Audit Committee Characteristics And Quality Of Financial Statement Of Quoted Consumable Companies In Nigeria

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Abstract
The study interrogated the audit committee characteristics and quality of financial statement of thirteen (13) consumable firms quoted on the Nigerian Stock Market using the Ex-post facto research design. The study gathered data from the NSE factbook and financial reports published by the quoted companies covering from (2010-2018). The data were analyzed using the Descriptive statistics, Panel Correlation Matrix, Ordinary Least Square (OLS), and Hausman test. The dependent variable Quality of Financial Statement was measured using the Beneish M-score model while the independent variable was measured using audit committee financial expert, audit committee size, audit committee independent, audit committee. From the analytical output, the result showed that audit committee financial expert and Audit committee size has a positive relationship and insignificant to the quality of financial statement. Also, audit committee independent and audit committee has a negative relationship with quality of financial statement. The study recommends that the audit committee members should consist of the independent non- executive director with sound accounting know-how.
Keywords: *Earnings Management, Quality of Financial Reporting, Audit committee Financial Expert, Audit Committee Independent, Audit Committee Size.*

I. Introduction

The global financial crisis that leads to the recovery in the accounting irregularities and inadequate disclosure of financial reports, companies are expected to satisfy the investor and another prospective investor to make available the annual financial statement as at when due. The financial statement represents the performance and financial position to the shareholder within the time frame as stipulated by the law. The reports provide the investor with an insight to make the decision. IASB (2008) viewed the financial statement as a report that has been presented in an organized manner, and it is easier to interpret by management in other to make an informed decision. The accounting regulatory bodies highlighted the essence of quality of financial reporting by identifying some areas of concern in prior research on the operationalization in the measure of quality (Beest, Braam and Boelens, 2009).

Samaila, (2014) in Ibrahim and Abubakar (2019) opines that the financial statement serves as a measure of communicating the accounting numbers of the company activities to the various shareholders, stakeholders, investors and other users of the accounting information, the regulatory authorities ensures the quality of financial reporting standards. He further emphasized that the financial statement can be mesmerized by three factors namely; the decision of standard setters, accounting system adopted by the board; and management verdict and measures in applying the selected alternates.

The essence of audit committee in every organization is to ensure transparency, accountability for public confidence. The financial statement is the most relevant tool in every organization the shareholders, investors and stakeholders are interested in the financial report to enable the users ascertain the performance and the liquidity position within the calendar year. Schipper and Vincent (2003) in their work posited that the essence of the financial report shows the transaction and the information contained in the financial serves as prospectus for investors and the yardstick in the determining the performance of the board. As noted by Madawski (2012) posited that the quality of financial reporting is centered on the characteristics of the audit committee in the discharge of their duties.

The sole responsibilities of the audit committee are to ensure that the financial statement is prepared in compliance with the regulatory standard, company's internal control system are effective, reviewing of the management analyses on relevant issues in financial reporting and are to ensure that the report are true and fair from misstatement or inaccuracy in the financial report. The responsibilities of the audit committee is

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encapsulated in the Financial Reporting Council of Nigeria Act, 2011, section 15(4) stated the responsibilities as; (a) to oversee the affairs of finance, accounting system and compliance, (b) bargain the external auditors fees, (c) reviewing of the financial statement and related information and (d) ensure that the council complies with other regulatory requirements.

The study attempt to interrogate the association between audit committee characteristics and quality of financial statements of consumables quoted companies on the Nigerian Stock Market.

This paper consists of five (5) sections, one (1) Introductory and problem statement, two (2) Discusses the literature review, three (3) Methodology, fourth (4) Analysis and discussion of findings and finally, the fifth (5) conclusion.

II.   Review of Related Literature

2.1.1   Audit Committee Characteristics

The audit committee improves corporate governance of an organization thoroughly, the audit of financial reports, reviewing the internal controls, and improving on the various policies adopted by the board of directors. The audit committee was established by the Nigeria Code of Corporate Governance and the CBN code of governance in ensuring that firm's disclosure the relevant information's in their financial report (Ogoun, Edoumiekumo & Nkak, 2020). Audit committee is statutory set up curb fraudulent financial manipulations and to enhance the financial reporting quality. Similarly, they stressed that the audit committee responsibility is statutory and vested with the power to overseeing the functions and process of the financial reporting (Menon & Williams, 1996; Ormin, Tuta & Shadrach, 2015; Ogaluzor & Ohaka, 201). The committee was coined based on two strands by the regulatory authorities for management accountability to the board of directors and board of director's accountability to the shareholders. An effective audit committee is the willingness of the committee members to report any earnings manipulation intended to occur. Marriam (1998) posited that an audit committee encompassed 5 directors with limited operation with the financial reporting, that the audit committee provides an insight in ensuring the effectiveness of the firm account, internal control mechanism, recommendations on appointment and renumeration of the internal auditor.

2.1.2   Quality of Financial Statement

The quality of financial statement has received emphasis from the viewpoints of the shareholders, investors, regulatory authorities and scholars. The financial report reveals the economic activities that transpired within an accounting year to the various users of the information and also assist the board to evaluate the performance and to strategize for the next accounting year. Adebayo (2005) posited that the financial report is a medium of communicating the financial position of the firm to various shareholders. Tang, Chen and Zhijun (2008) stressed that the financial reporting quality. According to IFRS the preparation and disclosure of the financial report should be enforced and the sole responsibility of the auditor to escalate if the financial statement complies with the stipulated requirements of the standard. Businesses or organizations that manipulates the financial statement are faced with threat from the shareholders and investors. It is expected that a business reports the events that occurred within the accounting circle.

This study used the M-score as a proxy for quality of financial statement because it reveals the earnings manipulated by the consumable firms. The consumable firms that had an M-sore of less than -2.22 recommend that the firm will not manipulate their financial statement while an M-score that is greater than -2.22 implies that the consumable firm is likely to manipulate the quality of financial statement.

2.2   Hypothesis Premise

Onyabe, Joshua and Terzengwe (2018) explore audit committee independence, size and financial reporting quality of 15 quoted deposit money bank in Nigeria from (2007-2016). The data were extracted from the Nigerian Stock Exchange fact book and analyzed using the modified Jones model to measure the financial reporting quality. Stata 13 was used to analyzed the data. Their study revealed that audit committee independence, has a negative and significant impact on FRQ, also the audit committee size has a positive but insignificant effect on FRQ. The study suggested that members in the board should be independent and also consider the provisions of Nigerian code of corporate governance. Similarly, Ogoun, Edoumiekumo, and Nkak (2020) explored the audit committee attributes and audit lag of quoted industrial companies in Nigeria, the data were gathered from the Nigerian Stock Exchange fact book within (2012-2019). Descriptive statistics Ordinary Least Square and the Hausman were used to analyzed the data. Their findings show that audit committee financial expect and audit committee independence had a positive relationship with ARL also the audit independence showed a significant effect on ARL, Furthermore, audit committee meeting, audit committee size and big 4 had a negative relationship with ARL. Thus, the audit the audit committee meeting was a statistically significant 5% level of significance. Their study recommended that members of the audit committee should be non-executive directors with financial expertise and the modification of compositional requirements in the

Nigeria corporate governance code should be members with sound knowledge in accounting. In the same view, Moses, Ofurum and Egbe (2016) investigated audit committee characteristics and quality of financial reporting of fifteen banks quoted in Nigeria covering a period of 2010-2014 using the correlation research design. Researchers extracted data were analyzed using the SPSS statistics 22.0 and adopting the Jones (1991) modified model to measure quality or financial reporting. Their result found that audit committee independence and audit financial expert had a negative relationship on earnings management although audit committee financial expert was statistically significantly at 5% level of significant. While audit committee size and audit committee meeting had a positive relationship and statistically insignificant to earnings management. Their study recommended that managers and administrations of the banks should be abide to the ethics governing the standard also continuous orientations of the audit committee members to ensure influence on the financial quality reporting on their part.

Dabor and Dabor (2015) interrogated audit committee characteristics, board characteristics and financial reporting quality of 9 (nine) deposit money banks in Nigeria. The investigator adopted the Ordinary Least Square regression to analyze the data collected. Their results show that audit committee activities and audit committee reporting. The audit committee activities had a significant effect on the quality of financial reporting at 5% level of significance. Their study recommended that the central bank of Nigeria should ensure that the banks meet four times within a calendar year,

Although, Musa, Oloruntoba and Oba (2014) in their work examined the relationship between audit committee characteristics and financial reporting of 24 deposit money banks in Nigeria. The investigator collected data from the annual report of quoted banks between (2007-2010) and employed the multivariate regression. Their result found that audit committee size had a negative relationship with QFR, also audit committee expert and audit committee independent had a positive and significant relationship with QFR. It recommended that boards of directors only appoint qualified members with wealth of experience into the audit committee.

Moses (2016) explored audit committee size on the quality of financial reporting of fifteen quoted Nigerian banks. The investigator gathered the data from the end of the year report of quoted banks and using the modified Jones (1991) model. The data were analyzed using the Pearson Correlation Statistical tool and linear regression. From the analytical output, the study showed that audit committee size has no significant impact on the quality of financial reporting. The researcher suggested that the audit committee should be expanded, and the members should have a knowledge of accounting. Similarly, in the work of Moses (2019) he interrogated the relationship between audit committee composition and financial reporting. The sampled size was fifteen commercial banks covering 2009-2018. The Jones Model and Ordinary Least Square method was utilized to regressed the data. The analytical output revealed that audit committee composition comprising of the independent member had a positive effect on the financial reporting quality. From the study, it recommended that board of directors should ensure that members of the audit committee should be comprised of independent members who are duly qualified for the role.

Umobong and Ibanichuka (2017) in their work investigated the audit committee characteristics and financial reporting quality of consumable firms listed on the Nigerian Stock Exchange. The data were obtained from the NSE and regressed using the multiple regression model. The result from the analysis showed that an increase in the audit committee independence and members with financial expertise, firm age and frequent audit committee meetings produces quality financial reporting. In the work of Oji and Ofoegbu (2017) conducted a study on the characteristics of an audit committee on the financial reporting quality in River State. The study developed 145 structured questionnaires and distributed to the administrative staff. The computed respondents were analyzed using the Ordinary Least Square. From the analyzed result, the study found that audit committee independence, audit committee members' qualification, and audit committee monitoring function had a positive and significant effect on financial reporting. Their study suggested that qualification should be criteria for a member to be in the audit committee in other to speed up the financial reporting quality.

Uwuigbe, Olorunshe, Uwuigbe, Ozordi, Asiriuwa, Asaolu and Erin (2019) in their work on corporate governance and financial statement fraud, the compositional audit committee characteristics had any relationship with financial statement fraud. A sample of 20 firms were drawn using the stratified and simple random techniques covering 2012-2016 and data were regressed using the multiple regression. From the researcher analytical output, the study adopted the Beneish M-score to measure financial fraud and the showed that audit committee independence had a negative relationship and insignificant to financial statement fraud. Their study recommended that board of director should that members of the audit committee should be an expatriate in finance to increase the quality of financial reporting. Similarly, Anichebe, Agbomah and Agbagbara (2019) interrogated the corporate governance and financial statement fraud using the Beneish M-score to measure financial fraud statement of firms under the agricultural sector covering 2013-2017. The longitudinal design and binary logit regression technique were used to analyze the data. From the result output, the study revealed that audit committee effectiveness had a positive and statistically significant impact on

financial fraud statement. The study suggested that the agricultural companies should increase its members with sound financial accounting knowledge in other to improve the effectiveness of the audit committee.

From the extant reviewed literature, numerous scholars have interrogated the audit committee and quality of financial reporting using the discretionary accruals to measure quality of financial reporting. The works of (Musa, Oloruntoba & Oba 2014; Dabor & Dabor, 2015; Moses, 2016; Moses, Ofurum & Egbe, 2016; Umobong & Ibanichuka 2017; Onyabe, Joshua & Terzengwe, 2018; Moses, 2019). Although, few studies in Nigeria explored the audit committee characteristics using the Beneish M-score to measure the financial statement fraud. In the works of (Anichebe, Agbomah and Agbagbara, 2019; Uwuigbe, Olorunshe, Uwuigbe, Ozordi, Asiriuwa, Asaolu & Erin 2019). In light of the aforesaid gap this study would explore the consumable companies listed on the Nigerian Stock Exchange.

The study developed the hypothesis premise between audit committee characteristics and quality of financial statement. The hypothesis is stated in the null form;

Ho₁: There is no significant relationship between audit committee size and quality of financial statement.

Ho₂: There is no significant relationship between audit committee financial expert and quality of financial statement.

Ho₃: There is no significant relationship between audit committee independent and quality of financial statement.

Ho₄: There is no significant relationship between audit committee meeting and quality of financial statement.

III.   Methodology

The research adopted the panel data to collate data from the financial report of thirteen (13) consumable firms registered on the Nigerian Stock Exchange covering from (2010-2018). The Beneish M-score model was used to measure the quality of financial reporting. The model was developed by Beneish (1999) to uncover frauds that occurred or intended to manipulate its earnings. Therefore, the study adopted the descriptive statistics to measure the means and standard deviation and the ordinary least square was utilize for the econometrics analysis. The population of the study includes;

Table 4.1: *Population of the Study*

S/N	Consumables
1	Cadbury
2	International Brews
3	Guinness
4	Honey well
5	Champion Brew
6	Dangote sugar
7	Flour mill
8	Nestle
9	Nigeria brew
10	Enamelware
11	Northern flour
12	Pz cusson
13	Unilever

3.1   Empirical Model Specification

The empirical evidences on the aforementioned hypotheses premise on the audit committee characteristics and quality of financial statement. The regression equation can be computed as:

$Y = a_0 + \beta x_1 + \beta x_2 + \mathcal{E}$

The equation can be transformed into econometric model as;

QFR= $a_0 + \beta x_1$Acfe $+ \beta x_2$ Acind $+ \beta x_3$Acmeet $+ \beta x_3$Acsize $+ \mathcal{E}$

Where;

B= coefficient of parameter

$\mathcal{E}$= error term

QFR= Quality of Financial Reporting Proxies by M-Score.

ACFE= percentage number of committee member who has sound accounting knowledge.

ACIND= the level of percentage of non-executive director on the audit committee.

ACMEET= the total number of times the committee meet to review the annual year-end report.

ACSIZE= the total number of members in the committee.

IV.   Data Analyses and Interpretation

In analyzing the data, the study adopted the ordinary least square regressions, descriptive statistics and correlation to identify the audit committee characteristics and the quality of financial reporting of quoted consumable firms in Nigeria.

Table 4.2: *Descriptive Statistics*

	MSCO	ACFE	ACINED	ACMEET	ACSIZE
Mean	-2.427987	14.41436	10.69573	2.017094	2.735043
Median	-2.564300	0.000000	0.000000	0.000000	0.000000
Maximum	9.503600	83.30000	33.33000	6.000000	10.00000
Minimum	-15.25390	0.000000	0.000000	0.000000	0.000000
Std. Dev.	2.155767	19.60050	14.05120	2.161509	2.998256
Skewness	0.084757	1.282228	0.736716	0.260797	0.278193
Kurtosis	20.68590	3.929242	1.795166	1.311399	1.309770
Jarque-Bera	1524.996	14.41436	10.69573	2.017094	2.735043
Probability	0.000000	0.000000	0.000146	0.000494	0.000445
Sum	-284.0745	117.0000	1686.480	1251.400	236.0000
Sum Sq. Dev.	539.0905	0.000000	44564.83	22902.59	541.9658
Observations	117	117	117	117	117

Source: *Researcher Computation, 2020*

Table 2 reveal the mean value of quality of financial reporting of sampled consumable firms stands as -2.427987 with (Beneish model) standard deviation of 2.155767. This shows an average of the consumable firms manipulate their quality of financial statements showing that the nonconformity among the firm is quite large. The Audit committee financial expert (ACFE) mean depict 14.41436 with maximum and minimum values of 83.30000 and 0.000000 respectively with a standard deviation of 19.60050. This indicates that 14% of the consumable firms had committee members with sound financial knowledge. The audit committee independent executive director (ACINED) mean was 10.69573 with maximum and minimum values of 33.33 and 0.000000 with a standard deviation of 14.05120. This showed that approximately 10% of the consumable firms have an independent committee. The audit committee meeting (ACMEET) mean represent 2.017094 with maximum and minimum values of 6.000000 and 0.000000 with a standard deviation of 2.161509. The result revealed that most of the committee members attends meeting twice. Audit committee size (ACSIZE) mean depict 2.735043 with maximum and minimum values of 10.000000 and 0.000000 with the standard deviation representing 2.998256. from the analytical output, the result showed that 2% the consumable firms had three members in the audit committee.

Table 4.3: *Pearson Correlation Matrix*

Covariance Analysis: Ordinary
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Sample: 2010 2018
Included observations: 117

Correlation	MSCO	ACFE	ACINED	ACMEET	ACSIZE	TOTAL_ASSET
MSCO	1.000000					
ACFE	0.013583	1.000000				
ACINED	-0.082386	0.751725	1.000000			
ACMEET	-0.026439	0.680370	0.784749	1.000000		
ACSIZE	-0.003330	0.718404	0.807816	0.858683	1.000000	
TOTAL_ASSET	-0.473296	0.033911	0.031732	0.007641	-0.002408	1.000000

Source: *E-view 10 output*, *2020*

The Pearson correlation matrix was used to crisscross for the association between each explanatory variable and the dependent variable. The correlation analysis show that there exists positive relationship between the quality of financial statement and audit committee characteristics, audit committee financial expertise, but audit committee independent non-executive director, audit committee meeting and audit committee size negatively related.

Table 4: *Regression Result*

Dependent Variable	Independent Variable	Coefficient	Std. Error	t-Statistic	Prob.
M-score	Constant	-2.045156	0.254932	-8.022358	0.0000
	ACFE	0.017804	0.014375	1.238548	0.2181
	ACINED	-0.039563	0.024430	-1.619467	0.1082
	ACMEET	-0.022031	0.168498	-0.130751	0.8962
	ACSIZE	0.076593	0.130120	0.588632	0.5573
	TOTAL_ASSET	-0.045537	0.007998	-5.693617	0.0000
R-squared	0.246206	Adjusted R-squared	0.212252	Durbin-Watson stat	2.013632
F-statistic	7.251031	Prob(F-statistic)	0.000007		

Source: Researchers' Computation, 2020

Table 4 explores the coefficient of the explanatory variables, the t-ratios were reported and the probability. The value of R correlation stood at 24.6 (25% moderately). Similarly, the adjusted R-square stood at 21% resulting that the total variations in the dependent variable (M-score) were explained by the independent variables leaving the remaining 79% unaccounted for. The overall F-statistics (goodness-of-fit test) capable of prediction stood at a value of 7.251031, while the Durbin Watson stood at 2.013632 indicating the presence of serial correlation.

Table 4.5: *Hausman Test*

Correlated Random Effects - Hausman Test
Equation: Untitled
Test cross-section and period random effects

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	3.179169	5	0.6724
Period random	0.346703	5	0.9967
Cross-section and period random	2.967440	5	0.7050

** WARNING: estimated cross-section random effects variance is zero.

Cross-section random effects test comparisons:

Variable	Fixed	Random	Var(Diff.)	Prob.
ACFE	0.019953	0.017082	0.000067	0.7257
ACINED	-0.013481	-0.039127	0.000323	0.1533
ACMEET	-0.259576	-0.016373	0.023366	0.1116
ACSIZE	0.131108	0.074300	0.003777	0.3553
TOTAL_ASSET	-0.046686	-0.045967	0.000010	0.8177

Source: E-view 10, 2020

The result table 4.5 above shows the Hausaman test that was used to test the Fixed/Random Effects and to ascertain the appropriate model. The null hypothesis represents the Random Effects Model at (p>0.05), while the alternate hypothesis represents the Fixed Effect Model at (p<0.05).
From the analytical output, the result showed that the p-value of (0.6724) which is greater than 0.05%. The result shows that the Random Effects Model is a better model for the above relationship than the Fixed Effect Model.

Results from the Ordinary Least Square are summarized via decomposition;
1.   Audit committee financial expert (ACFE) has a positive and insignificant relationship with quality of financial statement. This implies that an increase with members with the financial know-how will increase the quality of financial statement.
2.   Audit committee independent (ACINED) has a negative and insignificant relationship with quality of financial statement. In essence a percent increase of the independent director on the committee will enhance the quality of financial statement
3.   Audit committee meeting (ACMEET) has a negative and insignificant relationship with quality of financial statement. This shows that committee members should be committed in attending meetings in other to increase the quality of financial statement, and

4.   Audit committee size (ACSIZE) has a positive and insignificant relationship with quality of financial statement. This implies that the size of the committee had an influence in the QFS.

V.   Conclusion and Recommendation

The study investigated the audit committee characteristics and quality of financial statement of quoted consumable firms trading on the Nigerian Stock Market. The empirical analytical output the study concludes that the decomposing of audit committee financial expert and audit committee size has a positive relationship with the quality of financial statement. An audit committee that consists of financial experts will reduce the mesmerizing carried out in the financial statement by the non-accounting expert.

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Appendix

Dependent Variable: MSCO

Method: Panel Least Squares

Date: 06/06/20   Time: 22:33

Sample: 2010 2018

Periods included: 9

Cross-sections included: 13

Total panel (balanced) observations: 117

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-2.045156	0.254932	-8.022358	0.0000
ACFE	0.017804	0.014375	1.238548	0.2181
ACINED	-0.039563	0.024430	-1.619467	0.1082
ACMEET	-0.022031	0.168498	-0.130751	0.8962
ACSIZE	0.076593	0.130120	0.588632	0.5573
TOTAL_ASSET	-0.045537	0.007998	-5.693617	0.0000

R-squared	0.246206	Mean dependent var	-2.427987
Adjusted R-squared	0.212252	S.D. dependent var	2.155767
S.E. of regression	1.913355	Akaike info criterion	4.185514
Sum squared resid	406.3630	Schwarz criterion	4.327164
Log likelihood	-238.8526	Hannan-Quinn criter.	4.243022
F-statistic	7.251031	Durbin-Watson stat	2.013632
Prob(F-statistic)	0.000007		