

THE EFFECT OF AUDITORS' TENURE ON SHORT-TERM FINANCIAL LIQUIDITY – A CONCEPTUAL FRAMEWORK

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Abstract

There is an alarming increase in audit scandals worldwide, negatively affecting financial statement users. These scandals happen soon after firms get an unqualified audit report, which would have confirmed their short-term financial liquidity. In most of these scandals, auditors have long associations with clients. The main question is whether auditors' long association with a client affects a client's financial liquidity. This paper aims to analyse the impact of auditors' tenure on financial liquidity. The literature review and conceptual framework development approach have been applied as a methodology. The existing literature on the subject has been consulted, and the framework has been developed based on the reviewed literature. The paper has found no direct correlation between auditor tenure and short-term financial liquidity. Auditors' tenure, short-term financial liquidity, company culture, board of directors, management/leadership, and mandatory rotations play a major role in the increasing audit scandals. The auditors and accountants of firms must closely monitor these variables. The audit scandal will continue if appropriate risk-mitigating strategies are not in place to control all these variables. Future research may use quantitative methodologies to further contribute to the existing literature to get the direct correlation between the auditor's tenure and short-term financial liquidity

Keywords: Auditors tenure; short-term liquidity; auditor's independence; unqualified audit report

1. Introduction

Auditors play a vital role in corporate governance. They give credibility to the financial statements prepared by directors of the companies by issuing an audit opinion on whether the financial statements present the true and fair status of the company (Handoko et al., 2019). The audit opinion forms the basis for financial statement users such as shareholders, regulators, banks, and all others to make decisions per their

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different mandates; for example, shareholders make investment decisions (Hersan & Fettry, 2020). This shows how significant the auditors' role is.

To ensure that the auditors play their role effectively, they must be independent of their clients and be objective and transparent (Manap et al., 2023). Some regulations and good practices are implemented to monitor auditors' independence. The Independent Regulatory Board for Auditors (IRB) monitors auditors' independence in South Africa (IRBA). IRBA believes that long audit tenure negatively affects an auditor's independence, leading auditors to pay no heed to material misstatements in the financial statements (Ndaba et al., 2021). Despite all these measures, financial statement users continue to suffer from audit scandals.

Audit scandals are happening alarmingly worldwide. In the case of South, the freshest examples are the collapse of the VBS Bank and Steinhoff scandal in South Africa (Sambo & Kanyane, 2024; Schoeman, 2023), where the management and auditors colluded and enriched themselves at the expense of the investors and other stakeholders. These audit scandals have raised the eyebrows of financial statement users. As a result, the auditor's independence and integrity have been questioned (Handoko et al., 2019). The effect of an auditor's tenure is always a controversial subject. On the one hand, there is a school of thought that tenure is a variable contributing to the deterioration of an auditor's independence (Aminu et al., 2024). This view is not shared across the board: there is a contrary view that the audit scandal is from other factors such as poor financial management by directors, poor working capital management, and the current ratio that indicates the company's financial liquidity (Ajayi et al., 2024). Hence, this paper's main objective is to analyse the effect of auditors' tenure on financial liquidity and to develop a conceptual framework.

2. Methodology

This paper has applied a literature review and conceptual framework development approach: a qualitative method that builds a conceptual framework from existing literature. As a process of theorization, it uses grounded theory methodology. Conceptual framework development is not merely the collation of concepts related to a subject matter for inquiry. Rather, it analyzes the key factors, constructs, or variables. Jabareen (2009) instructively lays out several features of these methodologies. Four such features are of peculiar relevance to this study. Firstly, conceptual framework methods are interpretive: they interpret methods for the social reality. Secondly, they differ from quantitative methods in that rather than offering a theoretical explanation, they provide an understanding. Thirdly, the conceptual framework is developed through a process of systematic qualitative analysis. Fourthly, and much more importantly, the data sources comprise many discipline-oriented theories. Such theories in turn become the empirical data for analysis. This latter aspect underscores the interpretive nature of the inquiry as it helps generate new interpretations.

In this study, the existing literature on the effect of auditor's tenure on short-term liquidity has been reviewed. The publications, including books and articles, have been

consulted. This was to critically analyze what the other authors say about the correlations between the two variables: auditor's tenure and short-term financial liquidity. The literature review and conceptual framework development approach have guided this paper to see the gap on the subject and develop the conceptual framework that shows other variables that have a relationship with the auditor's tenure and short-term financial liquidity and how they coexist (Kamaludin et al., 2024)

3. Theoretical Framework: The Agency Theory

The study is primarily located within the agency theory: a contractual relationship in terms of which the principal delegates the duties to agents. Agency relations come in many forms, such as shareholder-auditor, shareholder-director, and many more (Onjewu et al., 2023). In the corporate world, the directors of the companies owe a fiduciary duty to shareholders as the shareholders have entrusted them to run and manage the company on their behalf. The directors are, therefore, accountable to shareholders. They execute the mandate of increasing shareholders' wealth. Because of the separation of ownership and control of the company, shareholders may end up losing control because the directors are the ones who have full information on the operations of the company.

The directors may be self-conflicted and pursue their interests at the expense of the shareholders. This is the key reason why the auditor-shareholder relationship comes in: to mitigate the agency risk of directors enriching themselves at the expense of the shareholders. The shareholders appoint the external auditor through the audit committee to form an audit opinion on the truthfulness and fairness of the directors' financial statements (Kuzey et al., 2023). The auditors must be independent from the directors to execute their mandate objectively and transparently. However, even in this auditor-shareholder relationship, there is an agency problem whereby the auditors are not independent of the directors; they may collude because of long association (number of years of audit tenure). Corporate governance addresses agency problems like this to mitigate the uprising audit scandals.

4. Financial Liquidity

Financial liquidity is the financial management concept that indicates the financial health of the company, that is, whether the company has more current assets as compared to its current liabilities. A company must have strong financial liquidity to continue its operations without disruptions. Strong financial liquidity means that the company can pay its short-term obligations when they fall due (Markonah et al., 2020). For instance, if the company cannot pay its suppliers, current taxes, and salaries to its employees, the probability of such a company continuing to operate without disruption is very low. All of the mentioned stakeholders will have a problem because they expect payment after offering services to a company; failing to maintain a good relationship with said stakeholders poses a competitive threat. Both employees and suppliers may switch to competitors, and the tax regulators may pose some penalties that may even stop the company's operations.

Financial liquidity is the capacity of the company to pay its short-term debts when they fall due. The company can use its assets to pay its short-term obligations. It is determined by dividing the current assets by current liabilities, where the current assets can be quickly turned into cash, and current liabilities are debts that the company owes to third parties, such as suppliers and overdraft facilities. The current ratio must be 1:1 or 100% for the company to be able to pay its obligations when they are due. The higher the ratio, the more liquid the company is said to be (Hersan & Fettry, 2020).

The concept of financial liquidity not only helps the company operate smoothly but also gives a competitive advantage to a company over its competitors. To be ahead of the competitors, a company and its stakeholders must have a strong relationship. The corporate environment is dynamic and needs active management to take advantage of any opportunity and overcome threats brought by the changing environment. The company can only be proactive in response to these changes with strong financial liquidity. This is how serious financial liquidity is to companies; hence, companies are willing to invest in finance professionals to manage their finances and maintain good liquidity.

5. Types of Financial Liquidity Analysis

Financial liquidity performance is measured using three ratios: current, quick, and cash. These three ratios indicate whether the company can pay its short-term debt when it falls due. However, they use different current and current liabilities variables to analyze the liquidity potential, which means that even their interpretations would differ.

5.1. Current ratio

The current ratio compares all current assets to current liabilities in total. This is calculated by dividing current assets by current liabilities. The generally accepted outcome from this calculation is 2:1 (Markonah et al., 2020). It indicates that the current assets cover the total current liabilities twice. The company may not face the problems of paying its short-term obligations. Short-term obligations refer to those that fall due within twelve months. It must however be noted that 2:1 is generally accepted, but to be more accurate, each industry has its accepted ratio.

The ratio can still be 1:1 and acceptable. It all depends on the nature of the business. Similarly, the high current ratio does not necessarily mean that the company is financially healthy. It may be a red flag that the working capital management is poor. For example, let us focus on the three variables of current assets: cash, receivables, and inventory. We hypothetically assume we have large figures on these variables and fewer total current liabilities. The current ratio can be high, yet it indicates the problem of good working capital management.

To elaborate more on this issue, the large amount of cash, inventory, and receivables may indicate that the business is holding too much cash and may be missing some investment opportunities. Too much inventory may be difficult to sell and become obsolete, and the company has invested too much funds in debtors who may be unable to pay. This shows

that management manages the working capital to benefit the company and its stakeholders.

5.2. Quick ratio

The quick ratio, called the 'acid test ratio', excludes the inventory in its calculation because it may be difficult to turn inventory into cash quickly. So, to be more precise in analysing the financial health, the inventory is not considered (Iskandar,2020). It is calculated by deducting inventory from the total current assets and then divide by the total current liabilities. Even though the quick ratio is considered more reliable than the current ratio, some variables, like receivables in the calculation, cannot quickly be converted into cash. Companies' management still needs to employ effective tools to manage working capital. For example, systems should be implemented to help collect debts within a reasonable time to avoid bad debts.

5.3. Cash ratio

Cash ratio compares to cash and cash equivalents to total current liabilities. It is, therefore, calculated by dividing cash and cash liabilities by total current liabilities (Alvian et al., 2022). The outcome is generally acceptable when it is greater than one. It means that the company can comfortably pay its short-term obligations whenever they fall due. This gives the investors' confidence as they see that the company is doing well liquidity-wise, increasing the business's value. However, too much of a cash ratio is not good for the company and investors. Investors are mainly interested in maximizing their wealth. This means that the company's directors are entrusted with increasing the shareholders' wealth by managing funds and making proper strategic and investing decisions accordingly. So, holding too much cash and cash equivalent may compromise maximizing the shareholders' wealth. This is because too much cash idling could have been used to take investment opportunities (Alvian et al.,2022).

At this point, agency theory plays a major role in ensuring that the directors act in the shareholders' interest when making company decisions. The auditors play a key role in giving the shareholders confidence that the directors are playing their fiduciary role accordingly. The auditors must be fully independent from the directors so that they can be objective when issuing the audit opinion on the financial statements prepared by the directors. The regulators put systems in place to strengthen the auditors' independence. Despite all of the measures and systems to strengthen the auditor's objectivity, some threats, such as the long association of auditors and directors, still threaten their objectivity.

6. The concept of auditors' tenure

Audit tenure is the relationship between the auditor and the client, measured in several years. There are different views on whether the long association between the auditor and the client impairs the auditor's independence and objectivity (Qawqzeh et al., 2018). Other researchers found that long association leads auditors to have a cosy relationship with the client. Because of this cosy relationship, they end up sympathising with the

clients at the expense of their principals. The more time the auditor spends with the client, the more the auditor understands the client's environment (UK et al., 2018). The long audit tenure adds strategic value to companies in terms of cost reduction strategy. The researchers have found that the long-term relationship between these two parties reduces client audit fees because the auditor no longer has to perform intensive audit procedures as the auditor is familiar with the client's environment (Saragih & Lubis, 2017; Handoko et al., 2019). Other researchers believe financial statement fraud comes with pressure from management and auditors because of the threat of familiarity created by long auditor tenure.

A long-term relationship involving auditors and clients may lead to collusion because both parties may want to achieve their financial benefits. Long auditors' tenure can lead to auditors willingly participating in this financial statement's fraud triangle out of ignorance. As long as an association with clients saves both time and costs for both parties, there is a threat that they can develop emotional relationships, which can reduce auditors' objectivity. This can be due to the auditor becoming too comfortable with the client and, as a result, trusting that the client has prepared the financial statements according to the requirements (Rahman et al., 2020).

The level of questioning mind can also be reduced intentionally where the auditor sympathises with the client because of their bond. As a result, auditors may intentionally ignore the red flags from audit procedures. When this happens, the external auditors may participate in the fraud, more especially when the company has low liquidity ratios because they may want to protect themselves from financial risk where the client could fail to pay their fees or they have developed a special relationship with the client and protecting the client from the embarrassment of not getting clean audit report. In their study, where they wanted to establish the relationship between auditors' tenure and financial statements fraud, Handoko et al. (2019) found that auditors' tenure does not significantly influence financial statements fraud, but auditors' rotation does. Rahman et al (2020) also showed that long auditors' tenure leads auditors to give wrong audit opinions. This can help the regulators emphasize the importance of audit team rotations, especially audit engagement partners.

7. The impact of auditors' tenure on financial liquidity

The auditor must perform analytical procedures such as liquidity ratios to prove that the company is a going concern. A long-term auditor's tenure can create the threat of conflict of interest where the auditor may fail to report the true picture of the outcome of the financial liquidity. The conflict of interest can arise for many reasons, including the auditor fearing it may not get its audit fees from the client if it reports short-term liquidity problems. It must be noted that the audit fees form part of the short-term liabilities as payables. However, Larasati et al. (2019) said that an auditor's tenure is unrelated to the financial distress that low liquidity ratios may cause. According to Qawqzeh et al. (2018), an auditor's tenure does affect financial reporting fraud where the auditors can fail to report the true picture from the evidence obtained through audit procedures, such as the

company having low short-term and long-term financial liquidity. Because of the long-term relationship between the auditor and the client, the bond between them may force the auditor to ignore that the directors have used creative accounting. When the company has short-term and long-term liquidity problems, the directors are motivated to use creative accounting, where they give the false impression to shareholders that the company is performing well, even though it may not.

Izzalqurny et al. (2019) found that if the current asset ratio and other profitability ratios are weak, there is a high possibility of financial statement fraud, where management and the auditors can intentionally mislead the investors through wrong financial statements and audit reports, respectively. They further cautioned financial statement users to raise their eyebrows and pay more attention to details of companies with poor liquidity performance because there might be a high possibility of misstatement. Contrarily, Saragih and Lubis (2017) say that short-term liquidity ratios do not influence auditors' decisions to give the wrong audit opinions.

In their research paper published in 2019, Simamora and Hendarjatno wanted to establish the impact of financial liquidity, leverage, audit shopping, and auditors' tenure on audit opinion. The secondary data was used on manufacturing companies listed on one stock exchange. The purposive sample used 16 companies, and logistic regression was used. They have indicated one advantage of long auditor tenure: the auditor's knowledge of the client's environment increases. The audit quality may increase because the auditor knows the risk better than other areas that need attention. A proper audit plan would be formulated to detect financial misstatements and result in a quality audit opinion.

However, they indicated one of the disadvantages of the long association with the client: the impairment of the auditor's objectivity as a strong relationship bond could emerge. The relationship can result in a self-interest threat where the auditors may financially or socially benefit from the bond; hence, they become vulnerable to expressing the objective audit opinion. They further said that companies with low liquidity ratios will likely get the going concern audit opinion from independent auditors. According to their findings, financial liquidity and auditor tenure do not affect the going concern. The auditor could still issue a going concern audit opinion regardless of the long association with the client and the status of corporate financial liquidity, whether the liquidity ratios are weak or strong. The authors concluded that the audit shopping and leverage ratio affect the going concern audit opinion. Weak short-term liquidity ratios could be a temporary situation that a strong financial management officer can turn around with the help of the whole management of the company, while on the other side, the long-term debt ratio can be hard to manage more, especially when the ratios are just too high. However, it is unclear whether auditors' tenure affects the short-term liquidity ratio, hence the objective of this study.

There are mixed views on auditors' tenure. According to Chen et al. (2022), the longer the auditor spends with the client, the better. The auditor becomes familiar with the client's systems and environment. As a result, there would be no audit delays, and they argue

that a high-quality report would be produced as the auditors know the riskier areas and can give more focus to such areas. On the other hand, Arianpoor and Mizban (2023) disagree with this view, saying that the longer the auditor's tenure, the riskier it becomes. The auditors become too comfortable with the client. This can negatively affect the audit plan. It is subjective to say that the auditors know which areas are riskier.

The client can take advantage of this and ensure everything is in order in the perceived areas to be more important and relapse in other areas. This can lead to poor audit opinion. Hence, there must be mandatory audit rotation. Even though it is believed that mandatory audit rotation can strengthen the auditor's independence, Dayanandan et al. (2023) found that mandatory audit rotation, together with the long audit tenure, are major contributing factors to corporate failures. They further stated that the regulators have not yet achieved the intended auditors' risk mitigation strategy by implementing mandatory audit rotation.

In response to the Enron scandal, the US strengthened its corporate governance by implementing the Sarbanes-Oxley (SOX) Act of 2002. The main objective of this law is to protect investors and other users of financial statements against fraudulent reporting by accountants and auditors. Investors tend to lose confidence in reports produced by an accountant and an auditor. This law punishes these professionals when they fail to comply with accepted reporting standards. SOX has amended laws such as the Securities Exchange Commission (SEC) in four areas: corporate responsibility, increased criminal punishment, accounting regulation, and new protections. SOX requires that the audit partner rotate every five years and mandates that the corporate directors make the written statement that the financial statements they have produced comply with SEC and other related laws.

They should show that the financial statements show the true status of the company at the time of reporting. The directors who sign off this statement knowing very well that what they would have written is not true should face harsh criminal punishments like imprisonment. The law further requires the directors and auditors to put internal controls and reporting systems in place and ensure that those controls work effectively. There is criticism about implementing internal controls and properly monitoring them, as there is an argument that it is way too expensive. It continues to show the three rules about record keeping. The first one is about destruction and falsifying records. The second one shows the time required to keep the records, and the last one entails the kind of communication that the companies must keep records of, including electronic communication with the SOX to increase transparency through the firm's reports and tightened corporate governance.

There is an ongoing debate about the long association between auditors and clients in the post-Enron era. The stakeholders and regulators have scrutinised the long audit tenure to determine whether it enhances or damages audit quality (Dayanandan & Kuntluru, 2023). The world is trying hard to strengthen the auditor's independence with the hope that auditors would regain the lost trust of the stakeholders. Many countries have initiated

mandatory Audit Rotation (MAR) to ensure the quality of financial reporting. The basis for MAR is that the auditor becomes too cosy with the management, compromising their objectivity. They fail to plan the auditor properly because they think they are familiar with the client's environment. So, the belief is that the rising audit scandals are due to the long association between the auditors and the client. However, as indicated earlier, there are some positive views about the long-term relationship between auditor and client.

Some countries do not agree with the MAR, including Austria, Canada, Greece, Latvia, Singapore, and Spain, to mention a few. USA has also dropped MAR after getting negative feedback from the regulators. The auditors complained about the switching costs they incurred when implementing MAR and that even the client incurred high fees when engaged in the new audit. The pushback includes recommending that companies strengthen internal controls by appointing a competent audit committee that regularly monitors auditors' independence. The European Union has implemented MAR every ten years, effective June 2016. The regulators firmly believe there is no benefit to a long relationship between auditor and client, but it threatens auditors' independence (Dayanandan & Kuntluru, 2023). As a result of the mixed view on whether auditors' tenure has a positive or negative impact on the quality of the report, many researchers are exploring this topic using different variables to check their relationship. According to Dayanandan and Kuntluru (2023), auditors' tenure and MAR have a negative impact on the audit quality. Their research has established the relationship between MAR regulation and audit quality in India, using modified audit opinion as a proxy for audit quality.

In South Africa, auditors' tenure has been largely unregulated. In the main, audit firms would do voluntary firm rotation or partner rotation. However, it is important to note that section 92 of the Companies Act 71 of 2008 provides for the tenure of individual auditors. It provides that auditors are not allowed to serve one client for a period exceeding five years. It provides for a cooling-off period of two years between the appointment cycles. Voluntary firm rotation was proved ineffective as much concern has been expressed over the quality of audits in South Africa and the corresponding recurrence of corporate financial scandals. There were increasing audit scandals in South Africa, such as VBS and Steinhoff. This has been associated with long and unregulated audit tenures. Audit firms have engaged with a single client for decades (Ndaba et al., 2021). It was not until 2017 that the Independent Regulatory Board for Auditors (IRBA) was influenced by the view that audit tenure must be regulated. The regulatory body, in turn, introduced the mandatory audit firm rotation (MAFR) regime in South Africa. In making this ruling, the regulatory body was following the trend set by the EU. The IRBA found itself obliged to introduce the regulation of audit tenure. It is argued that the increasing audit scandals that arise despite the clean audits given to such companies are attributed to long auditors' tenure with a client. They argued further that a long association with a client affects an auditor's independence, as many companies face liquidity problems shortly after a clean audit.

The rule provided that all auditors of public interest entities (PIEs) in South Africa shall comply with the principle of mandatory audit firm rotation (MAFR) effective from 1 April

2023. The promulgation of the rule was necessitated by, among others, the need to strengthen auditors' independence from their clients. The regulator noted unduly long audit relationships in South Africa; some were estimated to be more than a hundred years. Besides enhancing professional independence, the need for the rotation of audit firms in South Africa has other transformational purposes. In South Africa, the need to rotate audit firms also seeks to accelerate the profession's transformation and the need for de-concentration.

The extended tenure of audit firms in South Africa is partly due to certain audit firms' monopolies. For instance, in 2017, the then Minister of Finance, Malusi Gigaba, noted that there were 4283 registered auditors in South Africa; there were over 300 JSE-listed entities with a combined spend in audit fees amounting to around R4bn. The Minister noted that despite so many audit firms in South Africa, much of the JSE-listed audit market is mainly dominated by the big four global audit firms: PricewaterhouseCoopers (PwC), Deloitte Touche Tohmatsu (Deloitte), Ernst & Young (EY), and KPMG (The Account 2017). This has resulted in the undue concentration of the audit market, which excludes the majority of black-owned and indigenous audit firms. The rule has attracted a fair amount of criticism.

While praised for addressing audit independence and transformation, it is criticised for its inability to address capacity issues. Like all transformative initiatives, it is criticized for advocating for a rotation of firms 'for the sake' of it at the expense of merit. Ndaba et al. (2021) further criticise MAFR because there is no evidence that it is intended to improve auditors' independence or contribute to a more thorough audit approach. Instead, evidence suggests that newly recruited audit firms use it to familiarise themselves with the new clients, coupled with material tendering costs. However, it may decrease the profitability of audit engagements, affecting audit quality. Other factors that may affect the decline in audit quality are a loss of client experience and staff retention challenges.

The ruling by IRBA had two major requirements. Firstly, it provided that auditors' firms, as stated in the IRBA Code, should not continuously audit the public interest entities for more than ten financial years. Secondly, the auditors can only serve the same client again after five fiscal years have lapsed. The regulatory body used its rule-making powers in terms of section 10(1)(a) of the Act. The section gives the regulator powers to make rules on any issues relating to the audit profession. According to the Act, the regulator's general functions are to regulate the auditors, set and maintain standards, ensure ethical conduct by auditors, and enforce discipline.

The MAFR ruling generated controversy within the audit and accountancy fraternity. In the end, it was challenged in courts of law. The challenge started at the Pretoria High Court (East Rand Member District of Chartered Accountants v IRBA, 2021). The East Rand Member District of Chartered Accountants, a voluntary association, and its chairman instituted the cases. Some members of the association are chartered accountants who are registered auditors. They practice in small and medium audit firms. As a result, they

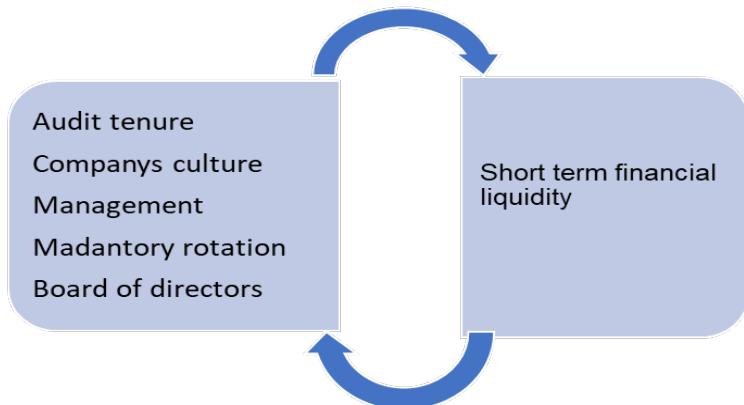
are subject to professional regulation by the IRBA. They instituted a case to challenge the 2017 MAFR ruling by the regulator (IRBA 2017).

The applicants disagreed with MAFR: they complained that it would negatively affect them because most of their members are small firms, so getting new clients would be difficult. In Court, the basis for their case was that they were not consulted before the Rule's promulgation. The High Court dismissed their case. The basis for the dismissal was largely technical: the Court did not assess the substantive merits and demerits of the MAFR rule. The High Court disagreed and dismissed their case because it was instituted after the time provided by section 7(1) of the Promotion of Administrative Justice Act, 2000 (PAJA). Dissatisfied with the ruling of the High Court, the applicants appealed to the Supreme Court of Appeal (East Rand Member District of Chartered Accountants v IRBA 2023). The Supreme Court of Appeal disagreed with the High Court and found that the IRBA does not have powers in terms of the referred Act.

The Supreme Court found that IRBA does not have the power to promulgate the MAFR ruling. In doing so, the regulator went beyond its powers in terms of sections 4(1) and 10(1)(a) of the Auditing Professions Act, 2005. The Court found that the Act only empowered the regulator to prescribe professional standards based on specific functions stipulated in the Act. Therefore, the court found that the MAFR ruling is not a professional standard for the specific functions of the regulator provided in the Act. The ruling restricts companies from appointing auditors firms they like. Hence, the Court decided that the MAFR ruling by IRBA was invalid because the regulator did not have the power to make it.

The net effect of this ruling is that, despite the good intention to introduce the regulation of audit firms in South Africa, the ruling has been declared unlawful. The pre-existing position where audit firms would audit entities for extended periods prevails. This is despite all the reasons advanced by the IRBA for introducing such regulation.

Figure 1 A Conceptual Framework



Source: Designed by the author with insight from the literature

8. Results

Based on the systematic analysis of the forgoing literature and conceptual framework, the study finds that there is no direct correlation between auditors' tenure and short-term financial liquidity based on the literature review conducted. Instead, several factors have a bearing on the independence of auditors: the number of years the auditor takes with the client, the values and morals together with the way firms do things, the type and risk appetite of the management, the effectiveness of the board of directors, mandatory audit rotation, and short-term liquidity. These cumulative factors can impair the auditor's independence – not tenure alone. This may lead to auditors issuing intentionally wrong audit opinions, particularly the favourable ones that resonate well with their conflicted interests.

9. Discussion, and Conclusion

The study set out to investigate the correlation between auditors' tenure and short-term financial liquidity. As the findings demonstrated, no direct evidence from the literature directly links audit tenure and short-term financial liquidity. The literature indicates that an auditor's tenure does affect auditors' independence negatively. This leads to auditors issuing poor-quality audit reports because they are compromised. The different view states that the auditor's tenure does not negatively impact the auditor's independence because the longer the auditor's tenure, the more advantageous it is to both the client and the auditor. The auditors become familiar with the client's environment, which reduces audit procedures and costs to the client. It is also found that the lower the company's financial liquidity, the more the auditors would want to verify the ongoing concern of the client.

The growing number of audit scandals that lead to the collapse of companies happen because such companies fail to pay their short-term obligations when they fall due. The literature indicates that the board of directors' effectiveness can help in such situations by adequately monitoring and controlling the management. Management must be given incentives such as a share option to motivate them to serve the interests of the shareholders. The management is also responsible for setting and maintaining a fraud-free culture. When companies are known for transparency in all their dealings, employees, including management, are not motivated to participate in fraud in financial statements. The regulators also implement mandatory audit rotation as a mitigation strategy, but there is no clear evidence that mandatory audits can reduce audit scandals. The regulators must continue to emphasise ethical behaviour to the auditors and accountants, putting severe punishment and implementing them to discourage unethical behaviour that leads to fraud in financial statements.

Future researchers may continue with the same research topic by exploring other methodologies, such as quantitative ones, to get the direct and clear relationship between auditor's tenure and short-term liquidity. This will help close the gap in the current literature, where no clear correlation between the two was found.

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