

**Effect of Audit Committee Characteristics on Financial Reporting Quality of Listed
Deposit Money Banks in Nigeria**

By

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November, 2017

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**A DISSERTATION SUBMITTED TO THE SCHOOL OF POSTGRADUATE STUDIES,
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ACCOUNTING AND FINANCE**

**Department of Accounting,
Faculty of Administration,
Ahmadu Bello University,
Zaria**

November, 2017

DECLARATION

I, Muazu Kabiru, hereby declare that this dissertation titled “Effect of Audit Committee Characteristics on Financial Reporting Quality of Listed Deposit Money Banks in Nigeria” is the product of my research efforts, in the Department of Accounting, Ahmadu Bello University, Zaria under the supervision of Dr. Ahmed Bello and Mal Abubakar Audi. All information derived from relevant literature have been duly acknowledged in the text and a list of references provided. No part of this dissertation was previously presented for another degree at this or any other institution.

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DATE

CERTIFICATION

This dissertation, titled “Effect of Audit Committee Characteristics on Financial Reporting Quality of Listed Deposit Money Banks in Nigeria” by Muazu Kabiru, meets the regulations governing the award of the degree of Master of Science (M.Sc.) in Accounting and Finance of the Ahmadu Bello University, Zaria, and is approved for its contribution to knowledge and literary presentation.

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DEDICATION

This dissertation is dedicated to my late brother, Abdurrahman Ibn Muazu

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I always give glory to my creator who answers my prayers and guides me unto the path of light.

He is the most exalted and the omnipotent.

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ABSTRACT

Several banking regulations reports as well as extant literature have established that Nigerian banks' audit committees are poorly constituted which may affect the quality of financial reporting. It is on this premise that this study investigated the effect of audit committee characteristics on the financial reporting quality of Deposit Money Banks (DMBs) in Nigeria. The study used correlational research design. The source of data was secondary which were collected from the published annual financial reports of the studied DMBs in Nigeria. The study covered all the 15 DMBs in Nigeria for a period of eight years, ranging from 2007 to 2014. The data collected were analyzed using multiple regression analysis, using STATA software. Findings from the analysis show that frequency of audit committee meeting and audit committee female membership have positive and significant effect on the financial reporting quality of DMBs in Nigeria while audit committee financial expertise has negative and significant effect on the financial reporting quality of DMBs in Nigeria. Furthermore, audit committee independence has no significant effect on the financial reporting quality of DMBs in Nigeria. Based on the above findings, the study suggests that banks should sustain frequency of audit committee meetings and increasing membership of females/women in audit committee would likely improve accounting quality.

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CHAPTER ONE

INTRODUCTION

1.1 Background to the Study

Corporate financial report provides fundamental information to a wide range of groups; its main purpose is to provide information which is supposed to give a true and fair view of the management's stewardship, company's performance and financial position for the various users of the information to make informed economic decisions (America Accounting Association, 1961). Financial reporting is the process by which corporate entities provide interested parties (users) with information on their transactions during an accounting period (Mbobo & Ekpo, 2016). Among the interested parties are shareholders, creditors, tax authorities, customers, financial analysts, and lenders. The parties need quality financial reports for economic decision making.

Financial report is one of the major means that corporate management uses in communicating financial information for a given period. In this regard, the International Accounting Standard (IAS 1) states that the purpose of financial reporting is to provide information about the financial position, financial performance and cash flows of an entity that is useful to a wide range of users in making economic decisions. Such information is communicated through financial statements. Ibadin and Dabor (2015) stated that financial statements show the results of the management's stewardship of the resources entrusted to it by revealing economic information on assets, liabilities, equity, income and expenses, including gains and losses; contributions by and distributions to owners in their capacity as owners; and cash flows. Such information, along with

other information in the notes, assists users of financial statements in predicting the entity's future cash flows and, in particular, their timing.

Moreover, accounting information contained in the financial statements is one of the very essential information needed by various stakeholders especially investors for making informed economic decisions. Investors in search of investment avenues use the accounting information contained in the financial statements of the intended investing company in pricing of shares. Market participants seek high-quality financial reporting or information to mitigate information asymmetry as such quality information should be a pre-requisite for a well-functioning capital market. Thus, companies that provide high-quality information have an added advantage in their rating in the capital market (Ibadin & Dabor, 2015).

The increasing demand for quality financial reporting creates the need for effective and efficient monitoring mechanisms. This is necessitated by the conflict of interest between managers, who serve as agents and resource holders, who serve as principals, wherein, managers carry out activities that are counter-productive in the realization of the interests of resource holders. Therefore, board of directors is instituted to monitor the activities of managers. The board sets several monitoring measures that will ensure the integrity of management's decision. One of committees is the audit committee. The quality of the monitoring process depends on effectiveness of the audit committee. The effectiveness of audit committee in exercising its monitoring role is defined as the extent to which they perform their duties which is associated with their characteristics (Dechow, Sloan & Sweeney, 1996; Beasley, 1996; Carcello & Neal, 2000; Klein, 2002). An effective audit committee ensures the provision of credible accounting information to financial statement users by constraining earnings management by managers (Dandago & Rufai, 2014).

It is in line with increasing loss of credibility of financial reports that the banking industry, through the Central Bank of Nigeria also developed its code, the recent of which is the CBN Code of Corporate Governance of 2006 (Ibadin & Dabor, 2015). Specifically, the code requires that companies should establish audit committees consisting of directors and shareholders. Under the code, audit committee is saddled with the responsibility of reviewing the scope and result of audit, the independence and objectivity of the auditor, among others. In spite of this, the quality of financial reports of banks has continued to be an issue of concern.

Consequently, the effect of audit committee characteristics on financial reporting quality has been under scrutiny. Audit committee independence is one of such characteristics (Klein, 2002). This is measured by presence of non-executive audit committee members who do not engage in the day to day running of firms. Presence of such members provides a necessary condition for the audit committee to carry out its oversight functions objectively. However, a contrary argument to this is that non-executive audit committee members might not have requisite knowledge of the internal financial reporting practices of an organization and therefore might not be able to ascertain possible areas of financial misstatements. Nonetheless, lack of audit committee independence in Nigerian may have influence in the increasing spate of financial scandals and bank failures.

Frequency of audit committee meeting is also considered relevant for the oversight functions of the audit committee (Jenkins, 2000). Menon and Williams (1994) contend that the more often an audit committee meets the more active it is being perceived, which leads to fewer financial

reporting problems. In practice, more frequent audit committee meeting gives the committee opportunity to critically examine financial statements and carry out follow-up actions. Similarly, Audit committee that meets frequently can reduce the incidence of financial reporting problems. Therefore, the more frequent the audit committee members meet, the more thorough they are prone to be in terms of assessing the quality of financial report. Contrary to this analogy, it can be argued that frequent audit meetings add cost to the organization. Payment of meeting allowances constitute cost which often times can be avoided. Managers even use such avenues to expropriate organizational resources. In the deposit money banks in Nigeria, the issue of frequency of audit committee meeting is worthy of emphasis especially in the light of increasing loss of credibility in the financial reports presented by management of banks whose financial reports are not well reviewed by the audit committees that meet rarely (Dabor & Dabor, 2015).

The existence of female board members could serve as a mitigating factor against manipulative accounting as there is bound to be less collusion. Relatedly, audit committee members with requisite financial expertise are prone to be more active in assessing the quality of financial reports. However, a contrary argument is that such members might rather aid management in manipulating accounts especially if their independence is compromised (Illaboya, 2012). Therefore, the role of the audit committee in monitoring the financial misstatements to ensure financial reporting quality cannot be overemphasized. It is against this backdrop that this investigation is carried out to examine the effect of audit committee characteristics on financial reporting with emphasis on Deposit Money Banks in Nigeria.

Statement of the Research Problem

Poor corporate governance practices have become a global phenomenon (Ahmad & Hassan, 2011). Nigeria has also experienced cases of corporate failure due to poor corporate governance practices (Dabor & Tijjani, 2011). Some of the cases include that of Lever Brothers plc and Cadbury Nigeria plc. Evidence from empirical studies (Mbobo & Ekpo, 2016) have shown that audit committee ineffectiveness is one of the major causes of global financial crisis not only in developing economies but also in developed ones. In most cases, audit committee was accused of not performing their responsibility effectively. For example, the investigation on Worldcom shows that the audit committee failed to effectively oversee the managers' duties. This action subjected the audit committee's role of overseeing financial reporting process into severe criticism thus, making the quality of accounting questionable.

A critical review of the Nigeria banking system over the years also shows that among the problems confronting the sector is the issue of weak corporate governance (Sanusi, 2010). The weakness in the corporate governance among others include, audit committee squabbles, fraudulent and self-serving peachment among members of the audit committee. The Central Bank of Nigeria post consolidation Code of Corporate Governance (2006) also reviews that poor governance is one of the key variables that lead to corporate distress (Sanusi, 2010). In the Nigerian banking sector, poor governance and unethical practices have become issues of worry as they have been proven to be linked to bank distress in Nigeria (Sanusi, 2010). Consequently, in 2005, one hundred and ten (110) cases of fraud and forgeries valued at ₦1.5 billion were reported while in 2010, the Central Bank of Nigeria injected 620 billion as liquidity into the banking sector due to threats of banking sector collapse. The above statistics reveal evidence of

poor display of oversight roles of corporate governance in the Nigerian banking sector.

Furthermore, it has been documented in the accounting literature (Anderson & Gillan, 2003; Bradbury, Mak and Tan, 2004 and Hermawan, 2011) that ineffectiveness of audit committee monitoring and oversight functions result in accounting irregularities; as such information contained in the financial statements may not display true and fair view of the earnings and financial position of the business. In such cases, the information becomes misleading and affects the quality of financial reports.

Most studies that examine the effect of audit committee characteristics on financial reporting quality in Nigeria, such as Oyejide and Soyibo (2001), Temple (2016) and Hassan (2012), have tended to focus on few variables of audit committee. In addition, a key observation which can be gleaned from the literature is that the effect of audit committee characteristics on financial reporting quality has not been adequately carried out in the Deposit Money Banks in Nigeria. This is in spite of the central roles that they play to national development (Hassan, 2012).

This study assesses the effect of audit committee characteristics on financial reporting quality with focus on Deposit Money Banks in Nigeria. The concentration of the study on DMBs is very timely as they have a wide range of investors who on daily basis need quality financial reports to make their informed economic decision. The absence of quality financial reports will not only mislead investors but negatively affecting quality investment decision in the whole country which will affect national development.

1.3 Research Questions

In view of the above statement of the research problem, the following questions are posed to serve as a guide:

- i. Does audit committee independence significantly affect financial reporting quality of listed Nigerian DMBs?
- ii. Does frequency of audit committee meeting significantly affect financial reporting quality of listed Nigerian DMBs?
- iii. Does accounting expertise of audit committee members affect financial reporting quality of listed Nigerian DMBs?
- iv. To what extent does female membership in audit committee affect financial reporting quality of listed Nigerian DMBs?

1.4 Objectives of the Study

The following are the objectives of the study:

- i. To examine the effect of audit committee independence on financial reporting quality of listed Nigerian DMBs.
- ii. To investigate the effect of frequency of audit committee meeting on financial reporting quality listed Nigerian DMBs.
- iii. To assess the effect of accounting expertise in audit committee on financial reporting quality of listed Nigerian DMBs
- iv. To determine the effect of female membership in audit committee on financial reporting quality of listed Nigerian DMBs.

1.5 Research Hypotheses

Based on the statement of the problem and objectives of the study, the following null hypotheses are developed and tested in the null form.

H0₁: Audit committee independence has no significant effect on financial reporting quality of listed Nigerian DMBs.

H0₂: Audit committee meeting frequency has no significant effect on financial reporting quality of the listed Nigerian DMBs.

H0₃: Accounting expertise among audit committee has no significant effect on financial reporting quality of listed Nigerian DMBs.

H0₄: Female membership in audit committee has no significant effect on financial reporting quality of listed Nigerian DMBs.

1.6 Scope of the Study

The study covers only Deposit Money Bank (DMBs) in Nigeria which are listed on the Nigeria Stock Exchange. The study covers a period of eight (8) years (2007 to 2014). The period is chosen to enhance wide coverage of number of years after the enactment of the Code of Corporate Governance in Nigeria. The study is restricted to four variables (Audit Committee independence, Frequency of the Audit meeting, accounting expertise of the Audit committee members and female membership in audit committee) of audit committee characteristics with respect to their influence on financial reporting quality.

1.7 Significance of the Study

The study will be significant to the government, investors, corporate management, regulatory bodies, educators, accounting professional bodies and researchers particularly in the field of auditing and accounting. To investors, it will enable them to appreciate the direction of AC characteristics and the significant impact it has on the financial reporting quality hence, narrow their checklist of assessing the quality of financial reports, decision and judgment in the area investing and financing.

Regulatory bodies, Particularly CBN, stand to benefit immensely from this research in that the findings will reveal possible loopholes and short comings in respect to the code of corporate governance. The result will be used by the CBN in improving its supervision, monitoring and enforcement of the code especially as it relate to AC. The financial Reporting Council of Nigeria and Accounting professional bodies will benefit from the study, in that the study could be helpful in making the council improve the reporting requirement of companies and improve guidelines for member of professional bodies.

To potential researchers, the study is beneficial in exploring and understanding the impact of Audit committee characteristics and financial reporting quality in the banking industry. The study is a library material for researchers, students, and educators. It will particularly enhance the quality of literature in the area thereby serve as a benchmark for future research.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter reviewed relevant literature on the subject matter of study. It examines audit committee characteristics and financial reporting quality. The operational measures for these variables employed in prior studies were discussed. The common audit committee attributes used in the literature are audit committee independence, audit committee expertise, frequency of audit committee meeting, and audit committee gender. A review of previous empirical works was carried out and the theoretical framework upon which the study is situated was also provided.

2.2 The Concept of Corporate Governance

The idea of corporate governance has been developed due to the need for regulation of companies. This is necessitated by the prevalence of information asymmetry. There are several definitions of corporate governance as briefly discussed below. The Organization for Economic Cooperation and Development's Principles of Corporate Governance (1999) defines corporate governance as a set of relationships that exist between a company's management, its board, shareholders and other stakeholders.

This definition implies that corporate governance is a chain that harmonizes the owners of a company with managers, employees, customers and the society generally. The concept of corporate governance can also be explained as a system of making directors accountable to shareholders for effective management of the company in the best interest of the company and the shareholders along with concern for ethics and values. This definition utilizes three concepts,

which are important to corporate governance, namely, direction, control and ethics. However, the definition limits corporate governance to the relationship that subsists between the company and its shareholders, which in practical terms, all stakeholders matter in the discourse of corporate governance.

Furthermore, the Central Bank of Nigeria (CBN), in its Code of Corporate Governance (2006), defines corporate governance as a system by which corporations are governed and controlled with the aim of increasing shareholder value and meeting the expectations of the other stakeholders (Afolabi & Dare, 2015). This definition is insightful in that it contains salient issues conventional corporate governance including ownership, control, corporate social responsibility as well as value creation. This study therefore adopts the definition.

2.3 The CBN Code of Corporate Governance

The CBN code of corporate governance that is relevant is the Code of Corporate Governance for Banks in Nigeria Post Consolidation which was developed in 2006 (Afolabi & Dare, 2015). This code was developed to complement the earlier codes and enhance their effectiveness for the Nigerian banking industry due to the weakness identified in the existing Corporate Governance Code for banks in Nigeria. Some of the weaknesses include, but are not limited to, disagreements between the board and management giving rise to Board squabbles, ineffective board oversight, fraudulent and self-serving practices among members of the board, management and staff (Sanusi, 2010).

The code also gives more emphasis on board of directors and its audit committee. It stipulates a maximum of 20 directors, most of whom should be non-executive directors with at least two of the non-executive directors serving as independent directors. Such non-executive directors are allowed to hold office continuously for a maximum of 12 years comprising of 3 terms of 4 years each. The compensation for the non-executive directors is limited to sitting allowance, directors' fee and reimbursement for travel and hotel expenses. The code provides, as a minimum, existing of number of board committees such as risk management committee, audit committee and the credit committee.

In 2008, a committee was inaugurated by the Securities and Exchange Commission (SEC) to address the weaknesses posed by the 2003 Code of Corporate Governance, improve mechanisms for enforceability and align the code with international best practices (Afolabi & Dare, 2015). This led to the development of the Code of Corporate Governance for public companies in 2011. The code as the preceding ones focuses on the board and its audit committee. The code stipulates that the Board should be of a sufficient size relative to the scale and complexity of the company's operations and composed in such a way as to ensure diversity of experience without compromising independence, compatibility, integrity and availability of members to attend meetings. The minimum number of board membership is placed at 5 people. Also, the Code makes provision for three committees, Risk management committee, audit committee and Governance/remuneration committee.

2.4 Separation of Ownership from Control and Board of Directors

Due to the separation between ownership and management, shareholders are unable to directly

observe the actions of management (Jensen & Meckling, 1976). This makes it necessary for shareholders to relinquish control to managers thereby creating agency relationship. Under this relationship, managers (the agents) are engaged by shareholders (the principals) to act on their behalf based upon a pre-determined legal arrangement. However, divergence of interests by both the managers and shareholders gives rise to conflict of interest, wherein, managers tend to pursue their interests at the detriment of shareholders. This makes it mandatory for shareholders to develop oversight functions to be carried out on the managers. One of such mechanisms is the board of directors.

The board of directors has received considerable attention in the literature. This is due to the central position of the board of directors in corporate governance. The board of directors serves as a set of corporate governance mechanisms that monitors and controls the company's management as well as protect shareholders' interest. Jensen (1983) asserts that one of the major roles of the board is in monitoring the activities of management especially on the reporting process with a view to ensuring the credibility and reliability of the financial statement and reducing information asymmetry.

Directors of a company are the custodians or trustees of the company's resources and properties, they are duly appointed to direct and manage the business of the company. The Companies and Allied Matters Act (2011) as amended states that directors are required to prepare financial statements for each financial period which give a true and fair view of the state of affairs of the company as at the end of the financial period and to safeguard the assets of the company, to prevent and detect fraud and other irregularities. The board of directors is seen as a control

mechanism used by shareholders to indirectly oversee management activities. This can also be inferred from the agency theory perspective which proposes that board's monitoring role operates to protect shareholders from agency costs which arises from the agency problem inherent in managing an organization.

2.5 Types of Directors/ Functions of Directors

Directors of companies can be generally categorized into two (Afolabi & Dare, 2012). These include executive and non-executive directors.

Executive Directors: Executive directors are directors that are responsible for ensuring smooth day to day management of the company. They do these in various areas such as finance, marketing, personnel. As such, they are called finance director, marketing director, personnel director as the case may be (Afolabi & Dare, 2012).

Non-Executive Directors: Non-executive directors differ from the executive directors in that they are not involved operational affairs of the company. Since they are not always involved in day-to-day affairs of the company, they tend to have high level of independence (Afolabi & Dare, 2012).

In spite of the classification of directors, all directors perform similar functions. The functions of directors are as elaborated below:

Serving as Company Officer: Directors serve as officers of the company. As company officers, they ensure compliance with legal and statutory pronouncements of the relevant authorities.

where there is a breach of the any legal provisions by the company, they directors held liable (CAMA, 2011).

Maintaining Proper Books of Account: Directors give stewardship reports to resource owners. They do this by maintaining books of account. The books are prepared according to prescriptions of the relevant laws. The books are intended to reflect the transactions of the company. This provides sufficient ground for assessment of the financial position of the company.

Preparation of Annual Accounts: As part of stewardship reporting, directors are required to prepare accounts to users annually. The annual accounts take bearing from the company's books of account and other relevant information. To ensure their usefulness and reliability, accounts prepared by directors are expected to depict 'a true and fair view of the company's affairs. The usual annual accounts prepared by directors include statement of financial position, statement of profit or loss and other comprehensive income, statement of cash flows, statement of changes in equity, statement of value added, among others (Afolabi & Dare, 2012).

Maintaining Registers and Other Documents: Keeping of registry for the company is also one of the responsibilities of company directors. The registry, as kept by the directors, contains records of key affairs and correspondences of the company. In keeping these records, directors are required to adhere to requirements of the law. They are also expected to ensure that the records are regularly updated as appropriate and made available to the appropriate parties.

2.6 Audit Committee

According to the Sarbanes Oxley Act (2002), an audit committee is a committee established by the board of directors for the purpose of overseeing the accounting and financial reporting processes and audits of the financial statements of the company. In Nigeria, audit committee was a creation of the companies Act of 1990 and can simply be described as a committee made up of equal representation of directors and shareholders; three each, vested among other duties with audit and accounting oversight functions. Audit committee is also conceived as a subcommittee of the board of director which is particularly designated to oversee the company's financial reporting process. It is in this light that the International Professional Practice Framework (IPPF) in 2002 posits that audit committee is a standing committee of a board that has the oversight function of financial reporting process, internal and external auditor's activities. Audit committee is a committee of the board of directors which assumes some of the board's responsibilities (Menon & Williams, 1996). Unlike other concepts related to financial reporting that have universal and legally accepted definition; audit Committee (AC) lacks such definition. This is because, in some environments, its setup is a mandatory requirement whereas in others, it is not.

The Nigeria audit committee initiatives are statutory, that is evolved through a legal process in CAMA section 359(4). As such, all listed companies in Nigeria are required to establish audit committee. Countries such as Canada, Britain, America and Singapore also operate statutory audit committees. However, there are few countries where audit committee is implemented as a code of best practice hence, compliance is optional. The code is seen as a set of voluntary rules which all listed companies are expected to abide by. Examples of countries with non-statutory audit committee are Hong Kong and Australia (Klein, 2002). In such countries, enforcement can

be achieved through persuasion. In this study, AC is held as a committee made up of at least six members consisting of board of directors and company shareholders as a requirement of CAMA 2004 as amended and vested with the oversight function of ensuring that financial reports produced and published are of high quality, that is, are not misleading and satisfy as much as possible the different needs of the various users of the reports.

Audit committee has significant roles to play in ensuring quality financial reporting (McMullen and Raghunandan, 1996; Read & Raghunandan, 2001). The audit committee is responsible, among others, to ensure the appropriateness of management selection of accounting policies and disclosures in compliance with approved accounting standards, ensuring timely submission of financial statements by management, reviewing significant or unusual transactions and accounting estimates, and determining whether the financial reports presents true and fair view of the company financial position and performance and compliance with regulatory requirements. The committee is expected to review the financial reporting process and facilitate the flow of information among the board of directors, management, internal and external auditors.

According to Dezbart (1997) and Blue Ribbon Committee (1999), audit committees are directly responsible for the hiring, performance evaluation and compensation of external auditors for their services. The committee also oversees financial reporting and disclosure by monitoring the choice of accounting policies and principles as well as the internal control processes. The financial reporting oversight function of audit committee includes review of financial statement,

review of accounting changes, communication with stakeholders, standard and statutory reporting practices (Illaboya, 2012).

Audit committee is focused on the protection of the rights of shareholders, particularly in implementing corporate governance principles. This suggest that in the event of any financial manipulation possibilities, the AC can take action, to ensure that all grey areas are corrected and transparent financial reports are produced for users consumption. The wide advocate for the formation of audit committees around the world suggests the importance of an audit committee as a governance mechanism.

The CBN code of 2011 provided that the audit committee will be responsible for the review of the integrity of the bank financial reporting system and oversee the independence and objectivity of the external audit. Specifically, effective audit committee are expected to enhance financial reporting quality by fulfilling its numerous responsibility including commenting on and approving accounting policies, reviewing the financial statements and maintaining and reviewing the adequacy of internal controls. Audit committees are also expected to play an important role in enhancing the effectiveness of external auditors over financial reporting quality by assuming responsibilities for the appointment and remuneration of external auditors and discussing the scope of and reviewing the auditors work (Abbot & Parker, 2000).

In summary, audit committee is seen as a committee established by a company and tasked with overseeing the integrity for a company's financial responsibilities, in addition to managing the organization's risks and controls related to financial data and internal and external audit process.

Their recommendation enables organizations to address the need for a strong ethical environment hence the quality of financial information and reporting.

2.7 Financial Reporting Quality in Nigerian Banks

According to Barde (2009), financial reporting is concerned with the dissemination of accounting information to furnish current and potential users with basis to assess the financial position and cash flow potentials of a firm. The definition above shows that the objective, of financial reporting is to provide financial information about the reporting entity that is useful to existing and potentials equity investors, lenders and other creditors in making decisions in their capacity as capital providers. It is from this view that the Financial Accounting Standards Board (FASB) (1999) and the International Accounting Standards Board (IASB) (2008), state the primary objective of financial reporting as the provision of high quality financial reporting information concerning economic entities, primarily financial in nature, which is useful for economic decision making. Financial reporting is an important means for management to communicate, among other things, the company's performance to external stakeholders.

The FASB (1999) states that financial reporting quality is the accuracy with which information about the firm operation is presented in financial reports especially the firm cash flows, in order to inform equity investors. Financial reporting quality is also defined as the degree to which the financial reports of a firm provide true and fair information about its underlying performance and financial position. The foregoing indicates that the concept of financial reporting quality is broad and includes financial and non-financial information disclosures and nonfinancial information useful for decision making. Financial reporting is a two party transaction in which the issuers of

the financial reports provides them to the user's, who use them with the expectation that these will enhance their decisions. Financial reporting quality can be explained as the precision with which financial reports convey information about the firms operation in particular its cash flows, in order to inform equity investors. However, this definition is defective as financial report should not be restricted to cash flow.

The need for quality financial report has always been an issue of interest among regulatory bodies, shareholders, researchers and the accounting profession itself. In fact, the objective of regulators and standard setters is to promulgate rules and regulations that help to ensure financial reporting quality. This could be explained on the fact that financial reporting is a principle means of communicating financial information to outside users, in assessing the economic performance and condition a business, in monitoring management actions and in making economic decisions. Financial reporting quality has been asserted as the mainstay of modern capital markets. Financial reporting quality is a prerequisite for efficient capital markets because several individuals and groups base their resource allocation decisions on financial information (Petra, 2007).

Furthermore, Atrill and McLaney (2001) outline certain key criteria that financial reporting should possess in order to meet the needs of users. These criteria are identified as relevance, reliability, comparability, understandability, timelines and cost/benefits. According to Atrill & McLaney (2001) the relevance and reliability of financial report can help to produce useful information but the lack of comparability understandability, timeliness and cost/benefit on getting the information in turn will limit its usefulness. By and large, it could be concluded that

quality financial reporting is of crucial importance to the decision making process of investors, the growth and development of the capital market and indeed the economy of any nation.

2.7.1 Measurement of Financial Reporting Quality

The measurement of the quality of financial reports has been an issue in financial reporting research. Beest, Braam and Boelens (2009) identify four broad but not restrictive categories; accrual models, value relevance models, specific elements of financial reports, and methods that operationalize the qualitative characteristics.

Accrual methods are based on the concept of earnings management. Earnings management is the manipulation of the external financial reporting process with the aim of obtaining some private gain (Schipper, 1989). Accrual model focuses on earnings quality measurement under current rules and legislation. This model assumes that managers use discretionary accruals (i.e. accruals over which the managers can exert some control) to manage earnings (Dechow, Sloan & Sweeney, 1996; Healey and Wahlen, 1999; Beest, Braam & Boelens, 2009). A widely used model by many researchers is the Jones model or its modified versions. This model has been used in the literature to capture earnings management, which is viewed as an inverse measure of earning quality. The other frequently used proxy for earnings and accruals quality is the Dechow and Dichev (2002) accrual quality measure that is based on how well accruals map into cash flows. This measure defines accrual quality as the error variance from a regression of working capital accruals on past, current, and lagged cash flows. Accruals models have been criticized for providing biased and noisy estimates (Jones, 1991). The main difficulty when using accrual

models, however is how to distinguish between discretionary and non- discretionary accruals (Healey & Wahlen, 1991).

The value relevance model is designed to assess whether particular accounting amounts reflect information that is used by investors in valuing firms' equity (Barth, 2001). Hoithausen and Watts (2001) classify value relevance studies in three categories; relative association studies, incremental association and marginal information content studies. Relative association studies focus on the relationship between stock market values or returns and various accounting numbers, based on standard regression techniques. Incremental association studies utilize regression models in order to examine if an accounting variable is useful in explaining value or returns over a long time period. Marginal information content studies are concerned with the relationship between returns or abnormal returns and investors available set of information. The most frequently employed model in value relevance research is on Ohlson (1995) and its subsequent modifications (Feitham & Ohisoll, 1996; Ohison, 1991). Value Relevance model can also be used to examine earnings persistence, predictive ability and variability, as elements of quality. The short coming of these models is that it cannot distinguish between relevance and reliability.

Accrual and value relevance models focus on information disclosed in financial statement to assess the financial reporting quality. However, a comprehensive measurement tool of financial reporting quality would at least include the complete annual report including both financial and non-financial information. Therefore, research on specific elements in the annual reports has also surfaced. Research on specific elements of financial report includes measurement tools that focus

on both financial and non-financial information of the reports. Such studies are concerned with examining the influence of specific information of the annual reports on the decision of the users. Studies in this area include, the examination of restatements in the financial statements; the use of narratives in the annual reports; the use of graph in the annual reports, among others (Palmrose, 2000). However, researches that focus on a specific element in the annual report has a partial focus and this does not provide a comprehensive overview of total financial reporting quality.

The fourth categorization includes methods that operationalize qualitative characteristics to assess the qualities of different aspect and dimensions of financial and non-financial information of financial reports in order to determine their usefulness (Beest, Braam & Boelens, 2009). This is achieved through the use of indexes or questionnaire created to capture the qualities of the qualitative characteristics which include relevance, faithful representation, comparability, timeliness and understandability.

This study uses accrual method to measure financial reporting quality. The choice of accrual model is hinged on the contention that it is much more objective. Accrual model focuses on earnings quality measurement under current rules and legislation.

2.8 Audit Committee Characteristics

The characteristics of AC consist of audit committee independence audit committee meeting frequency, and audit committee attendance. These characteristics are examined in the following sub- sections.

2.8.1 Audit Committee Independence and Financial Reporting Quality

An audit committee is expected to be independent of management in order for it to carry out its oversight functions effectively. However, it is worrisome that most audit committees lack this important quality. Lack of audit committee independence has caused stakeholders to question the reliability of financial reports prepared by management. There are varied understandings of the concept of AC independence among researchers. Notwithstanding, the United States Securities and Exchange Commission (SEC) defines independence in the context of compensation or advisory fees received by the directors or by the amount of control that the director has over the firm (SEC, 2003). The SOX (2002) considers that an audit committee member is independent if he or she does not receive any compensation from the company or its affiliates except in the capacity of audit committee member. A majority of the non-executives serving on committee should be independent of the company in terms of management or business or other relationship which could materially interfere with the exercise of their independent judgment as committee members. This position is supported by the SOX which requires firms to have audit committees comprised solely of independent directors who are not employees of the firm and not accepting any compensation from the firm other than directors' fees.

The issue of independence is sacrosanct to audit committee effectiveness. Examining the relationship between audit committee effectiveness and independence, Raghunandan, Read and Rama (2001) and Krishnan (2005) established a positive correlation between independence and audit committee effectiveness. To them, an adequate independent audit committee is likely to

guarantee efficient internal control. In addition, they reported that independence is likely to strength effective internal audit function.

Similarly, Cadbury Committee (1992) reported that audit committee provides a framework with which the external auditors can asserts his independence in the event of a dispute with management and also strengthen the position of the internal audit function by providing a greater degree of independence from management. Dezoort and Salterio (2001), found that independent, more knowledgeable AC members were more likely to support the auditor in dispute with the management. Klein (2002) also found a positive association between board size, proportion of outside board members and AC independence. In addition, a negative association was found between firm's growth opportunities, existence of large shareholders on the audit committee and firm size with AC independence. However, effect was found between creditors, CEO on compensation committee and outside member's shareholding with AC independence. This suggests that the independence of audit committee may be affected by the independence of the board in general.

Proxies for the audit committee's degree of independence include the percentage of outside members on the committee and dummy variables indicating a majority or totality of independent members. Baccouche, Hadriche and Omri (2013) empirically investigated the effect of the multiple directorships held by audit committee directors on the level of earnings management of listed French companies. The investigation was carried out on a sample of 88 non-financial French listed firms that belong to the SBF 120 index, for the financial year 2008. The results suggest that the accumulation of several outside directorships by audit committee members may

lead to a higher degree of earnings management, as measured by the magnitude of discretionary accruals. The study also used only one variable of audit committee characteristics.

Bryan (2004) investigated the effect of AC Independence on the quality of financial reporting and found that companies with independent AC were less likely to suffer sanctions by the SEC for fraudulent financial reporting. This is contrary to studies that found that AC independence influence FRQ. Felo, Krishnamurthy and Solieri (2003) found no relationship between audit committee independence and financial reporting quality. The study investigated perceived quality of financial reporting, proxy by membership ratings and the percentage of non-independent members on audit committees, a significant negative association between the changes in both variables over the 1989 - 1993 periods. Overall, these findings are consistent with audit committee independence enhancing financial reporting quality.

Klein (2002) sought to determine whether AC with majority independent outside members affect financial reporting quality than those associated with minority proportion of outsiders. The finding of the study supports the view that an audit committee with a simple majority of outsiders is more likely to fulfill its duties effectively than a committee without a majority. However, further increase in the proportion of independent members is unlikely to be associated with increase in financial reporting quality. The study also shows that a having an audit committee entirely composed of outsiders has no significant effect on the magnitude of abnormal accruals.

Menon and Williams (1996) conclude on the basis of their findings that AC activity and independence was positively associated as expected, with the proportion of outside directors on the board and that AC activity was greater for large companies. They studied 200 over the counter (OTC) firm in US for the year 1993. Klein (2000) conducted a study in US between the period of 1991-1993 on 803 S&P 500 firms that had SEC field proxy statements, regression analysis was used to analyze the data and the findings indicates a positive association between AC independence and AC size and AC independence and the proportion of outside board members in other listed companies.

Ormin, Tuta and Shadrac (2015) examined the influence of the audit committee attributes of independence, meeting frequency and attendance on the financial reporting quality of listed deposit money banks in Nigeria. Data was generated from the annual reports and accounts of six purposively sampled banks during the period 2003 to 2012. The data was analyzed using Pearson correlation statistics and OLS regression. The results show that audit committee independence has negative and significant influence on financial reporting quality of listed deposit money banks in Nigeria. While audit committee meeting frequency and attendance has positive and significant influence on financial reporting quality of listed deposit money banks in Nigeria.

Kantudu and Samaila (2015) examined the impact of monitoring characteristics on financial reporting quality of the Nigerian listed oil marketing firms. Financial reporting quality was represented with the qualitative characteristics of financial statement. Data for the study were obtained from an audited annual report and accounts of the sampled oil marketing companies for twelve years covering 2000 to 2011. Multiple regression was used to analyzed the data. It was

discovered that power separation, independent directors, managerial shareholdings and independent audit committee are all significant implying monitoring characteristics influence financial reporting quality of quoted oil marketing firms in Nigeria.

2.8.2 Audit Committee Meeting Frequency and Financial Reporting Quality

In practical terms, audit committee meeting frequency is expected to wield influence on financial reporting quality. Consistent meetings enable members of the audit committee to evaluate salient aspects of financial reports prepared by management. There are several dimensions that can be used to indicate audit committee activities such as meeting frequency, meeting duration and time allocation among different function, meeting regularly, information exchange at the meeting, and whether executive directors are present at meetings and level of attendance of audit committee members. Due to archival data constrain, the two dimensions of activity that are examined in this study are frequency of audit committee meetings, and the level of attendance of audit committee members. The second variable of attendance is chosen together with AC meeting frequency because even though the frequency of meeting is high, IF the attendance levels are poor this impairs the effectiveness of the audit committee.

Audit committee meeting frequency relates to the number meetings held per year by the audit committee. In Nigeria, CAMA provides that the AC meet at least three times in a year {S. 359 (3 and 4) of CAMA, 2004}. 1-lower, other regulatory statute does not specify the committee meeting frequency. For instance, the BRC report does not address how often audit committees should meet. Likewise, the US stock exchange regulations do not contain any specific rules regarding the frequency of audit committee meetings. Notwithstanding, Price Waterhouse (1993)

suggest that audit committees should meet at least four times a year and make provisions for special meetings when warranted (Beasley, 1996).

Wiralestar and Tanzil (2015) documented that audit committee is an essential pillar of corporate governance in establishing integrity and quality financial reporting. The research aimed to assess the impact of audit committee toward financial reporting's quality in non-financial issuers listed in Indonesia Stock Exchange. The dependent variable of the research was the quality of financial report. The proxy employed in the research was discretionary accrual using modified Jones model. The independent variable of the research was the audit committee characteristics such as skills, the size of the committee, and the frequency of the activity and meetings. The size of audit committee was measured by seeing the percentage of audit committee possessed by a company. Frequency of committee meeting or activity was measured as the percentage of meeting conducted by audit committee. The target population of the research was the Non-Financial Companies listed in Jakarta Stock Exchange (JSE). Probability sampling was used to arrive at 82 companies. Secondary data were collected and analyzed using multiple regression analysis.

The findings of the research indicated that the audit committee had significant impact on financial reporting's quality. Abbott and Parker (2000) found that an audit committee which meets at least twice a year significantly reduces the probability that a firm will be subject to an SEC enforcement action for aggressive or fraudulent financial reporting. The study sampled 83 companies over the period ranging from 1999 to 1999 and used multivariate regression for analysis. In another study, Abbott, Parker and Peters (2004) established the likelihood of earning restatement significantly decreasing during the period 1991-1999 for firms whose AC meeting at

least 4 times a year. Empirical research related to AC expertise variables, particularly in the US, has produced useful evidence with respect to several financial reporting quality surrogates. Jenkins (2002) reported that the proportion of financial expertise on the audit committee - mitigates income-increasing earnings management.

Mutalib and Lawan (2011) investigated whether the frequency of audit committee meeting has a significant impact on the equity return of listed insurance firms in Nigeria. Ten firms were selected. Results revealed that the frequency of audit committee meeting has a significant positive relationship with the equity returns of firms in the Nigerian insurance industry. They recommended that audit committee should meet regularly, as the more they meet, the better the return on equity for firms in the insurance industry. Regarding fraudulent financial reporting, Farber's (2005) matched comparison indicates slightly fewer meetings for fraud firms the year before the fraud is unveiled but the trend reverses significantly five years later.

An empirical study by Forgarty and Kalbers (1998) sampled 164 partners, chief financial officers and chief of internal audit for 90 companies and uses survey research and suggest that is difficult to measure the construct of power of the audit committee. With respect to audit committee meeting, Dabor and Dabor (2015) examined the relationship between audit committee characteristics, board characteristics and financial reporting quality in the Nigerian banking sector. Samples of nine banks were selected using the simple random sampling technique. Secondary data were drawn from annual reports and accounts of the selected firms for nine years (2006- 2014).Data for the selected banks were analyzed by employing ordinary least square regression technique. The period under review was ten years. The result of the study shows a

positive relationship between audit committee meetings and financial reporting quality. However, the study revealed that there is no significant relationship between board size, board expertise and financial reporting quality.

2.8.3 Audit Committee Financial Expertise and Financial Reporting Quality

Ojeka, Iyoha and Asaolu (2015) submitted that audit committee financial expertise is vital to the quality of financial reporting. This study empirically investigated the impact of audit committee financial expertise on the quality of financial reporting. The financial reporting quality was measured by reliability (total accrual quality) and relevance (audit report lag). Fifteen money deposit banks were selected and data was collected for the period (2003-2012). Analyses were carried out using correlation, Ordinary Least Square and Panel Least Square. The study found, after controlling for firm size, audit type, age of firm, audit committee meeting and audit committee size, showed that audit committee financial expertise has a positive significant impact on financial reporting quality in Nigeria. This implies that there is need for assessing financial expertise of directors being recommended to the audit committee. The study however, could not use most of the variables of audit committee characteristics which is the preoccupation of this study.

Ibadin and Dabor (2015) noted that financial reports published by companies serve as the major means of financial information. Hence, the quality of these reports determines the types of decisions investors make. By using secondary data from 150 companies in Nigeria, the study sought to know the relationship between corporate governance variables and accounting quality, proxy by timeliness. The data were analyzed using the Ordinary Least Square (OLS) of multiple

regressions along with the descriptive statistics to obtain the mean, standard deviation, minimum and maximum values. The findings of the study show that strict corporate governance mechanisms enhance financial reporting quality.

Aryan (2015) conducted study on 69 out of 91 industrial companies during the study period (2009-2014). Multiple regression was used to analyze the data, and the result showed positive relationships between audit committee meeting, audit committee size and companies profitability, while non-significant relationship between audit committee composition, audit committee members literacy, audit quality and companies profitability. Yang and Krishnan (2005), investigating the magnitude of quarterly earnings management during 1996 - 2000, reported insignificant effects regarding the presence of a financial expert on the audit committee but mitigating effects associated with governance and business expertise. Few studies have addressed financial reporting quality surrogates other than earnings management but the study uses earnings management as a surrogates.

Madawaki (2013) examined whether audit committees are associated with improved financial reporting quality for a sample of Nigerian listed companies prior to and after a corporate governance code mandated new regulations for audit committees in 2003. Using a sample of 70 companies listed on the Nigerian Stock Exchange, the study used archival data in the form of companies' annual reports to measure the association between audit committees and improved financial reporting quality. Dechow and Dichev (2002)'s model was used to measure earnings as a proxy for financial reporting quality. The results indicate that formation of audit committees was positively associated with improved financial reporting quality. It was also found that audit

committees having an independent chair and audit committee expertise were positively associated with financial reporting quality. Other audit committee characteristics examined were found to be insignificantly related to financial reporting quality.

Kibiya, Ahmad and Amran (2016) investigated the effect of audit committee characteristics on the quality of financial reporting of Nigerian listed firms. The study employed multivariate regression analysis with a sample size of 101 and firms-year longitudinal panels of 505 observations of non-financial listed companies on Nigerian Stock Exchange for the period 2010 to 2014. The study adopted McNicholas (2002) model to examine the monitoring mechanisms on the quality of financial reporting. The results show that audit committee share ownership, and financial expertise are positive and statistically significant, indicating that audit committee monitoring mechanisms influence the financial reporting quality of listed non-financial firms in Nigeria.

2.8.4 Audit Committee Female Membership and Financial Reporting Quality

Some studies have examined the effect audit committee female gender on financial reporting quality. Such studies have been carried out to evaluate the perception that female audit committee members have the tendency to ensure honesty and transparency in financial reporting. Illaboya (2012) conducted his study in Nigeria for the year 2011, among Accountants, Lawyers, Academic Bankers and Shareholders from Edo and Delta which formed the study group. Based on-test statistical technique which was used to analyse data, it was found that a structurally defective audit committee characterized by irregular meeting, unbalanced membership and absence of good leadership affect financial reporting quality.

Salleh and Haat (2013) examined the relationship between audit committee diversity and financial reporting quality in Malaysia after the revision of the Malaysian Code of Corporate Governance (MCCG) in 2007. The sample for this study was drawn from 280 companies listed on Bursa Malaysia in 2005, 2006, 2008 and 2009. Multivariate regression analysis was used to analyse the data collected. The study found that female directors show no effect in promoting financial reporting quality which may be due to the small size of female members in the audit committee.

It is quite clearer from the foregoing review that AC plays a significant role in ensuring high financial reporting quality. It is also pertinent to state that most of the studies on AC and FRQ are conducted in the US and other developed countries. Developing countries including Nigeria appear to document little research in this area. Though, studies are beginning to spring up in Nigeria and other developing countries the mixed results of studies conducted in the developed countries allows for modified or even replicative studies to be conducted in other environments. This study is therefore significant and has gap to fill.

2.9 Theoretical Framework

In examining the impact of audit committee characteristics and financial reporting quality in listed Deposit Money Banks in Nigeria the agency theory is found to be relevant.

2.9.1 Agency Theory

Agency relationship exists where one party (the principal) engages another party (the agent) to perform services on his behalf. Hence, the principals' interests require protection due to the

separation of ownership from control. The principals (owners) need quality information to monitor, control, and motivate the agents; whereas, the agents (management) have full control over the information flow. The agency theory was developed to address the issues relating to conflict of interest which may arise as a result of separation of ownership and control of the business between the principal and the agent.

The theory argues that, the agents may have motives and goals which they may pursue that are at variance with the company's goals, in other words, they may be driven by self-interest to act in such away which is not always in the best interest of the principals. In order to monitor any self-interest of the agent, the principals establish control and reporting process to regularly monitor agent's behavior and their performance to ensure they act in the owner's interest; this action gives rise to agency cost because monitoring is always associated with the cost which is borne by the owners. To reduce these costs, the owners institute a control mechanism through the board of directors and audit committees with a view to reducing management opportunistic behavior. The proponents of agency theory views board of directors as control mechanism that addresses the conflict of interest that may arise between the management and shareholders as a result of separation of ownership and control.

Agency theory is the theory that best explains the relationship between audit committee characteristics and financial reporting quality. According to the theory, the oversight function is established to mitigate reported earring manipulation thereby providing high quality financial information thus, result in high financial reporting quality.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter presents and discusses the methodology for the study. It explains the research design, the population of the study, sample size and sampling techniques, sources of data, study variables and their measurements and techniques of data analysis to be used for the study.

3.2 Research Design

In order to ensure that evidence obtained adequately addresses the research, the study uses correlational research in a bid to analyze the relationship between the dependent and independent variables. The choice of this research design is predicated on the ground that it provides basis for testing of expected relationships between audit committee characteristic and financial reporting quality of listed Deposit Money Banks in Nigeria and the making of predictions regarding such relationships. The research design hinges on positivism which emphasizes a more scientific, objective and systematic approach to research, through use of quantitative method (Saunders, Lewis & Thornhill, 2007).

3.3 Population of the Study

The population of the study comprises all the listed Deposit Money Banks (DMBs) in Nigeria as at 31st December 2015. There were fifteen (15) listed banks on the Nigeria stock exchange as at 31st December, 2015. These include Access Bank, Diamond Bank, Ecobank, Fidelity Bank First Bank First City Monument Bank, Guaranty Trust Bank, Skye Bank, Stanbic IBTC Bank, Sterling Bank, Union Bank, United Bank for Africa, Unity Bank, Wema Bank and Zenith Bank.

3.4 Sample and Sampling Techniques

Census approach is used. Because of this, all the Deposit Money Banks are used. The choice of all the Deposit Money Banks is informed by the need of the researcher to cover all the elements of the population such that possible generalization can easily be made. The selected banks share marked similarities in terms of their nature of work and environment of operations. They render financial services to customers and investors who need quality financial reports in order to make informed economic decisions.

3.5 Source and Method of Data Collection

The source of data for this study is secondary. The secondary data were collected from the published annual reports and accounts of the sampled banks. The annual reports are retrieved from the websites of the banks as well as the Nigerian stock exchange Fact Book. This is for a period of eight years from 2007 to 2014.

3.6 Variables Measurement

There are two sets of variables covered by this study. These are the explained and the explanatory variables.

3.6.1 The Explained Variable

The explained variable is the financial reporting quality. Financial reporting quality is measured by using Abnormal Loan Loss provision (ABLL) as a proxy for earnings management

which is measured in line with Kanagaretnam, Krishnan and Lobo(2010), Dabor and Ibadin (2013) as:

$$LLP_{it} = \alpha_0 + \alpha_1 LLAB_{it} + \alpha_2 NPLAB_{it} + \alpha_3 \Delta NPL_{it} + \alpha_4 NBLW_{it} + \alpha_5 \Delta TOTL_{it} + \epsilon_{it}(iv)$$

The residuals from equation above are the abnormal loan loss provision where;

NPLAB = Non-Performing Loans at the beginning,

LLP = Loan loss provisions,

Δ NPL = Change in Non-performing Loans,

NBLW = Net Bad Loans Written Off and

Δ TOTL = Change in Total Loan Loss

3.6.2 The Explanatory Variables

The explanatory variables are the independent and control variables:

Independent variables: Audit committee characteristics are independent variables.

The measurement of the audit committee characteristics which is a corporate governance mechanism variable include:

Audit Independence (ACIND): This is the proportion of audit committee members who are independent. This is measured as the proportion of independent audit committee members to total audit committee members (Krishnan, 2005).

Audit Committee Meeting (ACMEE): Audit Committee members number of meeting held by the committee during the year as measured by Wan-Hussin and Haj-Abdullah (2009) and Illaboya (2012) which is expressed as an absolute value or number.

Female membership in audit committee: This is measured as a proportion of female audit committee members to total audit committee members. This measure is intended to be used to find out whether female membership in audit committee affects financial reporting quality (Illaboya, 2012).

Accounting expertise of audit committee members: This is measured as a proportion of audit committee members with accounting experience to the total number of audit committee members. Accounting expertise is determined from the profile of the directors. Directors with degrees in accounting or finance are deemed to have accounting expertise (Ojeka, Iyoha & Asaolu, 2015).

Control variable: The control variable used in this research is firm Size (FSIZE): This is measured by taking the natural log of total assets as a proxy of size. Such control is necessary because the bigger the hank, the larger the expedited agency problem it will be experiencing (Dahar & Adeyemi, 2009).

3.7 Model Specification

The model for this study is:

FRQ = F(AC) which is further expressed in the form of a linear equation as:

FRQ = F (ACIND, ACMEE, ACFEP, ACFD, FSIZE, FAGE)

That is:

$$FRQ_{it} = \alpha_0 + \alpha_1 ACIND_{it} + \alpha_2 ACFREG_{it} + \alpha_3 ACFEP_{it} + \alpha_4 ACFD_{it} + \alpha_5 FSIZE_{it} + \alpha_6 FAGE_{it} + \epsilon_{it}$$

Where:

FRQ_{it} = Financial Reporting Quality for firm i in time t.

$ACIND_{it}$ = Audit Committee independence for firm i in time t.

$ACFREG_{it}$ = Audit committee frequency of meeting for firm i in time t.

$ACFEP_{it}$ = Audit committee financial expertise for firm i in time t.

$ACFD_{it}$ = Audit committee female members for firm i in time t.

$FSIZE_{it}$ = Firm size for firm i in time t

α_0 = Intercept.

$\alpha_1, \alpha_2, \alpha_3, \alpha_4, \alpha_5, \alpha_6$ = Model coefficients.

e_{it} = Error term.

3.8 Techniques for Data Analysis

Based on the data type and previous research studies, the study will use panel data regression technique. The major tool of data analysis that will be used is multiple regression analysis which will be carried out with the aid of STATA statistical software. The data will be further analysed using various robustness tests such as multicollinearity, normality and heteroscedasticity. To address panel effect of the data, fixed effect and random effect options will be explored. Hausman specification test will be used to provide direction as whether fixed effect or random effect will be used. The essence of these analyses is to improve the validity of all the statistical inferences that will be made. The choice of stata is predicated on the fact that it gives room for carrying out various robustness tests such as multicollinearity, normality and heteroscedasticity tests.

CHAPTER FOUR

DATA PRESENTATION, ANALYSIS AND INTERPRETATION

4.1 Introduction

The focus of this chapter is to present empirical results from analysis performed using data collected for the sampled firms from 2007-2014. The overall aim is to examine whether audit committee independence, audit committee meeting, audit committee gender, audit committee financial expertise, and firm size affect financial reporting quality of listed Deposit Money Banks in Nigeria. The chapter contains analysis of descriptive statistics, correlation matrix, robustness test, Hausman specification test, regression results, test of hypotheses, discussion of findings and policy implications.

4.2 Descriptive Statistics

The various descriptive statistics are displayed in table 4.1 below. The essence of the table is to provide understanding on the nature of data being used.

Table 4.1: Summary of Descriptive Statistics

Variables	Min	Max	Mean	StdDev	N
FRQ	0.0017	0.950	0.3529	0.3104	120
ACIND	0.3367	1	0.5472	0.3367	120
ACFREQ	2	6	4.1500	0.8565	120
ACFEP	0.2803	1	0.5378	0.2585	120
ACFD	0	0.2789	0.0919	0.7586	120
FSIZE	12.12	22.92	19.8983	2.0818	120

Source: STATA Output Version 11, 2016.

Table 4.1 reveals that the mean value of FRQ is 0.3529. The minimum value of FRQ for the

firms is about 0.0017. This implies that the lowest level of financial reporting quality of the firms is 0.0017. The maximum value of FRQ is about 0.950. This implies that the maximum level of FRQ of the firms is about 0.950. The standard deviation of FRQ is 0.3104, which implies that there is low variability in the level of financial reporting quality by the studied firms. ACIND has mean value of about 0.5472, minimum value of about 0, maximum value of about 1, with a standard deviation of about 0.3367. The standard deviation of 0.3367 suggests low variability in the level of audit committee independence of the studied firms over the period of study. ACFREQ has minimum value of about 1, maximum value of 6, with a standard deviation of 0.8585. The standard deviation of 0.8565 implies that there is low variability in the number of meetings of the audit committee of DMBs in Nigeria over the period of study.

The mean of ACFEP is 0.5378, which means that on average, DMBs in Nigeria have about 53.78 % of the members in their audit committee as financial experts. The minimum number of ACFEP is 0.0280, which suggests the lowest proportion of members of audit committee with financial expertise is about 3%. However, the maximum value is 1, a point where all the audit committee members have some level of financial expertise. The standard deviation is 0.2585, which indicates low variability in the level of financial expertise of members in the audit committee of DMBs in Nigeria. The minimum value of ACFD is 0 which suggests absence of a female audit committee in the audit committee composition of some of the DMBs in Nigeria. The maximum value is 0.2789 which implies that the maximum percentage of female audit committee members is about 27.89%. On average, about 9% of the audit committee members are female. The standard deviation is about 0.7586 which implies that there is low variability in the proportion of female audit members in the audit committee of DMBs in Nigeria.

FSIZE has mean value of 19.90 which shows that on average, the size of the DMBs in Nigeria is about 19.90. The minimum value is 12.12 while the maximum value is 22.92. The standard deviation is about 2.08 which mean that there is high variability in the size of the DMBs in Nigeria.

4.3 Correlation Matrix

The correlation matrix below reveals the correlation between the dependent variable and each of the independent variables as well as among the independent variables.

Table 4.2: Correlation Matrix of Dependent and Independent Variables.

Variables	frq	Acind	acfred	Acfed	Acfed	Acfed	Fsize
Frq	1.0000						
Acind	-0.0860 0.3504	1.0000					
Acfreq	0.1720 0.0608	-0.0352 0.7025	1.0000				
acfep	-0.1126 0.2206	0.0790 0.3913	-0.0378 0.6822	1.0000			
acfd	0.2659* 0.0033	-0.0983 0.2853	0.0450 0.6253	0.3552* 0.0001	1.0000		
fsize	0.3036* 0.0009	-0.0559 0.5545	0.0510 0.5801	0.2855* 0.0016	0.3218 0.0003	1.0000	

Source: Output from STATA.

From the correlation matrix above, it can be explained that ACFREQ, ACFD and FSIZE are positively correlated with FRQ of the DMBs in Nigeria. The implication is that the above variables move in the same direction with the FRQ of DMBs in Nigeria. On the other hand, ACIND and ACFED have negative correlation with FRQ, implying that they move in opposite direction with FRQ. Relatedly, the table indicates that there is positive correlation between

ACIND and ACFEP, ACFREQ and ACFD, ACFEQ and FSIZE, ACFD and FSIZE while there is negative correlation between ACIND and ACFREQ, ACIND and ACFD, ACIND and SIZE, as well as ACFREQ and ACFEG.

4.4 Robustness Tests

The following robustness tests are carried out to find out whether data used for analysis is reliable.

4.4.1 Test for Multicollinearity

Non- existence of multicollinearity is a key assumption of linear regression analysis. Multicollinearity occurs when the explanatory variables are not independent from each other. Multicollinearity is examined using tolerance and variance inflation factor (VIF) values. The result of multicollinearity test is shown in the table below.

Table 4.3: Tolerance and VIF values

Variables	VIF	1/VIF
ACFD	1.24	0.807564
ACFEP	1.21	0.823665
FSIZE	1.16	0.858594
ACIND	1.03	0.972524
ACFREQ	1.01	0.991636

Source: STATA Output, 2016.

Based on the evidence presented in Table 4.3, it can be concluded that there is no multicollinearity problem. This is because the VIF values for all the variables are less than 10 and the tolerance values for all the variables are greater than 0.10 (rule of thumb).

4.4.2 Test for Heteroscedasticity

Heteroscedasticity arises when the error terms along the regression are not equal. Heteroscedasticity was tested using Breusch Pagan's test. Based on the results, it can be concluded that there is no problem of heteroscedasticity as the chi square is 4.56, which is

significant, implying that there is presence of heteroscedasticity. Hence, robust test was carried out as presented in appendix 11 and the results shows that the data used for analysis is reliable and the variables chosen are suitable for the estimated model.

4.4.3 Fixed and Random Effect Tests

Fixed effect test and random effect test are carried out. The results of these are shown in appendix II. Hausman specification test produced chi-square value of 3.97, which is not significant. This implies that the variation across entities is assumed to be random and uncorrelated with the predictor or independent variables included in the model. On this basis, result for random effect test was used for analysis. Furthermore, Breusch and Pagan Lagrangian multiplier test for random effects was performed to ascertain whether the Ordinary least squares result of the random effect result should be used. The result suggests that random effect should be used as the χ^2 (120.01) was significant at 1%.

4.5 Random Effect Regression Results

The result of the random effect is presented in table 4.4 below.

Table 4.4: Random Effect Regression Result

VAR	COEFF	Z-value	P>(Z)
ACIND	0.0150025	0.29	0.776
ACFREQ	0.0498576	2.20	0.028
ACFEP	-2.492292	-2.57	0.000
ACFD	1.975432	4.47	0.010
FSIZE	0.0043205	0.24	0.810
C	-0.0042473	-0.01	0.992
R-Squared:	0.2123		
Wald-statistics	28.35		
Prob	0.0000		

Source: Output from *STATA* software, version 11, 2016

In table 4.4, it can be observed that the R^2 is 0.2123 which means that 21.23% of variation in FRQ of DMBs in Nigeria is explained jointly by the independent variables captured in the model. The wald- χ^2 is 28.35 which is significant at 1% . This is indicative of the fitness of the model.

4.5.1 Audit Committee Independence and Financial Reporting Quality

The coefficient of ACIND is 0.0150025 which means that ACIND has positive relationship with FRQ of DMBs in Nigeria. It also means that a unit increase in ACIND will lead to a corresponding increase in FRQ by 0.0150025. What this suggests is that independence of audit committee members helps to ensure the credibility of financial reporting. Audit committee members who are independent might be more objectively disposed to evaluate the accuracy of financial reports presented by management as well as their true and faithful representation of underlying economic substance.

The Z-value of ACIND is 0.29 while its p-value is 0.776 which is not significant. This means that although audit committee independence positively affects financial reporting quality of DMBs in Nigeria, the influence is not significant. Therefore, the first hypothesis of the study which states that audit committee independence has no significant effect on financial reporting quality of listed Deposits Money Banks is accepted. This finding is inconsistent with the finding of Kantudu and Samaila (2015), Ormin, Tuta and Shadrac (2015), Baccouche, Hadriche and Omri (2013) who submitted that audit committee independence has significant relationship with financial reporting quality of Deposit Money Banks in Nigeria.

4.5.2 Frequency of Audit Committee Meeting and Financial Reporting Quality

Similarly, the coefficient of ACFREQ is 0.0498576. This suggests that ACFREQ has positive coefficient with FRQ of DMBs in Nigeria. A unit increase in ACFREQ will lead to a corresponding increase in FRQ by 0.0498576. The positive relationship between frequency of audit committee meeting and financial reporting quality is in support to the a priori expectation of the study. It supports the understanding that the more frequent audit committee members meet, the more frequent they evaluate financial reports presented by management. Critical and frequent examination of management's financial reports ensures that misstatements of financial statements are checked.

The Z-value of ACFREQ is 2.20, with a p-value of 0.028 which is significant at 5%. This provides evidence against the second hypothesis of the study. On this basis, the second hypothesis of the study which states that frequency of audit committee meeting has no significant influence on financial reporting quality of the listed Deposits Money Banks in Nigeria is rejected. This finding is in support of the finding of Kibiya, Ahmad and Amran (2016) Madawaki (2013), Wiralestar and Tanzil (2015), Ojeka, Iyoha and Asaolu (2015) who reported that frequency of audit committee meeting has significant effect on the financial reporting quality of listed Deposit Money Banks in Nigeria.

4.5.3 Accounting Expertise of Audit Committee Members and Financial Reporting Quality

The coefficient of ACFEP is -0.2492292, indicating that there is negative relationship between ACFEP and FRQ of listed DMBs in Nigeria. This means that a unit increase in audit committee

financial expertise will lead to a decrease in the financial reporting quality of DMBs by 0.2492292. The negative relationship between audit committee financial expertise and financial reporting is against the a priori expectation of this study as audit committee members with financial expertise are expected to mitigate misstatements of financial reports. However, based on the findings of the study, it can be discerned that audit committee members with financial expertise might affect technical manipulation of financial reports.

The Z-value of ACFEP is -2.57 while its p-value of 0.000 which is significant at 1%. Based on this evidence, the third hypothesis of the study which states that accounting expertise of audit committee members has no significant influence on financial reporting quality of DMBs is rejected. This finding corroborates with the finding of Dabor and Dabor (2015), Wiralestar and Tanzil (2015), Aryan (2015) who found that accounting expertise of audit committee members significantly affect financial reporting quality.

4.5.4 Female Audit Committee Members and Financial Reporting Quality

Relatedly, the coefficient of ACFD is 1.975432. The implication of this is that there is positive relationship between ACFD and FRQ of DMBs in Nigeria. This positive relationship is to the extent that a unit increase in ACFD will lead to a corresponding increase in FRQ of DMBs by 1.975432. The positive relationship suggests that existence female audit committee members increase the credibility of financial reporting of DMBs in Nigeria. Female audit committee members might tend to be much more honest and committed in their duty of evaluating the truthful and fair representation of economic facts of financial reports prepared by management. The z-value of ACFD is 4.47 while the p-value is 0.010 which is significant at 1%. On this basis,

the fourth hypothesis of the study which states that female audit committee members do not significantly affect financial reporting quality of DMBs is rejected. This finding is in tandem with the finding of Wiralestar and Tanzil (2015), Madawaki (2013).

FSIZE has positive relationship with FRQ as its coefficient is 0.0042473 which means a unit increase in FSIZE will lead to about 0.0042473 increase in FRQ of DMBs in Nigeria. However, this relationship is not significant even at 10%.

4.6 Policy Implication of the Findings

Several policy implications can be gleaned from the findings of the study. The regression analysis shows that ACIND has no significant influence on the financial reporting quality of DMBs in Nigeria. What this implies that existence of audit committee members without substantial managerial shareholding does not ultimately lead to enhancement of financial reporting quality of DMBs in Nigeria.

The quantitative analysis also reveals that there is significant and positive relationship between ACFREQ and FRQ of DMBs in Nigeria. This suggests that if audit committee members meet frequently in a given accounting period, they will better evaluate the authenticity of the financial reports which might translate to quality of the financial reports.

The study also reveals that there is negative and significant relationship between ACFEP and FRQ of DMBs in Nigeria. The implication of this finding is that the financial expertise of audit

committee members plays a prominent role in the determination of financial reporting quality of DMBs in Nigeria.

Results from regression analysis show that ACFD has positive and significant relationship with the FRQ of DMBs in Nigeria. This implies that female audit committee members play crucial role in the determination of FRQ of DMBs in Nigeria.

CHAPTER FIVE SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

The study examined the effect of audit committee characteristics on financial reporting quality of DMBs in Nigeria. Chapter one addressed the background to the study which centered on issues regarding corporate governance and audit committee characteristics in Nigeria. It also highlighted the sparse literature as well as increasing level of poor oversight roles of the audit committee which leads to poor financial reporting quality. There are sparse literatures on the effect of audit committee characteristics on financial reporting quality. To investigate the effect of audit committee characteristics on financial basic research questions, research objectives and hypotheses, were raised. The scope of the study is from 2007 to 2014. The chapter also highlighted the significance of the study within the context of various stakeholders.

Chapter two which dwelt on literature, covering conceptual framework, review of empirical studies and theoretical framework. The basic concepts that underlie the study, concepts of corporate governance, board of directors, audit committee, financial reporting quality, audit committee independence, frequency of audit committee meeting, audit committee financial expertise, and audit committee female gender were explained. The agency theory was used to underpin the study.

Chapter three centered on the research methodology used by the study. The chapter suggests that correlational research designed is most appropriate for the examination of effect of audit committee characteristics on financial reporting quality of DMBs in Nigeria. The population/sample size of the study as revealed by the chapter is fifteen (15) deposit money

banks in Nigeria. The variables used by the study were explained and modeled based on multiple regression analysis.

Chapter four focused on data presentation and analysis. Descriptive statistics of the variables were explained. The correlations among the variables were explained. Further robustness tests were carried out. The regression result, based on random effect which was suggested by Hausman specification test was used. The results indicated that the all the predictor variables account for 21.23% of variation in the dependent variable, financial reporting quality.

5.2 Conclusions

Arising from the result of the analysis that was carried out in chapter four, the following conclusions can be made:

Frequency of audit committee meeting has positive and significant relationship with the financial reporting quality of DMBs in Nigeria. The more frequent the audit committee members meet, the higher the tendency for them to meticulously scrutinise all elements of financial reports.

The study also concludes that audit committee financial expertise has negative and significant influence on the financial reporting quality of DMBs in Nigeria. The presence of audit committee members with financial expertise will have profound influence on the financial reporting quality of DMBs in Nigeria.

Finally, the study concludes that existence of female audit committee members positively and significantly affects financial reporting quality of DMBs in Nigeria. Thus, existence of female audit committee members will help mitigate financial reports' misstatements.

5.3 Recommendations

The following recommendations have become necessary in view of the findings of the study:

- i. Banks should sustain frequency of audit committee meetings. This has become necessary in view of the fact that frequent meetings will avail the audit committee members to opportunity to scrutinize the financial reports carefully.
- ii. Audit committee members should be well motivated so that they will not derail from their traditional roles of evaluating authenticity of financial reports prepared by management. Such motivation is necessary so that they will not be easily lured into manipulation of financial statements to gain monetary gains.
- iii. More female audit committee members should be encouraged to make composition of audit committees of DMBs in Nigeria. Female audit committee members are proven to have some positive influence on the financial reporting quality of Deposit Money Banks in Nigeria.

5.4 Limitations to the study

Although the findings of this study can be relied upon, caution should be taken on the following limitations:

- i. The economic circumstances of banks keep on changing so also are their number. Therefore, the application of the finding of the study might only be suitable in the current era.
- ii. Some variables of audit committee characteristics were not included, the prominent of these is foreign diversity. Therefore, cognizance should be taken on the fact that other variables of audit committee characteristics might have varying relationship with financial reporting quality of DMBs in Nigeria.

5.5 Suggestions for Future Research

The study suggests that further investigations should be carried out in the following areas:

A replicated study should be carried out with wider scope, covering especially, the entire financial services industry as insurance firms were excluded from the study.

More variables of audit committee characteristics should be used so as to further analyse their influence on financial reporting quality of firms in Nigeria.

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Appendix 1: Population of the Study

S/No	Names of Bank	Year Incorporation	Year of Listing
1	Access Bank Plc	1989	1998
2	Diamond Bank Plc	1990	2005
3	Eco Bank Nig.Plc	1986	2006
4	Fidelity Bank Plc	1987	2005
5	First Bank Nig.Plc	1969	1971
6	First City Moment Bank Plc	1982	2004
7	Guarantee Trust Bank Plc	1990	1996
8	Skye Bank Plc	1989	2005
9	Stanbic-IBTC Bank Pc	1989	2005
10	Sterling Bank Plc	1992	1993
11	Union Bank Plc	1969	1970
12	United Bank Plc	1961	1970
13	Unity Bank Plc	1987	2005
14	Wema Bank Plc	1069	1991
15	Zenith Bank Plc	1969	2004

Source: (1) Nigeria Stock Exchange Annual Report, 2015

Appendix II: Regression Result



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 StataCorp
 4905 Lakeway Drive
 College Station, Texas 77845 USA
 800-STATA-PC <http://www.stata.com>
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 979-696-4601 (fax)

Single-user Stata license expires 31 Dec 9999:
 Serial number: 71606281563
 Licensed to: STATAForAll
 STATA

- Notes:
1. (/m# option or -set memory-) 50.00 MB allocated to data
 2. (/v# option or -set maxvar-) 5000 maximum variables

. edit

. *(8 variables, 120 observations pasted into data editor)

. xtset id year, yearly
 panel variable: id (strongly balanced)
 time variable: year, 2007 to 2014
 delta: 1 year

. summarize

Variable	Obs	Mean	Std. Dev.	Min	Max
id	120	8	4.338609	1	15
year	120	2010.5	2.300895	2007	2014
frq	120	.3528765	.3104617	.00017	.95
acind	120	.5471667	.3367446	0	1
acfreq	120	4.15	.8565124	2	6
acfp	120	.5378338	.2585455	.0280396	1
acfd	120	.0919215	.0758609	0	.278911
fsize	120	19.89825	2.08178	12.12	22.92

. pwcorr frq acind acfreq acfp acfd fsize, star (0.05) sig

	frq	acind	acfreq	acfp	acfd	fsize
frq	1.0000					
acind	-0.0860 0.3504	1.0000				
acfreq	0.1720 0.0603	-0.0352 0.7025	1.0000			
acfp	-0.1126 0.2206	0.0790 0.3913	-0.0378 0.6822	1.0000		
acfd	0.2659* 0.0033	-0.0983 0.2853	0.0450 0.6253	0.3552* 0.0001	1.0000	
fsize	0.3036* 0.0007	-0.0559 0.5445	0.0510 0.5801	0.2855* 0.0016	0.3218* 0.0003	1.0000

. reg frq acind acfreq acfp acfd fsize

Source	SS	df	MS	Number of obs =	120
Model	2.47097785	5	.49419557	F(5, 114) =	6.26
Residual	8.99901521	114	.07893873	Prob > F =	0.0000
				R-squared =	0.2154
				Adj R-squared =	0.1810
				Root MSE =	.28096
Total	11.4699931	119	.096386496		

frq	Coef.	Std. Err.	t	P> t	[95% Conf. Interval]
acind	-.015221	.0775569	-0.20	0.845	-.1688607 .1384188
acfreq	.0485252	.0301969	1.61	0.111	-.0112945 .108345
acfp	-.3406819	.1097638	-3.10	0.002	-.5581232 -.1232405
acfd	1.085687	.3778027	2.87	0.005	.3372626 1.834111
fsize	.0434659	.0133519	3.26	0.001	.0170159 .0699159
_cons	-.6216376	.2825841	-2.20	0.030	-1.181434 -.0618407

. vif

Variable	VIF	1/VIF
acfd	1.24	0.807564
acfp	1.21	0.823665
fsize	1.16	0.858594
acind	1.03	0.972524
acfreq	1.01	0.991636
Mean VIF	1.13	

. xttest0

Breusch and Pagan Lagrangian multiplier test for random effects

$$frq[id,t] = Xb + u[id] + e[id,t]$$

Estimated results:

	Var	sd = sqrt(Var)
frq	.0963865	.3104617
e	.0319172	.1786539
u	.0626866	.250373

Test: Var(u) = 0

chi2(1) = 120.01
 Prob > chi2 = 0.0000

. xtreg frq acind acfreq acfep acfd fsize, vce (robust)

Random-effects GLS regression Number of obs = 120
 Group variable: id Number of groups = 15

R-sq: within = 0.2123 Obs per group: min = 8
 between = 0.1135 avg = 8.0
 overall = 0.1411 max = 8

Random effects u_i ~ Gaussian Wald chi2(5) = 31.33
 corr(u_i, X) = 0 (assumed) Prob > chi2 = 0.0000

(Std. Err. adjusted for 15 clusters in id)

frq	Coef.	Robust Std. Err.	z	P> z	[95% Conf. Interval]	
acind	.0150025	.0173951	0.86	0.388	-.0190912 .0490963	
acfreq	.0498576	.0359462	1.39	0.165	-.0205957 .1203109	
acfep	-.2492292	.1186066	-2.10	0.036	-.4816938 -.0167645	
acfd	1.975432	.5060984	3.90	0.000	.9834971 2.967366	
fsize	.0043205	.0179883	0.24	0.810	-.030936 .039577	
_cons	.0042473	.2876269	0.01	0.988	-.559491 .5679856	
sigma_u	.25037297					
sigma_e	.17865389					
rho	.66262243	(fraction of variance due to u_i)				