

Determinants Of Audit Quality Among Consumer Goods Companies Listed On The Nigerian Stock Exchange

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Abstract

This study examined the determinants of audit quality among Consumer goods companies listed on the Nigerian stock exchange from 2009 to 2018. This study made use of secondary data obtained from fact books, annual reports, and account of selected consumer goods company under study. The relevant data were subjected to statistical analysis Pearson Correlation while the diagnostics test conducted were Multicollinearity, Autocorrelation, Normality, and Heteroscedasticity Test. The study's findings showed that board size and company liquidity have a substantial positive influence on financial results, while audit fees, firm size, and audit committee meetings have a negative but non-significant impact. The study concluded that, since board size has a substantial positive effect on audit quality, the governmental body should track firms to ensure that the required board size is met as part of strategies to enhance audit quality among Nigeria's publicly traded consumer goods companies.

Keywords: audit fees, audit quality, board size, consumer goods sector, firm size.

JEL Classification: D21, G32, L21.

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1. Introduction

The recent string of audit failures around the world, especially in Nigeria, has left financial information users dissatisfied. Corporate controversies like the Enron and Andersen debacles revealed a high-quality audit level and considerable exposure to a variety of conditions that can affect the audit's quality (Amahalu & Abiahu, 2017). The Nigerian business climate has been criticized by some as being hostile to both domestic and foreign investors. The inability of the financial results to meet the demands of these consumer groups is one of the reasons for this assertion. Management inefficiencies, on the other hand, can result in unstructured financial statements. Normally, these financial statements do not reflect the true state of affairs and financial position of the company and therefore can harm future investors' decisions. Poor investment results will undermine the financial statements' integrity, decreasing cash flow and deteriorating the economic environment's situation. As

a result, auditors must address these issues by carrying out the audit task effectively and efficiently and producing a quality report as a result. As a consequence, the study investigated the variables that may impact the quality of the audit assignment, as well as the extent and degree of relationships between these factors and the achievement of high audit quality in consumer goods companies listed on the Nigerian Stock Exchange. The creation of financial records without errors, omissions, or biases is referred to as a high-quality audit. According to the organizing principle, audited financial statements are a monitoring instrument that provides financial records users with confidence (Dang, 2004).

Amahalu and Ezechukwu (2017) described audit quality as detecting mistakes and errors in financial statements and then reporting these content mistakes and errors using a two-dimensional construct. Since these characteristics are completely unrecognizable, researchers have relied on indicators such as audit independence, audit tenure, audit firm size, audit hours, audit fees, integrity, litigation pace, and discretionary accruals to measure audit quality. According to Amahalu, Moses, and Obi (2017), audit tenure, audit firm size, and audit independence all have a favorable and statistically significant relationship with audit quality. The Board of Directors is responsible for the day-to-day affairs of the company and must keep a close watch on how shareholders' money is invested. The fact for financial reporting stakeholders is that corporate financial reporting issues have been on the rise in recent years.

Despite the presence of regulatory bodies, the difficulties of ensuring financial reporting transparency and auditing persist. As a consequence, to maximize the value of audit and assurance functions, it is important to explore the factors that influence audit quality. In the consumer goods industry, Nigeria is currently experiencing an increase in research in this area. This study aims to look into the factors that influence audit quality in consumer goods companies listed on the Nigerian Stock Exchange.

2. Literature Review

2.1 Conceptual Review

2.1.1 Audit Quality

Since the audit process requires the application of test protocols that may not be followed by consumers of financial statements, audit quality is debatable but difficult to understand (Knechel, 2013). (DeAngelo, 1981; Hussainey, 2009). DeAngelo (1981) described audit quality as the shared probability that the auditor would both (a) discover and (b) disclose a breach of the client's accounting systems. Audit standard, according to Hussainey (2009), is the consistency with which an auditor delivers evidence to investors.

The auditor's integrity, diligence, and consideration in the audit process will lead to a reliable and fair interpretation of financial statements, which is what audit quality is all about (Arrunada, 2000). The consistency of the audit was described by Arens, Elder, Beasley, Best, Shailer, and Fielder (2011) to demonstrate how well an audit identifies and reports material errors in financial statements. The identification facets represent auditor integrity, whereas reporting facets indicate ethics or auditor fairness, especially independence. The most prominent financial reporting errors are aggressive sales or discretionary accruals.

In this study, audit quality is described as the auditor's ability to carefully uncover and reveal significant misstatements in the financial report to the stakeholders. The most prominent financial reporting errors are aggressive earnings or discretionary accruals. Discretionary accruals are those that management can influence and are mostly used to achieve the optimal profitability or earnings. The auditor's job is to report any non-fair discretionary accruals in order to discourage financial statements from being misrepresented. Audit Quality (AQ) is one of the predictor variables discovered in this study.

2.1.2 Board Size

One of the well-known major determinants of audit quality is board size. Many researchers have concluded that greater board sizes mean more efficient governance, and therefore consequently larger boards are stronger. The board of directors' primary responsibility is to ensure that all stakeholders receive high-quality disclosures on the company's financial and operating performance (UNCTD, 2006). According to Adebisi (2017), a wider

board increases the quality of financial reporting. This is in line with Adams and Mehran's results (2002). The board, according to Fama and Jensen (1983), is the firm's highest-level management structure, with overall responsibility for managing the firm's operations.

Few academics, on the other hand, contend that a bigger board is counterproductive to successful audit quality. The view's supporters claim that the bigger the board, the more difficult it would be to make decisions. For example, Vafeas (2005) discovered that a large board size reduces the knowledge content of revenue, resulting in poorer audit quality.

2.1.3 Audit Committee Meeting

The existence of an audit committee was first suggested in 1967 by the American Institute of Certified Public Accountants in the hopes of strengthening the reporting process. According to the Sarbanes Oxley Act (2002), cited by Sukman and Barnawati (2020), an audit committee is a committee appointed by the board of directors to oversee the accounting and financial auditing processes of a company. This audit committee aims to assist the board of directors in carrying out their supervisory function and to increase the audit efficiency of corporate organizations (Putra & Ratnadi, 2018). (Li et al., 2012). To serve this role, the audit committee must meet regularly, since the more they meet, the more they debate and make decisions.

2.1.4 Audit Fees

The audit fee is defined as the amount payable to the auditor for completing an audit task. That is the amount charged by the auditor for any work done to express an opinion on the real and reasonable state of affairs or condition of the client's business. Iskak (1999) described the audit fee as the fee charged to a client for financial audit services by a public accountant, according to Suharli and Nurlaelah (2008). This is in line with the Securities and Exchange Commission's Final Rule (Yuniarti, 2011), which states that the audit fee is the amount paid with the most recent fiscal year's annual audits and financial statement assessments. The size of the audit fee will vary based on the complexity of the services, assignment risk, the Public Accountants Organization's cost structure, the appropriate level of expertise, and other professional considerations.

Furthermore, Hoitash, Markelevich, and Barragato (2007) assumed that the amount of the audit fees equaled the overall volume of the auditor's expenses. Turley and Willekens (2008) contributed to this by suggesting that the creation of audit fees is determined by three composite variables: sophistication, client size, and related risk. Audit fees are fees charged to auditors that represent the expense of the job performed by the public auditors as well as the possibility of lawsuits (Choi, 2009).

2.2. Theoretical Framework

Stakeholder theory

The stakeholder theory is the foundation of this study. The interaction between an organization and its stakeholders is the subject of stakeholder theory. While Roberts (1992) claimed that Ansoff (1965) was the first to use the word "stakeholder theory," research shows that the term "stakeholder," the fulcrum of the stakeholder theory, was first used in 1947. (Johnson 1947).

Stakeholder theory has given rise to certain conclusions. They can be found in stakeholder literature in a variety of areas, including strategic management, CSR, business and environment, and business ethics (Harrison & Freeman 1999; Freeman 2005; Belal 2008; Smith 2008).

These conclusions, which can be summarized as follows, suggest their scope and provide overall insight for this theory.

1. From the perspective of a single focal organization, stakeholders are defined.
2. To accomplish its objectives, an organization must successfully control its partners.
3. There are several types of stakeholders, and these groups frequently have competing interests.
4. A company needs to balance the competing needs of stakeholders in the external and internal worlds.

5. Stakeholders exert pressure on an organization because they foresee or have an interest in something.
6. The willingness of stakeholders to exert leverage on an organization is determined by the stakeholders' organizational characteristics.
7. An organization's owners have economic, social, and environmental commitments.

The stakeholder theory is a natural continuation of the organization theory. In every organization, more than the principal and their agents are concerned, according to the theory. Other relationships between those with a concern in the entity's affairs include the host party, creditors, bankers, government, among others. This means that the entity is under more pressure to supply information, and the auditor is under more obligation to audit the financial statement (Freeman, 1984; Jones & Wicks, 1999; Donaldson and Preston, 1995; Jones, 1995)

2.3. Empirical Review

2.3.1. Liquidity and Audit Quality

The empirical literature has looked at whether liquidity affects audit quality. In a survey of Taiwanese listed companies, Kuo and Lin (2014) discovered that market liquidity is positively linked to audit efficiency for those listed on the Taiwan Stock Exchange.

2.3.2 Audit Committee Meetings and Audit Quality

Salawu, Okpanachi, Yahaya, and Dikki (2017) examined the influence of audit committee meetings and experience on audit quality in a sample of Nigerian publicly traded consumer goods firms. The audit standard was assessed using discretionary accruals (DAC). An updated, cross-sectional variant of Jones' model was used to calculate DAC. Their results revealed that the audit committee meeting had a significant positive impact on the audit quality.

However, Asiriwa, Aronmwan, and Uwuigbe (2018) discovered that audit committee meeting frequency is not a major determinant of audit quality. As a result, the number of days the committee meets each month has no impact on the nature of the audits published by the companies.

2.3.3. Audit Fee and Audit Quality

Thornton and Moore (1993) investigated how audit fees are measured and how they affect auditor selection in Elke and Schroé (2010). Amahalu, et al. (2017) discovered that audit fees and audit efficiency have a clear and statistically significant relationship. At a 5% significance level, the audit fees were also empirically tested to see if they had a statistically relevant association with the audit quality of banks listed on the Nigerian Stock Exchange board.

2.3.4 Board Independence and Audit Quality

The theory behind board independence and audit performance is that the outside director has more time to review management so they have strong confidence in building and preserving their reputation as thoroughbred decision-makers. The efficiency of this power, on the other hand, is dependent on its autonomy from management. The independence of the board is also required to improve audit quality. The independence of the board is also required to improve audit quality. Chen and Zhang investigated the influence of the corporate governance code on earnings management for Chinese publicly traded firms (2012). For five years, Olaoye and Adewumi (2018) examined the effect of corporate governance on the audit quality of Nigeria's listed deposit money banks (2006 to 2015). They discovered that including an audit committee and independent managers helped to ensure a higher-quality audit. A panel data regression technique was used because the data had both time series and cross-sectional attributes. The independent directors on the board had a positive and significant effect on the audit quality of Nigeria's classified Deposit Money Banks, according to the study.

3. Methodology

3.1 Research Design

Ex post facto analysis is used in this report. Ex-post facto analysis design is used to establish a cause and effect association between the variables that correspond. The study's population consists of all twenty-five (25) consumer goods firms listed in the Nigerian Stock Exchange's (NSE) factbook and reported on the NSE's website as of December 31, 2018. The non-probability approach was used to determine the sample size. The study used the judgmental sampling approach, which was based on the availability of up-to-date annual financial statements. The sample-set for the study includes thirteen (13) of the twenty-five (25) consumer goods firms listed on the Nigerian Stock Exchange for which the researcher was able to access annual financial statements for the period ended December 31, 2018.

3.2 Measurement of Variables

Variables	Measurements	Sources
Audit Quality (AQ)	Measured as negative absolute value of the residual from the Dechow and Dichev (2002) model modified by McNichols (2002)	Dechow & Dichev (2002), McNichols (2002)
Independent Variables		
Board Size (BS)	Measured as the number of board members divided by the total assets.	Mgbame, Eragbhe & Osazuwa (2012)
Audit Committee meeting (AUDCM)	Measured as the number of times the audit committee members meet in a year	Salawu, Okpanachi, Yahaya & Dikki (2017)
Board Independence	Proportion of non-executive directors on the board	Olaoye & Adewumi (2018)
Audit Fees (AUDFEES)	Measured with natural logarithm of audit fees	Abdul-Rahman, Benjamin & Olayinka (2017).
Liquidity (LIQ)	Current assets divided by current liabilities	Hamidzadeh and Zeinali (2015)
Firm Size (FMS)	Measured with natural logarithm of total assets	Dehkordi & Makarem (2011)

Note: Author's Compilation 2020.

The dependent variable is measured using negative absolute value of Discretionary accrual obtained from modified Jones model:

To estimate abnormal accruals (DAC_{it}) for company i in year t , the following cross-sectional regression is run

$$TA_{it} / A_{i,t-1} = \beta_1 [1/A_{i,t-1}] + \beta_2 [\Delta REV_{it} - \Delta AR_{it} / A_{i,t-1}] + \beta_3 [PPE_{it} / A_{i,t-1}] + \varepsilon_{it} \quad (1)$$

Where:

TA_{it} = Total Accruals of firm i for year t .

The Total Accrual is obtained as Net Profit after Tax (NPAT) – Net Cash Flow from Operations (CFO)

ΔREV_{it} = change in revenue for company i at time t scaled by total assets at $t-1$;

ΔREC_{it} = change in revenue from year $t-1$ to year t for company i scaled by total assets at $t-1$;

PPE_{it} = Gross Property, Plant and Equipment of company i at year t

$A_{i,t-1}$ = lag of total assets in year $t-1$ for company i ;

ε_{it} = the residual of company i for time t ;

The industry year specific parameter estimates from the above model is then used to estimate company specific normal accruals (NA_{it}) for company i in year t as a percent of lagged total assets; that is,

$$NA_{it} / A_{i,t-1} = \beta_1 [1/A_{i,t-1}] + \beta_2 [\Delta REV_{it} - \Delta REC_{it} / A_{i,t-1}] + \beta_3 [PPE_{it} / A_{i,t-1}] \quad (2)$$

Discretionary or Abnormal Accruals for company *i* in year *t* is the error term in equation (2) which is given as

$$DAC_{it} = TA_{it} / A_{i,t-1} - (\beta_1 [1/A_{i,t-1}] + \beta_2 [\Delta REV_{it} - \Delta REC_{it}] / A_{i,t-1}) + \beta_3 [PPE_{it} / A_{i,t-1}] \quad (3)$$

The absolute value of discretionary accruals (DAC_{it}) is the measure of audit quality. The lower the absolute value of the discretionary accrual, the higher the audit quality.

Models Specification

The following models were used to test the hypotheses as follows:

$$AQ_{it} = \beta_0 + \beta_1 BS_{it} + \beta_2 AUDCM_{it} + \beta_3 AUDFEES_{it} + \beta_4 FMS_{it} + \beta_5 LIQ_{it} + \beta_6 BI_{it} + \mu_{it} \quad (4)$$

Where:

β_0 = Constant term (intercept);

β_{it} = Coefficients to be estimated for firm *i* in period *t*;

μ_{it} = Error term/unexplained variable(s) for firm *i*, in period *t*.

4. Results and Discussions

Diagnostic Tests

A variety of screening procedures must be performed to do regression analysis. Correlation analysis is a method for evaluating the course of a relationship between two variables. A normality test, a formal difference test to determine the type of regression, a heteroscedasticity test, and a multicollinearity test were also performed.

Pearson Correlation and Multicollinearity Tests

Before pointing at the coefficient of regression, the Pearson correlation matrix indicates the course and frequency of the relationship between the variables. In behavioural sciences, the correlation coefficients of .10, .30, and .50 are referred to as low, medium, and high coefficients, respectively. Table 1 indicates that board size (BS) has a weak positive association with audit quality (AQ), while board independence (BI) and audit committee meeting (AUDCM) have a weak negative correlation with audit quality (AQ). Audit fees (AUDFEES) have had a poor negative correlation with audit accuracy (AQ). Furthermore, audit quality was positively correlated with liquidity (LIQ) and firm scale (FMS) for firm characteristics.

Furthermore, Table 1 reveals that the Variance inflation factor for the variables is less than 10. This shows that the multicollinearity assumption was not broken and that the independent variables were not profoundly associated.

Table 1. Summary of Pearson correlation and Multicollinearity Test

Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)	Mean VIF
(1) AQ	1.000							
(2) AUDFEES	-0.004	1.000						
(3) FMS	0.034	0.815	1.000					
(4) LIQ	0.176	0.111	0.216	1.000				
(5) AUDCM	-0.074	0.147	0.254	-0.104	1.000			
(6) BS	0.238	0.187	0.235	-0.041	0.135	1.000		
(7) BI	-0.079	-0.485	-0.608	0.118	-0.385	-0.528	1.000	
VIF		3.07	4.19	1.21	1.21	1.43	2.53	2.27

Note: Author's Computation 2020.

Heteroscedasticity test and Autocorrelation Test

The non-significance of the Breusch-Pagan Test of p-values of 0.0001 suggests an issue with heteroscedasticity, as seen in Table 2 since the null of homoscedasticity is rejected at a 1% level of significance. The Wooldridge test, on the other hand, with a p-value of 0.1725, shows that there is no autocorrelation.

Table 2. Test of Heteroscedasticity and Autocorrelation

	Chi2	F	P – Value	Decision
<i>Breusch-Pagan Test</i>	15.59	-	0.0001	Reject Null
<i>Wooldridge test</i>		2.104	0.1725	Null not Rejected

Notes: Author’s Computation 2020.

Specification Tests

Table 3 shows the result of the various specification tests including the F-test which determines the presence of firm effect or otherwise and the Hausman test for the systematic difference in coefficient. Based on the result of the F-test, with a p-value of 0.1021, it can be concluded that there is no firm effect. The implication is that pooled OLS is appropriate for this study. In addition, the Ramsey RESET test with a p-value of 0.6235 indicates that the null hypothesis of no omitted variable bias could not be rejected implying that the model is correctly specified.

Table 3. Specification Tests Results

	Chi2	F	P – Value	Decision
<i>Firm Effect Test</i>	15.59	1.61	0.1020	Null not Rejected
<i>Hausman Test</i>		25.24	0.0003	Null Rejected
<i>Ommited Variable</i>		0.59	0.6235	Null not rejected

Note: Author’s Computation 2020.

Regression Analysis

The determinants of audit quality are examined in this study. The coefficient, or weight of regression, is needed when examining the determinants of audit quality. The orientation of the relationship between the dependent variable and the independent variables is shown by the negative or positive. Table 4 reveals that board size has a favorable effect on audit efficiency of listed consumer goods firms in Nigeria, which is large at 5%, with a coefficient and p-value of 0.128 and 0.0137, respectively. The finding suggests that the higher the number of directors on the board, the more likely the corporation is to deliver high-quality audits, as more members would allow for more control of auditing and associated operations in the company. The findings are consistent with those of Uwalomwa, Daramola, and Anjolaoluwa (2014), who discovered that board size has a substantial positive impact on audit results. The findings of the study agree with those of Aguilar and Barbadillo (2000), who discovered a strong and important association between board size and audit quality.

The results also reveal that firm liquidity has a favorable effect on the audit quality of listed consumer goods firms in Nigeria, with a 1 percent significance. This finding is consistent with Hamidzadeh and Zeinali's (2015) report, which found that liquidity has a substantial positive effect on companies listed on the Teran Stock Exchange.

Audit fees have a negative but non-significant impact on audit quality for consumer goods firms listed on the Nigerian Stock Exchange, as seen in Table 4. The assumption is that providing financial incentives to audit firms in the form of higher audit fees would not result in improved audit quality for Nigeria's publicly traded consumer goods companies. These findings contradicted those of Abdul-Rahman, Benjamin, and Olayinka (2017), who discovered that audit fees decide audit quality. The findings, on the other hand, support those who say that the audit fee has no substantial effect on audit efficiency.

Table 4 also indicates that board independence has a negative but non-significant effect on audit results, meaning that the number of directors on the board, rather than the percentage of non-executive directors, is what matters. Related findings have been published in previous studies. However, the outcome is contradictory to assumptions and previous findings that showed a substantial positive effect of board independence on audit quality (Chen & Zhang, 2010; Olaoye & Adewumi, 2018).

Furthermore, the findings in Table 4.5 showed that the scale of the firm and the number of audit committee meetings had a non-significant negative impact on audit efficiency. The presumption is that the size of the company has no bearing on the nature of the audit.

Table 4. Result of random effect regression analysis (Dependent variable = AQ)

Variables	Expected Sign	Coefficient	t – value	P - value
AUDFEES	+	-0.00615	-0.43	0.666
FMS	+	-0.000844	-0.09	0.911
LIQ	+	0.00408***	1.94	0.0071
AUDCM	+	-0.00692	-0.93	0.371
BS	+	0.128**	2.31	0.0137
BI	+	-0.0180	-0.34	0.664
Constant		-0.0317	-0.22	0.850
Number of Obs			116	
R ²			0.104	

Note: Authors Computation 2020 *** p<0.01, ** p<0.05, * p<0.1.

5. Conclusion and Recommendations

The determinants of audit quality among consumer goods companies listed on the Nigerian Stock Exchange group are examined in this study. Board composition, audit committee meetings, board transparency, audit costs, liquidity, and company size are also factors to consider. According to the findings of the study, board size and firm liquidity are significant determinants of audit quality among Nigeria's publicly traded consumer goods companies. Other control factors, such as audit committee meetings and board independence, had little impact on audit quality, according to this study. In addition, the study found no evidence that audit benefits, especially audit fees, have a major effect on audit quality. As a result of the findings, the study advises that consumer goods companies in Nigeria maintain a relatively small board of directors and pay close attention to the management of their liquidity risk, as these two factors have a major impact on audit efficiency in the field. Furthermore, as part of strategies to encourage audit efficiency among consumer goods firms in Nigeria, the regulatory agency should track the firms to ensure that they stick to the threshold board scale.

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