

AUDIT COMMITTEE NUMBER OF MEETINGS AND EARNINGS MANAGEMENT IN QUOTED NIGERIAN BANKS

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Abstract

The study investigated the effect of audit committee number of meetings on quality of financial reporting in quoted Nigerian banks. The investigation adopted archival data generated from fifteen banks whose stocks are bought and sold on the floor of Nigerian Stock Exchange at December 31, 2016. The research design applied in this investigation was 'correlational research design'. The Jones (1991) modified model offered the proxy for earnings management which represented the quality of financial reporting. Analyzing the data using the Pearson product moment correlation coefficient and regression analysis techniques with the aid of SPSS statistics 22.0, the interaction between the audit committee number of meetings and the quality of financial reporting of these banks was found to be statistically insignificant. Therefore, we recommend that audit committee members should meet frequently and adequately check the financial statements of these banks by so doing, earnings manipulation will be curtailed drastically.

Keywords: Audit committee, Audit committee number of meetings, Quality of financial reporting, Earnings management.

Introduction

In banks, the activity of financial reporting lies on the shoulders of the directors and this is executed by the accountants and confirmed by the auditors. The aim is to come up with a trust worthy and timely information that will enable users fortify their opinion. In the opinion of Kamaruzaman, Mazlifa and Maisarah (2009), financial statements should be able to discuss apposite, dependable, similar and all-embracing information. Johnson *et.al.* (2002) postulated that every twelve months report should be free from prejudice because the fiscal prodigy kept in annual disclosures is consistently being measured within the occurrence of uncertainty.

Yadirichukwu and Ebimobowie (2013) noted that the performance of these objectives depends on financial report being available on time to inform decision making. Warren and Reese (2004) assert that the use of economic disclosure is to get through to the economic performance and wellbeing of a business that seeks to trail managements' exploit and assist in making profitable decisions. This is as clear as crystal since financial reporting quality over the years has remained a critical issue of interest among regulatory bodies, shareholders, accounting professionals and scholars. This is due to the fact that financial reporting stands as a prime factor in transferring financial information to users outside the firm. Empirical studies in the financial reporting background (e.g. Wallace, 1988; Okike, 2000; Adeyemi, 2006; and Ofoegbu and Okoye 2006), indicated clearly that firms that try to provide their financial statements annually to the public hardly follow the approved standard.

In recent times, some empirical investigations on the audit committee have been undertaken, (for example, Soliman and Ragab, 2014; Yadirichukwu and Ebimobewei, 2013; Hamdan, Al-Hayale and Aboagela, 2012 and Odegunju, 2011). The above mentioned studies offer solid confirmation that financial reporting is influenced via audit committee characteristics which relates value maximizing motives. This study however, is a unique one utilizing only one attribute of audit committee characteristics (number of meetings) to check its effect in enriching the financial reporting quality in quoted Nigerian banks from 2010-2014.

Habbash (2010) opined that regulators around the world has generally recognized audit committee's significant duty as regards to economic recording long ago before the economic indignity happened at the expiration of the previous era. Audit committee exists so as to ensure the accuracy of financial reports (Felo and Solieri, 2009; Buchalter and Yokomoto, 2003). Klein (2002) submits that audit committee bridges the gap in information differences that exist between outside assessor and the manager and makes checking procedure easy and also heightens the independence of the auditors from management. It is expected therefore, that a well constituted and functional audit committee should be capable of increasing its supervisory role of financial reporting process and positing a good quality of financial control.

Theoretical framework

Having respect to agency theory, agency skirmishes emanates as likely discrepancy of concern amongst owners (principals) and directors. The setting aside of ownership and control in the contemporary business world brings about conflicts of interest between managers and shareholders. Predominantly, the onus of administrators remains to administer the business in a manner that it begets earnings to owners to enhance the turnover records (Elliot 2002). Generally, agency concept explicates how to superlatively arrange dealings where a given party decides the work, whereas the other party executes the work. This rapport depicts a situation where the principal hires an agent to perform a task in which he is not willing to do. There is the assumption that the principal and the agents are moved by self-interest. This assumption of egocentricity exposes the agency into unavoidable built-in conflicts.

Wealth maximization is a modern approach to financial management. In the past, profit serves as the primary concern of business and financial management. Today, the concept of wealth maximization exists as a higher goal when compared to profit maximization since it considers a wider perspective. The market price of the capital invested by shareholders is referred to as the wealth or value of a business. Wealth maximization implies the maximization of shareholders wealth. The wealth of the shareholders is maximized when the net worth of a company maximizes. Finance managers act for the shareholders and their primary concern is to look after the shareholders' interest. The shareholders expect good return on their investment.

Audit committee number of meetings

The workings of the group are determined by the aggregate sum of assemblies held twelve-monthly. The frequency at which the team meets depicts how effective audit committee spends time to amend any instant development and put forward an excellent reappraisal and controlled atmosphere. This may accelerate the detection of financial statement errors. The incidence of committee meetings in a year to a great extent determines its effectiveness Menon and Williams (1994). Bryan, Liv and Tiras (2004) remarked that the frequent meetings of audit committee enhance the clearness and unobstructed reporting of earnings,

thereby enhancing earnings quality. Oversight functions are carried out more effectively by audit committee members who meet on regular basis. This assertion corroborates with Lipton and Lorsch (2011) submission that improvement in the efficacy of the committee is noticeable as soon as the committee number of meetings upturns.

Aim and Objective of the Study

The aim of this paper is to empirically investigate the relationship between audit committee number of meetings and earnings quality in quoted Nigerian banks. Its specific objective is to determine the influence of audit committee number of meetings on earnings management in quoted Nigerian banks.

Research Question

In pursuance of the aim of and objective of the study, this paper poses the research question below to guide the research focus:

- To what extent does audit committee number of meetings influence earnings management in quoted Nigerian banks?

Research Hypothesis

H₀₁: Audit committee number of meetings has no significant influence on earnings management in quoted Nigerian banks.

Methodology

The study adopted the correlational research design otherwise called prospective research design towards investigating the relationship flanked by the explanatory variable and response variable of the study. One basic advantage of correlational research design according to Ofurum (2009), Tsegba and Herbert (2013), is its narrow study coverage which permits the generalization of research results and conclusions.

The population of the study is made up of all the fifteen banks whose shares are bought and sold on the floor of Nigerian Stock Exchange as at December 31, 2014. These banks are: Access Bank, Eco Bank, Diamond Bank, FCMB, Fidelity Bank, First Bank, GTB, Skye Bank, Stanbic IBTC, Sterling Bank, UBA, Union Bank, Unity Bank, Wema Bank and Zenith Bank.

In view of the research design and in agreement with the aim and objective of the study stated, the Pearson correlation was applied to determine the regression coefficient in the model specification while the linear regression was used to estimate the effect of the explanatory variable (i.e. audit committee number of meetings) on the response variable (i.e. “quality of financial reporting) represented by earnings management and measured by discretionary accruals”

Operational Measurement of variables

Variables applied in this paper remained measured as showcased in Table 1 below:

Table 1: Variables Measurement

Variables	Label	Measurement
Criterion variable		
Discretionary accruals	DAC	Determined by means of Jones (1991) modified model
Predictor variable		
Audit committee number of meetings	ACM	Aggregate of meetings held in a period

To investigate earnings management, this paper estimate total accruals and thereafter employed the revised Jones model to investigate discretionary accruals. We also estimated total accruals using items from statement of comprehensive income and statement of cash flow of banks in line with Dabor and Adeyemi (2009); Daniel and Paul (2000); Collins and Hribar (2002); William (2004); Keefe (2012); Ilanit (2007) and Dechow and Ge (2006).

$$TA_{it} = PBTE_{it} - CFO_{it} \dots\dots\dots(i)$$

Where;

TA_{it} = Total Accruals of banks I at time t

$PBTE_{it}$ = Profit before taxation and extraordinary activities of bank I at time t

CFO_{it} = Cash flow from operation of bank I at time t.

The modified Jones model is shown below:

$$DAC_{it} = \frac{TA_{it}}{A_{it-1}} - \left(\beta_0 + \beta_1 \frac{1}{A_{it-1}} + \frac{\beta_2 \Delta GE_{it} - \Delta NL_{it}}{A_{it-1}} + \beta_3 \frac{PPE_{it}}{A_{it-1}} \right) + \varepsilon \dots\dots (ii)$$

Where;

DAC_{it} = Discretionary Accrual of bank i at time t

TA_{it} = Total Accruals of bank i determined by subtracting profit before taxation, exceptional and extraordinary items and cash flow from operation for year t

A_{it} = Asset at the commencement of the year

ΔGE_{it} = Variation in Gross Earnings as of time t -1 to t

ΔNL_{it} = Change in the analysis of total loans and advances and non- performing loan as of time t-1 to t to reflect variation in Net Loans (ΔNL)

PPE = Gross Property, Plant and Equipment

E = Error term/random term

$$\text{Gross Earnings} = IINC + FCOM + TINC + INVINC + SHINC + OINC \dots\dots\dots(iii)$$

Where,

GE = Gross Earnings

IINC = Interest Income

FCOM = Fee Commission

FOREXINC = Foreign Exchange Income

TINC = Trusteeship Income

ININC = Investments Income

SHINC = Share Income

OINC = Other Income

$$NL = TL - NPL \dots \dots \dots (iv)$$

Where;

NL = Net Loan

TL = Total Loans

NPL = Non-Performing Loans

Model Specification

The analytical model considered in this paper took audit committee number of meetings as predictor variable and earnings management proxied by discretionary accruals as criterion variable. Having regards to the work of Ofurum and Lezaasi (2011), which is based on the studies by Tsegba and Herbert (2013), the study specified model on the attempt to ascertain the influence of audit committee number of meetings on earnings management of quoted banks in Nigeria as follows:

$$DAC = f(ACM) \dots \dots \dots (v)$$

$$DAC = \beta_0 + \beta_3 ACM + E \dots \dots \dots (vi)$$

Where;

DAC = Discretionary Accruals

β_0 = Intercept

$\beta_1 - \beta_4$ = Coefficient of predictor variables

ACM = Audit committee number of meetings

Results and Discussion

This paper used descriptive statistic as well as specific rigorous models for ascertaining the correlation between audit committee number of meetings and the quality of financial reporting represented by earnings management and measured by discretionary accruals. The hypothesis was analyzed with the Pearson product moment correlation coefficient and regression analysis techniques.

Table 2: Descriptive Statistics

	N	Minimum	Maximum	Mean		Std. Deviation
	Statistic	Statistic	Statistic	Statistic	Std. Error	Statistic
ABVDAC	75	.0019	.8743	.124523	.0146902	.1272212
ACM	75	2.0000	5.0000	3.853333	.1034423	.8958362
Valid N (listwise)	75					

The table above shows that the discretionary accruals which is in its absolute value possess an average mean of 0.124523 while the audit committee number of meetings shows an average meeting times of 3.853333 (approximately 4) which denotes that majority of the employed banks meet four times annually on the average. The standard deviation showing the level of variation or discrepancies in the movement of employed variables away or towards the average, it can be seen that the output shows very low standard deviation, showing that all employed variables lacked great variation from the average score but looking closer, the highest variation emanated from audit committee number of meetings (ACM): 0.8958362 as various quoted banks had various annual meeting times which ranged from two to six times yearly which varied for each bank, the least variation came from discretionary accruals (0.1272212) which shows that there exists very little discrepancies in the sampled banks discretionary accruals (see Table 4.1 in the main research work).

Bivariate Analysis

This shows the level of association between employed variables and the duration of movement amongst them. The Table 3 below is extracted from the SPSS statistic 22.0 output (see Appendix ii- iii in the main research work).

Table3: Extract of the Correlation Matrix of the Explanatory and Response Variables

Variables	ACM
Pearson Correlation	-0.001
Sig. (2-tailed)	0.993
N	75

From the output above in table 3, it can be seen that a negligible negative correlation was discovered between committee activities/meetings and discretionary accruals, as a negative coefficient of -0.001 was discovered at 0.993 significance level which appears to be greater than the 0.05 significance level, which signifies that committee activities/meetings do not result to a reduction in discretionary accruals of the banks. This illustrates that committee activities/meetings do not influence the discretionary accruals of listed banks as discovered by the study.

Regression

The study further moves to find the influence of the predictor on the criterion by carrying out a regression exercise as displayed below in table 4 which is a summary of the model estimate extracted from the SPSS statistic 22.0 output (see Appendix vi in the main research work).

Table 8: Extract of the Model Estimate

Variable	R	R ²	B	Std. Error	F	T	Sig.
ACM	0.001	0.000	0.000	0.017	0.000	- 0.009	0.993

Utilizing audit committee number of meetings by way of the explanatory variable and discretionary accruals by way of the response variable. From the table above, the R which represents the correlation coefficient shows a poor explanation of 0.1%, while the more decisive variable R² shows an output of 0.000, which signifies that variation in the explanatory variable (audit committee number of meetings) does not account for any variation in the response variable. This automatically resulted in the Analysis of Variance table (ANOVA) showing an insignificant regression at the 0.993 level which remains greater than the 0.05 level of significance, while the coefficient shows that audit committee number of meetings showcases that a neutral influence as denoted by its coefficient of 0.000 and has a very low shock level as shown by its standard error of 0.017 and was found to be statistically insignificant based on its t-statistics of -0.009 at the 0.993 significance level which stands greater than the 0.05 significance level.

Hypothesis Testing

The hypothesis posits that audit committee number of meetings has no significant influence on earnings management in quoted Nigerian banks. Employing the coefficient table in appendix vi in the main research work, and judging by the significance level of 0.993 which is greater than the 0.05 level as depicted in the regression table also in appendix vi in the main research work, the study therefore does not reject the null hypothesis and thus concludes that audit committee number of meetings has no significant influence on earnings management in quoted Nigerian banks during the period of the study.

Discussion of Findings

The study discovered that audit committee number of meetings has no significant/substantial influence on earnings management in quoted Nigerian banks during time of the study. This discovery is in disagreement with the finding of Collier (1992). This research submitted that the rate of audit committee meetings has a significant positive relationship with audit committee effectiveness. However, the discovery is in agreement with that of Bedard *et al* (2004) who established no association between audit committee number of meetings/activities and earnings management. Finally the present study refused to give a nod to the outcomes of Persons (2009); Vafeas (2005) and Abbott *et al.* (2004) who recorded a significant relationship between a higher level of audit committee activity and minor incidence of deceitful economic disclosure.

Conclusion and Recommendations

In line with the analysis and testing of the influence of audit committee number of meetings on earnings management in quoted Nigerian banks, the study concludes that committee number of meetings has no significant influence on earnings management in quoted Nigerian banks during the period covered by the study and therefore we recommend that audit

committee members should meet frequently and adequately check the financial statements of these banks by so doing, earnings manipulation will be curtailed drastically.

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