

TRANSFORMATIONAL LEADERSHIP AND PERFORMANCE OF AUDIT FIRMS

Pauline Kamwara – Otila

School of Business and Economics, Daystar University, Nairobi-Kenya

Joanes Kaleli Kyongo 

School of Business and Economics, Daystar University, Nairobi-Kenya

jkyongo@daystar.ac.ke

Abstract

The objective of the study was to establish the effect of transformational leadership on the performance of audit firms and a corresponding hypothesis was formulated and tested. The study targeted all the 45 employees of MK Certified Public Accountants audit firm in Kenya and all of them responded. The chosen firm represents all the other audit firms in Kenya hence the findings will be generalized. The study adopted a descriptive research design. SPSS Version 21 was used to analyze data using descriptive and inferential statistics. Research findings from the test of hypothesis established that transformational leadership affects performance of audit firms. The study findings support Transformational leadership theory which links transformational leadership to organizational performance. Further study can be carried out in other audit firms or otherwise in Kenya and other countries.

Keywords: Transformational Leadership, Organizational Performance, MK Certified Public Accountants

INTRODUCTION

The purpose of transformational leadership is to give a business a new lease of life (Bhat, Rangnekar, & Barua, 2013). Organizational performance is the capability to materialize goals like high profits, appropriate financial results, increased market share, superiority of products, and survival (Koontz & Donnell, 1993). Various studies have found a positive effect of

transformational leadership on organizational performance (Garcia-Morales, Llorens-Montes & Verdu-Jover, 2008; MacKenzie, Podsakoff & Rich, 2001) though there is no consensus whether the effect is significant (Obiwuru, Okwu, Akpa & Nwankwere, 2011). Given that professional firms are guided by a set of standards from ICPAK (Code of Ethics), ISQC1 (International Standards Quality Control), ISA (International Standards on Auditing) and IAS (International Accounting Standards), the extant study aimed to establish the effect of transformational leadership on organizational performance using a case of MK Associates CPA (K), a firm that is limited by a set of standards in their operations and leadership. The operationalization of organizational performance and the examination of transformational leadership in an audit firm are gaps that the extant study has addressed.

Transformational Leadership

Transformational leadership encompasses the process which changes and transforms individuals through an exceptional form of influence on followers to achieve surplus compared to what is usually expected of them and aims to give a business a new lease of life (Bhat, Rangnekar, & Barua, 2013). A transformational leader encourages others to innovate new and significantly improved norms to discourage the normalcy (status-quo) in order to change the environment successfully. The optimal profile of the leader is characterized by the presence of certain traits of transformational leadership. Bass and Avolio (1995) are quoted on the categorization of skills of transformational leaders, which are "4 I's" which includes idealized influence, individualized consideration, inspirational motivation and intellectual stimulation.

Leaders with idealized influence portray conviction, trust, present important values and purpose, commitment and ethical implications of a decision (Johnson, 2009). Inspirational motivation involves the process whereby the leaders encourage the subordinates to align employees' personal goals and objectives with those of the organization (Doody & Doody, 2012).

Anjali and Anand (2015) emphasized that intellectual stimulation enables the development of employees and their commitment to organizational success. Zacher, Pearce, Rooney, and McKenna (2014) considered individualized consideration as a process that involves the enthusiasm and capability of a leader to give nurturing support to the followers. A leader needs to give support and the needed directives to all the followers in the organization. The guidance and support by the leader will build a rapport with the employees as well as improve their performance in the related level of the organization.

Organization Performance

Organizational performance involves the transformation of inputs to outputs to attain particular outcomes (Chen, 2002). Organizational performance is measured by the effectiveness of both the leader and employees within the organization (Kunhert, 1994). Organizational performance of a firm should be maintained or rather enhanced for the better good of the business and the society.

Audit Firms in Kenya

The audit profession in Kenya is dominated by what is referred to as the big four of the largest auditing firms in the country, all of which have international backgrounds. The big four firms are the auditors of all the publicly traded firms in Kenya. The partners of the firms both locals and expatriates actively contribute in various committees of local professional accountancy body, The Institute of Public Accountants of Kenya (ICPAK). Of the rest, two other major firms in the country are also associated with one of the big five international audit firms in the country of origin and the other is a Kenya-based regional accounting firm (East Africa). As per the Institute of Certified Public Accountants of Kenya (ICPAK), the number of registered audit firms operating in Nairobi, Kenya as at September 2015 was 619. Out of these, only a few have extended their operations internationally. These audit firms comprise of Ernst & Young, KPMG, Deloitte and Price Waterhouse Coopers which have both local and international orientation. The bulk of audit firms however, are according to Githae (2004), small and medium sized audit firms, who because of their small operational outfit find it difficult to keep abreast with the new developments in the auditing and accounting field. The practitioners hold that the downturn in the economy during the previous years is continuously stressed to earn enough to remain afloat hence they cannot afford to spend money and time on training programs. SMEs' practitioners in Kenyan stay affected by inadequate access to suitable literature on application of recognized accounting and auditing standards.

Sheikh (2007) noted that failure to ensure compliance by auditors with International Accounting Standards (IASs) and International Standards on Auditing. This may not be because of lack of demand for accountability and transparency but due to capacity constraints in the smaller audit firms. Sheikh (2007) observes that whilst large Audit firms are able to carry out community related activities like sports, thereby giving themselves marketing advantage; it is not easy for the small and medium sized firms to do this as a competitive strategy. The accounting profession in general has recently been undergoing a lot of scrutiny. According to Leggatt and Martin (2003), global scandals like Enron, WorldCom and more recently Parmalat, have caused serious harm to the accounting profession, not only legally but also morally and ethically.

MK Associates CPA (K) is an audit firm registered in Kenya since 1986. It is a firm of registered accountants by the Institute of Certified Public Accountants of Kenya. This firm is located along Mombasa Road-Ramco Court. The firm is represented in the country with its headquarters in Nairobi and contacts in some major towns of Kenya, Nakuru, Eldoret and Embu. The firm also offers consultancy services to clients in the United States Washington, United Arab Emirates and the Democratic Republic of Congo. For expediency in executing assignments, which requires close monitoring, MK Associates CPA(K) has state of the art communication means such as internet connections on staff laptops, email and internet press conferencing facilities when handling international assignments. With this kind of organization and taking advantage of technology advancement in computers by use of laptops and mobile communication, they have always been efficient in executing their assignments. The partners of MK Associates CPA (K) emphasize the necessity to develop the leadership skills since they deem it necessary to inspire, influence and motivate its employees to accomplish results. The adopted leadership skills or traits by MK Associates CPA (K) partners has thus led to superior results which is associated with transformational leadership.

Transformational Leadership and Organizational Performance

A study by Rejas, Ponce, Almonte and Ponce (2006) conducted at Chile to determine whether leadership style affected the small firms' performance revealed a significant effect of the former on the latter. A study by Muterera (2012) carried out in the United States of America, established that transformational leadership positively affects organizational performance. De Jong and Bruch (2013), hold that transformational leadership strengthened organization by creating an environment of motivation for the employees. This motivated and energized employees enables them to achieve institutional goals hence increasing performance at large (De Jong & Bruch, 2013).

A research carried out by MacKenzie, Podsakoff and Rich, (2001) found a relationship between transformational leadership and organizational citizenship behavior/performance. Obiwuru, Okwu, Akpa and Nwankwere (2011) conducted a study on effects of leadership style on organizational performance using selected small scale enterprises in Ikosi-Ketu Council Development Area of Lagos State, Nigeria and found that transformational leadership style had positive but insignificant effect on performance. The cited studies indicate a positive significant effect of transformational leadership on organizational performance but there is no agreement as to whether the effect is significant. Thus, the H_1 : Transformation leadership has significant effect on the performance of audit firms.

METHODOLOGY

The study adopted a descriptive survey design. Primary data was collected from all the employees of MK Associates CPA (K) (total 45 in numbers) using a questionnaire. A pre-test was done and based on the pre-test results, the questionnaire was modified accordingly. The study used both descriptive and inferential statistics to analyze data. Data analysis was performed using SPSS version 21 and the results were presented using tables.

ANALYSIS AND FINDINGS

Simple linear regression analysis was used to establish the nature and magnitude of the relationship between the independent variable and the dependent variable, and to test the predicted relationship. The value of R squared shows the amount of variation in organizational performance caused by transformational leadership style. The unstandardized coefficients show the amount of change in the dependent variable attributable to the amount of change in the predictor variable. The F-statistics measure the goodness of fit of the model. The statistical significance of the hypothesized relationship was interpreted based on R^2 , F, t, β and p values. The regression model used was: $Y = \beta_0 + \beta_1 X_1 + \epsilon$, where Y=Organizational performance; β_0 = Intercept; β_1 = Coefficient; X_1 =Transformational leadership and ϵ =Error term.

Response Rate

This study targeted 45 respondents from the MK Associates CPA (K). Table 1 gives detailed information on the response rate of the study.

Table 1: Response Rate

| Response | Frequency | Percentage |
|---------------|-----------|------------|
| Responded | 45 | 100.0 |
| Not responded | 0 | 0.0 |
| Total | 45 | 100.0 |

As indicated in Table 1, all the questionnaires issued were all filled and returned. Hence, all were used for analysis representing a response rate of 100%. Mugenda and Mugenda (2003) prescribed 50% as the minimum required rate of response.

Distribution of Respondents by Age Group

The study sought to determine the distribution of respondents by age group. Table 2 shows the distribution of the respondents according to their age.

Table 2: Age

| Age Bracket | Frequency | Percent |
|----------------|-----------|---------|
| 21-30 years | 22 | 48.9 |
| 31-40 years | 17 | 37.8 |
| 41-50 years | 4 | 8.9 |
| Above 51 years | 2 | 4.4 |
| Total | 45 | 100.0 |

The results in Table 2 indicates that a majority of employees were between 21 to 40 years (86.7%) while the least age, 41-50 years 8.9 and above 51 years (4.4 %). This was attributed to the absorption of younger employees in the work environment.

Highest Level of Education

The distribution of the respondents according to the educational levels attained is presented in Table 3.

Table 3: Level of Education

| Educational Level | Frequency | Percentage |
|-------------------|-----------|------------|
| Certificate | 3 | 6.7 |
| Diploma | 7 | 15.6 |
| Graduate | 22 | 48.9 |
| Postgraduate | 13 | 28.9 |
| Total | 45 | 100.0 |

The results in Table 3 show that more than 77.78% (35) of the respondents had a graduate degree or postgraduate level of education, 15.6% (7) had diplomas. Further, only 6.7% (3) of the respondents had certificate level of education. This indicated that the respondents were educated enough to know about transformational leadership and organizational performance.

Test of the Hypothesis

The objective of the study was to establish the effect of transformational leadership on organizational performance. A hypothesis that transformational leadership has significant effect on the performance of audit firms was tested by using simple linear regression analysis. Table 4 presents the results of the analysis.

Table 4: Simple Linear Regression Results for the Effect of Transformational Leadership on the Performance of Audit Firms

| Model Summary | | | | | |
|---|-----------------------------|--------------------|--------------------------|-----------------------|-------------------|
| Model | R | R Square | Adjusted R Square | Std Error of Estimate | |
| | 1 | 0.840 ^a | 0.705 | 0.668 | 0.870363 |
| ANOVA | | | | | |
| Indicator | Sum of Squares | df | Mean of Square | F | Sig. |
| Regression | 22.311 | 4 | 5.578 | 8.2514 | .002 ^b |
| Residual | 27.065 | 40 | 0.676 | | |
| Total | 49.376 | 44 | | | |
| Regression Coefficients | | | | | |
| | Unstandardized Coefficients | | Standardized Coefficient | t | Sig |
| | B | Std. Error | Beta | | |
| Constant | 5.177 | 1.626 | | 3.184 | .002 |
| X ₁ | .259 | .183 | .140 | 1.419 | .158 |
| X ₂ | .173 | .146 | .112 | 1.185 | .238 |
| X ₃ | .170 | .205 | .080 | .830 | .408 |
| X ₄ | .289 | .222 | .134 | 1.298 | .197 |
| Dependent Variable: Organizational Performance | | | | | |
| Predictor Variable: Transformational Leadership | | | | | |

From Table 4, R is 0.840 showing a high positive correlation between transformational leadership and performance of audit firms. R^2 is 0.705, which indicates that 70.5% of the total variance of the dependent variable (organizational performance) is explained by the independent variable (transformational leadership). Only 29.5% of the variance of the dependent variable is explained by other factors which are not part of the study.

The ANOVA result shows that p-value (0.002) which is less than the level of significance (0.05) implying that the model is significant. Additionally, the F computed 8.2514 is greater than the F-critical (3.84) implying the model is significant in predicting the relationship between transformational leadership and organizational performance. The regression coefficients indicate that a one unit change in transformational leadership components leads to 0.259, 0.173, 0.170 and 0.289 increases in performance. The findings are in agreement with those of a previous study by Loof and Heshmati, 2006) who found that transformational leadership positively and significantly affects organizational performance but disagrees with those of Obiwuru, Okwu, Akpa and Nwankwere (2011) who established that transformational leadership had positive but insignificant effect on organizational performance.

CONCLUSION

The study sought to determine the effect of transformational leadership on the performance of audit firms. The study was conducted through a descriptive design. The study adopted both descriptive and inferential statistics to analyze the data. The study tested and confirmed the hypothesis that transformational leadership has a significant effect on the performance of auditing firms. The study recommends further investigation of the study variables not only in other audit firms in Kenya and beyond but also in other contexts.

REFERENCES

- Anjali, K.T., & Anand, D. (2015). Intellectual stimulation and job commitment: A study of IT professionals. *IUP Journal of Organizational Behavior*, 14(2), 28-41 http://www.iupindia.in/Organizational_Behavior.asp
- Bass, B. M., & Avolio, B. J. (2004). *Improving Organizational Effectiveness through Transformational Leadership*. California: Sage Publications.
- Bhat, A. B., Rangnekar, S., & Barua, M. (2013). Impact of Transformational Leadership Style on Organizational Learning. *Elite Research Journal of Education and Review*, 1(4), 24-31.
- Chen, L.Y. (2004). Examining the effect of organization culture and leadership behaviors on organizational commitment, job satisfaction, and job performance at small and middle-size firms in Taiwan. *Journal of the American Academy of Business, Cambridge*
- Doody, O., & Doody, C. M. (2012). Transformational Leadership in Nursing Practice. *British Journal of Nursing*, 20 (21), 1212-1224.
- Garcia-Morales, V. J., Llorens-Montes, F. J., & Verdu-Jover, A. J. (2008). The Effects of Transformational Leadership on Organizational Performance through Knowledge and Innovation. *British Journal of Management*, 19(4), 299-319.
- Johnson, J., Rockkind, J., & Doble, J. (2009). A mission of the heart: *What does it take to transform a school?*
- Koontz, H., & Donnell, C. (1993). *Introduction to Management*. New York: McGraw-Hill Inc.
- Kunhert, K. W. (1994). Transforming Leadership: Developing People through delegation. In B. M. Bass, & B. J. Avolios, *Improving Organizational Effectiveness Through Transformational Leadership* (pp. 10-25). California: SAGE.
- MacKenzie, S. B., Podsakoff, P., & Rich, G. A. (2001). Transformational and transactional leadership and salesperson performance. *Journal of the Academy of Marketing Science*, 29, 115-134.
- Mugenda O. & Mugenda, A. (2003). *Research Method: Quantitative and Qualitative Approaches*. Nairobi: Africa Centre for Technology Studies (ACTS).
- Löf, H., & Heshmati, A. (2006). On the relationship between innovation and performance: A sensitivity analysis. *Economics of Innovation and New Technology*, 15(4-5), 317-344.
- Obiwuru, T.C., Okwu, A.T., Akpa, V.O., & Nwankwere, I.A. (2011). Effects of leadership style on organizational performance: a survey of selected small scale enterprises in Ikosi-Ketu Council Development area of Lagos State, Nigeria. *Australian Journal of Business and Management Research*, 1(7), 100- 111.
- Pedraja-Rejas, L., Rodríguez-Ponce, E., Delgado-Almonte, M., & Rodríguez-Ponce, J. (2006). Transformational and transactional leadership: a study of their influence in small companies/liderazgo transformacional y transaccional: un estudio de su influencia en las pequenas empresas. *ingeniare: revista chilena de ingeniería*, 14(2), 159.

Zacher, Hannes; Pearce, Liane K.; Rooney, David; McKenna, Bernard / Leaders' Personal Wisdom and Leader-Member Exchange Quality: *The Effect of Individualized Consideration*. In: *Journal of Business Ethics*, 121(2), 171-173