EFFECT OF AUDIT FIRM CHARACTERISTICS ON FINANCIAL REPORTING QUALITY OF LISTED CONSUMER GOODS FIRMS IN NIGERIA

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Abstract
In Nigeria, like many other developing economies, improving investor confidence through enhanced information contained in financial statements of listed companies is a major concern of regulators. This study empirically examines the extent to which audit firm characteristics explain financial reporting quality of listed consumer goods firms in Nigeria. Audit firm characteristics utilized include audit firm size, audit firm rotation, audit delay and audit remuneration. Financial Reporting Quality was measured using the performance-enhanced modified Jones Model. Data were obtained from annual reports and accounts of listed consumer goods firms. The study utilized multiple regression to analyze the data. Findings of the study provide evidence of weak relationship between audit firm characteristics and financial reporting quality of affected listed firms. Specifically, the study found that audit firm size and audit rotation have negative but statistically insignificant effect on financial reporting quality. On the other hand, audit delay has an insignificant positive effect on financial reporting quality while auditor remuneration has a negative and statistically significant effect on financial reporting quality of listed consumer goods firms in Nigeria. The study recommends, among others, that companies in consumer goods sector who hire the services of audit firms should assess them on the basis of performance in prior engagements and not just the size of the audit firm. In addition, regulators (SEC, NGX) should ensure compliance with the statutory reporting timeline. They should also pay close attention to reporting quality of companies paying high audit fees.

Keyword: Audit Firm, Financial Reporting Quality,

Introduction
Audit scandals and corporate failures at firms like Enron, Tyco International, WorldCom, and Cadbury have drawn heavy criticism for the quality of audit services and weakened public trust in the integrity of the accounting profession globally. Due to these occurrences, there is

an urgent need to review audit services globally and to reposition the profession in order to provide better services. One of the main duties of management is financial reporting, which enables them to account for their stewardship. To help interested parties evaluate the performance and financial status of the reporting entity, managers of public firms are required to prepare and present yearly financial reports to shareholders, and other stakeholders. The provision of information on the financial performance and position of the reporting entity that is useful to various users, allowing them to assess the management's stewardship and make informed economic decisions, is therefore the primary goal of financial reporting (International Accounting Standards Board (IASB), 2008; Glautier, Underdown, & Morris, 2011). This means that financial reports that are produced but do not provide the users with the information they require, do not serve their intended function.

In order to form an opinion on a true and fair view of the financial statement and provide users with reasonable assurance, an external auditor must examine the organization's books, records, and accounts. This ensures that the financial statements prepared by the management are free from material omissions and willful mistakes. Users of financial statements are given some degree of confidence when a quality audit report is produced. Because they feel the independence of the auditor increases the certainty that the financial statement is free from error or material misstatement. Investors, in particular, tend to have confidence in financial statements that have undergone auditing. On the basis of audit evidence obtained throughout the course of an audit assignment, auditors form conclusions about the financial statements generated by management of an organisation.

The global incidence of financial and audit scandals has called to question, the reputation of audit firms world-wide. The importance of external auditors in preventing financial statement fraud and manipulation has been called into doubt by well-known financial and audit crises like WorldCom, Enron, and Cadbury Nigeria PLC. While some research show a connection between audit characteristics and reporting quality, others show a negative connection. The contradictory results show that research into the connection between audit attributes and financial reporting quality is inconclusive.

Empirical Review

Audit Firm Size and Financial Reporting Quality

Since large audit firms have a reputation to uphold and will thus go to great lengths to ensure a quality independent audit service, the size of the audit company has been used to gauge the extent of financial reporting quality. In comparison to smaller audit firms, larger audit firms have more advanced technology, financial resources, and research facilities, as well as greater expertise and skilled staff. Smaller firms provide more individualised services because of their sparse client portfolios and are expected to give in to management pressure, whereas larger firms have strong client portfolios that enable them to resist management pressure (Lys & Watts 1994). Therefore, an essential audit attribute that affects a company's financial reporting quality is the size of the audit firm. A favourable correlation between size and real audit quality as well as financial reporting quality has been called into question by corporate collapses like Enron and WorldCom. DeAngelo (1981) proposed that audit firm is positively correlated with audit quality because a big audit firm will be forced to disclose a major misrepresentation in a client's records if it discovers one.

The relationship between the size of an audit company and the calibre of financial reporting was explored by Sawan and Alsaqqa in 2013. Data collection involved using a questionnaire. Semi-structured interviews were undertaken to verify and complement the results of the questionnaire. The demand side (Libyan oil firms) and the supply side (audit firms working in Libya) provided the data for the study. Internal auditors, financial managers, and accounts managers were the three different types of respondents who provided the information for the Libyan oil companies. Data were acquired for the audit firms from employees at all levels of the company, including managing partners, audit supervisors, and auditors. The study's findings showed that the vast majority of oil companies and audit firms concur that Big Four firms outperform their non-Big Four counterparts in all reputation-related issues and that the size of the audit firm is positively correlated with Financial Reporting Quality. The use of a questionnaire, a subjective method of data collection, is a weakness of this study.

Enofe, Mgbame, Aderin, and Ehi-Oshio (2013) examined the factors that affect the quality of financial reporting in the corporate environment in Nigeria. Determinants such as audit tenure, audit firm size, board independence, and ownership structure are among the factors investigated. A survey with a Likert scale was created and utilised to gather information from a sample of 100 respondents in Nigeria's South-South geopolitical zone. The OLS regression method was used to analyse the data. According to the findings, financial reporting quality is positively (statistically significant) influenced by audit firm size, board independence, and ownership structure.

Ilaboya and Ohiokha (2014) looked at how audit firm characteristics affected the calibre of financial reporting. The study used the standard dichotomous variable of 1 if the big 4 audit firm and 0 if not to proxy financial reporting quality. The study examined a sample of 18 food and beverage firms that were listed on the Nigerian Stock Exchange market between 2007 and 2012. To estimate the study's model, a multivariate Logit and Probit regression was applied. The results show a negative relationship between the size of the audit firm and the financial reporting quality.

This study makes the following hypothesis in light of the review above:

Ho_1: Audit Firm Size has no significant effect on Financial Reporting Quality of listed Consumer goods firms in Nigeria

Audit Firm Rotation and Financial Reporting Quality.

The number of years an audit firm has been auditing an organization's financial statements is known as the audit firm tenure. The relationship between audit tenure and reporting quality has been the subject of extensive debate in academic literature and the accounting profession (Jenkins & Vermeer, 2013; Blandon & Bosch, 2015). The ability of auditors to retain an unbiased posture in carrying out their audit assignments, providing audit opinions, and guaranteeing high quality audit reports is at the heart of the dispute (Odia, 2015). Regarding the impact of audit tenure on reporting quality, there are two conflicting points of view. Some people believe that as the auditor-client relationship deepens, the auditor may become more closely involved with the client and lose their independence, which will eventually lead to poor audit quality and more effective earnings management (which will degrade reporting

quality) (Becker, DeFond, Jiambalvo &Subramanyam1998; Lys & Watts, 1994). The opposing argument is that as audit tenure increases, auditors have a greater grasp of their clients' operations, corporate strategy, and internal control over financial reporting, which will lead to higher reporting quality (Arens, Elder & Beasley, 2005; ling & Nopmanee, 2015). In order to ensure independence, the Nigerian Code of Corporate Governance 2018 recommends a five-year rotation of auditors.

All listed banks on the floor of the Nigerian Stock Exchange make up the population of Adeniyi and Mieseigha's (2013) study, which examines the relationship between the tenure of the auditor and reporting quality in Nigeria. Using a regression analysis method called ordinary least squares (OLS), cross-sectional data from fourteen (14) banks in the banking industry were examined from 2010 to 2015. The results show that, despite the variable's lack of significance, there is a negative link between auditor tenure and financial reporting quality.

Financial Reporting Quality and mandated audit firm rotation were both studied by Onwuchekwa, Erah, and Izedonmi in 2012. The information was gathered by sending questionnaires to investors, professors, consultants, accountants, and auditors in southern Nigeria. Percentage analysis was used to evaluate the data, and binary logistic regression was used to estimate the given model. Financial Reporting Quality and Mandatory Audit Firm Rotation (MAR) are shown to be negatively correlated by binary logistic ordered regression (AUDQ).

The association between audit tenure and Financial Reporting Quality is examined by Myers, Myers, and Omer (2013) utilising proxy variables such discretionary accruals and current accruals. The univariate results indicate that when auditor tenure is longer, the negative value of accrual measures was observed to be minimal. The study also employed multivariate analysis in order to examine if the discovered relationship between tenure and accruals is also influenced by other factors. The relationship between auditor tenure and accrual measures (proxies for reporting quality) was also observed to be consistent in multivariate analysis as in the univariate analysis. The study found that extended auditor tenure had a beneficial effect on the dispersion of accruals. The implication is that there is the tendency for auditors to place greater constraints on both income increasing and income decreasing accruals as the audit client relation lengthens. These results suggest that Financial Reporting Quality does not appear to deteriorate with tenure.

The following assertion is made in light of the positions taken in the literature discussed above:

Ho_2: Audit Firm Rotation has no significant effect on Financial Reporting Quality of listed Consumer goods firms in Nigeria.

Audit Delay and Financial Reporting Quality

A trustworthy audited financial statement is a crucial element that enhances stakeholders' decision-making. Financial analysts have recently suggested that it is impossible to overstate how crucial timeliness is as a fundamental quality of audited financial statements. The time

between the end of a company's fiscal year and the date of the auditor report is how Almosa and Alabbas (2007) define audit delay. According to recent studies, in order to increase the effectiveness of the capital market, the timeline for publishing audited financial statements should be shortened. There is evidence that additional information regarding earnings quality beyond that in the earnings report delay is provided by audit delay (Alkhatib & Marji, 2012). Investors are, in essence, disbelieved about the quality of the earnings when an extraordinary audit delay occurs, and they value the revealed earnings after discounting for this delay. Since investors disregard the value relevance of such earnings when making resource allocation decisions, the existing literature supports the concept that audit delays indicate low-quality earnings.

Using cross-section data from 628 companies in 2002, Mohammed-Nor, Shafie, and Wan-Hussin (2010) evaluated audit reports from Malaysian public listed corporations. Board of directors and audit committee characteristics were regressed on the audit lag. The findings indicated that larger, more active audit committees reduce audit lag, but there was no empirical support for the nexus between audit committee independence and expertise and the timeliness of audit reports.

Ho_3: Audit Delay has no significant effect on Financial Reporting Quality of listed Consumer goods firms in Nigeria

Audit Remuneration and Financial Reporting Quality

According to varying opinions in the literature, there is a connection between audit compensation and the financial reporting quality to some extent; most frequently, compensation given to external auditors has this effect. Additionally, according to Yuniarti (2011), the complexity of the services rendered, the expertise, the assignment's risk, and other professional factors affect the audit fee that the auditor charges. Higher Audit Remuneration increases a higher quality audit, the study further demonstrates. Supriyono (1988 in Wati & Subroto, 2003) expressed the opposite opinion, claiming that high audit fees can compromise public accountants' independence. He attributed this to the fact that high fees can make audit firms less willing to challenge the client's wishes, whereas low fees tend to keep the cost and duration of thorough audit procedures to a minimum. Although some research show a connection between audit remunerations and audit quality, others show a negative connection. The contradictory results show that further research into the relationship between audit compensation and audit quality has not yet yielded definitive results. Boeijink (2011) used a sample of 2767 businesses to investigate the effects of excessive auditor compensation (abnormal audit compensations) on audit quality in 13 different nations between 2004 and 2008. The study found no evidence of a significant relationship between aberrant audit compensation and audit quality.

Using information from Nigerian building material companies between the years of 2002 and 2011, Umar (2014) performed research on the audit attribute and financial reporting quality. The model chosen for this investigation was the Dechow and Dichev model from 2002, as modified by McNichol (2002), and it was analysed using OLS multiple regression (dependent variable). The study discovered a significant positive relationship between audit compensation and the quality of financial reporting.

Choi, Kim, and Zang (2010) used a multiple regression technique to investigate the relationship between Financial Reporting Quality, as measured by the size of absolute discretionary accruals, and abnormal Audit Remunerations, defined as the discrepancy between actual Audit Remuneration and the expected, normal level of Audit Remuneration. Depending on the sign of the aberrant Audit Remuneration, the findings of multiple regressions show that the link between the two is asymmetric. Financial Reporting Quality and abnormal Audit Remuneration do not significantly correlate for observations with negative abnormal Audit Remunerations. For observations with positive abnormal Audit Remunerations, however, there is a negative correlation between abnormal Audit Remunerations and Financial Reporting Quality.

Using a sample of 2,568 US-listed corporations having fiscal year 2010 financial data available, Karsemeijer (2012) examined the relationship between audit remunerations and audit quality. The study's findings revealed that there is a positive and significant relationship between audit compensation and the absolute value of discretionary accruals, as well as between non-audit compensation and this same relationship. Despite being done in industrialised nations with a sizable sample size, this study's findings could alter if it were to be re-conducted today because its time frame ended in 2010.

Using secondary data taken from the annual report of the sampled companies for a period of six years, Abdul-Rahman, Benjamin, and Olayinka (2017) studied the impact of audit remunerations on audit quality (a measure of reporting quality) of listed cement manufacturing companies in Nigeria (2010-2015). The link between the explanatory variable and the dependent variable was examined using the ordinary least square estimation approach. The study's findings indicate that audit quality is significantly influenced by factors such as audit remuneration, client size, audit tenure, and leverage ratio, with audit remuneration in particular having a considerable positive impact.

Ashbaugh et al., 2003 investigated the relationship between discretionary accruals, audit fee ratio, and overall fees in a sample of American businesses. The study shows that there is no statistically significant relationship between total audit fees and discretionary accruals. They also demonstrate a favourable association between the fee ratio and the discretionary current accruals of the absolute value firm. In their second experiment, they find no correlation between fee ratio and the probability that businesses would report minor earnings increases and a negative correlation between total fees and the probability that businesses will report small earnings increases. In contrast to Frankel et al. (2002), they discover no correlation between the fee ratio or total fees and firms reaching analyst estimates. They come to the conclusion that the argument that auditors breach their independence because customers pay excessive fees has no merit.

Ho_4 Auditor Remuneration has no significant effect on Financial Reporting Quality of listed Consumer goods firms in Nigeria.

Theoretical Framework: Monitoring Theory

Wilson (1983) developed the monitoring hypothesis, which is based on the agency theory. According to agency theory, an independent audit is one of the solutions to the issue of agent-principal conflicts, and agency cost is a potential remedy (Jensen & Meckling, 1976).

According to Wilson (1983), the monitoring role of audit minimizes the moral hazard and adverse selection problems that arise from the information asymmetries problem. Wilson (1983) explains the case of a moral hazard problem, the managers responsible for protecting a firm's assets may misuse the assets or fail to maintain them, in which case such actions are not directly observable by the owner and potential investors. In the case of an adverse selection problem, such assets have their own fixed values. The managers have more information about these values and they are able to manipulate information for their own personal gain. The independent audit can be generated by the principal (monitoring cost) or the agent (bonding cost). It is argues that agents can demand an independent audit because principals tend to neglect monitoring activity as they are able to shield themselves from the risk of loss by paying lower wages to an agent (Humphrey, 1997). The presumption is that principals will pay more to agents for work that has been verified by an independent audit than that which has not been so verified. The stewardship (monitoring) theory states that when one party is delegated decision making power, he has an incentive to agree to be checked if the benefits from such monitoring activities exceed the related cost Wallace (Wallace, 1980). Wallace (1980) noted that an independent audit provides an assurance that the financial reports that are provided by the managements have been carefully prepared and they are free from material errors. Thus, the market participants including the potential investors can use the audited financial statements without any hesitation. Moreover, an independent audit also mitigates financial statement fraud and illegal reporting and improves the internal control and operational efficiency of a firm (Wallace, 1980; Chow, 1982)

Methodology

This study employs Ex-post facto research design. The population of the study comprises of all the twenty (20) Consumer goods firms listed on the floor of Nigerian Stock Exchange (NSE) Market as at 31st December, 2021. In arriving at the sample size, all Consumer goods firms that suspended their operations for sometimes during the period covered by the study (2014 to 2021) are excluded because of the unavailability of data for the period they are not in operation. Only seventeen (17) firms out of the twenty (20) meet the above criteria. Secondary data sourced from the Annual Reports and Accounts of the various Consumer Goods Firms listed on Nigeria Exchange Group (NGX) were used. The study employs the use of panel multiple regression for data analysis. The study carried out data diagnostic assessment using multicollinearity test . The fixed and random effects regression models were applied; and in choosing the most appropriate model for the study, Hausman specification test was conducted to ascertain whether fixed or random effects model is most appropriate for the data. The Hausman results suggest random effect model is appropriate.

Model specification

To determine our proxy of financial reporting quality, Discretionary Accruals (residuals) is used (higher level of the residual indicates a lower level of accrual and earnings quality). To measure discretionary accruals, this study adopts a performance-matched modified-Jones (1991) discretionary accruals model. This is because Dechow et al. (1995) provide evidence that the modified Jones model had the highest statistical power in detecting earnings management, and Kothari et al. (2005) suggest matching for performance helps to control for changes in accruals models associated with client performance levels.

$$FRQ_{it} = \beta_0 + \beta_1 AUDFSZ_{it} + \beta_2 AUDROT_{it} + \beta_3 AUDDLY_{it} + \beta_4 AUDREM_{it} + \varepsilon_{it}$$

Where:

FRQ_{it} = Financial reporting quality of firm i in year t as measured by discretionary accruals

$AUDFSZ_{it}$ = Audit firm size of firm i in year t

$AUDROT_{it}$ = Audit firm rotation in firm i at year t

$AUDDLY_{it}$ = Audit delay in firm i at year t

$AUDREM_{it}$ = Audit remuneration of firm i at year t

$\beta 1$, $\beta 2$, $\beta 3$, $\beta 4$, are parameters estimates; $\beta 0$ intercept

ε = Residuals

$\beta 0$ = Constant

Audit Firm Size (AUDFSZ): Measured by dichotomous variable 1 if the company is audited by a Big 4 audit firm and 0 otherwise

Audit firm Rotation (AUDROT): Measured by dichotomous variable, 1 if there is a change in audit firm during a year, and 0 otherwise.

Audit Delay (AUDDLY): This is measured by the number of days from the company's accounting year end to the date of audit report.

Audit Remuneration: (AUREM) Total audit fees paid to the audit firm by a client at the end of accounting period.

Results and Discussions

Table 1 Correlation Matrix

	FRQ	AUDFSZ	AUDROT	AUDDLY	AUDREM
FRQ	1.000000				
AUDFSZ	-0.078145	1.000000			
AUDROT	0.177185	0.085717	1.000000		
AUDDLY	-0.055925	-0.155522	-0.135318	1.000000	
AUDREM	0.001405	0.244094	0.070866	0.292464	1.000000

From the individual correlation, it was gathered that audit firm size has a negative correlation with financial reporting quality. In the same light, there is low negative correlation between audit firm rotation and financial reporting quality of consumer goods firms. However, audit delay has positive correlation with financial reporting quality while audit remuneration has negative correlation with financial reporting quality. From the relationship between the audit characteristics and financial reporting quality, there is no indication of correlation problem because the relationship is less than 0.7% as asserted by Gujarati (2009)

Table 2: Regression Summary

Variables	Coefficient	t-values	P-values	VIF
AUDFSZ	-0.005924	-1.238049	0.2177	1.130282
AUDROT	-0.001291	-0.192036	0.8480	1.027637
AUDDLY	0.011197	1.373443	0.1717	1.182043
AUDREM	-0.024665	-5.757105	0.0000	1.205320
Constant	0.096057	4.172903	0.0001	
R^2	0.317697			

F-stat.	17.11173	0.000000
Hausman Specification Test	0.979050	0.9130
Breusch and Pagan LM Test	29.17	0.0000

In table 2, the multicollinearity of the audit characteristics variables indicates no multicollinearity problem because their VIF values is below 10. In addition, p-value of the F-Statistics indicates that the model is fit and appropriate while both the Hausman Specification test and Breusch and Pagan Lagrangian multiplier test for random effects results support the use of Random Effect Model. From the coefficient of determination, the audit characteristics used in the study explained 31.7% variation on financial reporting quality of consumer goods firms while the remaining variation is explained by other variables not included in the model. The model is fit with f-significance less than 5% level of confidence.

The finding shows that audit firm size has negative but insignificant effect on financial reporting quality of listed consumer goods firms in Nigeria. This finding is in line with findings from the study of Dehkordi and Makarem (2011); but not in line with the findings of Branda and Ann (2005); Sawan and Alsaqqa (2013); Enofe, Mgbame, Aderin, and Ehi-Oshio (2013); Ilaboya and Ohiokha (2014) that audit firm size has significant effect on financial reporting quality.

Audit firm rotation has negative but insignificant effect on financial reporting quality. This finding agrees with the findings of Adeniyi and Mieseigha (2013); Onwuchekwa, Erah and Izedonmi (2012) but disagree with the findings of Ebimobowei and Oyadonghan (2011); Carcello and Nagy (2010).

It was found that audit delay has positive but insignificant effect on financial reporting quality. This is in line with Mohammed-Nor, Shafie and Wan-Hussin (2010) but not in line with Iyoha (2012); Modugu, Eragbhe and Ikhatua (2012).

This study found that audit remuneration has negative and significant effect on financial reporting quality of consumer goods companies in Nigeria. This finding agrees with the findings from the study of Choi, Kim, and Zang (2010); Hoitash, Markelevich and Barragato (2007); Abdul-Rahman, Benjamin and Olayinka (2017) but it however does not align with the findings of Umar (2014); Boeijink (2011); Karsemeijer (2012); Oladipupo and Monye-Emina (2016); Yuniarti (2011).

Conclusion and Recommendations

The study ascertained the effect of audit characteristics on financial reporting quality of listed consumer goods firms in Nigeria. From the outcome, the study concludes audit firm size, audit firm rotation and audit delay have no statistical significant effect on financial reporting quality of consumer goods firms in Nigeria.

Since audit firm size does not exert any significant influence on financial reporting quality, Nigeria companies in consumer goods sector who hire the services of audit firms should assess them on the basis of performance in prior engagements and not just the size of the audit firm. Competence and experience of the audit firms rather than size should be considered. Also, users of audited financial statements should subject all audited financial

statements to the same scrutiny regardless of whether the audit report is from a big or small audit firm. This is to avoid making wrong investment decisions.

The study does not provide any significant statistical evidence showing that audit rotation has any significant effect on financial reporting quality. The recommendation in the Nigeria Code of Corporate Governance is encouraged.

Timeliness of audit report is important to make good investment and managerial decisions, and to achieve this the study recommends that, Nigerian Stock Exchange, Securities and Exchange Commission, Financial Reporting Council and other regulatory bodies should put in place measures to ensure strict compliance with the laid down rules and regulations regarding time frame for audit to be carried out on company's financial statement by external auditor. Also, companies should put in place measures to reduce the time lag between the financial year end and the Annual General Meeting (AGM).

The study in this circumstance recommends that auditor's remuneration should commensurate with the quantity and quality of audit expected to deliver. Attention of regulators should focus on reporting quality of companies paying high audit fee.

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