

AUDIT QUALITY AND EARNINGS MANAGEMENT OF LISTED INTERNATIONAL LICENSED COMMERCIAL BANKS IN NIGERIA

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ABSTRACT

The study examined audit quality and earnings management of listed international licensed commercial banks in Nigeria. The specific objectives were to; determine the effect of audit tenure on discretionary accruals of listed commercial banks in Nigeria, ascertain the effect of audit fee on discretionary accruals of listed commercial banks in Nigeria, examine the effect of audit tenure on conservatism of listed commercial banks in Nigeria, evaluate the effect of Audit fee on conservatism of listed commercial banks in Nigeria. This study adopted ex-post facto research design. The population and sample size of the study is the eight (8) listed commercial banks with international license in Nigeria stock exchange as at December 31st 2021. Secondary data was used as instrument. The formulated research questions were analyzed with descriptive statistics. The hypotheses were tested using the multiple regression analysis with the aid of E-view version 10. The study concludes that, there is no significant relationship between audit tenure and discretionary accruals of listed international licensed commercial banks in Nigeria. There is significant between audit fee and discretionary accruals of listed international licensed commercial banks in Nigeria. Hence, there is no significant relationship between audit tenure and conservatisms of listed international licensed commercial banks in Nigeria. There is no significant between audit fee and conservatisms of listed international licensed commercial banks in Nigeria. The study recommend that policy should be enacted on the banking industry, concerning too long audit tenure, and recommend that there should be change of audit firm within five to seven years in order not to have audit misstatements as a result of close working relationship. This in turn will reduce discretionary accruals and earnings smoothing. Listed international licensed commercial banks should continue with appropriate audit fee in order for better earnings quality in listed construction companies in Nigeria. The commercial banks sector should monitor the compliance with the provisions of the Nigerian code of corporate governance earnings management of conservatism. This will help strengthen the faithful representation of financial reports quality. To make reliable audit and financial reporting quality by management, commercial banks should maintain the level of audit fee to enhance the quality of financial reports in conservatism.

Keywords: Audit Quality, Earnings Management, Audit Tenure, Discretionary Accruals, Audit Fee and Conservatism

INTRODUCTION

In modern businesses, the manipulative behaviour of managers associated with the deliberate altering of financial statements through the use of judgment in structuring transactions to either mislead the firm's stakeholders about the true economic picture of the firm or to achieve some contractual benefit that is based on reported accounting numbers (Rao & Dandale (2008), Pajunen & Saastamoinen (2013). Earnings management is legal, thus has remained an issue of major concern among professional accountants, regulators and other users of financial information (International Accounting Standards Board (IASB), 2008, in Glautier et al., 2020). This is due to the fact that financial reporting has been a principal means of communicating the results of transactions and events which transpired within the organization to the outsiders; who may use such information in assessing the economic performance and condition of a business as well as a guide in making economic decisions (Ahmed et al. 2018). Hence, the directors of the companies

are saddled with the utmost responsibility of hiring reputable external auditors and it is expected that they make transparent and timely disclosures via quality audit practices.

A wide understanding of audit quality is recognized as the most important monitoring mechanism that can minimize agency costs and reduce conflicts of interest between management and owners and reduce the threats to objectivity and independence in modern business. Sayyar et al. (2016), viewed audit quality as those techniques the auditors use to recognize misstatements in clients accounting system or information and report the misstatements to the appropriate person(s). The quality of audit reports is a basic requirement to enhance the credibility of financial statements within the stakeholders to reduce investors risk in the organization.

Therefore, it is a basic ingredient in enhancing the credibility of financial statements to users of accounting information by providing an independent verification of financial reports presented by management. Audit of financial statements reduces information asymmetry in a firm and protects the interests of stakeholders through provision of assurance on the correctness, truthfulness and fairness of the financial statements prepared by management. This is in view of the fact that high quality audit is expected to detect material misstatements, errors, and losses which results from managerial opportunism in the quest to increase their economic largesse at the expense of other stakeholders of the firm.

Auditors have two major roles: the information role and the insurance role. As an information intermediary, an auditor is a person who independently and effectively verifies the company's financial statements before they are published. As an insurance provider, on the other hand, an auditor is a person who is legally accountable for damages to financial statement users. Auditors therefore have the primary responsibility of promoting transparency in the financial reporting processes that in turn generates high quality financial statements. In other words, auditors are deemed to be one of the key drivers that help promote the transparency of the stock markets. The public may therefore expect auditors to stop financial institutions from engaging in earnings management. Importantly earnings management may be one indicator that could gauge the quality of an audit. Most audit studies suppose that the auditor size would be a relevant proxy of audit quality and they use a binominal variable of whether the company is audited by the international big4 audit firms or not to investigate the influence of audit quality, the Big4; Price Waterhouse & Coopers, KPMG, Ernst & Young, and Deloitte, provide better quality of audit service than non-Big4. We consider that this is because the market shares between the Big4 and local audit firms stock market varies in different countries. In the global stock market, the Big4 mainly occupies the audit service market of large companies representing each country, while local accounting firms in each country are in charge of auditing small and medium-sized companies.

Statement of Problem

Earnings management is common in Nigerian listed companies and it seem as mostly aided by audit firms. Part of the reason is Nigerian regulators' reliance on accounting numbers to govern listed companies. For example, the Nigeria Securities Regulatory Commission (NSRC) requires listed companies to have a certain return on equity (ROE) before allowing them to issue new shares to existing shareholders (rights issues) (Uwalomwa et al., 2016). One peculiarity of Nigerian listed companies is that some are in financial distress and should be bankrupt by developed country standards. Unlike mature stock markets in developed countries, they are still listed in Nigeria.

As a result, Nigeria's audit quality lags behind many advanced jurisdictions. This has hampered efficient equity market growth. Due to firm earnings management supported by audit firms, the Nigerian market has far fewer analysts than developed markets. Investors in Nigeria frequently complain about the lack of or inaccuracy of financial information on banks. According to Peace and Donald (2015), there is no evidence of extreme aggressiveness in earnings management among Philadelphia manufacturing companies. These studies were examined both globally and locally. According to Beneish (2021), earnings quality has deteriorated over time. Rao and Dandale (2018), Pajunen and Saastamoinen (2017) conclude that earnings management is vital to the firm's survival. According to Feng-Li et al. (2015), earnings management increased the number of

stressed/bankrupt firms while decreasing the number of non-stressed/non-bankrupt firms. Thus, the findings from developed countries are inconsistent and cannot be generalized to the Nigerian economy.

Web metric analysis shows a draught in empirical literature on earnings management and financial reporting quality in Nigeria. Abbot 2016; Bouaziz 2019; Zaman 2017; Muhammed 2014; Dichev et al. (2002), etc. Other research has found a strong correlation between corporate governance and financial reporting quality. The researcher to the best my knowledge is unaware of any studies on earnings management and quality of financial reporting in Nigeria.

Given the above issues and the importance of addressing them, this researcher seeks to fill the content gap in the study titled audit quality and earnings management. Secondly, by focusing on the listed international licensed commercial banks in Nigeria to fill the analytical gap. Thus, the researcher was inspired to write about audit quality and earnings management listed international licensed commercial banks in Nigeria.

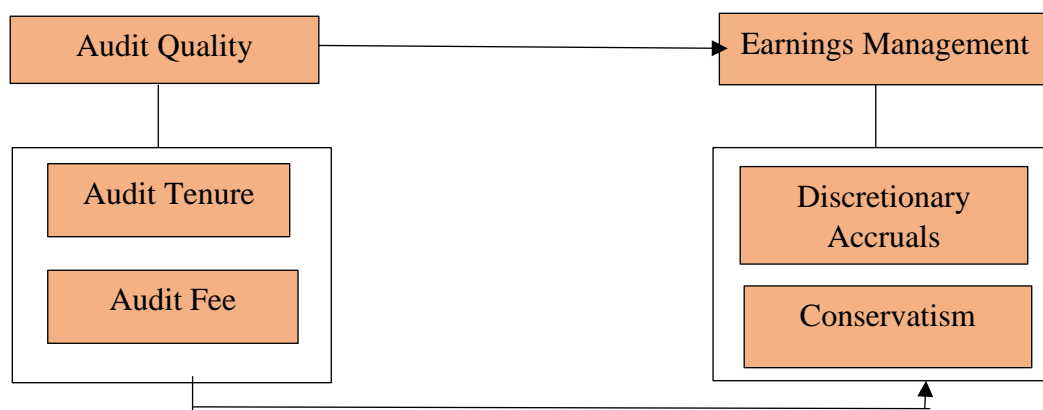


Figure: 1.1 Conceptual Framework of the effect of Audit Quality on Earnings Management.

Sources: Jayeola et al (2017); Abubakar et al. (2020) and researcher’s conceptualization, 2022.

Aim and Objectives of the Study

The main aim of this study is to determine the effect of audit quality on earnings management of listed international licensed commercial banks in Nigeria. However, the specific objectives are to:

1. determine the effect of audit tenure on discretionary accruals of listed commercial banks in Nigeria.
2. ascertain the effect of audit fee on discretionary accruals of listed commercial banks in Nigeria.
3. examine the effect of audit tenure on conservatism of listed commercial banks in Nigeria.
4. evaluate the effect of Audit fee on conservatism of listed commercial banks in Nigeria.

Research Hypotheses

Ho₁: Audit tenure does not significantly affect discretionary accruals of listed commercial banks in Nigeria.

Ho₂: Audit fee does not significantly affect discretionary accruals of listed commercial banks in Nigeria.

Ho₃: Audit tenure does not significantly affect conservatism of listed commercial banks in Nigeria.

Ho₄: Audit fee does not significantly affect conservatism of listed commercial banks in Nigeria.

Review of Related Literature

Conceptual Review

Audit Quality

Audit quality is defined as external auditors’ capability to detect and report material misstatements of the client’s financial statements. Audit failures such as in the case of Enron Corporation,

WorldCom Corporation, Global Crossing, ImClone Systems Incorporation and Tyco International have raised concerns on the auditors' ability in discharging their duties (Jonas & Blanchet, 2016). Abubakar et al. (2020), emergent economies are not exceptional from large corporate failures; for instance, the corporate failures in the Nigerian financial sector in the early 2000s and now brought auditors into sharp focus and have caused the public to question the role of accountants and auditors.

Ahmad et al. (2016), audit quality is related to the quality and effort of the auditor to identify material misstatement in the financial statements. It also concerned with the auditor willingness to disclose an unbiased audit report based on the audit result. Sayyar et al. (2016), viewed audit quality as those technics the auditors use to recognize misstatements in clients accounting system or information and report the misstatements to the appropriate person. The quality of audit reports is a basic requirement to enhance the credibility of financial statements within the stakeholders to reduce investors risk in the organization. Therefore, it is a basic ingredient in enhancing the credibility of financial statements to users of accounting information by providing an independent verification of financial reports presented by management (Kitiwong et al. 2107).

Audit quality is a measure of professional training, competence, skill and experience that was brought to bear on an audit assignment. It is a mirror through which total personality of an auditor or audit firm is assessed. Both professional bodies and the public can, to a large extent, rely on it for an unbiased evaluation (Ishaku et al., 2019). Audit Quality is among the factors that have an effect on the reliability of accounting information. This can be inspiration for more research on audit quality and the other factors that may influence it. Audit quality is defined as the possibility that an auditor would find out break in the owners accounting system and report the violated. The findings of misstatement measures quality in terms of the auditor's knowledge and ability, while the reporting of a misstatement is dependent on the auditor's incentives to disclose (Ozkan, 2018). Thus, the auditors should give a professional judgment concerning the creditability and reliability of accounting information enclosed in the annual reports and accounts for a particular period of time. However, the assessment carried out by auditors is vague. Therefore, the audit process is not mostly assessable and the appraisal of the quality of audit services must be indirect indication (Iwiyisi & Ifeanyi 2018).

Auditing is a monitoring device that is required for restoring sanity in financial reports prepared by directors which in most cases are perceived to contain fraud, errors or other irregularities. This is because high quality audit is expected to remove misstatements contained in financial statements and thus protect the interests of the owners. Stakeholders (creditors, potential investors, shareholders, and others) require financial information that is credible to make informed decisions. Fraudulent financial reports emanate because of information asymmetry occasioned by agency problem between shareholders (owners) and managers (agents). Therefore, audit quality is an auditor / audit firm which detects and corrects and reveal any material omission or misstatements in the financial statements in order to give high quality report.

Dimensions of Audit Quality

Audit Tenure

Audit tenure is "the number of periods-years an audit firm, an auditor audits a client or the number of years a company employs the same auditor". Audit tenure has been dissected into large and short audit periods. Long audit tenure might decrease the independence and professional care. On the other hand, shorter audit tenure reflects that the auditors have less knowledge about the client which may lead to low audit quality. Long audit tenure may increase the knowledge about the client's internal operations; but, the downside is that the auditor's independence may get compromised (Feleke, 2017). The clients change their auditors for many reasons, one of which is to obtain a reduced audit fee from a new auditor as the new auditor may offer services at a discount to win a new client (Oladipupo & Emina, 2016).

The auditor tenure may affect the quality of audits in a positive or negative manner. There are two arguments that revolve around this issue: (Short tenure) which reflects that the auditor will

less his experience in client's work, (Long period) meaning that the independence of auditor may decline (Knechel et al, 2012). It is widely assumed that the longer the audit firm's tenure, the lower the quality of the financial report, but there has been diverse opinion on audit firm tenure, most scholars (Seidman, 2013, & Anderson, 2018) are in support of longer audit firm tenure as short audit tenure will result to poorer quality of the financial report because at the earlier years of audit tenure, the auditor is not conversant with the ethical norms and internal control of the client companies. While Daniels & Booker (2011), and Firth, Rui, & Wu (2012) opined for shorter audit firm tenure period as it will enhance the independence of auditor and the quality of the financial report as issue of earnings management will be addressed. Audit firm in carrying their audit function are meant to be objective and free from bias in order to express an opinion on the financial report. This supports the idea of mandatory audit tenure rotation. If the auditor's independence has been compromised, it will reflect negatively on the financial report. This has resulted to corporate scandals in many countries as financial reports prepared are misleading. The questions are, do longer audit firm tenure affect or encourage earnings management? Or should audit firm tenure be reduced to enhance financial reporting quality?

As stipulated by the Financial Reporting Council of Nigeria (FRCN) code of governance 2016, *"external audit firms shall be retained for no longer than ten years continuously. External audit firms disengaged after continuous service to a company for ten years may be considered for reappointment seven years after their disengagement. Where an auditor's aggregate or cumulative tenure has already exceeded ten years at the date of commencement of this Code, such auditor shall cease to hold office as an auditor of the company at the end of the financial year that this Code comes into force."*

Audit Fees

Audit fee is the economic remuneration for auditors who provide audit services, which are an agency fee according to certain standards. The audit fee includes the total cost of audit through the overall audit work, the risk compensation and the profit demand. During the actual audit work, the audit fee influences not only audit quality, but also the development of accounting firms and audit industry.

Fees represent monetary compensation received by the auditor for services provided to clients. Fees charged by auditors are usually based on efforts exerted by them on the engagement including the level of risk inherent in the assignment (Huyghe, 2017). Audit fee can be explained to be the amount charged by the auditor for an audit assignment carried out. That is, the amount charged by the auditor for any work done in order to express opinion on the true and fair state of affairs or position of the client's enterprise.

Audit Fees are costs incurred by companies to pay public accounting firms to audit the company's financial statements. There are many studies related to the association of audit fees with audit quality research including Asthaana and Boone (2019). Also the effect of audit fees on auditor independence has been carried out by previous researchers such as Barkess (2020), Supriyono (2017), Rusmanto (2018). In the study of Asthaana and Boone (2012) they found that abnormal audit fees (audit fees that are outside the norm / above average) are negatively related to audit quality issued by audit firms.

Therefore, audit fee is always the research focus of domestic and foreign scholars. Simunic (2015), first explores the determinants of audit fees using empirical evidence. He finds that the complexity of the business, asset size, asset-liability ratio, etc. all affect the level of audit fees. From then on, many scholars continue to study the determinants of the audit fees basing on Simunic's audit fee model. Some scholars find that the market can recognize the characteristics that convey "high quality" signal and are willing to pay audit fee premiums to them. For example, "Big 4" usually obtain audit fee premiums Supriyono (2017), because audit clients believe that "Big 4" have higher audit quality Asthaana and Boone (2019). Besides, some researches find that there are different

levels of audit fees among "Big 4" Rusmanto (2018), and illustrate that the firms with industry specialization can acquire audit fee premiums Barkess (2020).

Earnings Management

Earnings management is the deliberate alteration of financial information to either mislead investors on the underlying economic status of a firm or to gain some contractual benefits that depend largely on accounting numbers (Ishaku et al., 2019). According to Hartwig (2018), earnings management is the most common form of micro accounting manipulation. Earnings Management is said to occur "when managers use judgment in financial reporting and in structuring transactions to alter financial reports to either mislead some stakeholders about the underlying economic performance of the company or to influence contractual outcomes that depend on reported accounting numbers". More contemporarily, Alhaddad and Whittington (2019), emphasize the alteration of financial reports can take place without violating general accounting standards. There are two broad ways in which managers can influence the content of their financial reports that result in unrealistic numbers (Hartwig, 2018). The first is through lobbying – managers hire lobbyists to change the guidelines of accounting in order to end up with a favorable result in their balance sheet. This is usually known as macro manipulation. On the other hand, when managers directly influence their financial reports, it is called micro accounting manipulation. In this case, the manipulation takes place without any systematic help from the outside.

Earnings management is the use of accounting techniques to produce financial statements that present an overly positive view of a company's business activities and financial position. Many accounting rules and principles require that a company's management make judgments in following these principles. Earnings management takes advantage of how accounting rules are applied and creates financial statements that inflate or "smooth" earnings (Burdeos, 2021). Earnings refers to a company's net income or profit for a certain period, such as a fiscal quarter or year. Companies use earnings management to smooth out fluctuations in earnings and present more consistent profits each month, quarter, or year. Large fluctuations in income and expenses may be a normal part of a company's operations, but the changes may alarm investors who prefer to see stability and growth. A company's stock price often rises or falls after an earnings announcement, depending on whether the earnings meet or fall short of analysts' expectations (Ozkan, 2018).

Measures of Earnings Management

Discretionary Accruals

Accruals are revenues earned or expenses incurred which impact a company's net income on the income statement, although cash related to the transaction has not yet changed hands. Accruals also affect the balance sheet, as they involve non cash assets and liabilities. Accrual accounts include, among many others, accounts payable, accounts receivable, accrued tax liabilities, and accrued interest earned or payable. Accruals and deferrals are the basis of the accrual method of accounting, the preferred method by generally accepted accounting principles (GAAP). Using the accrual method, an accountant makes adjustments for revenue that has been earned but is not yet recorded in the general ledger and expenses that have been incurred but are also not yet recorded. The accruals are made via adjusting journal entries at the end of each accounting period, so the reported financial statements can be inclusive of these amounts. Discretionary accrual is a non-mandatory expense/asset that is recorded within the accounting system that has yet to be realized. An example of this would be management bonus. The use of accrual accounts greatly improves the quality of information on financial statements. Before the use of accruals, accountants only recorded cash transactions. Unfortunately, cash transactions don't give information about other important business activities, such as revenue based on credit extended to customers or a company's future liabilities. By recording accruals, a company can measure what it owes in the short-term and also what cash revenue it expects to receive. It also allows a company to record assets that do not have a cash value, such as goodwill.

Modified Jones Model of Discretionary Accruals (1995)

Here in the model, account receivable was included by Dechow et al. (1995) to become modified Jones (1995) of Jones model (1991). Estimating of normal accruals in the first stage is similar to the model of Jones (1991).

The present model changes in revenue are modified for a change in receivables i.e (change in revenues minus change in account receivable). The model determination is as follows:

$$TA/Ait-1 = \alpha_1 (1/Ait-1) + \alpha_2 (\Delta REV_{it}/Ait-1) + \alpha_3 (PPE_{it}/Ait-1) + \epsilon_{it-1}.$$

$$DAit = TAC/Ait-1 - [\alpha_1 (1/Ait-1) + \alpha_2 (\Delta REV_{it}/Ait-1 - \Delta REC_{it}/Ait-1) + \alpha_3 (PPE_{it}/Ait-1)].$$

Where:

ΔREC = is a change in accruals receivables for firm i in period t , and other variables are as previously defined in Jones model (1991).

Conservatism

Prior researches on accounting conservatism focus on its association with debt, contracts, governance and management earnings forecasts. First, debt holders take care about the safety of the interests and the principle of the debts. The debtors should have enough net assets to pay off their debts. However, the value of net assets is uncertain in future. The lenders have strong motivations to verify the current value of net assets in a lower bound. During the life time of loans, the lenders monitor and even restrict the debtors' managerial activities to avoid the decrease of value of net assets. The debt covenants have the effects on limiting the reduction of net assets and applying for accounting conservatism in debtor's firms (Watts, 2013). It is noted that management has asymmetric incentives to be more forthcoming with good news against bad news. But the lenders are more worried about potential bad performance of the debtors.

Li (2019), Sheds light on the relationship between accounting conservatism and earnings management. It finds that accounting conservatism is negatively associated with real earnings management. Furthermore, it also tests that accounting conservatism has an effect that it can restrict on the innovation inputs which is measured by the extent of capitalized R&D. This effect of negative relationship between accounting conservatism and earnings management would increase under the situation that the firms have higher level of financial leverage. Conservatism is defined as "the accountant's tendency to require a higher degree of verification to recognize good news or positive economic performance as gains than to recognize bad news or negative economic performance as losses." These definitions are consistent with the traditional conservatism adage "anticipate no profits but anticipate all losses."

To settle the previous controversy on whether accounting conservatism is an efficient financial reporting mechanism, the IASB (2008) in a discussion paper related to improving conceptual framework states that prudence and conservatism, either conditional or unconditional, are no longer desirable qualities of financial reporting information because it believes that conservatism biases accounting information. Moreover, accounting conservatism violates neutrality which is one of fundamental qualities under the Conceptual Framework. Thus, the IASB changed its view concerning accounting conservatism compared with the previous IASB framework, while this change is not surprising given that prudence is likely to bias the reported financial position and financial performance. The IASB states that the understatement of assets and income or overstatement of liabilities and expenses in one period frequently leads to overstating financial performance in later periods a result that cannot be described as prudent. In 2010, the IASB has published another issue which also does not include conservatism or prudence in the Conceptual Framework because neither of them is considered as an aspect of faithful representation and including either would be inconsistent with neutrality. A few years later, the Conceptual Framework of IASB (2018) has officially reintroduced an explicit reference to the notion of prudence, a concept that was removed from the IASB (2010) Conceptual Framework. The IASB believes that prudence supports neutrality of information and therefore describes prudence as "the exercise of caution when making judgements under conditions of uncertainty".

The issue of restatement of financial statements to obtain management earnings, which is considered as a tool to promote financial statements reports, board of directors, and owners of capital, has recently faced investors with substantial losses. In other words, all the companies went bankrupt within recent years, have issued their financial restatements. Often, issuing financial restatements indicates that there are some problems in the internal control system, corporate governance, and misuse of the managers in the companies, which have lost their fame and values in market, and even sometimes led them to bankruptcy. Restatement of financial numbers provides conditions for managers to manipulate numbers of financial statements by changing time of report of items of assets and liabilities. The Dechow & Skinner Model would be used in the determination of Conservatism using the formula below:

$$CON/TA_{t-1it} = \alpha_0 1/TA_{it-1} + \alpha_1 FL_{it}/TA_{it-1} + \alpha_2 CONTG_{it}/TA_{it-1} + \epsilon_{it} \dots \dots \dots 5$$

$$Con_{it} = \epsilon_{it} = Con_{it} - (\alpha_0 1/TA_{it-1} + \alpha_1 FL_{it}/TA_{it-1} + \alpha_2 CONTG_{it}/TA_{it-1}) \dots \dots \dots 6$$

Where:

- Con = Conservatism for firm i at time t.
- FL = the Financial Leverage for firm i at time t.
- CONTG = the Contingent Gain for firm i at time t.
- TA = the Total Assets of firm i at time t.
- ϵ_{it-1} = error term for firm i at time t.

Theoretical review

Agency Theory

Formulated by Adams, (1994) agency theory is based on a premise that there exists an information asymmetry between the principals' and agent. This he notes has negative effects on the ability of the principals to effectively monitor if their interests are being served by agents. However, agency theory attempts to align the interests of a firm's principal to those of its managers. It is based on the assumption that there is an inherent conflict between the interests of a firm's owners and its management further noting that managers now possess superior knowledge and expertise to the firm's owners and are therefore in a position to pursue self-interested action at the expense of shareholders. Agency theory is concerned with resolving problems that can exist in agency relationships; that is, between principals (such as shareholders) and agents of the principals (for example, bank managers). The two problems that agency theory addresses are: the problems that arise when the desires or goals of the principal and agent are in conflict, and the principal is unable to verify what the agent is actually doing and the problems that arise when the principal and agent have different attitudes towards risk. Because of different risk tolerances, the principal and agent may each be inclined to take different actions.

Further, Agency theory contends to deal with the agent's tendency to self-interest and given that bank owners don't have full control over what accounting information system is being applied and what will be reported, internal auditors are employed to increase financial reporting and disclosures that would assist in reducing information asymmetry between banks owners, management and shareholders but to also improve financial reporting quality. Agency theory contends that internal auditing, in common with other intervention mechanisms like financial reporting and external audit, helps to maintain cost-efficient contracting between owners and managers. This research is anchored on this theory, reason been that Agency theory may not only help to explain the existence of internal audit in organizations but can also help explain some of the characteristics of the internal audit department, for example, its size, and the scope of its activities, such as financial versus operational auditing. Agency theory can be employed to test empirically whether cross-sectional variations between internal auditing practices reflect the different contracting relationships emanating from differences in organizational form. Linking this theory to the study, the researcher sought to unpack the effect of audit quality and earnings management of banks in Nigeria. Specifically audit quality in banks in Nigeria is an adjunct of the function performed by external audit created by senior managers to satisfy the demands for accountability made by external participants, especially shareholders. The focus of internal auditors in banks and

companies will in this case be geared towards financial audit, fraud prevention and internal control compliance work rather than operational reviews and management audits. This therefore means that internal auditors may be inextricably bound to the interests of shareholders and managers, for example through employee share ownership schemes. Arguably this shared interest lowers auditing fee, audit firm size and audit tenure and also affects the nature and scope of internal auditing activities and earnings management.

Empirical Review

Junaidu and Ahmed (2020) studied the relationship between audit quality and earnings management of listed non-financial companies in Nigeria. Ex-post-facto research design was used and data were extracted from the annual reports and accounts of the non-financial companies for the period 2012 to 2018. The data were analyzed using Arellano-Bond dynamic panel-data estimation technique. The findings revealed that the coefficient of the lagged Discretionary Accruals reveals a negative and statistically significant effect on current discretionary accruals, audit firm size has a negative and significant relationship with earnings management, auditor firm independence, auditor tenure and audit firm leading partner rotation has positive but not significant effect on earnings management. However, firm size, net cash flow to total assets and return on assets (ROA) exhibits a negative and significant relationship with earning management. The study concludes that audit quality reduces earning management of listed non-financial companies in Nigeria.

Ahmet et al. (2017), examined the association between audit firm tenure and audit quality. The cross-sectional version of modified Jones Model was used to estimate discretionary accruals. The result indicates that there is no association between long audit tenure and audit quality. Whether a big firm is of higher audit quality than a non-big firm is one of the most contentious research questions in empirical auditing studies. Empirical evidence however provides contradictory findings. The study then aims to revisit the issue and contributes to the literature on the association between audit quality and earnings management in the context of Southeast Asia. They develop a new probity model that helps predict the probability that auditors provide high audit quality. They are also the first study that measures audit quality by using the joint association between type of audit report and level of cross-sectional Jones discretionary accruals.

Ozkan (2018) analyze the association between audit quality and earnings management for non-financial firms quoted on Borsa Istanbul. Ordinary least square regression analysis was employed, and three different proxies for audit quality (auditor independence, audit industry specialization and auditor tenure) were used based on a sample of 97 non-financial firms quoted on Borsa Istanbul from 2013 to 2018. The findings indicate that auditor independence and audit industry specialization are negatively and significantly related with likelihood of earnings management, long-term auditor and client relationship enables the management of firms to more actively engage in earnings management. The findings support notion that the high-quality audit is one of the prominent factors that can mitigate earnings management practices.

Affes and Smii (2016), examined the impact of the audit quality on that of the accounting earnings in 20 Tunisian firms listed on the TSE (Tunisian Stock Exchange) for the period (2005-2009), confirms the significant impact of the audit quality on that of the accounting earnings. The study results also show that the variables: size of the audit firm, sector based specialization of the audit firm, the co-auditing and the size of the audit committee, improve the quality of the accounting earnings management.

Alzoubi (2018), examined the evidence regarding the relationship between audit quality, debt financing, and earnings management in Jordan. The study used the cross-sectional version of the modified Jones model, in which discretionary accruals were employed as a proxy for earnings management. Generalized least squares regression was employed to examine the influence of audit quality and debt financing on earnings management using a sample comprising 72 industrial companies during the selected period from 2006 to 2012. The results suggested that audit quality (auditor tenure, size, specialization, and independence) and debt financing (low debt) diminish the

potential of earnings management, and, in turn, enhance the financial reporting quality. Invariably, high debt would raise earnings management risk. The research raises probable implications for policy-makers in Jordan and other countries to consider in formulating a more comprehensive and reliable audit system.

Martinez and Moraes (2016) investigates the relationship between audit fees and earnings management in the Brazilian market using a sample of 300 firms listed on the BM & FBovespa for which it was possible to identify the amount paid to the auditors, using data gathered from the Econometric database and the website of the Brazilian Securities Commission. The study analyzed the data using multiple regressions and the findings revealed a negative and significant relationship between audit fee and earnings management meaning that audit firms that charge less for their service tend to be more relaxed regarding earnings management by their client companies.

Nawaish (2016) examined the prediction that external audit quality is positively associated with earnings management in Jordanian banking firms listed in Amman Stock Exchange (ASE). Ex-post-facto research design was used. Findings revealed that audit tenure, audit fees, and auditor specialization have significant relations with earnings management. It means, future earnings management forecast is predictable based on audit quality leading indicators (audit tenure, audit fees, and auditor specialization).

METHODOLOGY

This study adopted ex-post facto research design. The population and sample size of the study is the eight (8) listed commercial banks with international license in Nigeria stock exchange as at December 31st 2021. Secondary data was used as instrument. The formulated research questions were analyzed with descriptive statistics. The hypotheses were tested using the multiple regression analysis with the aid of E-view version 10.

Table 1.1 Listed Commercial Banks with International Authorization/license

S/N	Name of Listed Company	Sub-Sector
1	Access Bank Plc	International commercial licensed
2	Fidelity Bank Plc	International commercial licensed
3	First City Monument Bank Plc	International commercial licensed
4	First Bank of Nigeria Limited	International commercial licensed
5	Guaranty Trust Bank Plc	International commercial licensed
6	Union Bank of Nigeria Plc	International commercial licensed
7	United Bank for Africa Plc	International commercial licensed
8	Zenith Bank Plc	International commercial licensed

Source: Nigerian Exchange Group (NEG) as at 31 January, 2022

Operational Measurement of Variables

The aim of the study is to ascertain empirically, the measurements and values or amounts in the financial statements that will be used in the relationship, in terms of effect that exist between dimensions of independent variable 'audit quality' and the measures of the dependent variable 'earnings management' of listed international licensed commercial banks in Nigeria.

Audit Tenure, Tim and Contreras (2017); and Masoud et a. (2018); Zvi and Jing (2018).

Starting with the first dimension and the variable of interest, which is 'audit tenure'. Borrowing from the empirical studies of Tim and Contreras (2017); Masoud et a. (2018); Zvi and Jing (2018), because of audit tenures relations (long or short) audit firms and client enjoy over the years, it is difficult to ascertain the true and fair view of the financial statement, in other words there might be audit misstatements. Thus, other factors impact on audit tenure as a dimension of audit quality. Hence, to ascertain audit tenure, other control variables will be included. They are related to the client's or the audited firm characteristics: the type of auditor, age, growth, leverage, cash flows from operations, return on assets and firm size and.

- a. The first control variable is the type of auditor. To be more precise if the auditor belongs to the Big - 4 (Deloitte, PricewaterhouseCoopers, Ernst & Young and KPMG) or not, categories as the five or six biggest auditors are also used. According to DeAngelo (1981), bigger audit firms deliver higher quality reports. However, the subjects in this research are all audited by one of the four greatest audit firms within intervals of 5 years of the research period. (In addition to the continuous measure of auditor tenure, we also follow the literature (e.g., Johnson et al. 2002; Carey and Simnett 2006; Chen et al. 2008; Gul et al. 2009) and create two indicator variables to proxy for long and short auditor tenure. Long-Tenure is set to 1 for auditor tenure longer than or equal to 11 years, and to 0 otherwise. Short-Tenure is set to 1 for auditor tenure shorter than or equal to three years, and to 0 otherwise).
- b. Another control variable commonly used is age, measured as the number of years listed. According to Carey and Simnett (2006), younger firms have a larger chance of being in financial distress and engage more in earnings management.
- c. The next control variable corrects for the growth of a firm, is operating activities. Young (1999), states that non-discretionary accruals are positively associated with growth rates as a result of changes in working capital due to growth or shrinkage. Without controlling for growth rates, the non-discretionary accruals are overstated and these accruals will be attributed to the discretionary part. So, the expected relation between the variable growth and discretionary accruals is negative (Young, 1999).
- d. Leverage is included as control variable since banks (companies) with more debt might use the freedom in accounting in terms of accruals to stay away of violations of debt-covenants (DeFond & Jiambalvo, 1994). Cash flows from operations are controlled for since these flows are (negatively) correlated with accruals (Sloan, 2004). The control variable for operating cash flows is scaled by total assets. Dechow et al. (1995), recommend to control for firm performance (ROA), since this association is not captured in the model.
- e. The last control variable is the size of the client, measured by the natural logarithm of total assets. The variable is transformed to normalize the distribution of the variable (Carey & Simnett, 2016).

Thus, this leads to the regression equation, which will be used to study the effect of audit tenure on audit quality:

Thus:

Using the modified model, based on Carcello and Nagy (2004).

$$\log AT_i = X_i b + e_i \dots 1$$

$$\text{LogAT}(1 + \text{Duration}) = a + b_1 \text{APTENURE}_{it} + b_2 \text{APTENURE}_{it}^2 + b_3 \text{AFTENURE}_{it} + b_4 \text{AFTENURE}_{it}^2 + b_5 \text{AGE}_{it} + b_6 \text{GROWTH}_{it} + b_7 \text{LEV}_{it} + b_8 \text{OCF}_{it} + b_9 \text{ROA}_{it} + b_{10} \text{SIZE}_{it} + e_u \dots 2$$

Since the log of 0 is undefined, we add 1 to the duration dependent variable before taking the log transformation. We include various control variables that may be associated with the timeliness of misstatement discovery.

- AT_{it} = the amount of discretionary accruals scaled by lagged total assets (calculated through either the original Jones model or the modified version of it),
- APTENURE_{it} = the length of the current audit partner engagement at the firm (either just the number of years or the number of years squared),

AFTENURE _{it}	=	the length of the current audit firm engagement at the firm (either just the number of years or the number of years squared),
AGE _{it}	=	the number of years the firm is listed on the Nigerian Stock Exchange,
GROWTH _{it}	=	the percentage change in the firm's net sales relative to last year,
LEV _{it}	=	the proportion of the firm's total assets consisting of liabilities at the end of the year,
OCF _{it}	=	the net cash flows from operating activities over total assets at the end of the year,
ROA _{it}	=	the return on assets over the last year, and
SIZE _{it}	=	the natural logarithm of the firm's total assets at the end of the year

Discretionary Accruals (Jones Model of 1991)

Jones (1991), came up with the projected effective new model of determining nondiscretionary accruals. The model uses plant, properties and equipment (PPE) to manage changes in non-discretionary accruals arising from the change of depreciation, i.e. change of firm's activities. Also, sales variable is used to manage changes in non-discretionary accruals associated with working capital accounts which come from changes in the firm's economic environment. This model is based on the postulation that working capital accruals are related to changes in sales and depreciation is related to asset.

The following model are used to determine the total/normal accruals:

$$TA/A_{it-1} = \alpha_1 (1/A_{it-1}) + \alpha_2 (\Delta REV_{it}/A_{it-1}) + \alpha_3 (PPE_{it}/A_{it-1}) + \varepsilon_{it-1} \dots \dots \dots 3$$

$$DA_{it} = TAC/A_{it-1} [\alpha_1 (1/A_{it-1}) + \alpha_2 (\Delta REV_{it}/A_{it-1}) + \alpha_3 (PPE_{it}/A_{it-1})] \dots \dots \dots 4$$

Whereas TA_{it} = total accruals for firm i in year t .

A_{it-1} = total assets for firm i in the previous year,

ΔREV_{it} = change in revenues from i in year t ,

PPE_{it} = gross property and equipment for firm i in year t ,

ε_{it-1} = error term for firm i year t .

DA_{it} = discretionary accruals.

Conservatism (Dechow & Skinner 2000)

Conservatism is the accountant's tendency to require a higher degree of verification to recognize good news or positive economic performance as gains than to recognize bad news or negative economic performance as losses. The model measures conservative earnings in the banks. The Dechow & Skinner Model would be used in the determination of conservatism using the formula below:

$$CON/TA_{t-1it} = \alpha_0 1/TA_{it-1} + \alpha_1 FL_{it}/TA_{it-1} + \alpha_2 CONTG_{it}/TA_{it-1} + \varepsilon_{it} \dots \dots \dots 5$$

$$Con_{it} = \varepsilon_{it} = Con_{it} - (\alpha_0 1/TA_{it-1} + \alpha_1 FL_{it}/TA_{it-1} + \alpha_2 CONTG_{it}/TA_{it-1}) \dots \dots \dots 6$$

Where:

Con = Conservatism for firm i at time t .

FL = the Financial Leverage for firm i at time t .

$CONTG$ = the Contingent Gain for firm i at time t .

TA = the Total Assets of firm i at time t .

ε_{it-1} = error term for firm i at time t .

Table 1.2 Operational Measurement of Variables

Variable	Type of Variables	Measurement Scale	Source of Data
Audit Tenure (AT)	Dimension independent variable	Using the modified model, based on Carcello and Nagy (2004).	Annual report
Audit Fee (AF)	Dimension independent variable	The amounts stated as auditor's remuneration or fee in notes to the financial statement, other operating expenses	Annual report

Discretionary Accruals (DA)	Measure of dependent variable	The reverse measure of discretionary accruals using Jones' (1991) model proposed by Dechow and Dichev (2002).	Annual report
Conservatism (CO)	Measure of dependent variable	The reverse measure of conservatism using Modified Jones' (1994) model proposed by Dechow and Dichev (2002)	

Source: Research student compilation, 2022.

Model Specifications

To examine the implications of audit quality on earnings management, this study follows the works of Ewa et al. (2020); Siyanbola et al. (2017) and Oboh et al. (2018), but with some improvements in terms of the measurement of audit quality and the adoption of a more encompassing measure of earnings management. The functional specifications of the models are provided as: $\psi = \beta_0 + \beta_1 + \beta_2 + \psi \dots \dots \dots (.05)$

Thus;

$$EM = f(AT + AF)$$

- Where:
- ψ = index of outcome variable
 - β_0 = Constant term (y intercept)
 - $\beta_1, \beta_2, \beta_3$ = Coefficient of the independent variables
 - ψ = Error term (causes of discretionary accruals or discretionary provisions for loan loss persistence not explained by variables in the model)

The audit quality (AQ) components in the study are [audit tenure (AT) and audit fee (AF) defined as three components used in the study. Whereas earnings management (EM) its measures are discretionary accruals (DA) and Conservatism (CON)

The following 2 models were used to analyze the multivariate relationship between the variables.

The First Model: The first hypothesis test model; shows the relationship between discretionary accruals and audit tenure and audit fee:

$$DA_{it} = \beta_0 + \beta_1(AT)_{it} + \beta_2(AF)_{it} + \psi \dots \dots \dots 8$$

The Second Model: The second hypothesis test model; shows the relationship between conservatism and audit tenure and audit fee:

$$CON_{it} = \beta_0 + \beta_1(AT)_{it} + \beta_2(AF)_{it} + \psi \dots \dots \dots 9$$

Data Analyses and Interpretations

Table 1.3 Descriptive Statistics

	Mean	Median	Maximum	Minimum	Std. Dev.	Jarque-Bera	Prob. Val.	Observations
AT	1.2014	0.4205	4.2053	-0.0010	0.1034	0.0328	0.0893	80
AF	201.5273	189.3721	510.7262	167.6704	155.1328	41.4582	0.4235	80
DA	-0.0169	-0.0400	2.0220	0	-0.0321	0.0132	0.1010	80
CON	0.0131	0.00423	1.2016	0	-0.0210	0.0120	0.2920	80

Source: E-view (v.10) Analyzed Researcher's Result, 2022

The descriptive statistics for the data are shown in table 4.1. audit tenure and audit fee have mean values of 1.2014 and 201.5273 sequentially. On the hand, discretionary accruals and conservatism mean values are -0.0169, 0.0131 and 0.0303.

Jarque-Bera statistics [(JB (PValue > 0.05) = Accept Ho (Normal Distribution) and JB (P Value <0.05) = Reject Ho (Non-Normal Distribution)]. Thus, the p-value for the dimensions of the study; audit tenure and audit fee, were 0.0893 and 0.4235 sequentially, indicating normally distributed.

Test of Hypotheses:

Multivariate Analysis and Results Interpretations

The First Model: The first hypothesis test model; shows the relationship between discretionary accruals and audit tenure and audit fee:

$$DA_{it} = \beta_0 + \beta_1(AT)_i + \beta_2(AF)_i + \psi (.05) \dots\dots\dots 8$$

Table 1.4

Dependent Variable: DA
 Method: Least Squares
 Date: 09/05/22 Time: 00:07
 Sample: 2011 2020
 Included observations: 80

Variable	Coefficient	Std. Error	t-Statistic	Prob.
AT	0.407915	0.055147	0.143532	0.8876
AF	0.347136	0.165444	2.098213	0.0411
C	4.965624	0.287321	17.28248	0.0000
R-squared	0.989523	Mean dependent var	10.70450	
Adjusted R-squared	0.987674	S.D. dependent var	0.960939	
S.E. of regression	0.106688	Akaike info criterion	1.468175	
Sum squared resid	0.193499	Schwarz criterion	1.269218	
Log likelihood	-19.41584	Hannan-Quinn criter.	1.424996	
F-statistic	535.1751	Durbin-Watson stat	2.311585	
Prob(F-statistic)	0.000000			

Source: Researcher’s Statistical Computation from E-view (v.10), 2022.

From the output of table 4.6, the coefficient of AT and AF are 0.407915 and 0.347136 respectively. The standard error of the regression coefficients are 0.055147 and 0.165444 respectively for AT and AF. This value identifies limit of error is expected to be inherent in the result. T-statistics is above 2 is a sufficient statistically evidence of significant for AT is below 2 which is not a sufficient statistically evidence of significant. Thus, the Prob value of AT 0.8876, which means the relationship between AT and DA is not statistically significant at 5 percent significant level. Meanwhile the Prob values of AF and DA 0.4511, are statistically significant at 5 percent significant. The result showed that the coefficient of determination (R²) which measures the goodness of fit is 0.989523, meaning that 98 percent of the variation in the dependent variable (DA) can be explained by the dimensions of the independent variables. The result indicates that the model is proper and adequate for the study. The model goodness of fit and appropriateness is also supported by the outcomes of F-statistics and probability of F-statistics of 535.1751 and 0.000000 respectively. The Durbin-Watson statistics of 2.311585 also indicates the absence of serial autocorrelation.

Summary of Null Hypotheses Result Findings of the First Model Tested at 0.05 Level of Significance

Ho₁: There is no significant relationship between audit tenure and discretionary accruals of listed international licensed commercial banks in Nigeria.

Ho₂: There is significant between audit fee and discretionary accruals of listed international licensed commercial banks in Nigeria.

The Second Model: The second hypothesis test model; shows the relationship between conservatism and accruals and audit tenure and audit fee:

$$CON_{it} = \beta_0 + \beta_1(AT)_i + \beta_2(AF)_i + \psi (.05) \dots\dots\dots 9$$

Table 1.5

Dependent Variable: CON
 Method: Least Squares
 Date: 09/05/22 Time: 00:37
 Sample: 2000 2020
 Included observations: 80

Variable	Coefficient	Std. Error	t-Statistic	Prob.
AT	-1.561805	0.477536	-3.270551	0.1365
AF	-0.586054	0.159176	-3.681805	0.4018
C	-0.061630	0.829322	-0.074314	0.9416
R-squared	0.717012	Mean dependent var	1.580247	
Adjusted R-squared	0.697073	S.D. dependent var	0.533699	
S.E. of regression	0.307943	Akaike info criterion	0.651840	
Sum squared resid	1.612093	Schwarz criterion	0.850797	
Log likelihood	-2.844321	Hannan-Quinn criter.	0.695019	
F-statistic	14.35775	Durbin-Watson stat	1.961762	
Prob(F-statistic)	0.000340			

Source: Researcher's Statistical Computation from E-view (v.10), 2022.

From the output of table 4.7, the coefficient of AT and AF are -1.561805 and -0.586054 respectively. The standard error of the regression coefficients are 0.477536 and 0.159176 respectively for AT and AF. This value identifies limit of error is expected to be inherent in the result. T-statistics is negative and below 2 is not a sufficient statistically evidence of significant for AF and AF, Thus, the Prob value of AT 0.1365 and AF 0.4018, which means the relationship between AT and CON and AF and CON is not statistically significant at 5 percent significant level. The result showed that the coefficient of determination (R^2) which measures the goodness of fit is 0.717012, meaning that 71 percent of the variation in the dependent variable (CON) can be explained by the dimensions of the independent variables. The result indicates that the model is proper and adequate for the study. The model goodness of fit and appropriateness is also supported by the outcomes of F-statistics and probability of F-statistics of 14.35775 and 0.000340 respectively. The Durbin-Watson statistics of 1.961762 also indicates the absence of serial autocorrelation.

Summary of Null Hypotheses Result Findings of the First Model Tested at 0.05 Level of Significance

Ho₃: There is no significant relationship between audit tenure and conservatisms of listed international licensed commercial banks in Nigeria.

Ho₄: There is no significant between audit fee and conservatisms of listed international licensed commercial banks in Nigeria.

Summary Results Findings

Table 1.6 Summary Computation of Hypotheses Results

Hypotheses	Coefficient	Std. Error	T-Stat	P-Value 0.05	Statistical Decision	Result
HO ₁	0.407915	0.055147	0.143532	0.8876	Not Significant	Accepted HO ₁
HO ₂	0.347136	0.165444	2.098213	0.0511	Significant	Rejected HO ₂
HO ₃	-1.561805	0.477536	-3.270551	0.1365	Not Significant	Accepted HO ₄
HO ₄	-0.586054	0.159176	-3.681805	0.4018	Not Significant	Accepted HO ₆

CONCLUSION

Investors, shareholders, and users all want high-quality financial information, which can be obtained by having high-quality earnings, which is considered one of the most important indicators of capital market efficiency. This is one of the most important considerations when evaluating an entity's financial health and determining the level of reliability of reported earnings (Usman, 2013). Hence study concludes that, there is no significant relationship between audit tenure and discretionary accruals of listed international licensed commercial banks in Nigeria. There is significant between audit fee and discretionary accruals of listed international licensed commercial banks in Nigeria. Hence, there is no significant relationship between audit tenure and conservatism of listed international licensed commercial banks in Nigeria. There is no significant between audit fee and conservatism of listed international licensed commercial banks in Nigeria.

RECOMMENDATIONS

The study recommend that policy should be enacted on the banking industry, concerning too long audit tenure, and recommend that there should be change of audit firm within five to seven years in order not to have audit misstatements as a result of close working relationship. This in turn will reduce discretionary accruals and earnings smoothing. Listed international licensed commercial banks should continue with appropriate audit fee in order for better earnings quality in listed construction companies in Nigeria. The commercial banks sector should monitor the compliance with the provisions of the Nigerian code of corporate governance earnings management of conservatism. This will help strengthen the faithful representation of financial reports quality. To make reliable audit and financial reporting quality by management, commercial banks should maintain the level of audit fee to enhance the quality of financial reports in conservatism.

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