

AUDIT COMMITTEE EFFECTIVENESS AND FINANCIAL STATEMENT FRAUD OF LISTED CONSUMER GOODS FIRMS IN NIGERIA.

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ABSTRACT

The study empirically investigated the audit committee effectiveness and financial statement fraud. The population of twenty one consumer goods companies registered on Nigeria stock exchange was limited to ten entities employing the purposive random technique for a period of 2011-2020. The study utilize the time series data gathered from the published annual reports. The data obtained from the financial report of the entities were analyzed using the multiple regression with the aid of e-view. From the analytical output of the study it revealed that the audit committee size, audit committee meeting, audit committee independence has a positive and statistical significant relationship with financial statement fraud, while audit committee financial expert has a positive and statistical non-significant relationship with financial statement fraud. The study recommended the regulatory authorities such as (SEC) and the (NSE) should ensure strict compliance with the governance code best practices in order to protect the interest of stakeholders; however, an audit committee that consists of members with financial knowledge reduces the mesmerizing of the financial statement.

Keywords: *Financial Expert, Independent Non-Executive, Financial Statement, Fraud, Nigeria*

INTRODUCTION

One of the elements that make up corporate governance features is the audit committee. International corporate governance reform has centered on the development of audit committees in reaction to corporate management's misuse of control, which resulted in financial scandals, accounting fraud, stock valuation issues, and unreasonable accounting policy manipulation (Olowookere, Oyewole and Lamidi, 2021). The audit committee is established to oversee the mismanagement of resources by the management and ensure transparent financial report for the stakeholders who are interested in investing in the business. According to Ogoun, Edoumiekumo and Nkak (2020) added that the fundamental assumption underpins the entire concept of accounting as a tool for creating decision-relevant financial information. They believed that the accounting framework's entire machinery is choreographed to serve this primary duty. The information gap between users of financial accounting information and the creators of this information, which leads to the information asymmetry or injustice issue, demonstrates the importance of this function. Businesses are always under the risk of fraud from different sources as they relate to the firm. Although most fraud perpetrated by external sources are usually massive and serious. However, this is mostly done in collaboration with insiders. Majority of the fraud cases recorded in organizations indicate that fraud performed at the management level have a stringent and breath-taking effect on the organizational goals. This can be empirically attested to by constant collapse cases of reputable corporations such as WorldCom to Enron and Cadbury, Oceanic Bank, Intercontinental Bank, Access bank and much more, exploring that the successful penetration of such malicious act was inspired by directly or indirectly by top management. Businesses are always under the risk of fraud from different sources as they relate to the firm. Although most fraud perpetrated by external sources are usually massive and serious. However, this is mostly done in collaboration with insiders. Majority of the fraud cases recorded in organizations indicate that fraud performed at the management level have a stringent and breath-taking effect on the organizational goals. This can be empirically attested to by constant collapse cases of reputable corporations such as WorldCom to Enron and Cadbury, Oceanic Bank,

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Most of the frauds committed in organizations are perpetrated by an insider within the company. Similarly, Uwuigbe et al. (2019) posited that the majority of fraud incidents documented in companies show that fraud committed at the management level has a severe and life-threatening impact on the organization. The corporate collapse of reputable corporations such as WorldCom, Palmart, Enron, Cadbury, Oceanic Bank, Intercontinental Bank, and so on, demonstrating that the successful penetration of such malicious acts was inspired by top management, either directly or indirectly. The conflict of interest inherent in the connection between the principals and the managers was frequently the source of these scandals. The reliability of financial reports is jeopardized by these methods. It is fact that the financial statements are prepared to assist the users with factual, not fictional, true and fair, but not deceptive information that accurately depicts the company's current financial health and performance. Although, when an organization manipulates its earnings through operational actions, the information offered by its financial reports becomes unreliable, and many stakeholders will make decisions based on erroneous financial reports with manipulated earnings (Ibrahim, Bello and Kalgi, 2015).

A number of studies have carried out an empirical work on the relationship between audit committee effectiveness and financial statement fraud using different approach to measure financial statement fraud. Scholars like (Olowookere, et al., 2021; Oyedokun, Olatunji and Musa, 2020) used the discretionary accruals in measuring the financial statement quality, while, Uwuigbe et al., (2019) used the Beneish Model to measure financial statement fraud but the study covered 2012-2016 which our study used a more current data. This is the gap the study intends to fill.

Review of Related Literature

This study's framework is based on positive accounting theory as well as agency theory. Managerial accounting decisions are explained and predicted using positive accounting theory. Because accounting numbers are a control mechanism in the agency relationship, contracting parties'

opportunities can influence accounting choices. As a result, managements are responsible for reporting accurate financial statements free of deception and window dressing (Katherine, Marc, & Jeff, 2011) cited in (Ibrahim, et al., 2015).

The agency theory establishes a foundation for corporate governance through various internal and external control methods. These techniques are intended to align the interests of agents and principals, safeguard shareholders' interests, and thereby reduce agency costs (Martinez, 2010). Regardless of the type of interaction between principals and their agents, numerous elements, such as pressure, opportunity, and ethics, can lead to manipulation (Nicola, 2006). As a result, while the type of relationship between principals and their agents can help to lessen manipulation, it cannot completely eliminate it (Osma, 2008) cited in (Ibrahim, et al., 2015).

Empirical Literature

Olowookere, et al., (2021) explored the audit committee gender diversity on financial reporting quality from 2009 to 2019, of consumer goods firms that were listed on the Nigerian Stock Exchange. The researchers used diagnostic tests such as heteroskedasticity and multicollinearity, followed by regression analysis using STATA 15 and it indicated that having a diverse audit committee improves the quality of financial reporting. As a result, the findings indicate that audit committee composition be controlled to guarantee gender diversity in order to provide effective oversight roles.

Oyedokun, Olatunji and Musa (2020) their study observes the affiliation among audit committee traits and financial reporting quality of indexed consumer goods firms in Nigeria for 2013 to 2018. The study population was twenty-one (21) firms listed on the Nigerian Stock exchange. Their result display that audit committee expertise and frequency of meeting had positive and vast impact on financial reporting quality, whilst audit committee size and audit committee gender had any vast association with financial reporting quality. The study concluded that audit committee is a veritable device for enhancing financial reporting quality. The study recommended that extra accounting and finance professionals need to be appointed to audit committees of consumer goods agencies in Nigeria.

Uwugbe et al. (2019) investigated the association that exists between financial reporting fraud and governance among non-financial companies listed on the Nigeria Stock Exchange which covers the period of 2012 to 2016. The panel regression model was applied. The results show that there is no significant association between audit committee independence, board composition and financial reporting fraud. Their study suggests that when it comes to minimizing instances of financial reporting fraud, less emphasis should be placed on the independence of the audit committee, the composition of the board of directors.

Udisifan and Akeem (2019) in their work evaluated the influence of the audit committee on financial reporting quality listed companies selected on the Stock Exchange for the period 2009-2018. The study adopted the modified Jones discretionary management model to represent the quality of the financial statements. The results show that audit committee activity and audit committee size has a positive and negative significant influence on the quality of financial information, respectively. This suggests that audit committee members should be encouraged to take up directorships in other companies, as this enhances their ability to improve the quality of their financial statements.

Ibrahim, Bello and Kalgi (2015) investigated the impact of Audit Committee attributes on deterring real activities manipulation of listed manufacturing firms in Nigeria for the period of 2008-2013. The data were extracted from the annual report of Nigeria-listed manufacturers, and the residuals of Roychowdhury (2006) was to perform Real Activities Manipulation (RAM). Their result from the analytical output revealed that Audit Committee attributes, especially financial literacy, are effective in limiting RAM, while other Audit Committee characteristics such as independence, meeting and

size turns out that the effect of limiting the company's RAM practices is low of the understudy companies. Therefore, listed manufacturing companies are encouraged to increase the proportion of members with financial knowledge on the audit committee, as it may limit the operational behavior of the business.

METHODOLOGY

The study utilize the time series data gathered from the published annual reports of the listed consumer goods firms trading on the Nigerian Stock Exchange for the period of (2011-2020).

The target population of this study is consumer goods entities while the selected entities for the study are ten firms (Cadbury, International Brews, Guinness, Honeywell, ChampionBrew, Dangote Sugar, Flour Mill, Nestle, Nigeria Brew and Enamelware) with secondary data obtained from their financial statements.

Empirical Model Specification

The Beneish M-score model was used to measure the quality of financial reporting. The model was developed by Beneish (1999) to uncover frauds that occurred or intended to manipulate its earnings. The empirical evidences on the aforementioned hypotheses premise on the audit committee characteristics and financial statement fraud. The study of Agama, et al., (2021) adopted the beneish model regression. The study equation can be computed as: $Y = a_0 + \beta x_1 + \beta x_2 + \varepsilon$

The equation can be transformed into econometric model as; $FSF = a_0 + \beta x_1 Acfe + \beta x_2 Acind + \beta x_3 Acmeet + \beta x_4 Acsz + \varepsilon$ Where;

$B =$ coefficient of parameter
 $\varepsilon =$ error term

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FSF= Financial Statement Fraud Proxy by M-Score.

ACFE= percentage number of committee member who has sound accounting knowledge. ACIND=

the level of percentage of non-executive director on the audit committee.

ACSIZE= the total number of members in the committee.

ACMEET= the total number of times the committee meet to review the annual year-end report.

DATA PRESENTATION AND DATA ANALYSIS

Data were extracted from the published annual report of the sampled companies which are presented in Table 1 below. These figures represent aggregate figures of the ten samples companies for the period covering 2011 to 2020, the absolute aggregate figures of book values was used.

Descriptive statistics

	MSCO	AUSZ	AMEET	ACID	ACFE	FSIZ
Mean	-2.392693	5.540000	3.670000	49.60357	13.93334	6.849476
Median	-2.614400	6.000000	4.000000	50.00000	16.66670	6.461100
Maximum	9.503600	8.000000	5.000000	100.0000	50.00000	9.305900
Minimum	-15.25390	4.000000	1.000000	16.66670	0.000000	5.239400
Std. Dev.	2.314784	0.914750	0.910711	16.99896	15.06908	1.128486
Skewness	0.039390	-0.715499	-0.592947	1.347885	0.783351	0.820292
Kurtosis	18.25249	2.667934	2.906065	6.484812	2.727758	2.559846
Jarque-Bera	969.3524	8.991754	5.896533	80.87953	10.53614	12.02189
Probability	0.000000	0.011155	0.052431	0.000000	0.005154	0.002452
Sum	-239.2693	554.0000	367.0000	4960.357	1393.334	684.9476

Sum Sq. Dev.	530.4641	82.84000	82.11000	28607.49	22480.65	126.0745
Observations	100	100	100	100	100	100

The result reveals the mean value of financial statement fraud of the consumer goods firms which stood as -2.392693 with (Beneish model) standard deviation of 2.314784. These shows and average of the consumer goods firms manipulate their financial statements. The (ACFE) mean depict 13.93334 with maximum and minimum values of 50.00000 and 0.000000 respectively with a standard deviation of 15.06908. The result revealed that 14% of the consumer goods firms had members with sound financial know-how. The (ACID) mean was 49.60357 with maximum and minimum values of 100 and 16.66670 with a standard deviation of 16.99896. the result implies that 50% of the consumer goods firms has independent non-executive member in the audit committee. The (ACMEET) mean represent 3.67000, maximum and minimum values of 5.000000 and 1.000000 with a standard deviation of 0.910; which implies that the consumer goods committee members attends meeting thrice. (ACSZ) mean of 5.540000, with maximum and minimum values of 8.000000 and 4.000000 with the standard deviation representing 0.914750 which implies that 5% the consumer goods firms had five members in the audit committee.

Data Analysis

Dependent Variable: MSCO Method: Panel Least Squares Date: 12/30/21 Time: 14:23 Sample: 2011 2020

Periods included: 10

Cross-sections included: 10

Total panel (balanced) observations: 100

Variable	Coefficient	Std. Error	t-Statistic	Prob.
AUSZ	0.283053	0.184025	0.650141	0.0032
AMEET	0.291674	0.328174	1.125139	0.0004
ACID	0.014949	0.001470	0.098366	0.0219
ACFE	0.016072	0.003836	0.238662	0.8119
FSIZ	0.084295	0.235731	0.357589	0.7215
C	-0.619791	2.920253	-0.212239	0.8324

R-squared	0.618471	Mean dependent var	2.392693
Adjusted R-squared	0.533738	S.D. dependent var	2.314784
S.E. of regression	2.353508	Akaike info criterion	4.607815
Sum squared resid	520.6659	Schwarz criterion	4.764126
Hannan-Quinn			
Log likelihood	-224.3908	criter.	4.671077
F-statistic	0.353793	Durbin-Watson stat	2.331166
Prob(F-statistic)	0.000235		

Source: E-view output

The data analysis above revealed that, the independent variables combined significantly explained the variations in the dependent variable with an F-statistics value of 0.000235 at 5% significant level. The coefficient of determination value 0.618471 implies that 61% of changes in the dependent variable are accounted for by the combined effect of variations in the independent

variables. Also, the adjusted R- squared value of 0.533738 implies that the model used in testing the hypotheses for the study is a proper and good fit, with a confidence level of approximately 53% for acceptance of the goodness of the study model. Durbin- Watson statistics value 2.33 is approximately equal to the 2.0, which implies the non-existence of serial auto correlation among the independent variables.

The regression output showed that audit committee size has positive statistical impact on the financial statement fraud. However, audit committee meeting has a statistical positive influence impact on financial statement fraud. While, the audit committee independent non- executive has positive and statistically significant at 5% significant level. Also audit committee financial expert has positive and statistical non-significant at 5% significant level.

CONCLUSION AND RECOMMENDATIONS

The study empirically investigated the audit committee effectiveness and financial statement fraud, the secondary data was employed from the company's financial statements of sampled ten firms, with data covering from 2011 to 2020, the analytical output of the study concludes that the audit committee size, audit committee meeting, audit committee independence has a positive and statistical significant relationship with financial statement fraud, while audit committee financial expert has a positive and statistical non-significant relationship with financial statement fraud.

RECOMMENDATION

Based on the output from our investigations, we therefore recommended that:

- a. The regulatory authorities such as (SEC) and the (NSE) should ensure strict compliance with the governance code best practices in other to protect the interest of stakeholders.
- b. An audit committee that consists of members with financial knowledge reduces the mesmerizing of the financial statement.

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