AUDIT COMMITTEE CHARACTERISTICS AND FINANCIAL REPORTING QUALITY: EVIDENCE FROM NIGERIAN LISTED COMPANIES

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DECLARATION

I hereby certify that the substance of this thesis has not been submitted to any degree and is not currently being submitted for any other qualifications. I certify that all sources used have been acknowledge and referenced in this thesis.

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ABSTRACT

This research examines whether the formation of audit committees and its characteristics are associated with improved financial reporting quality. The sample of the study is the Nigerian listed companies prior to and after the introduction of mandatory audit committee requirements in The Code of Corporate Governance in 2003. The researcher uses an archival data from the annual reports, NSE and SBAInteractive. The model by Dechew and Dichev (2002) was used to measure the earnings quality as proxy for financial reporting quality. The result indicates that there was some evidence that earnings quality significantly reduced in the years after audit committee formation, thus providing some support for the notion that the formation of the audit committee improved financial reporting quality. Second finding shows that there was a weak association between the characteristics of audit committee and improved financial reporting quality. The audit committee independence and expertise are found to significantly associate with improved financial reporting quality. Audit committee meets 4 to 5 times a year and audit committee size consists of 4 members. The result also shows that 70% of the sample firms employed Non-Big 4 auditors. These findings provide evidence on the mandatory audit committee requirement under the NSE listing rules on how the companies respond towards The Code.

Key words: Audit committees, financial reporting quality, Nigerian listed companies.

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LIST OF ABBREVIATIONS

CBN= Central Bank of Nigeria

CAC= Corporate Affairs Commission

CAMA= Companies and Allied Matter Act

CPA= Certified Public Accountants

CEO= Chief Executive Officer

DD= Dechew and Dichev

SEC= Securities and Exchange Commission

SOX= Sarbanes-Oxley Act

NITEL= Nigerian Telecommunication Plc

NNSL= Nigerian National Shipping Line

NEPA= National Electric Power Authority

NRC= Nigerian Railway Corporation

NSE= Nigerian Stock Exchange

NYSE= New York Stock Exchange

NASDAQ= National Association for Securities Dealers

IMF= International Monetary Fund

CHAPTER ONE

INTRODUCTION

1.0 Background of the Study

A series of well publicized cases of accounting scandals such as Enron and WorldCom has captured the attention of investors and regulators alike. These highly publicised accounting scandals have greatly shaken the investors' confidence in the integrity of the corporate financial reporting in the United States (U.S). In order to restore the investor confidence, a number of efforts have been taken to reform the corporate governance in the U.S. The congress enacted the Sarbanes-Oxley Act which is known as the Corporate Oversight Bill in July 2002. In line with the congress efforts the New York Stock Exchange (NYSE) and the NASDAQ adopted new corporate governance rules for exchange listed firms which were approved by the Securities and Exchange Commission (SEC) in November 2003. Both the Sarbanes-Oxley Act and the new corporate governance riles of the NYSE and NASDAQ place much emphasis on greater independence from management and effectiveness of the board of directors and the board of audit committees (Persons, 2005). The cases of accounting scandals on these giant and international companies also indirectly capture the attention of investors and regulators in developing countries. The search for mechanism to ensure reliable, high quality financial reporting has largely focused on the structure of audit committees, whose function is to oversee the financial reporting process as well as the audit of financial statements. Quite understandably, expectations will be high on the audit committees to be more active and participative in ensuring the proper management of the companies. Audit committees are expected to resolve the agency conflicts and thus enhance the quality of financial reporting. Given the importance of audit committees, listed companies in Nigeria are required to include in their annual reports, a report

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