along with external auditors as both are deemed to determine the quality of financial reporting (Hamilton *et al.*, 2005), more reporting flexibility is likely to be gained by management with increased duration of this auditor-client relationship as a prolonged tenure may impair the independence of an auditor, enabling managements manipulation (Davis *et.al.*, 2000).

The amount of time and effort required by an auditor to understand a client's business reduces the effectiveness of an audit process fosters opportunities for managers to smoothen earnings (Geiger & Raghunandan, 2002) with the newly engaged auditor being heavily reliant on information presented by management and especially in the formative years as they try to gain a footing on the clients operations which hinders their ability to ascertain earnings management (Gul, Fung, & Jaggi, 2009). As audit tenure lengthens and increased business understanding is progressively attained, there is reduced reliance by auditors on estimates provided by management (Mayangsari, 2007). The acquisition of knowledge that is specific to the organization being audited over a longer period leads to lesser manipulative opportunities and an enhances the value of information presented (Myers *et al.*, 2003).

Auditor tenure constrictions are pre-supposed on the assumption that a protracted relationship lessens an auditor's independence in undertaking their oversight roles due to the anticipated alignment to the client's management making them complicit to or unaware of their indiscretions (Mayangsari, 2007). Regulators have therefore become increasingly concerned that a firm's choice of their basis of accounting and how they

report financial information faces the risk of being compromised by an extended relationship and have suggested MAR as a means of maintaining impartiality and re-assessment of audit effectiveness (Sajadi, Farazmand, & Ghorbani, 2012) with the aim of protecting shareholders' interests and mitigating potential conflicts of interest arising from the shareholders-managers relationship (Habbash, 2010). This has been carried out through the introduction of legislative proposals and regulatory changes which address the degree to which the auditor-client relationship span strengthens or prohibits the quality of information, this is aimed at producing higher quality earnings (Mayangsari, 2007).

1.1.4 Deposit Taking SACCO's in Nairobi County

The context of cooperatives sector in Kenya consists of primary SACCO's made up of marketing societies, farming societies, housing societies, consumer societies, producer society and financial societies (Odido, 2008) with the two main types being either being financial or non-financial cooperatives. Financial cooperatives comprise of DTS's that provide basic 'banking services' besides the basic savings and credit products and non-deposit taking Sacco Societies (Njihia & Muturi, 2015).

According to the 2016 Financial Access Household Survey, 75.3% of Kenyans were financially included in such formal institutions, with 3%, 9.1%, 67.5% and 20.4 of the population accessing SACCO's financial services daily, weekly, monthly and less than once a month respectively. It is estimated that the usage of SACCO's as a financial provider has consistently risen over the years from 13.1% (2006) although the sector experienced a dip in 2009 at 9% however this later picked with 11% in 2013 to peak at 12.9% usage in 2015. As at the end of 2015, 7.7% of Kenyans rated

SACCO's as third among the most trusted financial providers after commercial banks and micro-finance institutions.

Most SACCO's to be found in Nairobi County are formed by salaried formal sector employees where periodic contributions and loan repayments are withheld from salaries and transmitted to the Society (Kattambo, 1992). The survey also shows that Nairobi County, at 70% had the highest access to formally regulated financial institutions with 41 DTS's Licensed by SASRA for the period ending December 2016.

The Sacco Societies Act of the Laws of Kenya has mandated the regulation Sacco audits under Section 25 (3) to SASRA and require cooperative societies to audit their accounts once in every financial year by an auditor appointed under sub section (4). These auditors are appointed at the AGM from a list of auditors approved by the Commissioner in consultation with ICPAK. Additionally, the SACCO Societies Act CAP 490b, Section 54 requires SACCO's to recommend three names to the AGM which selects one Auditor to Audit its accounts in accordance with section 45 of the ACT.

1.2 Research Problem

In a survey carried out by Ernst and Young (2015) in Kenya on financial managers, results indicated that 41% of interviewees indicated that a majority companies of Kenyan companies managed earnings to report improved performances with 23% reporting having modified their firm's financial statements and over 150 interviews justifying the need for financial misstatement with more willing to manipulate financial information. As a result of the increasing accounting scandals in Kenya and faced with increasing demand to curb financial reporting misrepresentation, Kenyan

regulatory authorities have responded with new laws while at the same time strengthening existing ones (Wamwea & Kaboyo, 2014) with regulators continuously coming up with guidelines that enable pragmatic financial reporting (Okoye, 2002) through the reduction of information opaqueness, enhancing an auditors objectivity and enabling the greater protection of their interests by ensuring managers are not conflicted in the responsibilities to shareholders, thereby raising the level of confidence that stakeholders have in markets (Leuz, Nanda, & Wysocki, 2003).

Majority of studies conducted on audit tenure, mandatory auditor rotation and earnings management have looked at their effect on the independence and objectivity of Auditors and the extent to which tenure allows management the opportunity to use discretionary accruals. A review of the available studies indicates that while considerable attention has been given to EM in Kenya, this have been mainly in the context of corporate governance. AT, MAR and its relationship with EM remains a relatively unstudied area and the study sought to fill the research gap by examining the relationship between AT, MAR and EM with a focus on the DTS's in Nairobi County.

The question can be posed; with the recent Kenyan financial scandals where auditors had not raised any anomalies prior to the distress or collapse of some of these organizations and especially where auditors had served for long periods of time while putting into consideration the SACCO act requirement on auditor tenure; Does limiting audit tenure and implementing MAR as required by the Societies Act CAP 490b influence EM practices of DTS in Nairobi County.

1.3 Research Objectives

The study explores the relationship between audit tenure and earnings management of DTS's in Nairobi County.

1.4 Value of the Study

With the increasingly challenging economic environment and the increased pressure by shareholders for unrealistic results, EM has played a crucial role in defining the financial performance of organizations and related quality and reliability of financial information. Despite the critical role played by accounting estimates in determining organization performance having been established (Lee & Kwan, 2016), majority of the studies have contributed to the debate on AT and MAR by examining the audit tenure and quality association (Geiger & Raghunandan, 2002).

A review of the available studies indicates that while considerable attention has been given to EM in Kenya, this have been mainly in the context of corporate governance therefore, there exists scant observational information to show audit tenure and quality association from the perspective of EM and as far as the researcher could determine, the study was the first to look at the association in the context of DTS's in Nairobi County. The study sought to provide critical information for regulatory authorities, firm managers and users of financial information on the association between AT, MAR on EM and contribute to the earnings management literature.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

In this chapter, literature on EM, it's Kenyan Concept and audit tenure and auditor rotation will be introduced. This will give an overview of audit tenure, EM and then introduce the relationship between audit tenure and EM. There will be a subsequent review of the various theories and models alongside empirical studies that have previously been conducted on audit tenure and EM.

2.2 Theoretical Review

Agency and Stakeholder theories were utilized in the review of the association between AT, MAR and EM of DTS's in Nairobi County using discretionary accruals measure of EM as a proxy.

2.2.1 Agency Theory

Ownership of Sacco's is through shares where a share represents a unit of ownership that entitles the holder to partial ownership, becoming the principal. In turn, the members delegate the running of the Sacco to a management board as elected in their annual general as their agent (Alchian & Demsetz, 1972). Managers so appointed are then presumed to achieve the principal's best interests in the execution of their functions (Odera, 2012). According to Berle and Means (1932), managers may depart from maximizing shareholder returns with agency theory positing that where, due to the differing goals, managers are not acting in the shareholders best interests, this could lead to potential conflicts (Jensen & Meckling, 1976)

Agency results in information skewness where agents possess a greater deal of information comparative to the principals' which hinders their capacity to effectively monitor the maximization of their interests by the appointed agents (Farouk & Hassan, 2014) a condition which enhances earnings smoothing opportunism (Trueman & Titman, 1988). A high degree of information imbalance hinders shareholders ability to oversee managers which enables EM thus obscuring the real performance of a firm leading to agency costs. (Jiraporn *et al.*, 2003). To correct for opportunistic behavior brought by information asymmetry, this theory has a focus on accountability (Jensen & Meckling, 1976). Due to this information asymmetry, audit is critical to the principal-agent relationship in lowering information unevenness through the empirical confirmation of financial statements and mitigating conflicts arising out of agency relationships (Farouk & Hassan, 2014).

Agency problem creates demand for external audit services critical in monitoring and correction of information asymmetry through confirmation of the validity of information carried in the financial statements (Eilifsen, Messier, Glover, & Prawitt, 2010) where there is utility maximization by managers to protect their interests through external audits (Eilifsen & Messier, 2000) with auditors also acting as agents to maximize utility on behalf of the principals (Antle, 1982) through the assessment of financial information validity (Agunda, 2014). As indicated by Dechow, Sloan and Sweeney (1995), audit as a monitoring system reduces the opportunistic behavior of managers, lessens information inequality and ensures that managers put the shareholder interests at the forefront of their activities (Mills, 2009). Audit also increases the quality and reliability of reported earnings buy reflect a firm's fair financial performance (Gerayli, Yanesari, & Ma'atoofi, 2011).

2.2.2 Stakeholder Theory

Closely related to agency theory is the stakeholder theory which describes stakeholders as those directly or indirectly affected through an organizations activity in its quest to achieve its purpose and who are critical in activities success and its survival (Freeman, 1984). Stakeholders can be described as customers, suppliers, employees and everyone that can impress upon or be influenced by the company's activities (Freeman, 2002) including governments and their agencies (Kiel & Nicholson, 2003). A firm's responsibility is not only to their shareholders bit also to the society in which it resides and operates (McDonald & Puxty, 1979) which is made up of diverse stakeholders with varying degrees of expectation and need for satisfaction that every firm must work towards achieving (Abrams, 1951). Managers must strive to make decisions and work towards satisfying all direct or indirect stakeholders (Donaldson & Preston, 1995)

Demand for audit is created by managers desire to advance their interests or those of select stakeholders at the expenses of others and through earnings management (Hodge, 2006). Auditors are expected to play a monitoring role that is focused on protecting the interest of all stakeholders with an expectation that this will reduce the levels at which information is misreported thereby ensuring that stake holders need for accurate and reliable information is met (Palmrose, 1988).

2.3 Determinants of Earnings Management

Since independence, the Sacco movement in Kenya did not attract much interest from the regulatory authority with the Cooperative Societies Act (Cap 490) being the main legal framework. However, the rapid expansion in DTS's saw an increased interest by the regulatory authorities with passing of the Sacco Societies Act in 2010 and further

regulations with the Sacco Societies (Amendment) Bill, 2016 being tabled in parliament that seeks to further strengthen governance and management system. Chen, Li, Liang and Wang (1991) indicated that the sustained presence of the governments attention can be deemed to be political costs and provides motivation to manage earnings to counter these regulations in periods of sustained government attention (Watts & Zimmerman, 1986).

According to Rezaee (2011), alignment of managements and shareholders' interests can be achieved through corporate governance with the effect of increasing shareholder value creation while also protecting stakeholder interests with Charreaux (1997) adding that corporate governance plays a monitoring role that dissuades managers opportunistic behavior. The lack of such corporate governance would therefore tempt managers to smoothen organizational earnings.

Different studies have also identified varied incentives to manipulate earnings and can either be shareholder value maximization or self-interest maximization (Mehrani, 2009) including; Bonus compensation (Healy, 1985), elude violations of debt covenants (DeFond & Jiambalvo, 1994), desire to maintain high levels of earnings (Bugstahler & Dichev, 1997), regulatory or political costs (Jones, 1991); opportunity provided in the accrual method of accounting that allows managerial discretion; (Watts & Zimmerman, 2006), financial or social pressure to meet earnings forecasts (Murphy & Dacin, 2011), financial distress of the company (Healy & Wahlen, 1999), reduction of tax expenses imposed on earnings (Burgstahler & Dichev, 1997); normalization of earnings management in the organizational culture (Rockness & Rockness, 2005), improperly designed government regulatory systems (Rosenfield, 2000) while legislative changes and investor protection requirements also affecting earnings management (Cohen, Dey, & Lys, 2008).

2.4 Empirical Studies

Discretionary accruals have been used in most of the studies that have proxied earnings management in the examination of how this is affected by audit term in relation to their reported quality (Johnson, Khurana, & Reynolds, 2002) with results of these studies indicating that quality of earnings is low when a short audit tenure is associated compared to medium tenures however these studies also report that comparing medium and long tenures, no difference exists in earnings quality.

Longer audit tenure has been found to enable the use of discretionary accruals to manage income in a study by Davis *et al.*, (2000) supported by DeFond and Subramanyam (1998) which found out that before a change of auditor is affected and where previously prudential accounting was used, there is a reduction of elective accruals in the year preceding the change. Similarly, studies that find no association between EM and term include; with other studies report significant negative relationship between auditor tenure and EM; Reichelt and Wang (2010); Frankel, Johnson and Nelson (2002).

Davidson *et al.*, (2005), in a study of North America used the modified Jones (1991) model to examine firms that had changed auditors over the period 1993-1997 to identify 1,132 auditor changes. The study finding no evidence of EM after the auditor change neither did EM increase. The findings mirrored those of DeFond and Subramanyam (1998) who did not find any indication of EM in companies that had gone through an auditor change this was in contrast with Kramer, Georgakopoulos, Sotiropoulos and Vasileiou (2011) who in a similar study covering the period 1980 –

2006 and a sample of 460 auditor changes finding a potential positive effect on prudential accounting and earnings quality.

In a Zgarni, Hlioui and Zehri (2012) inquiry of the Tunisian BVMT following passing of financial legislations, which looked at 319 firm year observations for the period 2000-2010 and employing regression analysis to test tenure and its relation to accruals based earnings manipulation to test EM theory using the modified Jones (1991) model found no relationship between audit tenure accruals-based earnings management and that regulation did not affect the degree to which firms managed their revenues.

Mensing (2013) examined how the quality of earnings in the UK is influenced by changes in auditor o using the amount of absolute discretionary accruals in audited financial statements as a proxy through secondary data published in accounting reports of the sample companies of a sample of 240 of which 25 firms registered and auditor change in the specified period (2006 to 2011). Using the modified Jones Model (Kothari, Leone, & Wasley, 2005) and multiple regression analysis, the study concluded that EM does not increase after an auditor change however, under specific instances for example after a change from audit firms within to those outside of the listed biggest six audit firms as a result of a modified audit opinion, this has an effect on EM and thus on earnings quality of reported results with total accruals for financial institutions increasing at the end of audit term.

In a Nigerian study by Okalie (2014) of the quoted stock exchange non-financial firms within the 2006 – 2011-time frame and specifically looking at 57 companies tested the audit tenure and quality association using discretionary accruals as an EM measure. Using linear regression to examine this relationship, the results indicated

that audit quality as proxied by tenure had a significant and negative relationship with discretionary accruals.

Various studies have been done in Kenya on EM and most of these have been on their relationship to the concept of regulation and corporate governance among publicly listed companies including; Njogu, Mouni, Waititu and Omido (2014) carried out a descriptive study of nine Manufacturing firms quoted in the Nairobi stock exchange and seeking to establish the effect of executive compensation, an incentive for earnings management (Healy, 1995) and how this informs their creative accounting practices. 104 top managers and board of directors formed the population and using regression analysis, the results provided evidence of a significantly positive and significant influence of executive compensation on creative accounting practices.

Mirie, Iraya, and Muchoki (2015) examined the influence corporate governance on earnings management as proxied by discretionary on 49 firms listed in the Nairobi Stock Exchange for the period between January 2010 and December 2012. The study used secondary quantitative data employing a descriptive research design and linear regression to analyze data. Results indicated a negative association among earnings management and corporate governance ownership concentration, board size and independence variables but positively related to board activity and CEO duality.

Kamau, Namusonge and Bichanga (2015) carried out a study on firms listed in the Nairobi Stock Exchange using manager's compensation, contractual obligations, tax management, Share price performance management and insider dealings (Amat & Gowthorpe, 2004) as proxies for management's incentives to manage earnings. The study used the cross-sectional survey design and Systematic sampling method yielded thirty-nine of a population of sixty-four Companies publicly listed in the Nairobi

Securities Exchange for the year 2014 and using regression analysis, the results indicated a significant level of influence that incentives have on EM.

There exist no identifiable research studies on AT, MAR and EM among DTS's in Kenya and which informed the investigation with a view of filling this gap.

2.5 Conceptual Framework

The investigations conceptual framework has been developed to examine the influence of audit tenure on earnings management. In this framework, audit tenure is the independent variable with discretionary accruals being the dependent variable. Discretionary accruals will be used as proxies for EM and control variables will include; return on assets, firm growth, size, age and cashflows.

2.5.1 Audit tenure and earnings management

Davis *et al* (2000) posited that the production of financial statements is a joint effort comprising of managers and auditors and the existing relationship length determines the level of managements reporting flexibility due to an auditors impaired independence hence facilitating the opportunity to extensively manage earnings. On the other hand, Mayasangari (2007) argued that an increased tenure enables an auditor to gain industry and client specific knowledge and hence places lesser reliance on management which increases the quality of financial information presented as the auditor gains more specific knowledge thereby lessening earnings management severity. The law has been used as a means of achieving and enhancing auditor independence through mandatory auditor rotation through enactment of laws aimed at limiting the extent of the length of relationship between auditor-client and thereby limiting earnings management (Mayasangari, 2007).

As this study aims to establish how length of audit tenure impacts on the level of earnings management for DTS's in Nairobi County and in view of the term limit imposed by SASRA, the following hypothesis can be constructed.

H₁: The length of audit firm tenure positively affects the earnings management of DTS's in Nairobi County.

This study has included the control variables of return on assets, growth, size, age and cash flows to ensure that the found audit tenure and earnings management association is not influenced by other factors and therefore enhancing the accuracy of the dependent variable.

2.5.2 Return on Assets and earnings management

To gain further comprehension of how audit tenure influences earnings management, a study by Reichelt and Wang (2003) encompassed return on assets as a control variable. Earnings can be manipulated through forfeiture of future revenues in return for a positive outcome of current financial reporting through with a focus on operational activities (Gunny, 2010). The study approached return on assets with the view that small firms are expected to have low returns on assets and therefore would have an incentive to manager their earnings comparative to larger firms and the following hypothesis developed.

H₂: Return on assets positively affects earnings management of DTS's in Nairobi County.

2.5.3 Firm growth and earnings management

With ever increasing competition to attract more shareholders and grow the business, Managers are faced with an increasing pressure to present more favorable financial statements. Skinner and Sloan (2002) argued that higher growth organizations have greater incentives to meet earnings targets through using aggressive means and will highly engage in earnings management where younger firms have higher chances of managing earnings due to the additional pressure faced in meeting high growth targets that they face from shareholders (Erickson, Hanlon, & Maydew, 2006).

H₃: There is a negative relationship between the growth of a DTS and its earnings management

2.5.4 Firm size and earnings management

Studies on firm size show that the earnings management practices of large firms are decreased as these are audited by large audit companies, have a larger fear of the loss of reputation in comparison to smaller firms and the existence of internal audit functions limits the EM initiatives (Llukani, 2013) however large firms also suffer more pressure from investors and to meet these high expectations, they will guide earnings more as to the smaller sized firms (Barton & Simko, 2002) while the smaller firms fearing reporting losses have higher chances of managing their earnings than larger firms who face increased scrutiny and provide a vast amount of information lowering the level of information asymmetry and probability that they will manage their earnings (Lee & Choi, 2002).

H₄: There is a significant relationship between firm size and earnings management of DTS's in Nairobi County.

2.5.5 Firm age and earnings management

Bassiouny, Soliman and Ragab (2016) posed that longer term operating firms gain a favorable reputation, protect their value and reputation and are more aware of the regulatory requirements that govern their practices and tend to have low levels of earnings management. A longer operating history has also the effect of lowering the information skewness as their firms are likely to have over the years provided more information to the shareholders (Chiraz & Anis, 2013).

H₅: The age of a DTS has a positive relationship with earnings management

2.5.6 Firm cash flows and earnings management

This involves the use of operating decisions that influence cashflows to reach desired level of earnings (Healy & Wahlen, 1999) through managements departure from normal operating practices to achieve their self-interests (Roychowdhury, 2006).

H₆: The cash flows of a DTS has a positive relationship between firm size and earnings management.

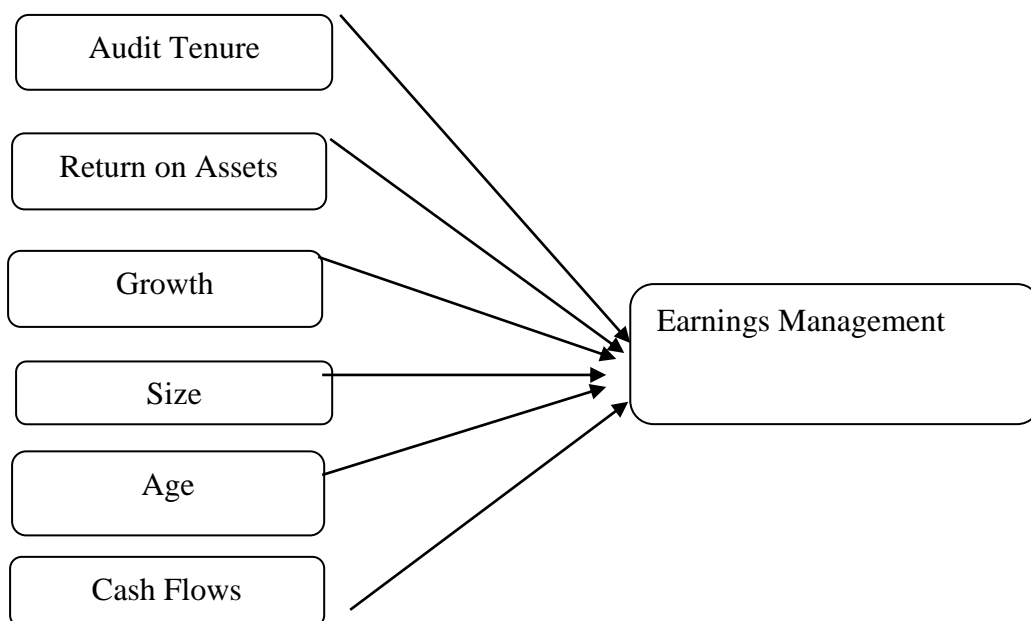


Figure 1: The conceptual framework between audit tenure and earnings management.

2.6 Summary of Literature Review

This chapter starts by providing an overview of audit tenure, EM and reviews discretionary accruals as a proxy of EM. Further review of empirical evidence has been done on audit tenure, auditor rotation and the theories aligned including the agency and stakeholder theory and their relationship with EM. A conceptual framework for the study was then established supported by the literature review,

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter describes the study's comprehensive research methodology (Dawson, 2009), the methods applied in carrying out the study (Zikmund, Babin, Carr, & Griffin, 2010) to achieve its objectives and outlines the research design, population covered under the study, sample design used, data collection, data validity and reliability, data analysis and model specifications.

3.2 Research Design

The design utilized by the study was descriptive and was achieved through data collection to test the hypothesis developed (Mugenda & Mugenda, 2003). The main purpose was to describe the existing. (Kothari, 2004). It employed the two-stage cross-sectional design where the results of one stage was employed in the next stage to generate the results of the study. Quantifiable data was collected on 41 DTS's over a 5-year period relating to the variables identified which was then analyzed to identify associated patterns (Bryman & Bell, 2007).

3.3 Population

The study encompassed Sacco's with common observable characteristics of being deposit taking and operating or being domiciled in the county of Nairobi. It consisted of the 41 DTS's licensed under the Sacco Societies Act (Cap 490B) to carry out deposit taking business in Nairobi County for the period ended December 2016. Conclusions to the study were then developed from the cumulation of these DTS's (Cooper & Schindler, 2003)

3.4 Sample Design

The study used census survey due to the relatively low number of DTS's licensed to operate in Nairobi County for the period of the study. Data was readily available from SASRA for all 41 DTS's with all of them being included as part of the study and conclusions drawn as to the population that was the target of the study (Mugenda & Mugenda, 2003).

3.5 Data Collection

This study used readily available secondary data obtained by abstraction from the SACCOs' audited financial reports of DTS's for the period 2012-2016 under study and key financial information on the variables of concern discerned from these reports.

3.6 Data Validity and Reliability

Using the Modified Jones Model enhanced reliability of the study as the model is an already tested research design across various sectors. This model has also been used in majority of studies about discretionary accruals as proxies for earnings management which confirms its validity (Bjurman and Weihagen 2013).

According to legal and regulatory provisions spelt out in acts of law, DTS's are required to provide their audited financial reports for approval by SASRA and it's from these approved reports where all the necessary data for the study was stated and acquired. Reliability was enhanced further by removing the effect of small Sacco's, through choosing DTS's with asset bases of KES 1 Billion and above.

3.7 Data Analysis

The research study area has consistently used the Modified Jones (1991) Model with its ability and accuracy in designating accruals into discretionary and non-discretionary and role in increasing. Studies have employed various modifications to the original Jones (1991) Model including; Healy (1985); DeAngelo (1986); Kothari, Leone and Wasley (2005) however, this study employs the Dechow et al. (1995) which with its ability to handle large data sets, has been proven to provide the more accurate measures.

3.7.1 Specification of the Model

The dependent variable of the study was EM as proxied by Discretionary Accruals Equation 1; The first step involved the computation of the total accruals using the cash flow approach which offers more accuracy as opposed to the balance sheet approach (Collins & Hribar, 1999)

$$TA_{it} = \text{Net Income}_{i,t} - \text{Cashflow from Operations}_{i,t} \quad (1)$$

Step 2 involved computation of non-discretionary accruals;

$$NDA_{it} = \alpha_{1i} \frac{1}{A_{it-1}} + \alpha_{2i} \frac{\Delta REV_{it} - \Delta AR_{it}}{A_{it-1}} + \alpha_{3i} \frac{PPE_{it}}{A_{it-1}} \quad 2)$$

Step 3 calculated discretionary accruals using the Modified Jones (1991) Model as developed by Dechow et al. (1995).

$$DA_{it} = \frac{TA_{it}}{A_{it-1}} - NDA_{it} \quad (3)$$

Where:

TA_t = total accruals for firm i in year t

A_{t-1} = total assets for firm i in year $t-1$

ΔREV_t = revenues for firm i in year t minus revenues for firm i in year $t-1$

ΔAR_{it} = accounts receivable for firm i in year t minus accounts receivable for firm i in year $t-1$

PPE_{it} = gross property, plant and equipment for firm i in year t

t = year index, ranging from 2012 to 2016

I = DTS index, ranging from 1 to 41

α = regression coefficients in the estimation period

Earnings Management as proxied by discretionary accruals was the identified dependent variable in each financial year of the study and to measure how it was potentially impacted by audit tenure, the association was tested using linear regression analysis allowing for control variables of audit period, DTS growth, age and size, net cash flows and change in period were then be used to ensure that associations between the variables were not caused by other factors thereby increasing the accuracy of the dependent variable.

$$DA_{i,t} = \alpha + \beta_0 AT + \beta_1 ROA + \beta_2 GROW + \beta_3 SIZE + \beta_4 AGE + \beta_5 CFO + \varepsilon \quad (4)$$

Where;

AT = represents the length of auditor-client relationship: '1' if 3 years or less & '0' if otherwise

ROA = Net Income scaled by average total assets at the end of year t

$GROW$ = growth rate of revenue over the previous year.

Firm size = this is defined as the natural logarithm of the total assets of the firm.

Firm Age = It is the age of the firm since its establishment.

CFO = Cashflow from Operating activities scaled by the value of total assets at the end of year t (CFO/TA)

CHAPTER FOUR

DATA ANALYSIS, PRESENTATION AND DISCUSSIONS

4.2 Introduction

This chapter focuses on data analysis, presentation and interpretation. Using descriptive statistics, it presents the research findings on the main objective of the study which was to examine the audit tenure and earnings management association in reference to deposit taking SACCOs in Nairobi County for period 2012-2016.

4.2 Response Rate

Data was readily available from audited financial statements of all DTS's for the period of study 2012-2016 thereby creating a response rate of 100% that was deemed satisfactory for the purposes of drawing conclusions to the study.

4.3 Data Validity

According to the Sacco Societies Act and Regulations (2010) DTS's are required to provide their audited financial reports for approval by SASRA and it's from these approved reports where all the necessary data for the study was stated and acquired.

4.4 Descriptive Statistics

The study considered Mean, Median, Minimum, Maximum and Standard Deviation with the aim of establishing the relationship between earnings management because of the audit tenure variables under the study from 2012-2016 i.e. audit tenure, return on assets, growth, Firm size, Firm age, and cashflows. Their mean, median, maximum, minimum, skewness and kurtosis.

Table 4.1: Descriptive Statistics Results

	DA	AT	ROA	AGE	GROW	SIZE	CFO
N Valid	205	205	205	205	205	205	205
Mean	.0026	1.000	.0226	36.1707	.1996	21.4377	.0162
Median	.0022	1.000	.0177	39.0000	.1793	21.2138	.0129
Std. Deviation	.0705	.0000	.0306	9.2379	.23615	1.1655	.0586
Range	.525	.000	.417	43.000	2.433	5.871	.384
Minimum	-.222	1.000	-.060	11.000	-.787	18.474	-.155
Maximum	.302	1.000	.357	54.000	1.646	24.345	.229

Table 4.1 presents the primary characteristics of the quantitative data collected as summarized by the descriptive statistics Hair *et al.*, (2003) for DA as a proxy for earnings management and independent variables; *ROA*, *GROW*, *SIZE*, *AGE* and *CFO* as derived from the sample of DTS's for the period 2012 – 2016.

The results further show; Discretionary accruals mean is equal to 0.0026, a minimum of -0.222, maximum of 0.302 and a standard deviation .0705. AT had a mean of 1.00 with a minimum of 1.00, a maximum of 1.00 and standard deviation of 0.000. The average ROA was .0226, a minimum of -.060, maximum of .357, and standard deviation of .0306. In comparison, AGE had a mean of 36.1707, a minimum of -11.000 with a maximum of 54.000, and standard deviation of 9.2379. The mean of GROW was .1996, with the minimum being -.787, maximum of 1.646, and standard deviation of .23615. SIZE of the DTS's on the other hand averaged at 21.4377, minimum of 18.474, the maximum being 24.345 with a standard deviation of 1.1655. Lastly, CFO's had a mean of .0162, a minimum of -.155 with a maximum of 0.229, and fluctuations from the mean estimated at 0.0586

4.5 Correlation Analysis

The study sought to investigate the relationship between audit tenure and earnings management of deposit taking SACCO's in Nairobi County. To check how the dependent, independent and control variables were related, Pearson Correlation analysis was used at 95% and 99% confidence levels.

Table 4.2: Correlation Analysis

		DA	AT	ROA	AGE	GROW	SIZE	CFO
DA	Pearson Correlation	1	. ^a					
	Sig. (2-tailed)		.					
AT	Pearson Correlation	. ^a	. ^a					
	Sig. (2-tailed)	.	.					
ROA	Pearson Correlation	.232**	. ^a	1				
	Sig. (2-tailed)	.001	.					
AGE	Pearson Correlation	.014	. ^a	-.105	1			
	Sig. (2-tailed)	.848	.	.135				
GROW	Pearson Correlation	-.065	. ^a	.014	-.242**	1		
	Sig. (2-tailed)	.358	.	.839	.000			
SIZE	Pearson Correlation	-.047	. ^a	-.100	.273**	-.008	1	
	Sig. (2-tailed)	.507	.	.155	.000	.914		
CFO	Pearson Correlation	-.882**	. ^a	.209**	-.056	-.002	.005	1
	Sig. (2-tailed)	.000	.	.003	.428	.973	.949	

** . Correlation is significant at the 0.01 level (2-tailed).

a. Cannot be computed because at least one of the variables is constant.

The correlation analysis enabled the testing of study's hypothesis that audit tenure influences earnings management. Results in Table 4.2 show that there was no relationship between Discretionary Accruals and audit tenure however there existed a significant positive relationship between discretionary accruals and; ROA (R =0.232, P=<0.001) and negative relationship with; CFO (R = -0.882 p < 0.001). Insignificant

relationships existed at AGE ($R = 0.14, p > 0.001$) GROW ($R = -0.065, p > 0.001$) and SIZE ($R = -0.47, p > 0.001$)

4.6 Regression Analysis and Hypothesis Testing

Linear regression was used to measure the relationship between audit tenure and earnings management. The regression model's data match expectation was determined using overall correlation and the coefficient of determination between the independent variables and discretionary accruals.

4.6.1 Model Summary

Table 4.3 presents a correlation coefficient of 0.981 and determination coefficients of 0.963. This depicts a strong relationship between the dependent and independent variables with 96.3% of ROA, AGE, GROW, SIZE and CFO being attributable to the variations in earnings management as proxied by discretionary accruals

Table 4.3: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.981 ^a	.963	.962	.013698	2.193

a. Predictors: (Constant), CFO, GROW, SIZE, ROA, AGE

b. Dependent Variable: DA

Auto correlation between the model's residuals were checked using the Durbin Watson (DW) test with a score of 2.193, this being close to 2.0, It can thus, be concluded that there was no autocorrelation among the variables.

4.6.2 Analysis of Variance

To test the significance of relation exists between variables, ANOVA was applied Table 4.4 shows that the probability related to the F statistic ($p < 0.001$) showing the models significance level at 99%

Table 4.4: ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.977	5	.195	1041.146	.000 ^b
	Residual	.037	199	.000		
	Total	1.014	204			

a. Dependent Variable: DA

b. Predictors: (Constant), CFO, GROW, SIZE, ROA, AGE

4.6.3 Regression Coefficients

Table 4.5: Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.002	.018		.086	.932
	ROA	1.003	.032	.435	31.009	.000
	AGE	.000	.000	-.015	-1.018	.310
	GROW	-.023	.004	-.077	-5.451	.000
	SIZE	.000	.001	.005	.323	.747
	CFO	-1.170	.017	-.973	-69.879	.000

a. Dependent Variable: DA

Table 4.5 shows that the regression coefficients of independent variables establishing the regression model;

$$DA = 1.003*ROA - 0.023*GROW - 1.170*CFO$$

The findings show that the coefficient of Discretionary accruals is positive which

would indicate that holding AT, ROA, GROW, SIZE, AGE, CFO constant, earnings management of deposit taking Sacco's will be 0.002

while age of the DTS has no influence on discretionary accruals. As the DTS grows, this results in discretionary accruals decrease by 0.023 with size of the DTS having no influence however, an increase in cashflows as scaled by total assets will occasion a decline in discretionary accruals by 1.170.

4.7 Discussion of Findings

Discretionary accruals has a mean value of 0.0026 which indicates that on average, 0.26% of earnings management of the sampled DTS's have an upward trajectory however this change is not significant as the standard deviation is 0.0705 ($p > 0.001$). This finding compares to studies conducted by Chi et al., (2005); Chen et al., (2008); Menon and Williams (2004); Myers et al., (2003) and shows that deposit taking Sacco's in Nairobi county engage in earnings management however at a significance level of 0.0705 which is greater than 0.001, earnings management by DTS's is considered insignificant, a finding consistent with Bassiouny, Soliman and Ragab (2016).

There is also significant correlation between discretionary accruals and return on assets, the growth of the DTS's, its size age and cashflows as denoted by the P value of 0.000, which is less than 0.001 with 96.3% of the predicting variables triggering a change in the response variable.

The results of the study indicate that audit tenure which represented the number of years the firm had retained the same auditor had a mean of 1.00 with a minimum of 1.000, a maximum of 1.0 and standard deviation of 0.000 this shows that for the 5-

year period 2012 – 2016. This shows that audit tenure has no influence on earnings management further indicating that all DTS's under the study changed auditors at least once. The correlation analysis shows a no relationships between discretionary accruals and audit tenure and the study rejects hypothesis that the length of audit tenure influences earnings management. This contradicts studies that found a negative relation undertaken by De Fond and Subramanyam (1996); Rinalds et al. (2009); Zenginand and Ozkan (2010); Bazrafshan (2010) and Ahmadzade et al (2012). Carcello and Nagy (2004) who found that earnings management mostly occurs within the first three years of the auditor-client relationship while there existed a positive relationship between audit tenure and earnings management as posed by Gul et al. (2010); Chi et al. (2011).

Return on Assets was measured by scaling the net income against average total assets at time=t. results an increase in return on assets will lead to an increase in earnings management by 1.003 and at a significance of level of 0.000 which is less than 0.001, it can be posited that return on assets positively affects discretionary accruals thus the hypothesis that return on assets positively affects the earnings management of DTS's in Nairobi County is be accepted.

GROW was measured revenue growth and was assumed that poorly performing DTS's would have an incentive for earnings management and the hypothesis that there exists a negative relationship between the growth of a DTS and earnings management developed. Results indicate a significant negative relationship of -0.23 at significance level of 0.000 which is less than 0.001 and thus the is accepted. These are inconsistent with (Chen & Lui, 2010) who in their study found an inverse relationship between a firm's growth and its earnings management. However, the findings are inconsistent with Huguet and Gandía (2016)

SIZE in the she study was measured as the natural algorithm of total assets. Results indicate no relationship between SIZE and discretionary accruals and hence the size of a DTS does not influence earnings management, therefore the hypothesis of there being a significant relationship between firm size and earnings management is rejected. The results of the study are consistent with Becker et al. (1998) who did not find any relation between natural logarithm of total assets and earnings management and inconsistent with; Watts and Zimmerman (1980); Kim et al (2003); Krishnan (2003); Forman (2006); Moeinadin, Heirany and Moazen (2013) whose findings showed that size influenced earnings management

AGE of the firm was represented as the period between registration and the end of each financial year. The results indicate no relationship with earnings management this contradicts earlier studies by; Rangan, (1998); Ching, Firth and Rui (2002); Llukani (2013); Debnath (2017), which showed that there was a significant positive relationship between age and earnings management with older firms having high levels of manipulation. Therefore, the hypothesis on the age of a DTS having a positive relationship with earnings management was rejected.

Statistically, there is a significant negative relationship between CFO and earnings management with a coefficient of -1.170 and significance 0.000, ($p=0.000<0.001$) therefore the hypothesis cash flows of a DTS have a positive relationship between firm size and earnings management of DTS's in Nairobi County is rejected. This is consistent with studies conducted by; Roychowdhury (2006) who found out that cashflows have a significant effect on earnings management.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter describes the study's summary findings and discussion, recommendations for further studies on related issues of the current study well as recommendations and limitations addressed by the study.

5.2 Summary of Findings

The intention of the study was to interrogate the linkage between the auditor tenure and level of earnings management practices of deposit taking Sacco's in Nairobi County during the 5-year period between January 2012 and December 2016. Discretionary accruals were used as proxies and measured using the modified Jones model. The study employed a descriptive research design and used multiple regression analysis. The dependent variable was discretionary accruals and audit tenure, return on assets, growth, firm size, firm age and cashflow from operations as the independent variables in defining the relationship that existed among audit tenure and earnings management of deposit taking Sacco's in Nairobi County. The study used secondary data from proxy financial information for the 5-year period with the statistical population consisting of 41 DTS's operating in Nairobi County as Licensed by SASRA.

The study reveals that while DTS's engage in earnings management, there exists no significant relationship between the length of audit tenure-client relationship and earnings management with the only significant relationship being that of return on assets, growth and cashflows.

Deposit taking Sacco's were fully in compliance with Sacco Societies Act (Cap 490B) of the Laws of Kenya which regulates audit of SACCO's under Section 25 (3), that requires DTS's to change their auditors every three years.

5.3 Conclusions

Audit facilitates the monitoring of financial reports as prepared by managers, an enriched process that produces realistic and dependable earnings information by limiting managements opportunism for maximizing earnings. The 5-year period between 2012 – 2016 study was conducted to ascertain the associative nature between audit tenure and extent of earnings management of deposit taking SACCO's in Nairobi County in Nairobi County using discretionary accruals as proxies with the Modified Jones (1991) Model providing a measure. Regression model control measures included; return on assets, growth, size, age and cashflows. The statistical population consisted of 41 DTS's operating in Nairobi County and secondary data collected from SASRA as the regulatory authority. It employed a descriptive research design and re-examined prior research on relations existing among audit tenure and earnings management.

Inferences from the examination indicate insignificant engagement in earnings management by deposit taking Sacco's in Nairobi county showing that managers were keen to optimize shareholder wealth over their own opportunistic rewards. Further results indicated there was full compliance with the regulatory imposition of audit firm 3-year term limit where all firms had changed auditors at least once within a 3-year term which led to the conclusion that earnings management of DTS's could not be related to audit tenure.

For variables age and size of the DTS, the study considered that large firms were under more scrutiny, had a lot more reputation to lose and increased investor pressure therefore had less incentive to manipulate earnings comparative to smaller firms who would be under pressure to report profits. Older firms were also thought to be keener to protect their reputation with appreciation of the regulatory changes over time while having a low level of disproportionate information therefore would be less keen to manage their earnings. However, from the evidence provided, the study was able to conclude that age and size had no impact.

Indicative variables included return on assets, growth of the DTS and cash flows from operating activities. The study showed an increase in earnings management with every increase in ROA. Healthy earnings per share is a means of attracting membership thereby, increase in net income results in increased earnings available to distribute to the membership and therefore provide an incentive for earnings management as supported by the results of the study. Increased membership can also contribute to increased revenue which results of the study indicate that DTS's in Nairobi have grown at an average of 20% over the 5-year period 2012 – 2016 thereby concluding that the DTS's are engaging in less earnings management with increased revenue growth.

The results of the study show that increases in cashflow from operations will lead to a reduction in earnings management concluding that DTS's have increased operational efficiency resulting in higher revenues and profits this can be seen through enhancement of existing income generating activities and revenue collection while bringing on board new income streams including real estate. This increased efficiency can also reduce managers opportunism to divert a firm's resources for their own

personal gain. The study therefore concluded that the increased efficiency lead to reduced earnings management.

5.4 Recommendations

SASRA has a list of 227 authorized auditors as at the end of 2016. Of these, only 7% of these firms were involved in the audit of deposit taking Sacco's with a single audit firm taking in 35% of the work for the period under study. While this results in firms gaining extensive industry specific industry knowledge this may have the effect of restricting firms on their audit firm choices while also providing a one-sided look. DTS's may be encouraged to go outside the pool of existing audit firms to get a perceived fresh look and auditors that are less likely to agree with management.

76% of the DTS's had assets worth KES 1 Billion and above and were audited by small and medium tier audit firms with only 2 DTS's engaging the audit services of firms considered to be the big 4. The results indicate that deposit taking Sacco's in Nairobi county engage in earnings management and with the assumption that large sized DTS's are better placed to hire the big four audit firms who can offer more independence, detection of earnings smoothening stands a higher chance.

Results indicate that only 6% of the audit work was conducted by two of the Big 4 audit firms, 3% by a mid-tier firms and 91% by small firms and especially with previous research posing that the top-4 firms are better placed to identify earnings management practices; DeAngelo (1981); Becker et al., (1998); Krishnan (2003); Okolie (2014). SASRA may want to consider guiding auditor selection by DTS's according to the asset based size classification and revenues generated.

Sacco's are increasingly becoming major players in providing financial access with 35% of the countries national savings being attributable. There is anticipated accelerated growth in the coming 5- 10 years (Oluoch, 2016). With the increasing attractiveness of Sacco's among Kenyans, audit firms should devise measures of determining the quality of earnings as reported and penalties designed for DTS's that are found to be manipulating their earnings to generate membership.

5.5 Limitations of the Study

The consideration of the study comprised a period of 5 years (2012 – 2016) and with DTS's required to change auditors every 3 years beginning the year 2010, there is a possibility of this change may have only happened once within the study period which in turn has resulted in the measure of audit tenure immaterial. A mitigating factor would have been to conduct a study with a larger period and include other audit firm changes, voluntary or mandatory while considering the limitation of the quality and quantity of data available as before 2010, DTS's may not have kept adequate records.

Many other factors have an influence on earnings management including maximization of self-interest (Mehrani, 2009), bonus compensation (Heal, 1985), regulatory or political costs (Jones, 1991), prestige, future promotions, and job security (Xie et al., 2003), contracting motivation and regulations tied to accounting information (Healy and Wahlen, 1999) among other factors and the inability of the study to capture these factors thereby limited the multivariate regression analysis. This study is therefore unable to conclusively demonstrate whether the positive audit tenure and earnings management association of deposit taking SACCO's can only be attributed to audit tenure.

SASRA's legal and regulatory authority was operationalized by the gazettelement of the Sacco Societies Act in the year 2010. This study has looked at a period of 2012 - 2016 and the audit firm tenure is assumed in this study to have commenced in 2011. However according to the authority, DTS's are required to change auditors every 3 years and thus this change in audit firm may have happened 3 years after the operationalization of the ACT and there also exists a possibility that even before the Act, DTS's out of good practice could have been changing or rotating audit firms and this may influence the median results.

5.6 Suggestions for Further Research

The average firm age for DTS's in Nairobi County is 37.5 years and this study focuses only on a 5 – year period between, 2012 – 2016 and there exists an opportunity to conduct research for a longer period and especially using data for the period before and after the imposition of the audit firm tenure, probably 5 years before and after while also widening the net to capture DTS's within the nationwide context. This can also help in providing an understanding of the levels of earnings management before audit tenure limitations and the effect such limitations have had on the levels.

Audit terms that span a long period of time have been shown to allow auditors to acquire more industry specific knowledge and there by relying less on management, increase independence and objectivity which then can have an effect of lowering the extent to which organizations manage revenues. As DTS are required to select an auditor from an approved list provided by SASRA, it can be argued that this list contains firms that have extensive knowledge of the DTS's industry and thus would rely less on management. This provides an opportunity for further research to help

determine the effect of industry experience on the earnings management levels of DTS's.

The study incorporated all 41 DTS's regardless of size with results showing that size of the DTS's had no influence on earnings management. According to SASRA's classification, DTS are classified as Small (assets less than 1 Billion), Medium tier DTS's with assets of between 1 – 5 Billion and Large DTS'S that possess assets more than 5 Billion. Further studies which reduce the effect of size may be appropriate and especially in determining each size classifications level of earnings management.

REFERENCES

- Abrams, F. (1951). Management responsibilities in a complex world. *Harvard Business Review*, 29 (5), 29–34.
- Ahmadzade, Y., Hassanzadeh, R.B., Pooryegane, N & Ebrahim, H. (2012). *Australian Journal of Basic and Applied Sciences*, 6(13), 267-273.
- Amat, O. & Gowthorpe, C. (2004). *Creative accounting: nature, incidence and ethical issues*, Universitat Pompeu Fabra Economics and Business. Working Paper No. 749. Universitat Pompeu Fabra, Barcelona.
- Andreas, A. (2017). Analysis of Operating Cash Flow to Detect Real Activity Manipulation and Its Effect on Market Performance. *International Journal of Economics and Financial Issues*, 7(1), 524 – 529
- Antle, R. (1982). The auditor as an economic agent. *Journal of Accounting Research*, 20 (2), 503-527.
- Archambault, J., & Archambault, M. (2003). A multinational test of determinants of corporate disclosure. *International Journal of Accounting*, 38(2), 173-194.
- Arel, B., Brody, R. G. & Pany, K. (2005). Audit firm rotation and audit quality. *The CPA Journal*, 75 (1), 36-39.
- Babbie, E. R. (2012). *The Practice of Social Research*. (13th ed.). Belmont, USA: Cengage Learning.
- Baker, C. R. & Owsen, D. M. (2002). Increasing the role of auditing in corporate governance. *Critical Perspectives on Accounting*, 13 (6), 783 796.

- Bamahros, H.M. & Wan-Hussin, N. (2015). Non-audit services, audit tenure and earnings management. *Asian Academy of Management Journal and Finance*, 11 (1), 145-168.
- Barton, J., & Simko, P. J. (2002). The balance sheet as an earnings management constraint. *The Accounting Review*, 77(1), 1-27.
- Bassiouny, S. W., Soliman, M. M. & Ragab, A. (2016). The impact of firm characteristics on earnings management: an empirical study on the listed firms in Egypt. *The Business and Management Review*, 7 (2), 91 – 101.
- Becker, C.L., DeFond, M.L., Jiambalvo, J. & Subramanyam, K.R. (1998). The effect of audit quality on earnings management. *Contemporary Accounting Research*, 15(1), 1-24.
- Bedard, J. & Johnstone, K. (2010). Audit partner tenure and audit planning and pricing. *Auditing: A Journal of Practice & Theory*, 29 (2), 45–70.
- Berle, A. & Means, G. (1932). *The Modern Corporation and Private Property*. New York, USA: Macmillan
- Bigus, J. & Zimmermann, R.C. (2008). Non-audit fees, market leaders and concentration in the German audit market: A descriptive analysis. *International Journal of Auditing*, 12 (3), 159-179.
- Bjurman, A., & Weihagen, E. (2013). *How Reliable Are Earnings? A Study About Real Activities Manipulation and Accrual-Based Management in Europe*. Unpublished Doctoral Thesis, Umeå School of Business
- Bryman, A. & Bell, E. (2007). *Business Research Methods. 2nd Edition*. Oxford, UK: University Press.

- Burgstahler, D. C., Hail, L. & Leuz, C. (2006). The Importance of reporting incentives: Earnings management in European private and public firms. *The Accounting Review*, 81(5), 983-1016.
- Cameran, M., Vincenzo, D. & Merlotti, E. (2005). *The Audit Firm Rotation Rule: A Review of the Literature*. Working paper, Bocconi University
- Carey, P. & Simnett, R. (2006). Audit partner tenure and audit quality. *The Accounting Review*, 81(3), 653–676.
- Charreaux G. (1997). *Le gouvernement de l'entreprise*. Paris, France : Economica,
- Chen, C., Lin, C. & Lin, Y. (2008). Audit partner tenure, audit firm tenure, and discretionary accruals: Does long-term auditor tenure impair earnings quality? *Contemporary Accounting Research*, 25(2), 415 – 445.
- Chen, D., Li, J., & Liang, S. & Wang, G. (2011). Macroeconomic control, political costs and earnings management. Evidence from China listed real estate companies. *China Journal Accounting Research*, 4(3), 91 – 106.
- Chi, W., Huang, H., Liao, Y., & Xie, H. (2009). Mandatory audit partner rotation, audit quality, and market perception: Evidence from Taiwan. *Contemporary Accounting Research*, 26(2), 359–391.
- Ching, C. P., B.H., San, O.T. & Hoed, H. Y. (2015). The Relationship among audit quality, earnings management, and financial Performance of Malaysian public listed companies. *International Journal of Economics and Management*, 9 (1), 211 – 229.
- Chiraz, D. & Anis, J. (2013). Earnings management and performance of French IPO companies. *Journal of Accounting and Taxation*, 5 (1), 1-14.

- Cohen, D., Dey, A. & Lys, T. (2008). Real and accrual-based earnings management in the pre – and post – Sarbanes Oxley periods. *Accounting Review*, 83 (3), 757 – 787.
- Cooper, D.R., & Schindler, P.S. (2003). *Business Research Methods*. (8th ed.). Boston: 15 McGraw-Hill Irwin.
- Davidson, W.N. III, Jiraporn, P. & DaDalt, P. (2005). Causes and consequences of audit shopping: an analysis of auditor opinions, earnings management, and auditor changes. *Quarterly Journal of Business and Economics*, 45 (2), 69-87.
- Davis, L.R., Soo, B., & Trompeter, G. (2000). *Auditor Tenure, Auditor Independence and Earnings Management*. Working paper, Michigan Tech University and Boston College.
- Davis, L. R., Soo, B. S. & Trompeter, G. M. (2009). Auditor tenure and the ability to meet or beat earnings forecasts. *Contemporary Accounting Research*, 26 (2), 517–548.
- Dawson, C. (2002). *Practical Research Methods*, New Delhi, India: UBS Publishers' Distributors
- Debnath, P. (2017). Assaying the Impact of Firm's Growth and Performance on Earnings Management: An Empirical Observation of Indian Economy. *International Journal of Research in Business Studies and Management*, 4(2), 30-40.
- Dechow, P. M., Sloan, R. G. & Sweeny, A. P. (1995). Detecting earnings management. *The Accounting Review*, 70 (2), 193-225.

- Defond, M. L. and Jiambalvo, J. (1994). Debt covenant violation and manipulation of accruals. *Journal of Accounting and Economics*, 17 (1 & 2), 145 – 176.
- DeFond, M. L., & Subramanyam, K. R. (1998). Auditor changes and discretionary accruals. *Journal of Accounting and Economics*, 25(1), 35-67.
- De Vaus, D. A. (2001). *Research design in social research*. London, UK: SAGE.
- Donaldson, T. & Preston, L. E. (1995). The stakeholder theory of the corporation: Concepts, evidence, and implications. *Academy of Management Review*, 20(1), 65-91.
- Eilifsen, A. & Messier, W.F. (2000). The incidence and detection of misstatements: A review and integration of archival research. *Journal of Accounting Literature*, 19: 1-43.
- Eilifsen, A., Messier, W.F., Glover, S.M & Prawitt, D.F. (2010). *Auditing and Assurance Services International Edition*. London: McGraw-Hill.
- Erickson, M., Hanlon, M., Maydew, E.L., 2006. Is there a link between executive equity incentives and accounting fraud? *Journal of Accounting Research*, 44 (1), 113-143.
- Ernst & Young. (2011). *PCAOB Rulemaking Docket Matter No. 37*. Concept release on auditor independence and audit firm rotation.
- Ernst & Young. (2013). Navigating today's complex business risks Europe. *Middle East, India and Africa Fraud Survey*
- Fairchild, R. (2008). Auditor tenure, managerial fraud and report qualification: a behavioral game-theoretic approach. *International Journal of Behavioral Accounting and Finance*, 1(1), 23–37.

- Farouk, M. A., & Hassan, S. U. (2014). Impact of audit quality and financial Performance of quoted cement firms in Nigeria. *International Journal of Accounting and Taxation*, 2(2), 1-22.
- Ferraini, G. & Giudici, P. (2005). *Financial Scandals and the Role of Private Enforcement: The Parmalat Case*. Paper presented at the EU Corporate Law-Making Conference, Cambridge: London.
- Financial Sector Deepening Kenya. (2016). *FinAccess Household Survey*
- Firth, M., Rui, O. & Wu, X. (2012). How do various forms of auditor rotation affect audit quality? Evidence from China. *The International Journal of Accounting*, 47(1), 109–138.
- Francis, J. R. & Dechow, W. (2008). The joint effect of investor protection and big 4 audits on earnings quality around the world. *Contemporary Accounting Research*, 25 (1), 157-191.
- Francis, J. & Krishnan, J. (1999). Accounting accruals and auditor reporting conservatism. *Contemporary Accounting Research*, 16 (1), 135-165.
- Francis, J.R., Mydew, E.L. & Sparks, H. C., (1999). The role of big 6 auditors in the credible reporting of accruals. *Auditing: a Journal of Practice and Theory*, 18, 17-34.
- Frankel, R., Johnson, M. & Nelson, K. (2002). The relation between auditors' fees for non-audit services and earnings management. *The Accounting Review*, 77, 71–105.
- Frederick, W., Post, J. & St Davis, K. (1992). *Business and Society: Corporate Strategy, Public Policy, Ethics* (7th ed.). New York: McGraw-Hill.

- Frederick, W., Post, J., & St. Davis, K. (1992). *Business and society: Corporate strategy, public policy, ethics* (7th ed.). New York, NY: McGraw-Hill.
- Freeman, R.E. (1984). *Strategic Management: A Stakeholder Approach*. Marshfield, MA: Pittman,
- Freeman, R. E. (2002). *Stakeholder Theory of the Modern Corporation, 7th ed.* Englewood Cliffs, NJ: Prentice Hall
- Geiger, M., Raghunandan, K. & Rama, D. (2005). Recent changes in the association between bankruptcies and prior audit opinions. *Auditing: A Journal of Practice and Theory*, 24 (1), 21–35.
- Gerayli, M. S., Yanesari, A. M. & Ma'atoofi, A.R. (2011). Impact of audit quality on earnings management: Evidence from Iran. *International Research Journal of Finance and Economics*, 66 (1), 77-84.
- Giroux, G. (2004). *Detecting Earnings Management*. Hoboken, NJ: John Wiley & Sons, inc
- Ghosh, A. & Moon, D. (2005). Auditor tenure and perceptions of audit quality. *The Accounting Review*, 80 (2), 585-612.
- Gul, F. A., Fung, S. Y. T., & Jaggi, B. (2009). Earnings quality: Some evidence on the role of auditor tenure and auditors' industry expertise. *Journal of Accounting and Economics*, 47 (3), 265–287.
- Habbash, M. (2010). *The Effectiveness of Corporate Governance and External Audit on Constraining Earnings Management Practice in the UK*. Doctoral thesis, Durham University.
- Hamilton, J., Ruddock, C., Stokes, D., & Taylor, S. L. (2005). *Audit Partner Rotation, Earnings Quality and Earnings Conservatism*. Working paper.

- Healy, P. M. (1985). The effect of bonus schemes on accounting decisions. *Journal of Accounting and Economics*, 7(1), 85-107.
- Healy, P., & Wahlen, J. (1999). A review of the earnings management literature and its implications for standard setting. *Accounting Horizons*, 13(4), 365-383.
- Healey T.J. & Kim Y.J. (2003). The benefits of mandatory audit rotation. *Regulation*, 26 (3), 10-12.
- Healy, P. and K. Palepu. 2001. Information asymmetry, corporate disclosure, and the capital markets: A review of the empirical disclosure literature. *Journal of Accounting and Economics*, 31 (1), 405–440.
- Hodge, M. (2006). *The British CSR Strategy: How a Government Supports the Good Work*. London: John Wiley and Sons.
- Hussey, R. & Lan, G. (2001). An examination of auditor independence issues from the perspectives of UK finance directors. *Journal of Business Ethics*, 32 (2), 169-178.
- Jensen, M.C. & Meckling, W.H. (1976). Theory of the firm: managerial behavior, agency costs and ownership structure. *Journal of Financial Economics*, 3 (4), 305-360.
- Jiraporn, P., Miller, G. A., Yoon, S. S., & Kim, Y. S. (2008). Is earnings management opportunistic or beneficial? An agency theory perspective. *International Review of Financial Analysis*, 17(3), 622–634.
- Johnson, V. E., Khurana, I. K., & Reynolds, J. K. (2002). Audit-firm tenure and the quality of financial reports. *Contemporary Accounting Research*, 19(4), 637–660.

- Johnson, W. B. & Lys, T. (1990). The market for audit services: Evidence from voluntary auditor changes. *Journal of Accounting and Economics*, 12 (1), 281–308.
- Jones, J. (1991). Earnings management during import relief investigations. *Journal of Accounting Research*, 29 (2), 193 – 228.
- Kamau, C.G., Namusonge, G.S. & Bichanga, W.O. (2015). Practices influencing creative accounting among corporations listed in the Nairobi Securities Exchange. *International Journal of Business and Management*, 2(2), 2230-2248.
- Kang, S. & Kim, Y. (2011). Does earnings management amplify the association between corporate governance and firm performance? *International Business and Economics Research Journal*, 10(2), 53-66.
- Kiel, G., & Nicholson. G. (2003). Board composition and corporate performance: How the Australian experience informs contrasting theories of corporate governance. *Corporate Governance: An International Review*, 11(3), 189–205.
- Kim, J.B., Min, C. & Yi, C.H. (2004). *Selective Auditor Rotation and Earnings Management: Evidence from Korea*. Working Paper, Hong Kong Polytechnic University, Hong Kong
- Kivuvo, R.M. & Olweny, T. (2014). Financial performance analysis of Kenya's SACCO sector using the Altman Z Score Model of corporate bankruptcy. *International Journal of Business and Social Science*, 5 (9), 34-52.

- Kothari, C. R. (2004). *Research Methodology –Methods and Techniques*, (2nd ed.).
New Delhi: New Age International (P) Ltd.
- Kothari, S. P., Leone, A. J. & Wasley, C. E. (2005). Performance matched discretionary accrual measures. *Journal of Accounting and Economics*, 39(1), 163-197.
- Kramer, S. T., Georgakopoulos, G., Sotiropoulos, I. & Vasileiou, K. Z. (2011). Audit firm rotation, audit firm tenure and earnings conservatism. *International Journal of Business and Management*, 6(8), 44-57.
- Lambright, K.T. (2009). Agency theory and beyond: Contracted providers' motivations to properly use service monitoring tools. *Journal of Public Administration Research and Theory*, 19 (2), 207-227.
- Lavrakas P. (2008). *Encyclopedia of Survey Research Methods*. Los Angeles, USA: Sage Publications.
- Lee, B. B., & Choi, B. (2002). Company size, auditor type, and earnings management. *Journal of Forensic Accounting*, 3, 27–50.
- Lennox, C., Wu, X. & Zhang, T. (2014). Does mandatory rotation of audit partners improve audit quality? *The Accounting Review*, 89 (5), 1775–1803.
- Leuz, C., Nanda, D. & Wysocki, P.D. (2003). Earnings management and investor protection: an international comparison. *Journal of Financial Economics*, 69(3), 505-527.
- Llukani, T. (2013). Earnings management and firm size: An empirical analyze in Albanian market. *European Scientific Journal*, 9 (16), 135 – 143.

- Lu, T. & Sivaramakrishnan, K. (2010). *Does mandatory audit firm rotation improve or impair corporate investment efficiency?* Working Paper, University of Houston.
- Mattingly, J. E., Harrast, S.A & Olsen, L. (2009). Governance implications of the effects of stakeholder management on financial reporting, corporate governance, *The International Journal of Business in Society*, 9 (3), 271 - 282.
- Mautz, R. K. & H. Sharaf, A. (1961). *The Philosophy of Auditing*. Monograph No. 6. American Accounting Association.
- Mayangsari, S. (2007). The auditor tenure and the quality of earnings: is mandatory auditor rotation useful? *Unhas Makassar*, 26 (28), 1-25
- McDonald, D. & Puxty, A. G. (1979). An inducement-contribution approach to corporate financial reporting. *Accounting, Organizations and Society*, 4(1), 53-65.
- Mendonça, M. M., Costa, F. M., Galdi, F. C. & Funchal, B. (2010). The impact of the Sarbanes-Oxley Act (SOX) in the quality of earnings of Brazilian companies that issued ADRs. *Magazine Accounting & Finance - USP*, 21 (52), 1-24.
- Mehrani S & Bagheri B. (2009). The survey of the effect of free cash flows and institutional shareholders on earnings management of companies listed in the Tehran Stock Exchange. *Journal of Accounting Research*, 1(2), 50-71.
- Mensing, G.H. (2013). *Agency, auditing and the unregulated environment: some further historical The Effect of Auditor Changes on Earnings Quality: Support for Mandatory Audit Firm Rotation as proposed by the European Commission?* Unpublished thesis, University of Amsterdam

- Mugenda, O.N & Mugenda, A.G. (2003). *Research Methods: A Quantitative and Qualitative Approach*. Nairobi: ACTS press.
- Murphy, P., & Dacin, M. (2011). Psychological Pathways to Fraud: Understanding and Preventing Fraud in Organizations. *Journal of Business Ethics*, 101(4), 601-618.
- Mirie, M., Iraya, C. & Muchoki, G.W. (2015). The Effect of corporate governance practices on earnings management of companies listed at the Nairobi Securities Exchange. *European Scientific Journal*, 11 (1), 169-178.
- Myers, J. N., Myers, L. A., & Omer, T. C. (2003). Exploring the term of the auditor-client relationship and the quality of earnings: A case for mandatory auditor rotation? *The Accounting Review*, 78(3), 779–799.
- Njogu L., Mouni, G., Waititu A. & Omido K. (2014). Executive compensation consequence on dividend payout among listed manufacturing companies in Kenya. *Prime Journal of Business Administration and Management*, 4(2), 1364-1368.
- Nunnally, J. C. (1978). *Psychometric theory* (2nd Ed.). New York: McGraw-Hill
- Odera, O. (2012). Corporate Governance Problems of Savings, Credit and Cooperative Societies. *International Journal of Academic Research in Business and Social Sciences*, 2(11), 89-103.
- Okolie, A. (2014). Audit firm size and cash-based earnings management of quoted companies in Nigeria. *European Journal of Accounting Auditing and Finance Research*, 2, (5), 48-75.

- Okoye, I. E., & Alao, B. (2008). The Ethics of creative accounting in financial reporting: The challenges of regulatory agencies in Nigeria. *The Certified National Accountant*, 16 (1), 45-55.
- Pai, K. & Tolleson, T. D. (2015). Indias Saytam Scandal: Evidence the too large to indict mindset of accounting regulators is a global phenomenon. *Review of Business and Finance Studies*, 6 (2), 35 - 43.
- Palmrose, Z.-V. (1988). an analysis of auditor litigation and audit service quality. *Accounting Review*, 63(1), 55.
- PwC (2011). *PCAOB Rulemaking Docket Matter No. 37*, Concept release on auditor independence and audit firm rotation
- Reichelt, J. K. & Wang, D. (2010). National and office-specific measures of auditor industry expertise and effects on audit quality. *Journal of Accounting Research*, 48 (3), 647– 686.
- Rezaee, Z. (201). *Financial Services Firms: Governance, Regulations, Valuations, Mergers and Acquisitions*. Hoboken, New Jersey.
- Richardson, V.J., (2000). Information asymmetry and earnings management: some evidence. *Review of Quantitative Finance and Accounting*, 15 (4), 325-347.
- Rockness, H., & Rockness, J. (2005). Legislated ethics: From enron to Sarbanes-Oxley, the impact on corporate America. *Journal of Business Ethics*, 57(1), 31-54.
- Rohaida, B. (2011). *The Relationship between Governance Practices, Audit Quality and Earnings Management: UK Evidence*. Doctoral thesis, Durham University

- Rosenfield, P. (2000). What drives earnings management? *Journal of Accountancy*, 190 (4), 106-109.
- Roychowdhury, S. (2006). Earnings management through real activities manipulations. *Journal of Accounting and Economics*, 42 (3), 335 – 370.
- Ryan, S. G., Hertz, R. H., Iannaconi, T. E., Maines, L. A., Palepu, K., Schrand, C. M., Skinner, D. J. and L. Vincent (2001). Commentary. SEC auditor independence requirements: AAA Financial Accounting Standards Committee. *Accounting Horizons*, 15 (4), 373-386.
- SACCO Societies Act No. 14 (2008). Revised Edition 2012
- SACCO Societies (Deposit- Taking SACCO Business) Regulations, 2010.
- SACCO Societies Regulatory Authority. (2013). *SACCO Supervision Annual Report*
- Sainty, B.J., Taylor, G.K., & Williams, D.D. (2002). Investor dissatisfaction toward audits. *Journal of Accounting, Auditing and Finance*, 17 (2), 111-137.
- Sajadi, S. H., Farazmand, H. & Ghorbani, S. (2012). The effect of Auditor tenure on audit quality. *Journal of Accounting Advances*, 4 (1), 81 - 109.
- Sarbanes, P. & Oxley, M. 2002. *Sarbanes-Oxley Act of 2002*. Washington, D.C: U.S. Congress
- Schipper, K. (1989). Commentary on earnings management. *Accounting Horizons*, 3(4), 91-102.
- Shafie, R., Yusof, M.A.M. & Hussain, H.M.M. (2004). *Laissez-Faire or Mandatory Auditor Rotation: The Case of Audit Firm Tenure and Audit Firm Switching*.

Proceedings of the 4th Asia Pacific Interdisciplinary Research in Accounting Conference, July 4-6, Singapore.

Skinner, D.J. & Sloan, R.G. (2002). Earnings surprises, growth expectations, and stock returns or don't let an earnings torpedo sink your portfolio. *Review of Accounting Studies*, 7 (2), 289-312.

Solomon, I., Shields, M. D. &Whittington, R. O. (1999). What do industry specialist auditors know? *Journal of Accounting Research*, 37 (1), 191-208.

Sori, Z. M., Mohamad, S., & Karbhari, Y. (2006). *Auditor Reputation and Auditor Independence: Evidence from an Emerging Market*. Working paper series, centre of excellence for applied financial and accounting studies and Cardiff Business School, University Putra Malaysia.

Wallace, W. (1980). *The economic role of the audit in free and regulated markets*. New York, University of Rochester.

Wamwea, G.M. & Kaboyo, O.W. (2014). *Motivation Factors for Earning Management Practice in Public Listed Corporations in Kenya*. Research paper presented at the 5th African international business and management conference

Watts, R. & Zimmermann, J. L. (1986). *Positive Accounting Theory*. Englewood Cliff: Prentice Hall, Inc.

Xie, B., Davidson III, W.N. & DaDalt, P.J. (2003): Earnings management and corporate governance: The role of the board and the audit Committee. *Journal of Corporate Finance*, 9 (3), 295-316.

Yin, R.K. (1989). *Case Study Research Design and Methods*. Newbury Park: Sage

Zawawi, M. B. M. (2007). *Audit-Firm Tenure and Financial Reporting Quality in Malaysia*. Unpublished master's thesis, International Islamic University, Malaysia.

Zikmund, W. G., Babin, B. J., Carr, J. C., & Griffin, M. (2010). *Business research methods (8th ed.)*. Mason, HO: Cengage Learning.

Zgarni, I., Hlioui, K. & Zehri, F. (2012). Audit quality and earnings management in the Tunisian context. *International Journal of Accounting and Financial Reporting*, 2 (2), 2162-3082.

APPENDICES

APPENDIX I: DEPOSIT TAKING SACCOS IN NAIROBI COUNTY

No.	Name of DTS	No.	Name of DTS
1	Afya Sacco Society Ltd.	22	Nacico Sacco Society Ltd.
2	Airports Sacco Society Ltd.	23	Nafaka Sacco Society Ltd.
3	Ardhi Sacco Society Ltd.	24	Naku Sacco Society Ltd.
4	Asili Sacco Society Ltd.	25	Nassefu Sacco Society Ltd.
5	Chai Sacco Society Ltd.	26	Nation Sacco Society Ltd.
6	Chuna Sacco Society Ltd.	27	Nyati Sacco Society
7	Comoco Sacco Society Ltd.	28	Safaricom Sacco Society Ltd.
8	Elimu Sacco Society Ltd.	29	Sheria Sacco Society Ltd.
9	Fundilima Sacco Society Ltd.	30	Shirika Sacco Society Ltd.
10	Harambee Sacco Society Ltd.	31	Stima Sacco Society Ltd.
11	Hazina Sacco Society Ltd.	32	Telepost Sacco Society Ltd.
12	Jamii Sacco Society Ltd.	33	Tembo Sacco Society Ltd.
13	Kenpipe Sacco Society Ltd.	34	Ufanisi Sacco Society Ltd.
14	Kenversity Sacco Society Ltd.	35	Ukristo Na Ufanisi Sacco Ltd.
15	Kenya Bankers Sacco Society Ltd.	36	Ukulima Saco Society Ltd.
16	Kenya Police Staff Sacco Society Ltd.	37	Unaitas Sacco Ltd.
17	Kingdom Sacco Society Ltd.	38	UN Sacco Society Ltd.
18	Magereza Sacco Society Ltd.	39	Wanaanga Sacco Society Ltd.
19	Maisha Bora Sacco Society Limited	40	Wanandegge Sacco Society Ltd.
20	Mwalimu National Sacco Society Ltd.	41	Waumini Sacco Society Ltd.
21	Mwito Sacco Society Ltd.		