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IFRSandAudit Committee Mechanisms Impact on Audit Quality ofListed Firms inNigeria

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Abstract

This research investigates IFRS interaction with audit committee mechanisms on audit quality of listed firms in Nigeria. Data were collected from listed firms in Nigeria. Audit committee independence and audit committee meeting were interacted with IFRS audit quality, factoring in instrumental variables in the construct. The findings indicate that audit committee independence and audit committee meeting were significant and negative on audit qualitysince IFRS adoption in Nigeria. The study suggests that future researchers should examine the effect of audit committee religion, spirituality, ethnicity, nationality and attitude to risks under IFRS adoption on how they translate to audit quality of listed firms on a country specific basis and cross-country level using other estimation methods.

Keywords: IFRS Adoption, Audit Committee Independence,Audit Committee Meeting, Audit committee Gender Diversity, Audit Quality.

1.0 INTRODUCTION

Since emergence of the international financial reporting standard(IFRSs) by the international accounting standard board(IASB), firms in over one hundred and fifty (150) developed and developing countries have embraced it for the purpose of reporting earnings in a uniform manner.The international financial reporting standards were published in 2001 with the aim of providing a single set of high qualityand uniform accounting standards among firms globally. For firms in Nigeria, adoption of IFRS was from the year 2013 upward. Wu and Zhang (2009) state that the adoption of IFRS particularly in the emerging markets affects the role of accounting conservatism in firms, enables auditors to thoroughly assess the quality of the financial reports before issuing unqualified audit opinion regarding the true and fair view of the concerned firm state of affairs.

Chand and White (2007), posit that reporting in the same regulatory framework across different jurisdictions and continents improves transparency, enables accounting results to be more informative for valuation purposes and enhancement of investment decision making by investors. The end point of IFRS adoption and implementation is to influencefinancial reporting and audit quality in firms. The audit committee is a vital component of corporate governance which oversees the financial reporting process in firm (SOX, 2002; DeZoort & Hermanson, 2002).It is as an integral part of corporate governance mechanism which assist in the coordination ofboard directors, the internal auditors, and the statutory auditors to achieve quality financial report and audit in a company. Hence, Majiyebo, Okpanachi and Nyor (2018) point out that audit committee is the fundamentalto quality financial reporting and audit in firms in the light of incessant corporate collapse. Firms which frequently engage financial experts on their audit committee tend to report higher quality earnings than those which do not (Fela et al. 2003; Bedard et al .2004; Abbot, Parker and Peter, 2003; Krishnan, 2005; Dhaliwal et al .2006).

Majiyebo etal. (2018), Magrath and Weld (2002), Rezaee (2005), Al-Absy, Ismail and Chandren (2018) further stress that the corporate collapse like Enron WorldCom and Arthur Andersonafter the external auditor reportwas hinged on the lack of formidable audit committee in the firms.Prior to the demise of the multinational firms, incidence of earnings manipulation and smoothing by the board directors and managers was rife in addition to the existence of ineffective audit committee (Hasnan, Abdul-Rahman &

Mahenthiran, 2013; Sulaiman, Danbatta, & Rahman, 2014). Al-Najjar and Clark (2017) add that if audit quality may be at its peak, audit committee mechanisms possess a remarkable capacity to contribute to the environment of legitimacy and public trust in financial statements of firms and the capital markets at large.Miko and Kamardin(2015),note that the role of the audit committee membersin reducing manipulation of accounting numbers in firmsand in certifying the quality of financial reporting is premised on the depth of their accounting expertise, IFRS knowledge and training from time to time.Thus, audit committee members' versatility in accounting standards is not onlya basic impetus for transparent financial reporting but is fundamental in reducing the possibility of managers and board directors engaging in earnings manipulations in firms. The presence of at least one member in the audit committee consisting of independent members with financial and accounting standard expertise is associated with a lower chance of positive discretionary accruals in firms (Bedard, et al. 2004; Carcello et al. 2006, DeFond, Hann & Hu, 2005).

The Securities and Exchange Commission Code of 2011 emphatically stress that for the audit committee to be fully effective, majority of the members must be independent directors with the requisite accounting expertise to discharge the expected duties. Birla Committee (2000) opine that a qualified and independent audit committee with requisite financial and knowledge of accounting standards in a firm goes a long way enhancing the credibility of the financial disclosures and promotion of transparency. This underscores the interplay between audit committee independence and accounting standards at enhancing audit quality. Duchin, Matsusaka and Ozbasc (2010) stress that a relatively high proportion of independent directors in audit committee would enhance the objectivity, reliability and transparency of the financial reporting and disclosures which in turn impacts on audit quality, strengthens the confidence of investors, both potential and existing investors in capital market. The Sarbanes- Oxley Act of 2002 strongly encouraged that firms with less than 100% independent audit committee members be delisted (Romano, 2005). This directive has the likelihood of strengthening oversight function,discouraging undue management manipulation and reduces conflicting pressure of powerful groups in firms (Hundal, 2013).

Besides the financial expertise of members of the audit committee, they are expected to demonstrate competence, independence and diligence, which among others include regular holding of meetings to assess issues peculiar to pecuniary and non-pecuniary in nature. Chan, Liu and Sun (2015); Ghafran and O'Sullivan (2017), Lisic, Myers, , Seidel and Zhou (2019) opine that academic researchers now concentrated on the usefulness of audit committee characteristics and how they influence audit quality in the light of IFRS adoption. Specifically, Ghafran and O'Sullivan (2017) state that audit committee strands viz – a – viz audit committee size, independence, meeting frequency and the presence of financial expertise are correlates of quality financial reporting and audit in firms.When audit committee members are independent and hold meetings frequently, it assists them to effectively monitor, report and challenge the unethical activities of managers and external auditors (Gopinath & Allen, 2010). Abbot,et al. 2003); Carcello and Neal (2000, 2003) surmise that the frequency of audit committee meeting is fundamental to reducing firm-specific agency cost variables and influence the thoroughness of external auditors' reports in a firm which is capable of boosting investors' confidence.

Frequency of meeting by members of audit committee is very germane towards overseeing the activities of the board of directors and to see the extent with which the external auditor is objective in the discharge of audit assignment in a firm. Beasley, Carcello and Hermanson (2000) point out that the audit committee meetings have the possibility of reducing fraudulent financial reports. Thiruvadi and Huang (2011) add that audit committee frequency of meeting implies better financial reporting and good corporate governance outcomes. The frequency of audit committee meeting enables the audit committee to remain informed and knowledgeable about accounting and auditing issues in order to direct internal and external audit resources for addressing the matter in a timely manner (Abbott, et al , 2003). Ruzaidah and Takiah (2004) further add that the frequency of audit committee meeting in a firm assist in better financial reporting and timely release of audited financial statements because they help in monitoring management roles and responsibility.

There has been strong advocacy for female gender inclusivity in corporate board and audit committee of firms in the past decade. This is in view of the positive attendant effect of having women in boards and strategic committees, including audit committee in firms. Majority of women with requisite accounting knowledge are often segregated against in firms by the male counterparts perhaps because of policy bias and sentiments. Never the less, women inclusivity in boards and audit committee have been observed to influence operational process and earnings.Du, Jian and Lai (2017) opine that discretionary accruals is negatively and significantly associated with the presence and ratio of women in audit committee of firms in China.Thus, audit committee gender diversity can be regarded as a veritable factor to promoting negative discretionary accruals in firms. The effect of IFRS moderation with audit committee gender diversity on audit quality has received sparse empirical evidence (Sun et al. 2011; Thiruvadi & Huang, 2011). This informs the need to undertake this research with a view to bridging the research gap in the context of Nigeria.

2.0 LITERATURE REVIEW

2.1Empirical Review

The relationship between audit committee independence and audit quality has continued to occupy the front burner in empirical researches in developed and developing countries.The empirical researches on the nexus between audit committee independence and audit quality are inconclusive (e.g, Zaman, Hudah&Haniffa, 2011; Vafeas &

Waegelein, 2007; Mitra, Hossain &Deis, 2007;Bansal & Sharma, 2016). Carcello, Hollingsworth (2006); and Mitra et al. (2007) reported significant negative impact of audit committee independence on audit quality. Krishnan and Visvanathan (2009), and Zaman et al. (2011) reported a positive impact of audit committee independence on audit quality. The inconclusiveness of the relationship between audit committee independence and audit quality may be predicated on perhaps audit quality measure differentials, sample size, sample period and estimation methods.

Bryce, Ali and Mather (2015) examined accounting quality in the pre-/post adoption periods and the impact on audit committee effectiveness of 200 listed firms in Australia. They used both the univariate and multivariate regression methods to analyze the data. The result indicates that accounting quality is not significantly enhanced subsequent to the adoption of IFRS in Australia. The study also showed audit committee was more effective in maintaining accounting quality under IFRS than under previous Australian GAAP. Matta et al. 2011) empirical research showed that audit committee are more effective in minimizing earnings management under IFRS than the prior GAAP in Italy.

The study of Churiri and Januarti (2017) on the effect of audit committee characteristics and integrated reporting using a sample of 58 firms listed on the Johannesburg stock Exchange showed no association exists between independent audit committee members and audit quality and integrated report. Bliss, Muniandy and Majid (2007) argued that having sufficient independent directors on audit committee is associated with higher audit quality. Baotham and Ussahawanitchakit (2009) empirical study result showed that audit committee independence has a positive relationship with audit quality; and audit quality has a positive correlation with audit credibility.Krishnan (2005) in an empirical investigation reported that independence of audit committee is another key characteristic for effective monitoring of the financial reporting process and audit exercise among listed firms. Independent directors within the audit committee are better at monitoring their insider counter parts (Defond & Francis, 2005).

The gender and independence of a member of the audit committee contributes to effectiveness of operational processes in firms. Stewart and Munro (2007) emphasized that female representatives on audit committees demonstrate superior communication skills and are better prepared for meetings. Also, Thiruvadi and Huang (2011) submits that in comparison to committees that are totally male, a woman's presence makes members more diligent. This has the tendency of reducing weak audit quality (Ittohen, Miettinen&Vahamaa, 2010). Kuang and Chen (2010) state that a feminine presence on the Chinese corporate board is closely correlated with demands for higher quality external auditing.

Xiang and Qin (2015) argued that having women on the audit committee can significantly increase audit the quality of financial reporting and the efficacy of internal control, thus promoting audit quality in Chinese firms just like in every other country company. Sun et al. (2011) empirical study revealed that the representation of women on fully independent audit committee exert significant effect on audit quality. The primacy of IFRS interactive effect with audit committee independence on audit quality remains insufficiently investigated in GCC and other Arab countries including Saudi Arabia. Premised on this gap, this study hypothesis that IFRS adoption has no significant interactive effect with audit committee independence on audit quality of listed non - financial firms in Saudi Arab.

The association between audit committee meeting and audit quality has been attracting the attention of researchers in accounting and auditing literature for some decades. The study of Churiri and Januarti (2017) on the effect of audit committee characteristics and integrated reporting using a sample of 58 firms listed in the Johannesburg stock Exchange showed that audit committee expertise and frequency of meetings by members of audit committee positively translates to high audit quality and integrated reporting.

Hogue, Rabiulslain and Azam (2013) report that meeting frequency permits the audit committee more effectiveness in overseeing the financial reporting process and internal controls. Regular meeting by audit committee members in firms improves the quality of accounting information and audit (Song &Windram, 2004). In the view of Mangena and Tauringana (2008), audit committee who meet more regularly perform better supervisory roles in financial reporting than those who do not meet regularly. Chariri and Januriti(2017) concluded that frequency of audit committee positively influences audit quality. Besides the fact that frequency of audit committee meeting induces audit quality, the role of audit committee at overseeing the financial reporting cannot be separated from the independence of its members (Al-Najjar, 2012; Hamid, Othman and Rahim, 2015). Carcello and Neal (2003) posit that independence is the cornerstone of audit committee effectiveness.

3.0METHODOLOGY

The focus of this study to determine howIFRS interacts with ownership structure onaudit quality of listed firms in Nigeria. Following this,the ex-post-factresearch design is employed. Seventy (70) listed firms were selected using the simple random sampling technique in the period 2014 to 2019. This represents four hundred and twenty (420) firm-annual observation. Descriptive statistics, correlation matrix and general method of moment (SGMM2) were employed to analyze the data after applying diagnostic tests.

$$DA_{it} = \beta_0 + \beta_1 DA_{it-1} + \beta_2 ACI * IFRSdummy_{it} + \beta_2 Acm * IFRSdummy_{it} + \beta_3 \sum control\ variables_{it} + \beta_4 \sum audit\ comittee\ control\ vairbles_{it} + \varepsilon_{it} \dots\dots\dots\dots 1$$

AQ_{it} = Audit quality of i company in t period; $IFRSD_{it}$ = level of implementation or adoption with 0 code; for local accounting standards' implementation code 1 for implementing IFRS; ACI*IFRSdummy= interaction of IFRS with audit committee independence; Acm*IFRSdummy= Interaction of IFRS adoption with audit committee meeting;i = Individual company in the sample size; t = Period the study covers; ε = Error term acting as a surrogate in the models; β_0 = Intercept; $\sum Control\ variables_{it}$= consists of audit firm size AFS. Leverage Lev, and Company size CS of i company in t

period and $\sum audit\ committee\ control\ varibles_{it}$ = consists of audit committee gender diversity and audit committee size of $i$firm in t period.

4.0RESULTS AND DISCUSSION

This sub-section concerns the empirical analysis and discussion of the data analyzed. Tables of the data analysis are in appendix 1.

4.1 Diagnostic tests, Descriptive statistics and Correlation Analysis

Table 1 reveals that the mean of the variance inflation factor (VIF) of 1.03 is indicative of absence of multicollinearity among the variables in the study. Table 2 represents summary of the descriptive statistics. Audit committee independence (ACI) mean value is 3.05% with a standard deviation of 15.65 in the sample firms. This underscores the fact that the sampled firms do not maintain corporate governance policy that encourages high independent audit committee membership. This may trigger high risks which encompass low independent monitoring of the executive directors and external auditor over quality earnings management and increase in accruals in the firms.

Frequency of meetings by the audit committee members (ACM) has a mean value of 6.33%. It can be adduced that the audit committee members failed to meet regularly to access perhaps, the decisions by the executive directors regarding earnings management, quality financial reporting and thoroughness of the external auditor commitments at ensuring quality audit report during the audit exercise.

The control variables of audit committee gender diversity (ACGD), that is, women representation in the audit committee of the listed firms revealed a mean value of 0.04%, which can be interpreted as less than 1%. It is an explicit reflection that women are segregated against in terms of appointment and recognition into key positions and strategic committees in financial firms in Nigeria. This low proportion of women in the audit committee could affect them in monitoring activities of the board of directors and other key committee members over earnings management.

Table 3 is suggestive of absence of multicollinearity between mechanisms of audit committee and discretionary accruals excluding audit firm size, leverage and company size control variables as revealed by the mean of the variance inflation factor (VIF). Audit committee independence is weak and negatively associated with discretionary accruals by a coefficient value of ($r= -0.0078$). While audit committee meeting (ACM) is positive and weakly correlated with discretionary accruals ($r=0.0221$). The control variables, audit committee independence (ACI) and meetings are correlated positively with audit committee gender diversity (ACGD) and negatively with audit committee size (ACZ). This implies the few percentage of frequency of meetingsheld enabled the audit committee to effectively checkmate earnings manipulations in Nigeria firms. However, the negative association between discretionary accruals, audit committee independence, audit committee gender diversity is suggestive fewer representation of women and low percentage of independent directors in the audit committee in the firmsadversely affectstheir oversight function and ability to act as watch dog on behalf of the shareholders.

Tables 4, 5 and 6 results reveal that the specification tests of AR (2), Hansen and test are economically insignificant and thus valid. An indication thatthe empirical models were properly specified and fit for interpretation purpose. The diagnostic tests results indicate absence of Heteroscedasticity and serial autocorrelation effects.

Table 4, column (4) shows the coefficient value of lag discretionary accruals (DA) is less than 0.268. The coefficients values of audit committee independence (0.004) and audit committee meeting (0.069) exerted significant positive effects on discretionary accruals. By implication, these audit committee mechanisms though significant, contribute to low audit quality of listed non- financial firms in Nigeria particularly in the absence of IFRS adoption. The findings are consistent with Chariri and Januriti (2017). Overall, the result is suggestive that in the absence of international accounting standards, audit committee mechanisms might not be effective on audit quality in non- listed firms.

Audit committee gender diversity exerted a positive and significant effect on earnings management. Implying that the proportion of females in auditing committees is not active at the monitoring level of earnings manipulations in the firms under the reference period. The size of the firm audit committee was negative and significant on discretionary accruals. The size of the constituted audited committee is a major driver of high audit quality of Nigeria listed firms. While the leverage and company size was favourably signed and significant on discretionary accruals. Audit firm size maintained inverse and significant effect on audit quality. Size of a company and debts determine the capacity to engage a big 4 audit firm in order to have objectivity and independence during audit engagements. The findings are consistent with Hoque et al. (2013); Baotham and Ussahawanitchakit (2009) and Ittohen et al. (2010)

In table 5, the coefficients of IFRS interaction with audit committee independence (IFRSACI) is negative (-0.006) and significant at 99% level on discretionary accruals. This result implies that IFRS interaction with audit committee independence is a driver of high audit quality of listed firms in Nigeria. While the empirical finding negates Mitra et al (2007), it is in line with Krishnan and Visvanathan (2009).

IFRS interaction with audit committee meeting (IFRSACM) coefficient value is negative (-0.006) and significant at 99% level on discretionary accruals. The implication is that IFRS interaction with audit committee meeting contribute to high audit quality of listed firms. The finding is in tandem with Beasley, Carcello and Hermanson (2000) where they stated that frequency of meetings by audit committee has the possibility of reducing fraudulent financial reports and increasing quality of audit reports.

Table 6 emphasis the robustness check of the panel data estimation. The AR (2) and Hansen results are economically insignificant and hence valid. Interaction of IFRS with audit committee components (ACCOMIFRS) has a significant negative coefficient value (-0.083) in column (2) on discretionary accruals (DA). Thisportends that audit committee mechanisms interaction with IFRS leads to a negative discretionary accruals and thus enhance audit quality of listed firms in Nigeria. The finding is consistent with Bryce et al. (2015); and Matta et al. 2011).

5. CONCLUSION AND RECOMMENDATIONS

The study investigatedimpact of IFRS interaction with audit committee mechanisms on audit quality of firms in Nigeria. The research finding indicates audit committee mechanisms improved audit quality of firms in the period of IFRS adoption than under the Statement of Accounting Standards (SASs)inNigeria. The study concludes that interaction of IFRS with audit committee mechanisms is a veritable tool to influence high audit quality of listed firms in Nigeria. The research finding has some implications for policy makers. Thelow percentage of women and independent members in the audit committee of listed firms in Nigeria necessitate the need for the government and policy makers to legislate for certain quota of women and non-executive members with requisite accounting expertise to drive a negative discretionary accruals and high audit quality.The study suggests that future researchers have to examine the effect of audit committee religion, spirituality, ethnicity, nationality and attitude to risks under IFRS adoption on how they translate to audit quality of listed firms on a country specific basis and cross-country level using other estimation models.

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APPENDIX 1

Table 1: Test for Multicollinearity

VIF

Variable	**VIF**	**1/VIF**
ACM	1.04	0.958827
ACI	1.02	0.984981
ACZ	1.05	0.95538
ACGD	1.01	0.989424
AFS	1.01	0.986351
CS	1.06	0.946364
LEV	1.01	0.993397
Mean VIF	**1.03**	

Table 2: Descriptive Statistics

Variable	Obs	Mean	Std. Dev	Min	Max
DA	420	0.54	8.60	-0.01	266.95
ACI	420	3.06	15.66	0.00	100.00
ACM	420	6.33	2.38	0.00	16.00
ACGD	420	0.05	0.21	0.00	1.00
ACZ	420	5.25	1.73	1.00	9.00
AFS	420	0.52	0.50	0.00	1.00
LEV	420	13.72	0.44	-0.04	13.74
CS	420	6.37	0.87	3.55	8.66

Table 3: Audit committee Mechanisms and Audit Quality

	DA	ACI	ACM	ACGD	ACZ	AFS	LEV	CS
1	1							
2	-0.0078	1						
3	0.0221	0.0547	1					
4	-0.0042	0.0249	0.0767*	1				
5	-0.0129	-0.0424	-0.0054	-0.0271	1			
6	0.0281	-0.0622	-0.0458	0.0251	0.0169	1		
7	-0.9856*	0.0048	-0.0223	0.0073	0.023	-0.0307	1	
8	-0.0754*	-0.0426	-0.1050*	-0.0165	0.1577*	0.0858*	0.0599	1

Note * *represents* 5% level of significance

Table 4: Digenetic test and direct effect of audit committee mechanisms and audit quality

	(4) DGMM1	(5) DGMM2	(6) SGMM1	(7) SGMM2
L.DA	0.271	0.130^{***}	0.306	0.289^{***}
	[0.39]	[0.03]	[0.30]	[0.02]
ACI_P	-0.003	-0.002	0.004	0.004^{***}
	[0.01]	[0.00]	[0.01]	[0.00]
ACM	0.206^{**}	0.052^{*}	0.078	0.069^{***}
	[0.11]	[0.03]	[0.06]	[0.00]
ACGD	-0.158	0.297	0.631	0.768^{***}
	[1.36]	[0.38]	[0.62]	[0.07]
ACZ	-0.565^{**}	-0.137^{*}	-0.102	-0.075^{***}
	[0.28]	[0.08]	[0.13]	[0.01]
AFS	-0.145	-0.012	0.215	0.175^{***}
	[0.37]	[0.06]	[0.22]	[0.02]
LEV	-15.916^{***}	-18.549^{***}	-17.435^{***}	-18.968^{***}

	[1.37]	[3.00]	[0.82]	[1.75]
CS	-1.729*	-0.854***	-0.686*	-0.608***
	[0.96]	[0.21]	[0.36]	[0.04]
CONSTANT			243.994***	264.455***
			[11.13]	[24.07]
Observations	660	660	825	420
No. of instruments	50	50	81	18
No. of groups	165	165	165	70
Arellano-Bond: AR(1)	0.252	0.133	0.126	0.071
Arellano-Bond: AR(2)	0.843	0.221	0.691	0.201
Hansen test (p-val)		1.000		0.194

Table 5: IFRS Interaction with Audit Committee Mechanisms on Audit Quality

	(1) aci	(2) Acm
L.DA	0.431**	0.208***
	[0.17]	[0.02]
ACGD	0.584*	0.618**
	[0.33]	[0.29]
ACZ	-0.069**	0.090***
	[0.03]	[0.01]
AFS	0.196***	-0.026
	[0.05]	[0.02]
LEV	-19.406***	-19.368***
	[1.39]	[0.01]
CS	-0.524***	-0.129***
	[0.11]	[0.03]
ACI	0.005***	
	[0.00]	
IFRSACI	-0.006***	
	[0.00]	
ACM		0.023
		[0.01]
IFRSACM		-0.006**
		[0.00]
Constant	270.263***	266.409***
	[19.03]	[0.17]
Observations	825	420
No. of instruments	54	25
No. of groups	165	70
Arellano-Bond: AR(1)	0.014	0.049
Arellano-Bond: AR(2)	0.279	0.152
Hansen test (p-val)	0.972	0.786

The table represents the variables in the construct. DA, discretionary accruals; ACI represents audit committee independence; IFRSACI represents IFRS adoption's interaction with audit committee independence; ACM represents audit committee meetings; IFRSACM represents IFRS adoption's interaction with audit committee meetings. .ACGD represents audit committee gender diversity; ACS represents audit committee size; AFS represents audit firm size; LEV represents leverage while CS represents company size.Standard errors in brackets $^{*}p< 0.1$, $^{**}p< 0.05$, $^{***}p< 0.01$ represent 10%, 5%, and 1% significance levels, respectively.

Table 6: Interaction of IFRS adoption with Audit Committee Compositeon audit quality

	ACM
L.DA	0.142^{**}
	[0.07]
ACCOM	0.045^{***}
	[0.00]
ACCOMIFRS	-0.083^{***}
	[0.00]
ACGD	0.486^{**}
	[0.22]
ACZ	-0.115^{***}
	[0.01]
AFS	0.268^{***}
	[0.02]
LEV	-18.735^{***}
	[1.58]
CS	-0.887^{***}
	[0.06]
Constant	263.853^{***}
	[21.64]
Observations	420
No. of instruments	70
No. of groups	29
Arellano-Bond: AR(1)	0.484
Arellano-Bond: AR(2)	0.280
Hansen test (p-val)	0.086

Standard errors in brackets
$^{*}p< 0.1$, $^{**}p< 0.05$, $^{***}p< 0.01$