THE AUDIT COMMITTEE CHARACTERISTICS AND EARNINGS MANAGEMENT IN POST IFRS NIGERIA

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THE AUDIT COMMITTEE CHARACTERISTICS AND EARNINGS MANAGEMENT IN POST IFRS NIGERIA

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ABSTRACT

This study is designed to examine the impact of audit committee characteristics on earnings management in Nigerian listed companies after the adoption of International Financial Reporting Standards (IFRS). The study consider a total of 71 listed companies in Nigerian Stock Exchange, the period cover is 2012 to 2014. The data mainly obtained from secondary source, through the financial reports of the sample companies and DataStream. The multiple regression results indicated that audit committee independence, audit committee financial expertise and audit committee stock ownership were found to be negatively and significantly associated with earnings management. In contrast, audit committee size and audit committee activity are not associated with earnings management. The result also shows that firm performance is negatively and significantly correlated with earnings management, while leverage is found to be not significantly related with earnings management. However, firm size is positive and significantly related with earnings management. Finally, the results suggest that the policy makers in Nigeria shall make policies that will further strengthen the audit committee independence, and financial expertise since are found to be significant in preventing earnings management. The results also suggest that the companies should be encouraged to have outside directors with significant stock ownership, as this is also found to be important in preventing earnings.

Key words: Audit Committee, IFRS, Earnings Management

ABSTRAK

Kajian ini bertujuan untuk mengkaji kesan ciri-ciri jawatankuasa audit keatas pengurusan pendapatan dalam syarikat tersenarai di Nigeria selepas menerima pakai Piawaian Laporan Kewangan Antarabangsa (IFRS). Kajian ini mengambil kira sebanyak 71 syarikat yang tersenarai di Bursa Saham Nigeria, untuk tempoh masa 2012 sehingga 2014. Kebanyakan data diperolehi daripada sumber sekunder, iaitu melalui laporan kewangan syarikat-syarikat dan Datastream. Keputusan regresi berganda menunjukkan bahawa jawatankuasa audit bebas , jawatankuasa audit dengan kepakaran kewangan dan pemilikan saham jawatankuasa audit mempunyai kaitan yang negatif dan signifikan dengan pengurusan perolehan. Sebaliknya, saiz jawatankuasa audit dan aktiviti jawatankuasa audit tidak mempunyai kaitan dengan pengurusan perolehan .Hasil kajian juga menunjukkan bahawa prestasi firma adalah negatif dan signifikan dengan pengurusan perolehan, manakala leverage didapati tidak signifikan dengan pengurusan pendapatan. Namun, saiz firma menpungai habungan positif dan signifikan dengan pengurusan perolehan. Akhir sekali, keputusan mencadangkan pembuat dasar di Nigeria hendaklah membuat dasar-dasar yang akan mengukuhkan lagi jawatankuasa audit bebas dan kepakaran kewangan oleh kerana tidak signifikan dalam mencegah pengurusan pendapatan. Keputusan juga menunjukkan bahawa syarikat-syarikat perlu digalakkan untuk mempunyai pengarah dari luar dengan pemilikan saham, kerana ia juga didapati penting dalam mencegah pendapatan.

Kata kunci: Jawatankuasa Audit, IFRS, Pengurusan Pendapatan

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CHAPTER ONE

INTRODUCTION

1.0 BACKGROUND OF THE STUDY

Financial statement is the tool that is used to assess and analyze the firms' performance, all stakeholders rely heavily on the financial statement information in their value judgment, and hence, its free from any manipulation cannot be over emphasized. Managers use different methods to manipulate financial statement including earnings management.

For any financial statement to be useful, reliable and yield economic benefits, shall contain all relevant information that are cost-effective and timely to users as opined by Ho, Tower and Baraka (2008). Also best disclosure practice increased the performance of the company. According to Dembo and Rasaratnam (2014), examination of financial reports revealed that, company with best disclosure practice have excellent performance.

Despite the fact that financial report is the major tool relies upon by users of the financial information, but it becomes no longer reliable for right decision making. The investors' confidence on the reliability and credibility of the contents of the financial report has been deterred due to some tragic corporate scandals across the globe. The sudden happenings and bankruptcy of the world giants like Enron, WorldCom, Lehman Brothers and Xerox are some of the reasons that demoralized confidence of the investors (Fodio, Ibikunle, & Oba, 2013).

Also Fodio et al. (2013) argued that the corporate scandals of these world giants were greatly related to earnings management due to deceitful acts of the management and weak operating system. Investigation also discovered that insiders apply earnings manipulation to hide the firm performance to the outsiders, so that they can protect their personal interest (Leuz, Nanda, & Wysocki, 2003). In other words, managers do series of choices in estimation and judgments in reporting their operations to shareholders, in the process of meeting the assumption and expectation of investors and analysts, the former manipulate the accounting information by employing earnings management.

The term earnings management refers to the process or act use by managers and company executives to manipulate the accounting numbers in the financial statement. Even though the acts might have complied with the existing accounting rules, but the managers use some opportunity to achieve their personal interests against the other stakeholders' interests. Managers alter financial reports by delaying the recognition of revenues or delaying the recognition of expenses in order to increase or decrease the reported earnings (Park & Shin, 2004).

Healy and Wahlen (1999) revealed that earnings management happens in a situation where executives utilize judgment, while reporting transactions to manipulate the reports either to mislead other stakeholders about the performance of the company or to influence contracts that are based on financial reports. This indicated that managers use their judgment discretions to misstate financial information, with the aim of misleading investors or influence contractual decisions of stakeholders that rely on these financial reports.

Different studies revealed that company executives employ various means to manipulate their reported earnings. For example, Roychowdhury (2006) found that managers manipulate their real activities to conceal their reported losses, thereby reporting unrealistic earnings. Roychowdhury further found evidence that some managers temporarily increase sales through price discounts, lower cost of goods sold through overproduction and decreasing the discretionary expenses to increase reported earnings.

Reporting time also determine the nature of earnings management embarked upon by firms as revealed by several studies. Firms managed their earnings upward to hide earnings reduction and avoid reporting losses (Park & Shin, 2004). They further suggested that companies manage their earnings aggressively during the initial public offering. Managers intentionally manipulate financial information to maximize their incentives. Therefore, executives manage their earnings usually whenever their incentives are attached to firm's performance.

Some researchers investigated the impact of firms ownership structure on the type of earnings management embarks by the company. Siregar and Utama (2008) stressed out that there was evidence companies with large family ownership have more efficient earnings management than company with no family ownership structure. This showed that firms which have no family ownership structure engage in more aggressive earnings management than those firms with large family ownership.

There has been widely believed among researchers and financial analysts that improved accounting regulations can be used to restrict earnings management. Consequently, adoption of high quality regulations such as International Financial Reporting Standards (IFRS) and International Accounting Standards (IAS) restricts earnings management. Highly improved corporate governance framework also prevents earnings management.

The adoption of IAS or IFRS by most of the countries of the world is no longer a new story. Convergence and full adoption are the two approaches used for the adoption of IAS/IFRS (Mulyadi, Soepriyanto, & Anwar, 2012). Convergence means, the standards setting bodies adjust the national GAAP to be the same or similar to the provisions with IAS/IFRS, in other words, adapt and domesticate the IAS/IFRS provisions. On the other hand, the full adoption means IAS/IFRS is fully implemented.

The overall logic of the adoption is not limited to provide avenue for uniformity in cross boundaries accounting practices, but also to improve the financial reporting quality. Hence, the earnings quality (financial reporting quality) increases with the mandatory adoption of IFRS (Houqe, Ziji, Dustan, & Karim, 2012). The adoption of IFRS among the various countries of the world was due to demand for uniformity, comparability and reliability of the financial reports of companies (Okpala, 2012).

Nigeria was not isolated in this demand. In its decision issued on 28th July, 2008 through the then minister of trade and investment, the Nigerian government required all listed companies in the country as from 1st January, 2012 to ensure compliance with IAS/IFRS in preparing their financial statements (Ayuba, 2012). He further added that the adoption was aimed at enhancing the globalized nature of the financial statement, competitiveness, homogeneity, and investors' friendly oriented and internationally recognized accounting standards. This showed that the major purposed of the adoption was to improve the financial reporting quality, thereby increasing the stakeholders' confidence on the financial reports. Therefore, bearing the aforementioned objectives/benefits in mind, the decision to adopt IAS/IFRS in a developing and important economy like of Nigeria cannot be overemphasized.

To improve the quality of financial statement in Nigeria, firms listed on its stock exchange are required to prepare their IFRSs based financial reports by December, 2012 (Isa, 2014). He added that IFRS based prepared financial reports increased relevance of the reports in decision making by accounting information users, comparability of financial statements prepared in different countries and also it ensured growth in business transactions globalization. The overall benefit is provision of information in comprehensive form and reduction of information asymmetry.

The popular corporate scandals involving world giants like Lehman Brothers, Enron and WorldCom will not be unconnected to earnings management practices. Apart from adopting the improved financial accounting regulations such as IFRS/IAS, different countries strategized extra measures to prevent or reduce the effect of earnings management thereby improving the financial reporting quality. As part of the measures taken to check this outcry was rethinking the issue of corporate governance, in addressing this, governance codes, norms and standards were introduced by most countries of the world (Dembo & Rasaratnam, 2014).

Following the scandals in US and other countries, the attention of investors have been drawn to demand more effect audit oversight through active audit committee to improve the financial information quality (Bédard, Chtourou, & Courteau, 2004). As response to this regulators adopted new measures, for instance, the Sarbanes-Oxley Act (SOX) of 2002 was enacted in the United States, the Act required that at least a member of the audit committee should have a financial expertise; in addition to that, all members of the audit committee shall be independent directors. The committee is responsible for overseeing the process of preparing of the company's financial reports and also audit of these financial reports.

According to Badolato, Donelson, and Ege (2014) despite the emphasis of the SOX (2002) on the need for financial expertise of audit committee members with the aim of improving the quality of financial reports, it also requires the board of directors to contain majority of independent directors to improve the effectiveness of the board. The assumption was boards with large number of independent directors will be more effective and efficient in discharged of their duties.

The collapse of Australian giants OneTel and HIH, the Australian Stocks Exchange (ASX) introduced its Principles of Good Corporate Governance and Best Practices Recommendations' guidelines of 2003 (Bryce, Ali, & Mather, 2014). The documents outlined the guidelines for establishing the audit committee and its responsibilities. The guidelines stated that the board shall have an audit committee, and the committee shall contain large number of independent directors. Also the chairman of the committee shall be an independent director who is not the chairman of the board. Furthermore, the membership of the committee shall not be less than three.

The Code of Corporate Governance of Nigeria (CCGN) stated that it has been generally believed that weak corporate governance was the cause of the recent corporate failures in the country (SEC, 2011). The Nigerian Securities and Exchange Commission (SEC) took measures to improve the corporate governance by setting up a committee in September 2008, under the chairmanship of Mr. M. B. Mahmoud to review the CCGN of 2003. The major aim of this task was to address the weaknesses of the CCGN and also to improve the framework mechanism for its full enforcement. The SEC believed that the new improved CCGN will increase highest transparency and accountability standards and will promote good corporate governance.

The new CCGN requires that all public companies in Nigeria and all companies seeking to raise funds through issuance of stocks, all those were seeking to be listed in the capital market to ensure compliance with the provisions of the CCGN 2011. The code reemphasized the establishment of an audit committee in each of the board of directors of the public companies, as required by the Section 359(3) and (4) of CAMA 1990 as amended (SEC, 2011). The members of audit committee shall have basic financial literacy and can read financial statements, and at least one member should be knowledgeable in the areas of accounting or financial management. The committee has primary responsibility of ensuring that the financial reports are free from any manipulation. In addition, the committee shall ensure that the financial statements are complied with legal and other regulatory requirements, also the qualification and independence of external auditor.

1.1 PROBLEM STATEMENT

Earnings management has become the issue of considerable attention among the stakeholders, such as regulators, financial analysts, investors, members of press and tax authorities (Xie, Davidson III, & DaDalt, 2003). They further argued that earnings management is rampant to the extent that, the CEOs consider earnings management as a mechanism use to ensure that their companies achieve earnings expectation. Therefore, earnings management is said to be one of the methods been used by managers and CEOs to misguide other stakeholders by reporting unrealistic or manipulated accounting figures, despite the various measures of check and balances.

According to Miko & Kamardin, (2015) some series of corporate scandals around the world eroded the trust in the financial reports and created doubt about the reliability of the results, thereby losing the investors' confidence across the globe. They cited some corporate scandals like Enron, WorldCom, and Xerox cases in the developed economies, in Nigeria, Cadbury Nigeria Plc., and Lever Brothers Plc. are some of examples that attracted the attention of investors. Therefore, there is still needs for a research to investigate the extent to which managers and CEOs manipulate their financial reports in Nigeria by apply earnings management techniques, especially after the adoption of IFRS in the country. After the adoption of IFRS by most of the countries, researchers in these countries undertook researches on impact of this adoption of IFRS on earnings management.

In Brazil, a study conducted by Pelucio-Grecco, Geron, Grecco, and Lima (2014) on the effect of IFRS on earnings management in the listed non-financial companies in the country noted that the adoption the standards had resticted earnings management among the observed companies. Therefore, there is a need to conduct similar research in Nigeria to find out the relationship, because both the countries are considered as developing economies.

Moreover, Salihi (2014) investigated the relationship of board characteristics and earnings in the listed companies in Nigeria, where it was found that there is a significant negative relationship between the audit committee size and earnings management. However, the study did not consider the impact of the other characteristics of the audit committee such as independence, activity of the committee and stock ownership of the members on earnings management.

Introducing code of corporate governance in insurance industry and the adoption of IFRS in Nigerian is expected to improve the reported earnings quality thereby reducing the application of creative accounting in the industry (Fodio, Ibikunle, & Oba, 2013). Having studied the effects of board size, board independence and audit committee size on earnings management, they recommended further research on the ownership concentration (in the audit committee members) and audit committee diligence (activity) in the sectors of the Nigerian economy other than insurance industry. Therefore, this research investigated the effect of audit committee characteristics like committee stocks ownership, committee activity (diligence) among others.

1.2 RESEARCH QUESTIONS

The research questions are as follows:

1. Does the audit committee independence influence earnings management in Nigerian listed companies?
2. Does the audit committee size affect earnings management in Nigerian listed companies?
3. Does the audit committee financial expertise influence earnings management in Nigerian listed companies?
4. Does the audit committee activity influence earnings management in Nigerian listed companies?
5. Does the audit committee stock ownership influence earnings management in Nigerian listed companies?

1.3 RESEARCH OBJECTIVES

The main objective of the study is to assess the impact of audit committee characteristics on earnings management, with particular attention to post IFRS adoption period in Nigeria. In pursuing the main objective, the following specific objectives will also be achieved.

1. To examine the relationship between audit committee independence and earnings management in financial reports of the listed company in Nigeria.
2. To examine the relationship between audit committee size and earnings management in financial reports of the listed company in Nigeria.
3. To examine the relationship between audit committee financial expertise and earnings management in financial reports of the listed company in Nigeria.
4. To examine the relationship between audit committee activity and earnings management in financial reports of the listed company in Nigeria.

5. To examine the relationship between audit committee stocks ownership and earnings management in financial reports of the listed company in Nigeria.

1.4 SIGNIFICANCE OF THE STUDY

Earnings quality is common concern of the financial reports users, while the managers and CEOs always battle with the conflicting agency interest of managing their earnings by manipulating the accounting numbers. This attracted the interest researchers, in assessing the quality of reported earnings. This makes researchers employing different means to determine the method used in managing earnings by CEOs and the extent of earnings manipulation.

The research investigated the effect of audit committee characteristics on earnings management, with particular reference to post IFRS adoption in Nigeria. Therefore, findings contribute to the body of existing knowledge, by highlighting the importance of using improved accounting standards for accounting practice such as IFRS.

The research also is motivated by the recommendation of other researchers, to investigate the impact of other audit committee characteristics like stock ownership and activity of the committee on earnings management in Nigeria. Hence, this research also contributes to other stakeholders like regulators to appreciate the impact of the other audit committee characteristics on earnings management, especially with the total compliance with the provisions of IFRS by all listed companies in the Nigerian Stock Exchange in preparation and presentation of their financial statements.

1.5 SCOPE AND LIMITATION OF THE STUDY

According to Hassan (2015) Nigeria has joined the trend of IFRS adoption on January 1, 2012. The Nigerian Stock Exchange required all first tier listed public companies to comply with the provisions of the IFRS from 2012, while other listed companies to comply with standard by 2013, lastly, the small and medium scale enterprises are to use it by 2014 (Edogbanya & Kamardin, 2014). Therefore, the study considers the IFRS adoption period in Nigeria to find out the impact of audit committee characteristics (like audit committee independence, audit committee size, audit committee financial expertise, audit committee activity and audit committee stock ownership) on earnings management.

Nevertheless, like any other research, this research is not without its own shortcomings which can impact on the scope the generalization of its results. The study initially intended to cover all listed companies in Nigeria. However, some of the companies have to be excluded from the consideration, as they don't disclose the required information that served as data of the research.

1.6 RESEARCH ORGANISATION

The research has been organized in five chapters, introduction of the study is discussed in chapter one, while related literatures were reviewed in chapter two, whilst chapter three discussed the methodology used, chapter four contained the results and discussions, and lastly chapter five contained the summary, conclusion and recommendations.

CHAPTER TWO

LITERATURE REVIEW

2.0 INTRODUCTION

In this chapter, related literatures were reviewed, therefrom, literatures relevant to earnings management and audit committee characteristics are considered. This introduction is followed by conceptual review, where the concepts of earnings management and audit committee characteristics such as audit committee independence, audit committee size, audit committee financial expertise, audit committee activity and audit committee stock ownership are discussed. It also highlighted the concept of IFRS adoption. Next part of the chapter contained empirical review, where empirical works on the relationship between audit committee characteristics and earnings management, the chapter also discussed empirically the effect of IFRS adoption on earnings management. Lastly the underpinning theories that guided the research are also discussed.

2.1.0 CONCEPTUAL REVIEW

The importance of reviewing conceptual issues in a research cannot be overemphasized, because, it provides more light and explanation of concepts used in the research. In view of this, conceptual issues of the variables of this research are been discussed.

2.1.1 Earnings Management

The concept of earnings management has been traced to work of Ball and Brown (1968). This has led to about 1000 publications in the leading academic journals in the areas of accounting and finance in last decades (Kothari, 2001). The heterogeneous nature of the components of earnings rendered the figure to be a meaningless number (Ball & Brown, 1968). They added that the earnings are been perceived as the outcome of a set of procedures like X_1, X_2,… and a set of events like Y_1, Y_2… that have substantive definite meaning. In other words earnings is the product of the function of X and Y, that is earnings = F(X).

The concept of earnings management has been viewed from different perspectives. According to Scott (2015), it can be seen from two perspectives, either financial reporting perspective or contracting perspective. In a financial reporting perspective, usually, to meet the analysts performance forecasts or to conceal loss. Therefore, managers use earnings management with a hope to avoid negative stocks reaction in the capital market, due to failure to meet the expectations of investors. While from the contracting perspective, the managers use earnings management to prevent the firm from the effects of eventualities like unforeseen events as contracts are tight to firms performance.

While descriving earnings management, Healy and Wahlen (1999) opined that earnings management happens when the executives use judgment in financial reporting and in reorganizing their record of transactions, to adjust the financial reports either to misguide some of the users of the reports, about the company's economic performance, or tempt the results of contracts that rely on reported income.

One of the most important aspects of this definition is the managers' power of judgment. For instance, managers' decision is needed for numerous economic events like life-span of long-term assets, employees' pension and benefits obligations, provisions for deferred taxes, assets impairments and bad debts (Healy & Wahlen, 1999). Another aspect is managers' choice of accounting methods in reporting. This includes methods of depreciation like straight-line or reducing balance method, or method of stock's valuation such as first-in first-out (FIFO), last-in first-out (LIFO) or weighted average.

In similar argument, study by Weil (2009) managers use judgment and estimations in reporting the operations of business, for instance, estimations are required when measuring revenue as to when debtors will meet their obligation, how many of the debtors will be declared bad debt. In other words, a business might have a net income of 5% of the total revnue, changing the estimates on bad debt can increase the net income to 7% which is higher than the initial 5% to be reported. Timing of transactions also can be used to manage the earnings of the company, managers can use their descration to time when to report a transaction, and the time used for reporting the transaction affects the reported income of the given period.

Liu and Lu (2007) while investigating the conspicuous situations that are common to earnings management practices by listed companies, and found that the most common ones are: companies engage in eanings management for fear of delisting; and they also manage their earnings to report higher return on equity (ROE) in order to get right to access to additional share issuance through right issue. These reasons or situations are obvious, because, consequences of the delisting of a company on its operations cannot be overquantified. Secondly, managers may desparate in rising capital especially when there is need for further capital, therefore, they can explore all means available to them to justify that, they are qualified to raise such capital.

Investors usually like managers that make decisions that maximize shareholders wealth. Managers in this situation use their descretion over some transactions or accruals to report predetermined level of net income (Nogara, 2014). Opportunistic managers can resort to use measures that are counter productive to conceal the real firm’s performance. This happens because interests of the stakeholders usually differ.

The term earnings management has been coin, phrase or use in different words by authors and authorities, McKee (2005) in his book; Earnings management: an executive perspective, identified number of phrases that are used to mean earnings management practices, these include:

- Creative accounting
- Income smoothing
- Window dressing
- Financial statement manipulation
- Aggressive accounting
- Financial shenanigans
- Accounting hocus-pocus
- Juggling the books
- Accounting alchemy
- Financial statement management
- Borrowing income from future

- Reengineering the income statement
- Banking income for the future
- The numbers game
- Accounting magic

Ronen and Yaari (2008) itemized some methods or techniques employed in earnings management, these are as follows: Management use discretion of choosing the accepted GAAP like FIFO or LIFO in inventory valuation, this can be used to manage their net income (Zeff, 1993); management also used the timing of adoption of new standards like IFRS to manage earnings (Ali and Kumar, 1994); the judgment apply in GAAP that requires estimation, such as depreciation, assets valuation and pension accounting (Brown, 2004); items sometimes are been clssified into below the line operations (continues operations) or above the line operations (income from non-continuing operations) (Godfrey and Jones, 1999); transactions restructuring towards the targeted earnings (Gordon and Henry, 2005); revenues and expenses recognition time is use to manage earnings (Bartov, 1992); management as well use real production and investment decision such as R&D, distribution and administrative expenses (Roychowdhury, 2006 and Singer, 2007).

2.1.2 Corporate Governance

According to Kumar (2013) corporate governance can be seen as a broad term that combines some issues that arises as a result of interactions among senior executives, investors, board of directors and other stakeholders. The definition of the context of corporate governance has been restructured following the high profile scandals in the corporate governance, where the term is defined as "corporate governance deals with the appropriate board structures, processes and values to cope with the rapidly changing demands of both shareholders and stakeholders in and around their enterprises" (see Kumar, 2013).

The greatest milestone in the regulatory framework in the public companies corporate governance was the Sarbanes-Oxley Act of 2002 which is known as SOX (2002). Following the recent corporate scandals of world giants and the indictment of major accounting firms in such scandals led to demand of more effective audit committee by investing community as a means of improving of financial reporting quality, this led to introduction of new regulations like SOX of 2002 (Bedard et al., 2004). The Act provides for the more sophistipicated audit committee in the areas of financial expertise of the members of the committee, the independency of the members and also the activities of the committee. The committee is responsible for the financial reporting process.

In the same vein, Ronen and Yaari (2008) stated that SOX of 2002 motivated by the accounting scandals of 2001 and 2002, most popular was WorldCom of 2002. The enactment of the Act was an outcome of the combined efforts of two US congressmen, Senator Paul Sarbanes the then chairman Senate Committee of Banking, and Congressman Michael Oxley who was the chairman of House Committee of Financial Services. A bill seeking the strengthening of the independence of auditor and establishment of regulatory board of public companies accounting was introduced by Reps Oxley on February 13, 2002. A Similar bill was introduced in the floor of the senate on June 25, 2002 by Senator Sarbanes. The passed bill was signed into law on July 30, 2002 by the then US president (Ronen & Yaari, 2008).

Badolato et al., (2014) identified two main reasons for relevant status of corporate governance can improve effectiveness of audit committee. Firstly, there is need for audit committee to have power and ability to be respected by managers for them to influence the process of financial reporting (Pollock, Chen, Jackson, & Hambrick, 2010). Therefore, it is believed that relevant enhanced regulations change the influence of the audit committee and also how they command respect from managers (D' Aveni, 1990). Secondly, highly empowered committee is most likely to be very active overseer, more willing to inquire for comprehensive information, and more importantly, is less likely to be indifferent in querrying any potential that it foresees (Badolato et al., 2014).

Mohamad-Nor, Shafie, and Wan-Hussin (2010) asseverated that the primary responsibilities of audit committee according Bursa Malaysia Corporate Governance Guide of 2009 was the oversight of process of financial reporting. The revised version of Malaysian Code on Corporate Governance of 2012 makes some recommendations as follows: the audit committee shall make sure that financial reports are in conformity with the provisions relevant reporting standards; the audit committee shall put in place policies and procedures to ascertain adequate of independence of external auditors; and also the internal auditor shall report directly to audit committee.

As any other economy, Nigeria was also faced with series of corporate scandals due to corporate governance failure such as the case of Cadbury Nigerian plc, Lever

Brothers plc (Ajibolade, 2008). Sanusi (2010) identified poor corporate governance, as one of major causes of 2008 financial sector crisis in Nigeria. The crisis led to restructuring of the banking sector. This brought the consolidation in the banking sector through mergers and acquisitions among the existing banks in Nigeria (Adekunle & Taiwo, 2013). Poor ethical standards and weak corporate governance in most of private and public organizations affects the institutional perfomance of these organizations. Perharps, the quality of both private and public institutions have been adversly affected by poor corporate governance, to the extent that they are manipulated for personal interest, thereby, rendering the regulations and law enforcement ineffective (Sanusi, 2010).

Adekunle and Taiwo (2013) stated that, in Nigeria, the requirement and process of disclosure of corporate financial reporting is contained in the Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria (CAMA) 2004. Issues related to financial reporting are provided in sections 331-356, while audit committee related issues are covered in sections 357-369 (Dembo & Rasaratnam, 2014).

However, the CGCN of 2011 provides additional strenght to the provision of CAMA 2004, to restore the investors confidence (Miko & Kamardin, 2015). In addition Section 359 (3) and (4) of CAMA 2004 stated that each listed company in Nigeria is required to have an audit committee, the board shall ensure that at least one member of committee has finacial expertise and the committee is effective in discharge of its statutory duties and responsilities.

SEC (2011) further added that, the audit committee members shall have basic financial literacy, so that they can read financial reports; the committee can also seek external technical support; the committee shall oversight compliance with provisions of regulations in the preparation of financial reports. The committee shall ensure that functional internal audit process has been put in place, and effective internal control in the company's financial reporting.

2.1.3 International Financial Reporting Standards (IFRS) Adoption in Nigeria

Doupnik and Perera (2015) traced the development of international accounting standards setting, to the establishment of the International Accounting Standards Committee (IASC) in 1973, and later, the International Accounting Standards Board (IASB), which replaced IASC in 2002. IFRS developed and issued by IASB was to unify the common reporting language among the capital markets and also improved the financial reporting quality (Ball, 2006).

The changeover from local accounting standards to international accounting standards like IFRS, by most of the countries have been seen as a major transformation in accounting practice (Doukakis, 2014; Yaacob and Che-Ahmad, 2012). It was argued that over 100 countries across the world so far either adopted IFRS or allowed their listed companies to use the provisions IFRS in preparing their financial statements (Houqe, Easton, and van Zijl, 2014; Zehri and Chouaibi, 2013). The purpose of this was to have a uniform standards for easy comparism and improving the financial reporting quality.

Bryce et al., (2014) identified some benefit of having a uniform and hence, the adoption of IFRS among countries to include: cross-boundry listing of stocks due to globalization of capital markets; demand of transparent and accurate financial information by potential investors to enable to an informed investment decision; it is also argued that adopting the globally accepted standards can ease comparison of financial statements prepared in different economies; IFRS adoption can reduce differences in financial reporting practices; and will remove some barriers in flows of international capital among different countries.

Follwing the appreciation of numerous benefits associated with IFRS, European stock markets required all their listed companies to prepare financial reports using the provisions of IFRS, beginning from January 1, 2005 (Muller, 2014). Consequently, parent companies that are listed on the European stock markets are required to prepare their consolidated financial statements based on IFRS standard. Also Brad, Dobre, Turlea, and Brasoveanu (2014) stressed that all listed companies in Romanian Bucharest Stock Exchange (BSE) are to compulsorily adopt IFRS in their individual financial reporting effect from 2012. Similarly, parents companies on the BSE are also mandated to prepare their consolidated financial statements using IFRS provisions.

In compliance with regulation 1606/2002/EC issued by the European Parliament on 19 July, 2002, on the adoption of IFRS by EU listed companies as at December 2005, France require all its listed companies to comply with IFRS provisions in their financial statements latest by 2005 (Zeghal, Chtourou, & Sellami, 2011). The quest for adoption of the generally accepted accounting standards was not limited only to the developed countries, but, also the emarging economies were not left out in the race (Zehri & Abdelbaki, 2013).

For instance, China as an emarging economy, harmonized its local accounting standards with almost all provisions of IFRS in 2006, this was considered as full adoption of IFRS by the country (Cang, Chu, & Lin, 2014). Following the development, all listed companies in SSE (Shanghai Stock Exchange) and SZE (Shenzhen Stock Exchange) became IFRS based in their financial reporting. In similar studies, Jeanjean and Stolowy (2008) asserted that among the developing economies adopted IFRS include Brazil and India apart from China. Bursa Malaysia also required its listed companies to prepare their annual reports using the provisions of IFRS (Yaacob & Che-Ahmad, 2012).

Nigeria was not left out in the quest of the convergence of international accounting standards. According to Hassan (2015); Aanu, Clementina, and Folashade (2013) the Nigerian Federal Executive Council in its July 28, 2010 meeting approved January 1, 2012 as the effective for IFRS adoption in the country. The IFRS adoption was launched in Nigeria by the Honorable Minister of Commerce and Industry Senator Jubriel Martins-Kuye in September 2010, with planned to take effect from 2012 (Okpala, 2012).

Nevertheless, like any other transformation, the transtion from Nigerian local GAAP to globally accepted accounting standards is not without problem. One of the greatest among the challenges was the necessitation for amendment of existing laws in the country (Ofoegbu & Okaro, 2014). They added that there was a common views among the researchers of IFRS implementation on the emphasis for the need and importance of laws (like CAMA 2004) for the smooth implementation of the project.

Okoye and Akenbor (2014) concluded that adoption IFRS framework in Nigeria requires approach and timeline for the transition to achieve a sustainable reporting structure. According to Edogbanya and Kamardin (2014) the implementation of the adoption was organized into stages from 2012 until 2014 based on the level or categories of companies. For example, the first tier listed companies in the stock exchange shall adopt it by 2012, while all other public companies other than first tier list are to adopt the standard by 2013. Lastly, all the small and medium scale enterprises have to apply it by 2014.

2.2.0 EMPIRICAL REVIEW

There are previous researchers that undertook different researches in different fields, therefore, related previous empirical studies would be reviewed in this part.

2.2.1 Review of Earnings Management Practices

Despite the number of researches carried out on earnings management, but there are inconsistancies in the approaches and findings of such studies (Dechow , Ge, & Schrand, 2010). They identified two main approaches after reviewing over 300 literatures on earnings quality, the approaches are: the determinants approach and the consequences approach.

Brown and Higgins (2001) found evidence that there was increased in managing earnings among US managers than non US managers in the recent years. Contrarily, in the view of Francis (2004), there was sufficient evidence that the actual audit quality was high among the US companies. Due these two conflicting views there is need for further research on earnings management.

Leuz et. al. (2003) indicated that it is difficult to compare among countries, because of the economic and institutional differences among the countries. Also investigating the existance of earnings management among 48 countries, Shen and Chih (2005) discovered that it does exist, but it varries among the countries. While Nogara (2014) ascerted that managers manage earnings by altering discretionary expenses like R&D. Therefore, despite the fact that earnings management has been studied, there is still need for futher studies in individual countries, such as Nigeria.

There was also evidence that managers in Nigerian companies engage in earnings management. Some empirical studies (see Fodio et. al., 2013; Salihi, 2014) revealed that some companies executives restate or manage their earnings.

2.2.2 Audit Committee Characteristics and Earnings Management

The need for audit committee publicly qouted companies in Nigeria as reported in Atu (2014) was first emphasized in the work of Olowokure (1989) titled A Case for audit committees in Nigeria, published in The Nigerian Accountants. He argued that the audit committee will restore the reliability and credibility of financial reporting process in the country. Establishment of audit committee in all public companies in Nigeria was contained in Section 359(3) CAMA of 2004 (as amended). Among other things, the committee surpervises the process of financial reporting and external auditing. However, Atu (2014) argued the committee was just set up by companies to satisfy the requirement of the law.

2.2.3 Audit Committee Independence and Earnings Management

The importance of independence of audit committee cannot be overstressed, in view of this MCCG (2012) contended that the independent directors mitigate the conflicts of interest through bring independent and objective judgment on the board. To ensure the independence, Section 359(4) of CAMA (2004) provides that the audit committees should contained equal number of directors and shareholders represntatives, this is its independence (please refer to Atu, 2014).

On the impact of audit committee independence on earnings management, investigations revealed that the committee with more independent directors is more likely to improve the financial reporting quality (see Beasley & Salterio, 2001; Bedard, et. al., 2004; Klein, 2002). In related study by Menon and Williams (1994) found more indipendence audit committee is more active in its function, thereby improving the financial reporting quality. On the other hand, some studies indicated contrary opinion, for example, Lin et. al. (2006) established that audit committee independence has less or no impact on reported earnings quality, while Xie et. al. (2003) consider the committee independence less import on improving reported earnings quality.

Some studies in Nigeria also investigated the relationship between audit committee independence and earnings management, but revealed opposing views. For instance, Miko and Kamardin (2015) found that the committee's independence has a positive relationship with reported earnings quality. But different study by Fodio et. al. (2013) discovered that reported audit committee independence is negatively related with earnings quality in Nigeria. This contradictory findings calls for further research to determine the possible appropriate relationship between the audit committee independence and earnings management or reported earnings quality.

2.2.4 Audit Committee Size and Earnings Management

The size of a committee is very instrumental in improving its quality and functioning, this is the reason for setting the maximum number or minimum number of membership of the audit committee. Mohamad-Nor, et. al. (2010) noted that listed companies in Bursa Malaysia are required to compose audit committee from among their directors with membership no fewer than three, but they are silent about the maximum membership of the committee. However, in Nigeria, Atu (2014) stated that Section 359(4) of CAMA (2004) (as amended) proovides that the maximum membership of the committee shall not be more than six.

Investigation on the literatures showed opposing findings on the relationship between audit committee size and earnings management. Some studies observed inverse relationship between the size of audit committee and earnings management (see Ayemere & Elijah, 2015; Fodio et. al., 2013; Lin, Li, & Yang, 2006; Saleh, Iskandar, & Rahmat, 200; Salihi, 2014). These results showed that the reported earnings quality is affected significantly by the size of the audit committee.

However, some researchers also established that the relationship existng between the audit committee size and earnings management was insignificant or weak (Hussain-

Alkdai & Mohd-Hanefa, 2012; Bedard et. al., 2004; Ghosh, Marra, & Moon, 2010). This implied that the committee size has no impact on earnings quality, which is contrary to other findings. This contradiction forced most of these researchers to call for further inquiry into the relationship. They further argued that their results could not be generalized especially with regards to developing countries.

2.2.5 Audit Committee Financial Expertise and Earnings Management

The educational background and professional expertise especially, in the areas of accounting, auditing and and finance. In appreciation of the importance or role played by expertise, companies listed in the NASD (National Association of Securities Dealers), AMEX (American Stock Exchange), NYSE (New York Stock Exchange) are mandated that all mambers of their audit committees to be financilly literate and at least one should have financial expertise (Ronen & Yaari, 2008).

Other countries also make such provisions. In Indonesia listed companies are required to have at least one of their audit committees members who has accounting and/or finance skills (Siregar & Utama, 2008). According to Saleh et. al. (2007) MCCG of 2006 stated that the audit committee members should have adequate understanding of financial reporting issues; Bursa Malaysia suggested that at least one member of the committee is a registered member of a professional accounting body, and so qualified for not less than three years. In Nigeria Section 30(2) of CCGN (2001) provided that at least one member of the committee should have accounting or financial management, while other members shall preliminary literacy on finance and to be able to read financial reports. McDaniel, Martin and Maines (2002) consider audit managers as financial experts while executives who are MBA graduates as financial literates.

Some researches had proven that one of the most important audit committee attributes that plays role in assuring financial reporting quality is audit committee financial literacy and expertise. For instance, Park and Shin (2004) study Toronto Stock Exchange on the board characteristics and earnings management, they found that the committee financial expertise is significantly negatively related to earnings management. Similar studies by Bedard et. al. (2004), Miko and Kamardin (2015), Xie et. al. (2003), and Zhang et. al. (2007) among others also agreed that audit committee financial expertise constrains earnings management.

2.2.6 Audit Committee Activity and Earnings Management

According to Ronen and Yaari (2008) a committee activity is defined by the number of meetings held by the committee members. Therefore, the level of the committee deligence and meetings denote the level of activity of the committee. SEC (2011) suggested that the audit committees should meet separately and some times with the management, internal auditors and external auditors. However, the corporate governance code did not specify or silent on the frequency or number of times of the meetings required.

Bryce, Ali, and Mather (2014) investigated 200 listed companies in ASX from 2003-2008 and concluded that the frequency of audit committee meetings constrain managers form managing their earning. Similarly, other studies made the same conclusions (see Ayemere & Elijah, 2015; Saleh et. al., 2007; Srinivasan, 2005; Xie et. al. 2003). However, some studies had found a contrary results, because of the weak or absence of relationship between the audit committee activity and earnings management or the accounting quality (Bedard et. al., 2004; Ghosh et. al., 2010; Lin et. al., 2006). This contradictory views called for further, especially in developing countries like Nigeria, because, according to Ghosh et. al. (2010) their result cannot be generalised on the developing countries, hence, its applicability.

2.2.7 Audit Committee Stock Ownership and Earnings Management

According to Ronen and Yaari (2008) stock ownership shows the extent of equity holdings to which directors' incentives maximization are aligned. The higher the director's equity holdings the greater the alignment of directors to the company (Menon & Williams, 1994). It is very common in some countries like Canada to have a significant or a large blockholder director that owns about ten percent of a company's stocks and this can affect the performance of the audit committee (Beasley & Salterio, 2001).

Yang and Krishnan (2005) study the effect of audit committee stock ownership on earnings management and confirmed that, there is a positive relationship between the stock ownership and the earnings management. Whereas, some other evidence indicated that the greater the directors' stock ownership, the higher the likelihood of managing earnings in New Zealand (Kuang, 2007). On the other hand, Beasley (1996) found that outside directors' stock ownership has negative association with earnings management. However, Lin et. al. (2006) failed to support their hypothesis that there is a significant relationship between the committee stock ownership and earnings management, where they found insignificant association between the stock ownership of the committee members and earnings management.

Based on these contradictions, there is need for further studies to expolore the appropriate nature of the relationship. Especially, considering the recommendation of Fodio et. al. (2013) thus, future research shall investigate among other corporate governance characteristics such as audit committee activity or deligence and audit committee stock ownership concentration in Nigeria.

2.3.0 EMPIRICAL REVIEW OF IFRS ADOPTION AND EARNINGS MANAGEMENT

IFRS developed and issued by International Accounting Standard Board (IASB) was to unify the common reporting language among the capital markets and also improved the financial reporting quality (Ball, 2006). Currently, some of the available literatures pointed out that, presently not less than 100 countries have either adopted or indicated their interest to adopt the stanadards or even converge towards IFRS (Zehri & Abdelbaki, 2013). Okoye and Akenbor (2014); Ayuba (2012) posited that the commencement date set up for IFRS adoption in Nigeria was January 1, 2012. In addition, Hassan (2015) insisted that the adoption was to be completed by January 1, 2014 by all the stakeholders.

In analysis on the effect of IFRS adoption on earnings quality by Houqe et. al. (2012) suggested improved earnings quality. Also a study by Marra, Mazzola and Prencipe (2011) on non-financial Italian listed companies discovered that audit committee constrained earnings management after the adoption of IFRS in the country. Similar investigation on some listed Brazilian companies observed a restricted effeted of IFRS adoption on earnings management (Pelucio-Grecco et. al., 2014). Study in UK and French stock markets by Iatridis (2012) and Zéghal et. al. (2011) respectively highlighted the same result as well.

Additionally, study in first three countries that adopted IFRS namely Australia, France and UK indicated that there was no evidence that earnings management had decreased with the adoption of the standard (Jeanjean & Stolowy, 2008). Likewise, inquiry from 22 European countries by Doukakis (2014) revealed that the mandatory adoption of IFRS has no significant effect on earnings management.

The adoption of IFRS can improve the credibility and quality of financial statements in Nigeria (Okpala, 2012). Aanu et. al. (2013) recommended that members of the audit committees be subjected to an urgent training to enable them understand the application of the new standards. Following the above scenarios, there is need for further research on the effect of audit committee on earnings management bearing in mind, the recent adoption of IFRS. This further motivated by Brad et. al. (2014) where they maintained that literatures on earnings management revealed both positive and negative impacts of IFRS adoption.

2.4.0 THE UNDERPINNING THEORIES

Theory according to Ittonen (2010) refers to systematic broad scope of idea, as a result of human imagination, which includes a group of empirical law concerning relationship existing between or among variables that are observed and posited. In other words, theory is a well articulated explanation of some relationship in a phenomena supported by scientific proofs. The underpinning theories in this study are agency theory and positive accounting theory as suggested by Scott (2015) as some of the theories used in accounting research.

2.4.1 Agency Theory

According to Salihi (2014) stated that agency theory is the outcome of a research by Jensen and Meckling (1979). Jensen and Meckling (1979) examined the complexity of the contractual relationship exists in a firm between principals (who are the shareholders) and the agents (who are managers) and defined the nature of agency costs generated by the conflict of interests in the agency. Developments in the firms' theory suggested the need of monitoring (independent auditing) the performance of agents in the firms (Watts & Zimmerman, 1983).

It has been also argued that agency costs can exist when the firm sells out equity of the company especially when there is debt claims against the company (Beasley & Salterio, 2001). While some literatures argued that managers manipulate accounts mainly, due to their desire to influence the transfer of wealth among the various stakeholders (Molenear, 2009), which can also be considered as conflict of interests between managers and other stakeholders. Iturriaga and Hoffmann (2005) expostulated that agency problem could arise when management window dress the financial statements, in order to improve their position, influence contractual outcome that rely on reported earnings, or becloud some facts or information that other stakeholders ought to know.

Badolato et. al. (2014) reported that the monitory role of audit committee for the financial reporting process intended to constrain managers from manipulating the process. They further added that, the task justified the dogma of agency theory. From the agency theory point of view, the need monitoring agent (management) stems from the conflict of interests between the agent and other stakeholders (Menon & Williams, 1994). Contributing to this Brown and Higgins (2001) believed that because of separation of ownership from management, there is possiblity for information asymetric. In this case corporate governance is a mechanism to reduce the agency costs or problem.

2.4.2 Positive Accounting Theory

According to Scott (2015) positive accounting theory "tries to make good predictions of real world events and translate them to accounting transaction." Scott added that unlike normative theories which emphasizes on what should be done (what is), positive accounting theory focuses on which policies to be chosen (what ought to be). The theory was emanated from the work of Ball an Brown (1968), which suggests the use of emprical methods in finance for research in financial accounting that led to information perspective (Isa, 2014).

Watts and Zimmerman (1986) postulated that accounting numbers are use for contracting debt and compensation, and also the choices of accounting policies is affected by political process. Positive accounting theory contributed in highlighting the association between accounting numbers and returns on stock and motivation of management in financial reporting (Kabir, 2013). Isa (2014) in his part asserted that the theory contributed significantly to accounting research specifically, with the postulation of information perspective and widening of research in the area.

The managers use their discretion in financial or accounting judgment, either to optimize their remuneration (which is call bonus plan hypothesis), or to reduce the cost of regulatory penalties (this is called political cost hypothesis. Nevertheless, the Generally Accepted Accounting Principles (GAAP) emphasizes a fair judgment in financial reporting process (Salihi, 2014). Therefore, adoption of highly improveed GAAP like IFRS will no doubt increase the fair judgment in the process of financial reporting.

2.5.0 SUMMARY OF THE CHAPTER

The chapter contained the conceptual review among others, where the concepts of earnings management and audit committee characteristics like audit committee independence, audit committee size, audit committee financial expertise, audit committee activity and audit committee stock ownership are discussed. It also highlighted the concept of IFRS adoption. Next part contained empirical review, where empirical works on the relationship between audit committee characteristics and earnings management, the part also discussed empirically the effect of IFRS adoption on earnings management. The chapter also discusses the underpinning theories that guided the research.

CHAPTER THREE

RESEARCH METHODOLOGY

3.0 INTRODUCTION

The chapter contained the theoretical framework of the research as well as methodology employed in conducting the research. It also discusses the research hypotheses, sample, the data used and its collection procedure, and the techniques used in data analysis.

3.1 THE THEORETICAL FRAMEWORK

The study used earnings management as its dependent variables while audit committee characteristics which include: audit committee independent, audit committee size, audit committee financial expertise, audit committee activity and audit committee stock ownership served as independent variables. Therefore the theoretical framework shown in Figure 3.1 in the next page explicates the relationship between the independent variables in one hand and the dependent variable on the other hand.

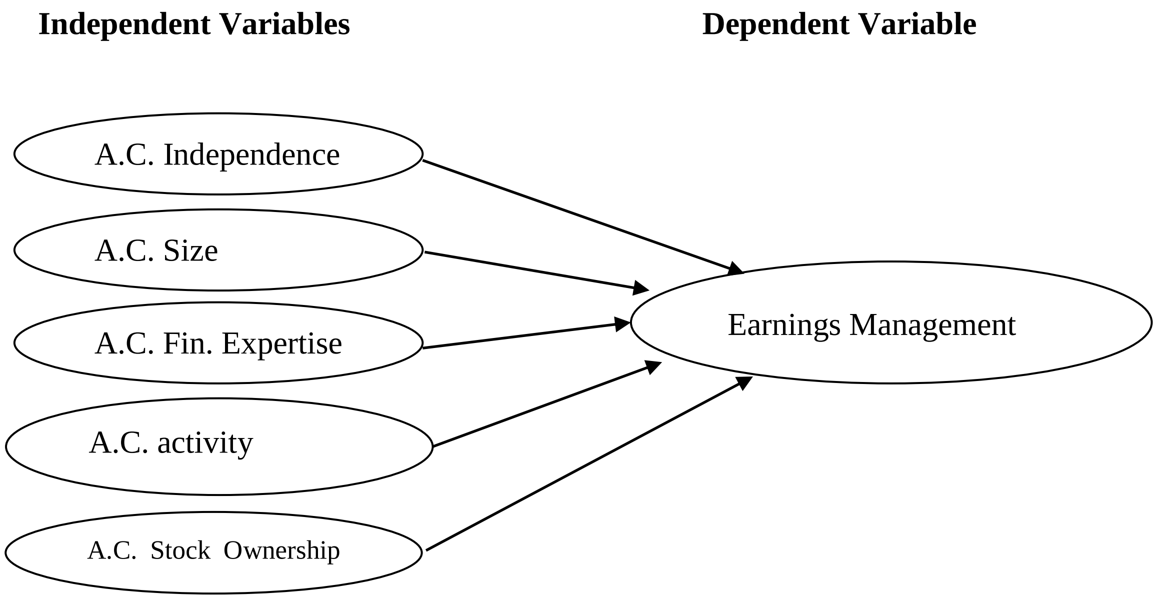

Figure 3.1: Research Framework

3.2 HYPOTHESIS DEVELOPMENT

Hypothesis "is a tentative statement made by a researcher regarding the underlying problem in his research. It provides the direction of a research study such as the variables of interest, the method of data analysis, and the format of report writing" (Awang, 2012). For the purpose of this research, five hypotheses have been developed to ascertain the extent of relationship between the independent variables (audit committee independent, audit committee size, audit committee financial expertise, audit committee activity, and audit committee stock ownership) and dependent variable (earnings management). Evidence from some of the recent studies suggested that there are important aspects of audit committee characteristics that are not been explained (Salihi, 2014). Based on the above premised, the following hypotheses were developed to explain the impact of these unexplained audit committee characteristics on earnings management.

3.2.1 Audit Committee Independence and Earnings Management

The role of the audit committee is improving the quality of financial reporting, contributing to minimize earnings manipulations (Miko and Kamardin, 2015 and Fodio et. el., 2013). SEC (2011) stated that for the audit committee to be fully independent and effective committee, the majority of the members must be independent directors or non-executive directors. Studies conducted by other researchers indicated that a lower level of earnings management is associated with greater independent outside representation on the board (Xie, et. al., 2003; Zhang, et. al., 2007). Based on these findings a negative relationship can be predicted. To examine the association between audit committee independence and earnings management the following hypothesis has been developed:

H1: There is a significant relationship between audit committee independence and earnings management.

3.2.2 Audit Committee Size and Earnings Management

Investigation on the literatures showed that there is a negative relationship between audit committee size and earnings management. For instance, some studies concluded that there is inverse relationship between the size of audit committee and earnings management (see Ayemere & Elijah, 2015; Fodio et. al., 2013; Lin, et. al., 2006; Saleh, el. at., 2007; Salihi, 2014). Thefore, considering the above conclusions, a negative association can be predicted. The following hypothesis has been developed to examine the association.

H2: There is a significant relationship between audit committee size and earnings management.

3.2.3 Audit Committee Financial Expertise and Earnings Management

Some researches had proven that one of the most important audit committee attributes that plays role in assuring financial reporting quality is audit committee financial literacy and expertise. For instance, Park and Shin (2004) established that the committee financial expertise is significantly negatively related to earnings management. Similar studies by Bedard et. al. (2004), Miko and Kamardin (2015), Xie et. al. (2003), and Zhang et. al. (2007) among others also agreed that audit committee financial expertise constrains earnings management. This is because audit committee that has a member who is financial expert is effective in detecting and deterring earnings management tendency. Based on this argument the following hypothesis has been developed:

H3: There is a significant relationship between audit committee financial expertise and earnings management.

3.2.4 Audit Committee Activity and Earnings Management

An active, well-functioning, and well-structured audit committee may be able to prevent earnings management. In his paper, Bryce (2014) investigated 200 listed companies in ASX from 2003-2008 and concluded that the frequency of audit committee meetings constrain managers form managing their earning, similarly, other studies made the same conclusions (see Ayemere & Elijah, 2015; Saleh et. al., 2007; Srinivasan, 2005; Xie et. al. 2003). This is because more active audit committee is more likely to be effective in monitoring management than inactive committee. The hypothesis is thus:

H4: There is a significant relationship between audit committee activity and earnings management.

3.2.5 Audit Committee Stock Ownership and Earnings Management

Yang and Krishnan (2005) studies the effect of audit committee stock ownership on earnings management and confirmed that, there is a positive relationship between the stock ownership and the committee. It was found that earnings management decreases as the stock ownership of the outside directors (such as audit committee member) increase (Beaseley, 1996; Shivdasani, 1992). Based on These findings the following hypothesis has been formulated to examine the relationship between the two variables:

H5: There is a significant relationship between audit committee stock ownership and earnings management.

3.3.0 MEASUREMENT OF THE RESEARCH VARIABLES

According to Sekaran (2003) the hypotheses formulated cannot be tested to answer the research questions, unless some ways use to measure the variables of the research. Measurement of variables enables the research to test the research hypotheses. The variables are assigned scales or numbers by the researchers (Zikmund, Babin, Carr, & Griffin, 2013).

3.3.1 Dependent Variable

This study adopted the accruals approach of Jones (1991) as modified by Dechow et. al. (1995). Ronen and Yaari (2008) desciribed Jones accruals model of 1991 as a milestone in the study of earnings management. Jones (1991) developed the model to examine the accruals of US companies during the import relief audit by ITC

(International Trade Commission), the agency responsible for protecting domestic producers in US.

The modified Jones (1991) model by Dechow et. al. (1995) has been seen to perform better in detecting earnings management than the other discretionary accruals (Ayemere & Elijah, 2015). The model according to Park et. al. (2004); Saleh et. al. (2007) has been widely used by many researchers of accruals management. The model has been found in the past to be robust in measuring earnings management (Bryce, et. al., 2014). Salihi (2014) disclosed that the model became accepted because, is able to disintegrate between discretionary and non-discretionary accruals.

3.4.0 INDEPENDENT VARRIABLES

3.4.1 Audit Committee Independence

This study consider the independence of the audit committee as the percentage of independent directors contained in the audit committee as revealed in many studies (Ayemere & Elija, 2015; Beasley & Salterio, 2001; Ghosh et. al., 2010; Menon & Williams, 1994).

3.4.2 Audit Committee Size

The study utilizes the number of the members of the audit committee to determine the size of the audit committee as disclosed in several studies (Hussain-Alkdai & Mohd-Hanefah, 2012; Saleh, et al., 2007; Xie, et. al., 2003).

3.4.3 Audit Committee Financial Expertise

The study uses the accounting or financial knowledge background (proxied by professional accounting body membersip or experience as a financial officer) of the audit committee chairman as the proxy for the audit committee financial expertise as used by some previous researchers (Ayemere & Elijah, 2015; Badolato, et. al., 2014; Bédard, et. al., 2004; Hussain-Alkdai & Mohd-Hanefah, 2012; Kuang, 2007; Saleh, et. al., 2007).

3.4.4 Audit Committee Activity

The research regards the number of the audit committee meetings per annum the proxy of the audit committee activity as applied in some studies (Ayemere & Elijah, 2015; Ghosh, et. al., 2010; Saleh, 2007; Xie, et. al., 2003)

3.4.5 Audit Committee Stock Ownership

The stock ownership is measured in the study by the proxy of stock holding percentage of the audit committee members as employed in other studies (Ghosh, et. al., 2010; Klein, 2002; Kuang, 2007; Liu & Lu, 2007; Srinivasan, 2004).

3.5.0 CONTROL VARIABLES

According to Kuang (2007) control variables are used to check the effects of some counfounding variables and also can improve the robustness of the tests. Therefore, firm leverage, firm performance and firm size are used in the study as control variables. This will no doubt improve the robustness of the tests of the relationships between audit committee characteristics and earnings management.

3.5.1 Firm Leverage

Dechow et. al. (1995) and Klein (2002) opined that there is common assumption that debt convenants is considered as one of the factors that influence earnings management. To control this influence, leverage ratio (LEV) is included in the model. The firm leverage is measured long term debt divide by total assets of the firm. In other words, firm leverage is the ratio of total debt to total assets (Hussain-Alkdai & Mohd-Hanefa, 2012). Moreover, the relationship between the dependent and independent varibles is control by the firm levarage.

3.5.2 Firm Performance

Firm performance for a specific year is reflected by the firm profitability of the given year (Hussain-Alkdai & Mohd-Hanefa, 2012). Managers conceal negative firm performance on product or investment to avoid reporting losses, therefore, they employ means to report non-existing profit (Salihi, 2014). The firm performance is measured by return on assets as posits by Saleh et. al. (2007). Nonetheless, this study check the effect of concealing profit by using firm performance as control variable.

3.5.3 Firm Size

Liu and Lu (2007) argued that the size of firm is defined by the natural log of its total assets. The firm size is found to be negatively related with the earnings management (Park & Shin, 2004). The firm size is used as a control variable while measuring corporate governance and voluntary disclosure (Ho, et. al., 2008). In line with the work of Klein (2002), this study also employs firm size to control other variables in examining the association between earnings management and audit committee characteristics.

3.6.0 OPERATIONAL DEFINATION

The study operationalizes the research variables by basing on previous literatures reviewed in the process of the research. Therefore, to test the linearity fit of the model and the desirability of variables, reference is made to other studies like Bedard et. al. (2004); Dechow, Sloan and Sweeney (1996); Jones (1991); Klein (2002); Menon and Williams (1994); Xie et. al. (2003); Zhang et. al. (2007).

Consequently, the study employs Jones (1991) as modified by Dechow et. al. (1995) to check the occurrence of earnings management. The model is been considered more accurate in measuring earnings management proxy by accruals, for its ability to disintegrate between nondiscretionary and discretionary accruals, to avoid the possible estimation error. Furthermore, earnings in this regard refer defined as income before tax and extraordinary activity (IBTE). While cash flow from operations (CFO) is deducted from IBTE to arrive at total accruals (TAC), in addition, to determine the discretionary accruals (DAC), nondiscretionary accruals (NDA) is deducted from the TAC. The models of research are given blow:

Earnings = IBTE

TAC = IBTE – CFO

Where:

IBTE = Income before tax and extraordinary activity

TAC = Total accruals

CFO = Cash flow from operations

Based on the previous literatures reviewed total accruals can be further divided into nondiscretionary and discretionary accruals (Saleh, et. al., 2007), as stated below:

$TAC_{it} = IBTE_{it} - CFO_{it}$ …....…………………………………………………….. (1)

As stated earlier TAC of company i for period t is the balance of company's IBTE minus CFO.

$TAC_{it} = NDA_{it} + DAC_{it}$ …………………………………………………………….. (2)

The above model shows that total accruals of firm $_C$ comprise nondiscretionary and discretionary accruals of the firm.

$$TAC_{it} = \alpha_1 \left(\frac{1}{A_{it-1}}\right) + \alpha_2 \left(\frac{\Delta REV_{it}}{A_{it-1}}\right) + \alpha_3 \left(\frac{PPE_{it}}{A_{it-1}}\right) + \ell_{it} \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots \quad (3)$$

$$DAC_{it} = \frac{TAC_{it}}{A_{it-1}} - \left\{ \frac{a\,(1)}{A_{it-1}} + b \left(\frac{\Delta REV_{it}}{A_{it-1}}\right) + c \left(\frac{PPE_{it}}{A_{it-1}}\right) \right\} \ldots\ldots\ldots\ldots\ldots\ldots\ldots \quad (4)$$

Where:

DAC_{it} = Discretionary accruals of the company i for period t.

TAC_{it} = Total accruals of the company i for period t.

ΔREV_{it} = Change in receivable of the company i for period t.

PPE_{it} = Gross property, plant and equipment of the company i for period t.

A_{it-1} = Total assets of the previous year for the company i for period t.

ℓ_{it} = Prediction errors which is also considered to be the DAC of the company i for period t.

Accordingly, to examine the association exist between earnings management which is given as DAC and the audit characteristics (independence, size, financial expertise, activity and stock ownership) cross sectional regression has been utilized. To effectively achieve this, firm size, leverage and profitability are used as control variables as used by previous researchers (Bryce, et. al., 2014).

$$DAC = \beta_0 + \beta_1 ACI_{it} + \beta_2 ACS_{it} + \beta_3 ACE_{it} + \beta_4 ACA_{it} + \beta_5 ACO_{it} + \beta_6 FSZ_{it} + \beta_7 PER_{it} + \beta_8 LEV_{it} \quad \ldots\ldots (5)$$

The summary of the definition aforementioned variables and their measurement is given in Table 3.1 below:

Table 3.1
Measurement of Research Variables

S/N	Variable	Definition	Type	Measurements	Prediction
1	ACI	Audit Committee independence	IV	Percentage of outside Directors in the Audit Committee	Negative
2	ACS	Audit Committee size	IV	Number of Directors in the Audit Committee	Negative
3	ACE	Audit Committee Financial Expertise	IV	Dummy variable, "1" if the Audit Committee is accounting or finance expert, otherwise "0"	Negative
4	ACA	Audit Committee Activity	IV	Number of Audit Committee meetings per year	Negative
5	ACO	Audit Committee Stockownership	IV	Percentage of shares own by the members of the Audit Committee	Positive/ Negative
6	FSZ	Firm Size	CV	Log of total assets.	Positive
7	PER	Firm Performance	CV	Income before tax/Owners' equity	Positive
8	LEV	Firm Leverage	CV	Long term debt/Total assets	Positive

3.7.0 DATA COLLECTION

3.7.1 Sample Size

According to the Nigerian Stock Exchange 2013 fact book there were 148 listed companies in Nigeria, these companies formed the population of this research, out of which, 47 firms fall under financial sector were dropped, because they have their peculiarities and different regulations from the other sector. According to Saleh et al. (2007) the sector is highly regulated. For the purpose of this research, 71 listed companies in the Nigerian Stock Exchange equivalent to 50% are considered. The companies in the sample size were randomly selected; therefore every member of the target population had a chance of being selected.

3.7.2 Method of Data Collection

The study uses secondary data which was sourced from the annual financial statements of the sampled companies. The periods covered was 2012 - 2014, because, the years were the adoption periods set for all companies in Nigeria to ensure full compliance with the provisions of IFRS, as stated by Edogbanya and Kamardin (2014). These periods are been considered much appropriately, bacause they can give full insight into the impact of the adoption of the standards in the country. The extracted data on the dependent variable downloaded from the data stream of the university library. The data on the independent variables were excerpt from the report on corporate govrenance, while those for control variables were taken from statement of financial position and also comprehensive income statement.

3.8.0 DATA ANALYSIS

The study uses descriptive statistics i.e. minimum, maximum, mean and standard deviation to describe the distribution of the data. Also autocorrelation, heteroscedasticity and multicollinearity tests were carried out. The research models were also analyzed to see the ability of the model in explaining the dependent variable, to analyze the nature of the relationship among the variables regression analysis has been utilized.

3.9.0 CHAPTER SUMMARY

This chapter contained the research framework where the relationships among the variables were shown. This is followed by the hypotheses developed to answer the research questions. The chapter also discussed the method employed in data collection and method of data analysis.

CHAPTER FOUR

RESULT AND DISCUSSION

4.0 INTRODUCTION

This chapter contains the statistical results and the discussions of the results about the impact of audit committee characteristics on earnings management after the adoption IFRS in Nigerian listed companies. The chapter begins with the presentation of descriptive statistics of the variables used in the study. In the chapter, diagnostic test has been carried out, namely multicollinearity and normality test. To determine the relationship among the independent variables of the study, multicollinearity test was conducted where variance inflation factor (VIF) is used. In addition also the autocorrelation test heteroscedasticity were conducted. Moreover, to assess the relationship between the independent variables and the dependent variables, panel regression analysis has been used.

4.1 DESCIPTIVE STATISTICS

The descriptive statistics refers the presentation statistical characteristics of the variables used in the study model.

The Table 4.1 below shows the descriptive statistics of the variables of this study. From the table, the dependent variable of the study, which is discretionary accruals (DAC) has a minimum value of -4.0217 and the maximum value of 15.5609, this signified the range which managers of listed companies in Nigeria manage their earnings. The mean value of DAC is -0.6712 and its standard deviation is 1.33008.

The descriptive analysis of the independent variables from the table indicated that, the minimum and maximum values of the audit committee independent are 0 and 67 percent respectively. These show that no company has more than 67 percent of independent directors in its audit committee, but despite the encouragement by CCGN (2011) some companies do not have independent directors in their audit committee. While the mean value of the audit committee independence is 41.54, the standard deviation is 10.013. The independence of the audit committee might not be unconnected with the effort of these listed companies to curb the tendency of agency problem as suggested by Jensen and Meckling (1976).

The minimum value of audit committee size is 3 and the maximum value is 6, this indicated that none of the listed companies in Nigeria has less than three members in its audit committee and has more than six members. Its mean value is 5.58 and the standard deviation 0.764. Furthermore, the minimum and the maximum values of audit committee financial expertise are been 0 and 1 respectively, this is because dummy variable is used to denote the expertise and otherwise.

It was also shown that its mean value is 0.63 with a standard deviation of 0.484. Additionally, 1 and 7 are the minimum and maximum values respectively of the audit committee, while 3.54 and 0.998 are values of mean and the standard deviation respectively. Moreover, the table shows the minimum value audit committee stock ownership of 0.00 and a maximum value of 37.05, meanwhile, its mean value is 3.4144 and a standard deviation of 6.53070.

For descriptive analysis of the control variables, it is shown that the company leverage has -9.91 and 72.17 as minimum and maximum values respectively; also, 23.3405 and 16.38499 are the mean value and the standard deviation. In addition, the descriptive analysis also shows -29.44 as the minimum value of company performance and the maximum value of 54.36, and also has a mean value of 7.5987 and the standard deviation of 9.17364. Lastly, the also indicates the minimum and maximum values of company size of 13.288 and 41.3817 respectively, while the mean value and the standard deviation stood at 16.8685 and 2.25515 respectively.

Table 4.1
Descriptive Analysis

Variables	Minimum	Maximum	Mean	Std. Dev.
DAC	-4.0217	15.5609	-.6712	1.33008
ACI	0	67	41.54	10.013
ACS	3	6	5.58	.764
ACE	0	1	.63	.484
ACA	1	7	3.54	.998
ACO	.00	37.05	3.4144	6.53070
FSZ	13.288	41.3817	16.8685	2.25515
PER	-29.44	54.36	7.5987	9.17364
LEV	-9.91	72.17	23.3405	16.38499

NB: There are 213 observations covered by the above analysis.

Where:

DAC = Total accruals – nondiscretionary accruals.

ACI = Percentage of outside directors in the audit committee.

ACS = Number of directors in the audit committee.

ACE = Dummy variable, “1” if the audit committee has one accounting or financial expert, otherwise “0”.

ACA = Number of audit committee meetings per year.

ACO = Percentage of shares own by the members of the audit committee.

FSZ = Log of total assets.

PER = Income before tax/owners' equity.

LEV = Long term debt/total assets.

4.2 AUTOCORRELATION ANALYSIS

The autocorrelation analysis is used to test correlation among the error terms and also there are different methods employed to test the autocorrelation (Gujarati, 2012). The Wooldridge test is used in this study to test for autocorrelation in the panel data to determine whether or not serial correlation does exist, the result of the test is shown below:

$$F(1, 65) = 0.448$$

$$\text{Prob} > F = 0.5056$$

The null hypothesis (H_0) cannot be rejected based on the above result. Therefore, it is concluded that there is no autocorrelation problem because the probability value is not significant as suggested by Drukker (2003).

4.3 HETEROSCEDASTICITY TEST

The test for heteroscedasticity is used to ascertain consistency of the variance of random error (Gujarati, 2012). The Modified Wald test for GroupWise heteroscedasticity is used where it predicted that:

H_0: sigma (i) ^2 = sigma^2 for all i

The Modified Wald test for GroupWise heteroscedasticity result depicts that the chi-square value of 7.5e+05 and probability value of 0.0000 as shown below:

$$\text{Chi2}(67) = 7.5e{+}05$$

$$\text{Prob} > \text{chi2} = 0.0000$$

Based on the above given value of The Modified Wald test for GroupWise heteroscedasticity, the result suggested decisive rejection of null hypothesis given the fact that, the probability value is very significant (Baum, 2001). Therefore, the error of this test indicates the presence of GroupWise heteroscedasticity by rejection of the null hypothesis. This is according to Bailey and Katz (2011) might not be unconnected with problem of time-series-cross-section data, which is usually, characterized by recurrence of some observations in the time series of some cross sections of the variables, especially in a data where the period covered in the times-series are not much. To take care of this problem, panel-corrected standard errors (PCSE) can be used in testing hypothesis (Gujarati, 2012). The use of PCSE solves the problem of underestimated computed standard errors occasioned by the presence of heteroscedasticity.

4.4.1 MULTICOLLINEARITY ANALYSIS

According to Zikmund et. al. (2013) is the most popular technique for showing association between two variables. This analysis is used to test whether or not multicollinearity does exist among the independent variables. Correlation coefficient values range from -1 and +1, that is negatively correlated (-1) to uncorrelated (0) to positively correlated (+) (Greene, 2008). The correlation coefficient interpretation by Zou, Tuncall, and Silverman (2003) depicts that -1.0 value means the association is perfect negative, where -0.8, -0.5 and -0.2 signify strong negative, moderate negative and weak negative correlation respectively, while 0.0 indicates no relationship, also +0.2, +0.5, +0.8 and +1.0 show weak, moderate, strong and perfect positive correlations.

From the Table 4.2, the highest correlation is between company performance and company leverage (-0.405 significant at 1% level). These figures indicated that the problem of multicollinearity does not exist, because all the bivariate correlations are less than 0.70 (see Hair Jr, et. al., 2010).

Table 4.2
Pearson Correlation Analysis

	ACI	ACS	ACE	ACA	ACO	FSZ	PER	LEV
ACI	1							
ACS	.113	1						
ACE	-.164*	.127	1					
ACA	.038	.202**	.071	1				
ACO	.016	-.137*	-.065	-.037	1			
FSZ	.082	.285**	.157*	.115	-.237**	1		
PER	-.008	.270**	-.054	.212**	.041	.202**	1	
LEV	-.130	-.105	-.046	-.165*	-.030	.012	-.405**	1

*. Correlation is significant at the 0.05 level (2-tailed).
**. Correlation is significant at the 0.01 level (2-tailed).
NB: The above variables as previously defined.

4.4.2 Variance Inflation Factor (VIF)

Further, in order to check the multicollinearity problem among the independent variables, a test was conducted using Variance Inflation Factor (VIF) as shown in Table 4.3 below. The test is been used to ascertain a variable that can be explained by other variables (Hair Jr, et. al., 2010). The result has shown that the VIF value for each of the independent variable is less than two. This justified that multicollinearity problem does not seriously exist among the variables (Salihi, 2014).

Table 4.3
Multicollinearity Analysis

	Collinearity Statistics	
Model	Tolerance	VIF
ACI	.912	1.096
ACS	.825	1.212
ACE	.902	1.109
ACA	.920	1.087
ACO	.924	1.083
FSZ	.817	1.223
PER	.713	1.402
LEV	.787	1.270

NB: The above variables as previously defined.

4.6.1 REGRESSION ANALYSIS

According to Zikmund et. al. (2013) regression analysis is one of the techniques for measuring the linear relationship between dependent and independent variables. Therefore, multiple regression techniques have been used in this analysis.

4.6.2 Hausman Test

The Hausman specification test is used to choose between fixed effect (fe) and random effect (re) (Gujarati, 2012). The null hypothesis in this specification test is based on random effect. From the Table 4.4 below the probabilty of 0.6259 is said to be not significant, therefore, the null hypothesis cannot be rejected. Hence, random effect model has been favored by the result.

Table 4.4
Hausman Specification Test Estimation Results

	---- Coefficients ----			
	(b)	(B)	(b-B)	sqrt(diag(V_b-V_B))
	fe	re	Difference	S.E.
ACI	-57702.16	-144167.6	86465.46	75343.6
ACS	1.22e+07	2830049	9343861	1.03e+07
ACE	-4360185	-3749511	-610674	1437117
ACA	332821	139361.3	193459.7	232841.7
ACO	-2184669	-2114859	-69809.81	1618575
FSZ	783661.8	1426859	-643197.6	451969.5
PER	-194088.4	-252149.3	58060.9	144577.9
LEV	-58585.56	3841.871	-62427.43	85519.45

b = consistent under Ho and Ha; obtained from xtreg
B = inconsistent under Ha, efficient under Ho; obtained from xtreg
NB: The above variables as previously defined.

Test: Ho: difference in coefficients not systematic
chi2(8) = (b-B)'[(V_b-V_B)^(-1)](b-B)
= 6.19
Prob>chi2 = 0.6259

4.6.3 Correlated Panels Corrected Standard Errors (PCSEs)

In a time-series-cross-sectional (TSCS) data repeated observations over time in some cross sections is obvious, there is tendency for this type of data to display some problem such as unit cross section heteroscedaticity. This make the standard errors estimated by ordinary least squares (OLS) incorrect (Katz & Bailey, 2011). The panel-corrected standard errors (PCSE) is designed to take care of these deviations and correct the estimation errors common in TSCS data estimated using othe linear models. As indicated earlier in the heteroscedasticity test, the estimation result reveals heteroscedasticity problem. Thus, PCSE model is employed to correct this problem.

Table 4.5 presents the analysis of linear relationship between audit committee characteristics (audit committee independence, size, financial expertise, stockownership and activity) and earnings management. The relationship of control variables (company size, leverage and performance) and earnings management also indicated in the table. The linear regression analysis used earnings management (measured by discretionary accruals) and audit committee characteristics and the control variables.

The result shows that the audit committee independence is significantly negative at 10% confidence level and it supported the hypothesis of the study. This indicated that listed companies in Nigeria with higher number of independent directors in their audit committee are less likely to manage their earnings. This is line with other findings that found a negative ralationship between the variables (Xie, et. al., 2003; Zhang, et. al., 2007). The implication here is that the indepedence of audit committee has significant impact in deterring earngs management.

The audit committee financial expertise also found to be negatively significant at 1% confidence level which is in line with the research hypothesis. This implies that the Nigerian listed companies that have financial expert in their audit committee have less tendency of managing their earnings. This is similar with the findings of other studies (Ayemere & Elijah, 2015; Badolato, et. al., 2014; Bédard, et. al., 2004; Hussain-Alkdai & Mohd-Hanefa, 2012; Kuang, 2007; Saleh, et. al., 2007).

Also the result further revealed that, the audit committee stock ownership has a significant negative association with earnings management at 5% level of significance. This signifies that stock ownership of directors in audit committee of the Nigerian listed companies have significant negative impact on earnings management.

This indicated that, the result supported the hypothesis of the study. Also is similar with findings of other studies (see Beasley, 1996; Shivdasani, 1993).

However, the remaining other independent variables are found to be insignificant. The audit committee size is found to be positively insignificant, this shows that the size of the audit committee of listed companies in Nigeria has no relationship with earnings management. This result did not supported the research hypothesis, but is similar to findings in other studies (Hussain-Alkdai & Mohd-Hanefa, 2012; Bedard et. al., 2004; Ghosh et. al., 2010). Meanwhile, the audit committee activity also indicated no relationship with earnings management. This signifies that earnings management is not related with the activity of audit committee of Nigerian listed companies. This is in contradiction with the research hypothesis which projected negative significant relationship. However, this result is in line with other findings (Bedard et. al., 2004; Ghosh et. al., 2010; Lin et. al., 2006).

Moreover, the control variables also reveal opposing findings. The company performance is negatively and significantly related with earnings management at 5% level of confidence. The result suggested that less performing Nigerian listed companies have higher likelihood of engaging in earnings management. This result is similar to other findings (see Salihi, 2014; Saleh et. al., 2007). However, the company size indicated a positive significant association at 10% level of significant. This implies that bigger Nigerian listed companies have more likelihood of managing their earnings than the smaller size companies. This suppported the earlier assumption of positive linear relationship. The company leverage is found to be positive but not significantly related with the earnings management. This shows that the leverage of listed companies in Nigeria is not related with earnings management.

Table 4.5
Result of the Panel-corrected standard errors

DAC	Coef.	Panel-corrected Std. Err.	z	P>|z|	[95% Conf. Interval]	
ACI	-169283.9	90109.22	-1.88	0.060	-345894.7	7326.945
ACS	1017755	2955395	0.34	0.731	-4774712	6810222
ACE	-3486470	1285371	-2.71	0.007	-6005750	-967189.8
ACA	123152.5	107433.1	1.15	0.252	-87412.51	333717.4
ACO	-2038680	1012324	-2.01	0.044	-4022800	-54560.95
FSZ	1616500	847449.9	1.91	0.056	-44471.04	3277472
PER	-262341.8	131120.4	-2.00	0.045	-519333.1	-5350.534
LEV	12821.92	88279.63	0.15	0.885	-160203	185846.8
cons	-1.47e+07	1.51e+07	-0.97	0.330	-4.43e+07	1.49e+07

NB: The above variables as previously defined.

4.7 CHAPTER SUMMARY

The chapter contained descriptive analysis, autocorrelation analysis, heteroscedasticity test, multicollinearity test, Pearson correlation analysis and regression analyses. The descriptive result suggested that none of the Nigerian listed companies has more than 67% of independent directors in its audit committee. In addition, the audit committee size of Nigerian listed companies ranges between three and six. Also the audit committees meet between one and seven times in a year, while the highest portion of stock ownership for directors in audit committee of Nigerian listed companies is 37.05%. The multicollinearity analysis using VIF shows that multicollinearity problem does not seriously exist as the VIF value for all variables is less than two. For the autocorrelation analysis, the result suggested that there is no autocorrelation problem as the probability value is not significant. The heteroscedasticity test indicated the tendency of heteroscedasticity problem as the probability value is significant. Additionally, Pearson correlation analysis is been used to test the bivariate relationship among the variables of the study.

Lastly, in ascertaining the effect of the variables on earnings management, regression analysis is conducted. Earlier, the random effect and pool OLS test has been used where the result favored random effect as the result is significant. The Hausman specification test is further conducted and the result is not significant, thereby favoring the random effect. Then PCSE is used in testing the hypothesis in this study. The result supported H1, H3 and H5, while, H2 and H4 are not supported by the result. Finally, two of the control variables are significant whilst the remaining one is not significant.

CHAPTER FIVE

CONCLUSION, IMPLICATION AND RECOMMENDATION

5.0 INTRODUCTION

The chapter contained conclusion of the study based on the findings of the research, the implication of the study is also discussed and the recommendations for further studies are made.

5.1 CONCLUSION

The main objective of this study is to determine the relationship between audit committee characteristics (audit committee independence, size, financial expertise, activity and stock ownership) and earnings management. Based on the findings the following conclusions are been made. The finding supported the argument that large number of independent directors in the audit committee prevents companies from managing their earnings, it is therefore, concluded that highly independent audit committee is more efficient this is in line with previous studies.

The study also backed the argument that financial expertise of one of the audit committee members has a significant impact on earnings management. This leads to conclusion that financial knowledge of a member of audit committee is important in deterring earnings management. The findings also show that, in line with the hypothesis, that the stock ownership of audit committee has negative significant impact on earnings management, concluded thus; the higher number of shares holds by directors in audit committee the higher the possibility it prevents earnings management. According to Beaseley (1996) as the stock ownership of outside director increases, there is a likelihood that the earnings management decreases. This may not be unconnected with willingness of the unaffiliated high block owner to be more effective in checking the activities of management.

The regression result did not favor hypothesis on audit committee size and audit committee activity, where audit committee size is proved to be positive and insignificant. Also audit committee activity is found to be positive and insignificant. Hence, it can be concluded that these two variables have no impact on earnings management. For the control variables, company performance is found to be negatively significant, this lead to conclusion that the performance of the company has negative impact on earnings management, however, the firm size is found to be positively significant, while, firm leverage is not significant. Overall, the results supported H1, H3 and H5, while H2 and H4 are not supported.

5.2.0 IMPLICATION OF THE STUDY

Research is useful only when it has theoretical, practical and/or policy implications contribution. Below are the implications/contributions of this study.

5.2.1 Theoretical Contribution

One of the most important contributions of the study, it serves as an addition to the existing body of literature, especially, as it is the first study consider the impact audit committee characteristics on earnings management after the adoption of IFRS in Nigeria. Therefore, it enhances understanding of the concepts discussed and serves as point of reference to future researchers.

5.2.2 Practical Contribution

The practical contribution refers to the implication of the study to the practitioners. The study can be used by other stakeholders to understand the lope holes use by managers to manipulate their earnings. They can also use findings of the research to know the appropriate audit committee characteristics to be improved in order to prevent managers from managing earnings.

5.2.3 Policy Contribution

The research is very important to policy makers such as Nigeria Stock Exchange Commission. They can use the findings of the study to know what to do, to enhance the effectiveness of audit committee to prevent the possibilities managing earnings by companies. The authorities can also use the findings on control variables to focus on companies that have possible features of managing earnings.

5.3 RECOMMENDATION

There is a need for the policy makers in Nigeria to strengthen the independence of audit committee of Nigerian listed companies, and also make it compulsory for the companies to have higher number of independent directors in their audit committee. Also there is a need for policy makers to ensure that the listed companies abide by the provision of CAMA (1990) as amended and the provision of code of corporate governance. There is need also for the other stakeholders to seek for a more improved policy and practice in preparing financial statements. The future researchers can compare the impact of audit committee in pre and post IFRS adoption periods in Nigeria, in order to assess the quality of financial reports.

5.4 LIMITATION OF THE STUDY

Some of the major limitations of this study are time and data constraint, this forced the researcher to focus on post IFRS adoption period, which is between 2012 and 2014. Therefore, it is recommended that future researchers shall consider pre and post IFRS adoption period to enable comparison between these periods.

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