Audit firm characteristics and audit quality in Nigeria

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Abstract: This study examines the impact of audit firms’ characteristics on audit quality. We proxy the dependent variable (audit quality) using the usual dichotomous variable of 1 if big 4 audit firm and 0 if otherwise. Data for the study were sourced from the financial statements of 18 food and beverage companies listed on the Nigerian Stock Exchange market within the period studied (2007-2012). The multivariate regression technique with emphasis on Logit and Probit method was used to estimate our model for the study. The findings indicate that there is a positive relationship between firm size, board independence and audit quality whereas there is a negative relationship between auditor’s independence, audit firm size, audit tenure and audit quality. The study suggests the need for the Nigerian Financial Reporting Council and other regulatory bodies in line with best practices to look critically into the three years professional requirements for auditors.

Keywords: Audit Quality, Audit Tenure, Audit Independence, Board Independence

1. Introduction

At the thrust of the functioning of the capital market is the role of the external audit as both owners/shareholders) and the professional managers would want to rely on the report of the external auditor in furthering their sometimes divergent interest arising from agency relationship that exists(Barbadillo & Aguilar, 2008) High-quality external audit has become an important policy issue following corporate scandals such as Enron, WorldCom, Global crossing, Cendant, Sunbeam(United States); BCCI, Independent Insurance, Equitable Life, Maxwell(United Kingdom), Metallgesellschaft(Germany), and Lever Brothers, African Petroleum, Cadbury, Savanna Bank, Wema and Intercontinental Bank (Nigeria).

The seemingly persistent bank failures in Nigeria have raised some fundamental issues on the quality of audit and the independence of the external auditor amidst others. In particular, regulators have often expressed their concern that the length of the auditor-client relationship (or auditor tenure) and executives association with auditors could impair auditor independence and thus audit quality (Darlis, Soo & Trompeter, 2003). The quality of an audit depends simultaneously on several audit firm features such as auditor specialty, auditor independence, auditor tenure, audit firm size, audit fee, auditor enterprise, audit company type. (Abedalgader Ibrahim & Baker, 2010)

Auditors express their audit opinions on a financial statement presented to them based on audit evidence. The objective of an audit, therefore, is to plan and perform the audit to obtain appropriate audit evidence that is sufficient to support the opinion expressed in the auditor’s report. Insufficient or inappropriate audit evidence may lead to wrong conclusions and this may affect the quality of the report. Hence, the issue of audit quality has received increased attention due to highly publicized audit failures culminating in corporate scandals, corporate fraud, corporate failure. This concern motivated the current study of the relationship between firm characteristics and audit quality.

The issues above raise some fundamental questions: is audit tenure, audit firm type, auditor independence, audit firm size and audit fee factors that map into the auditor-client relationship and thus influences audit quality?

Against the above backdrop, the main objective of this study is to examine the relationship between audit firm characteristics and audit quality in Nigeria, using Nigerian listed companies as a reference point.

The study reveals that there is a positive relationship...
between company size, board independence and audit quality while there exists a negative relationship between audit independence, audit firm size and audit quality. While issues of firm characteristics and audit quality cannot be said to be novel in Nigeria, there exists conflicting reports on the relationship between explanatory variables and audit quality. Therefore, this study extends and contributes to extant empirical literature with a view to resolving the inconsistency.

The remainder of the paper is structured as follows: in section 2, conceptual framework on audit quality and prior empirical studies were considered, in section 3, data estimation technique was addressed. Section 4 focused on the estimation result and discussion of findings. The final section addressed conclusion and policy implications.

2. Literature Review

2.1. Concept of Audit Quality

Audit quality according to DeAngelo (1981, p.186), “is market-assessed joint probability that a given auditor will both (a) discover a breach in the client accounting system and (b) report the breach.” Jackson, Moldrich and Roebuck (2008) view the quality of audits from actual and perceived quality. Actual quality shows levels of risk of material errors in financial statements that can be reduced by the auditor. Perceived quality indicates the level of confidence of users in financial statement and the auditor’s effectiveness in reducing material misstatement in financial statements prepared by management. Titman and Trueman (1986) see audit quality as the accuracy of the information reported by auditors. DeAngelo definition captures attribute critically to the role played by auditors in financial statement preparation. Thus, audit quality combines the ability of an auditor to detect a breach (auditor competence) and a willingness to report such a breach (auditor independence).

Financial Reporting Council (2006b) considers five factors that influence audit quality to include: audit firm culture, skills and personal qualities of audit partners and staff, the effectiveness of the audit process, and the reliability and usefulness of audit reporting, amongst factor that are exogenous to the auditors. Earlier studies used observable outcomes as proxies for audit quality this includes; audit opinions, auditors’ selection and change, decisions, financial statements outcomes and analysts forecast. Francis (2004) reviewed 25 years of empirical researches and found that difference exists in the audit quality which can be concluded by examining different auditors. Moizer (1998) examines the issue of audit quality from a behavioural perspective, typically identifying attributes that are perceived by financial statement preparers, auditors and users that are related to audit quality. He found out that the big audit firms provide quality service.

Sutton and Lampe (1990) used a group of experts with practicing auditors to develop and evaluate a model of audit quality. Their model included 19 attributes of audit quality that they classified into three categories; planning, fieldwork and administration. Each of the 19 factors included one measure (or item). The first UK study to examine audit quality attributes was undertaken by Beatie and Fearnley (1995). They investigated finance directors of 210 listed UK companies to identify the importance of 29 desirable auditor characteristics. An exploratory factor analysis was used to identify five main factors: integrity of the firm, the technical competence of the firm, the quality of the working relationship with audit partner, the reputation of the firm and the technical competence of the audit partner.

In relation to the quality of auditing, Geiger and Raghuinanand (2002) surveyed 117 US corporations with significant liquidity issues between 1996 and 1998 and observed the chance of restrictions on going concern opinions to be lower in the first year of the assignment based on a higher reporting error rate of the auditor, based on sanctions by the Stock Exchange Commission (SEC). Factors that affect audit quality are various. The researches on audit quality focus on empirical analysis and the results indicate that audit tenure, audit firm size, auditor independence, etc. Have an impact on audit quality.

Since audit quality is not observable or quantifiable, various proxies are used in prior studies. One commonly used proxy is earnings quality, which is in turn measured using discretionary accruals as a proxy for audit quality (see Balsam, et al 2003) Carey and Simnett (2005) used the type of audit opinion as a proxy for audit quality in examining the relationship between the length of partner tenure and the propensity for audit partners to issue a modified audit opinion. Adeniyi and Miesiegha (2013) and Enoife, Mgbame and Enabosi (2013) measured audit quality by the likelihood that a sampled company employs the services of any of the big four audit firms. A dummy value of 1 is used or ‘0’ if otherwise.

2.2. Audit Tenure and Audit Quality

Prior studies have shown that audit tenure has a significant influence on audit quality. This effect was either positive or negative. Watts and Zimmerman (1983) found that the longer the auditor tenure, the more dependence on clients. Auditor’s objectivity and independence will be destroyed and hence, audit quality reduces. Copley and Doucet (1993) opined that the longer the period of engagement, the higher the risk of lower audit quality. This was supported by the findings in: (Arrunada & Paz-Ares, 1998, Dopuch, King &Schwarts 2001, Ebrahim, 2001.), Walker, Lewis and Casterella (2001) also investigated the link between the length of the audit engagement and audit failures and found that auditor rotation may not necessarily improve audit quality. Carcello and Nagy (2004) explored the association of changing the auditor and audit quality from the point of view of fraudulent reporting. They found no significant relationships intended of the long-term tenure of the auditors. They concluded that mandatory changes of auditors might have a negative impact on audit quality.

Abedalgader, Ibrahim and Baker (2010) investigated by using discretionary accruals as proxy for audit quality against auditor’s tenure and firm size in Jordan and found that
better and would be easier for the auditors to fight earnings
point of view, there is no difference in audit quality between
by providing high-quality audit. Lack of financial affiliation
longer audit tenure. Nashwa (2004) investigated the
relationship between long-term auditor-client relationship
and found that risk increase early in the auditor client-
that investors and information intermediaries perceive
auditor’s tenure as improving audit quality. Myers, Myers
and Omar (2003) found that higher earnings quality with
longer audit tenure. Nashwa (2004) investigated the
relationship between long-term auditor-client relationship
and found that risk increase early in the auditor client-
relationship and declines overtime. Barbadillo and Aguilar
(2000) investigated the relationship between auditor tenure
and audit quality and suggested that auditors tend to be more
dependent in the first years of the auditing engagement.

2.3. Audit Firm Size and Audit Quality

DeAngelo (1981) found that auditors with more clients
have more to lose by failing to report a discovered breach in
a particular client’s records when incumbent auditors earn
client-specific quasi-rents. Since then many researchers
support this conclusion (Teoh & Wong, 1993, Francis
& Krishman, 1999, Reynolds & Francis, 2000). Bae and Lee
(2013) concluded that audit firm size is positively associated
with audit quality measured by discretionary accruals and
modified opinions. Also audit firm size is positively
associated with audit fees. However, Imhoff (1988) was
against DeAngelo’s conclusion; he found that from analyst’s
point of view, there is no difference in audit quality between
top-eight audit firms and non-top-eight firms.

2.4. Auditor Independence and Audit Quality

DeAngelo (1981) relates the probability of detection to
auditor competence and probability of revelation is
associated with auditor independence. Due to larger client
portfolios, big auditors can exert more pressures on
management. Large international accounting firms have
established brand reputation and had motives to maintain it
by providing high-quality audit. Lack of financial affiliation
with clients makes bigger auditors more independent.
(Jeong & Rho, 2004). This independence provides big
auditors with stronger negotiation stance with their chart
compared with smaller audit firms (Nelson, Elliott & Tarpley,
2002). Other prior studies that have shown that auditor
independence affects audit quality positively, include
(Windsor & Warning-Rasmussen, 2009 and Alim, Trisni, &
Lilik, 2007). It therefore follows that auditor independence is
directly proportional to audit quality.

3. Methodology

3.1. Theoretical Framework and Model Specification

A framework for the analysis of the relationship between
audit firm characteristics and audit quality is the stakeholder
theory. The stakeholder theory, originally defined by
Freeman (1984, p.120) ‘is a theory of organizational
management and business ethics that addresses morals and
values in managing an organization’. In this theory, the
concept “stakeholders” refers to managers, shareholders or
other users of financial reports which are influenced, either
directly or indirectly by the actions of the auditor. A
fundamental characteristic of stakeholder theory is therefore
to attempt to identify individuals and groups that states,
organizations and companies are accountable to. This has
also been part of the theory’s challenge (Anheier, 2005).

According to Australian Accounting Standard Board
(AASB) (2011), variations in stakeholders’ perspective of
audit quality suggest that no single element should be assured
as having the dominant influence on audit quality explained in
this study as “audit tenure”, “auditor independence, audit firm
size and auditor expertise”. This means that a broader and
deeper understanding of the complexities of the issue needs to
be addressed through investigating the impact of these
variables more holistically in line with the response Divergent
Stakeholders theory (Freeman, 1984). This requires that
different stakeholders should carefully analyzed their actions
so as to determine the effects of their actions and their impact
on the perspectives of audit quality reason been that audits
provide assurance to shareholders, managers, investors,
creditors and other stakeholders, thus, providing confidence on
the financial reporting.

3.2. Model Specification

Flowing from the extant empirical literature and the above
theoretical frame-work, audit tenure is seen to impact audit
quality (Nashwa, 2004; Adeniyi, et al, 2013). Therefore, the
relationship between audit tenure and audit quality can be
represented as;

\[
AUDQUAL = f(AUDTEN)                        \quad (1)
\]

In the same vein auditors’ independence is believed to
influence the quality of audit (DeAngelo, 1981, Nelson et al
2009). Therefore, the relationship between auditor
independence and audit quality can be expressed as;

\[
AUDQUAL = f(AUDIND)                      \quad (2)
\]

Supposing audit quality depends on audit firm size, even
though a mixed relationship has been identified. While some
reported positive relationship (e.g DeAngelo 1981, Teoh &
Wong 1993, Francis & Rishman 1999 and Beynolds & Francis 2000). Others believe that a negative relationship exists (Imhoff, 1998; Abdelgader et al. 2010; Bae & Lee, 2013). Therefore, the relationship can be represented as:

$$AUDQUL = f(AUDTEN; AUDIND; AUDSIZE)$$  \hspace{1cm} (3)$$

Combining the three equations, we have:

$$AUDQUL = f(AUDTEN; AUDIND; AUDSIZE)$$  \hspace{1cm} (4)$$

Introducing two control variables of company size and board independence, we have:

$$AUDQUL = f(AUDTEN; AUDIND; AUDSIZE; COYSIZE; BODIND)$$  \hspace{1cm} (5)$$

In econometric form:

$$AUDQUL_t = \alpha_0 + \alpha_1 AUDTEN_t + \alpha_2 AUDIND_t + \alpha_3 AUDSIZE_t + \alpha_4 COYSIZE_t + \alpha_5 BODIND_t + \mu$$  \hspace{1cm} (6)$$

Where:

- **AUDQUL**: Audit Quality.
- **AUDTEN**: Audit tenure.
- **AUDIND**: Auditor independence.
- **AUDSIZE**: Audit firm size.
- **COYSIZE**: Company size.
- **BODIND**: Board independence.
- **\( \mu \)**: Error term.
- \( \alpha_1, \alpha_2, ..., \alpha_5 \): Unknown coefficient of the variables. It is presumptively expected \( \alpha_1, ..., \alpha_5 > 0 \).

The variables in the model are operationalised in Table 1 below.

<table>
<thead>
<tr>
<th>S/N</th>
<th>Variables</th>
<th>Definition</th>
<th>Type</th>
<th>Measurement</th>
<th>Authors</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>AUDQUL</td>
<td>Audit Quality</td>
<td>Dependent</td>
<td>If audited by the Big four ‘1’ and ‘0’ if otherwise</td>
<td>Adeniyi (2013); Enofe et al. (2013)</td>
</tr>
<tr>
<td>2.</td>
<td>AUDTEN</td>
<td>Audit Tenure</td>
<td>Independent</td>
<td>Length of auditor-client relationship ‘1’ if 3 years and ‘0’ if otherwise</td>
<td>Bafqi et al. (2013); Ebrahim (2001)</td>
</tr>
<tr>
<td>3.</td>
<td>AUDIND</td>
<td>A measure of auditor’s independence</td>
<td>Independent</td>
<td>Ratio of audit fees to company’s revenue</td>
<td>Adeniyi et al. (2013)</td>
</tr>
<tr>
<td>4.</td>
<td>AUDSIZE</td>
<td>Audit firm size</td>
<td>Independent</td>
<td>Natural log of audit fees</td>
<td>Bafqi et al. (2013)</td>
</tr>
<tr>
<td>5.</td>
<td>COYSIZE</td>
<td>Company’s size</td>
<td>Independent (Control)</td>
<td>Natural log of company’s total non-current assets</td>
<td>Bafqi et al. (2013)</td>
</tr>
<tr>
<td>6.</td>
<td>BODIND</td>
<td>Board of Director’s independence</td>
<td>independent (Control)</td>
<td>Ratio of non-executive directors to the company’s board size</td>
<td>Enofe et al. (2013)</td>
</tr>
</tbody>
</table>

Source: Researcher’s Computation, 2014

4. Data Source and Estimation Technique

The population of the study comprises the entire companies quoted on the food and beverages sector of the Nigerian Stock Exchange as at 31st December, 2012. Yamane (1967) model was used scientifically to determine the sample size of 18 companies with relevant data. The study used the panel binary logit and probit technique due to the dichotomous nature of the dependent variable. Prior to the estimation, we carried out the usual regression diagnostic tests of auto-correlation, normality and heteroscedasticity.

4.1. Estimation Result and Discussion

Table 2. Descriptive Statistics.

<table>
<thead>
<tr>
<th>Variables</th>
<th>Mean</th>
<th>Median</th>
<th>Maximum</th>
<th>Minimum</th>
<th>Std. Dev</th>
<th>Skewness</th>
<th>Kurtosis</th>
<th>Jarque-Bera</th>
<th>Probability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audqul</td>
<td>0.482517</td>
<td>0.086910</td>
<td>182.7236</td>
<td>4.200000</td>
<td>3562.000</td>
<td>2482159.</td>
<td>309047.9</td>
<td>2.860022</td>
<td>0.000000</td>
</tr>
<tr>
<td>Audind</td>
<td>0.001349</td>
<td>0.240000</td>
<td>4.200000</td>
<td>0.000000</td>
<td>0.400000</td>
<td>2.500000</td>
<td>1.000000</td>
<td>-2.706072</td>
<td>0.000000</td>
</tr>
<tr>
<td>Audsize</td>
<td>1.000000</td>
<td>3.607552</td>
<td>5350.000</td>
<td>2.58E-06</td>
<td>309047.9</td>
<td>2482159.</td>
<td>1.000000</td>
<td>0.000000</td>
<td>0.000000</td>
</tr>
<tr>
<td>Compsize</td>
<td>0.501451</td>
<td>5.010992</td>
<td>837.0577</td>
<td>0.501099</td>
<td>0.333422</td>
<td>0.333422</td>
<td>0.333422</td>
<td>0.298227</td>
<td>0.000000</td>
</tr>
<tr>
<td>Bdind</td>
<td>0.000000</td>
<td>0.000000</td>
<td>0.240000</td>
<td>5.010992</td>
<td>0.000000</td>
<td>0.000000</td>
<td>0.000000</td>
<td>0.000000</td>
<td>0.000000</td>
</tr>
<tr>
<td>Audten</td>
<td>0.000000</td>
<td>0.000000</td>
<td>0.000000</td>
<td>0.000000</td>
<td>0.000000</td>
<td>0.000000</td>
<td>0.000000</td>
<td>0.000000</td>
<td>0.000000</td>
</tr>
<tr>
<td>Observations</td>
<td>143</td>
<td>143</td>
<td>143</td>
<td>143</td>
<td>143</td>
<td>143</td>
<td>143</td>
<td>143</td>
<td>143</td>
</tr>
</tbody>
</table>

Source: Researchers’ Computation, 2014
Table 2 presents the descriptive statistics. As observed, AUDQUAL has a mean value of (0.482517) and a maximum value of (1.000000). The standard deviation of (0.501451) is considerably low and suggests that audit quality across the sample size exhibits considerable clustering around the mean. Audit independence has maximum and minimum values of (3.607552) and (2.58E-06) respectively with a mean value of (0.086910). The standard deviation of (0.451513) shows no significant deviation from the mean. The variable of AUDFSIZE has maximum and minimum values of (5350.000) and (0.240000) respectively with a standard deviation of (837.0577) which suggests a considerable variation or dispersion from the mean value of (182.7286). The COMPSIZE variable has a mean value of (71823.99) and a maximum value of (2482159) and a minimum value of (11.000000). The standard deviation of (309047.9) shows a significant dispersion from the mean. The other variables BDIND and AUDTEN exhibited considerable clustering around the mean. The Jarque Bera statistics revealed fairly large values which indicates that the data satisfy normality as well as the absence of outliers in the series.

Table 3. Result of the Correlation Analysis

<table>
<thead>
<tr>
<th>Correlation</th>
<th>t-Statistic</th>
<th>Probability</th>
</tr>
</thead>
<tbody>
<tr>
<td>AUDQUAL</td>
<td></td>
<td></td>
</tr>
<tr>
<td>AUDIND</td>
<td>-0.132665</td>
<td>1.000000</td>
</tr>
<tr>
<td></td>
<td>-1.589361</td>
<td>-----</td>
</tr>
<tr>
<td>AUDFSIZE</td>
<td>-0.202617</td>
<td>0.505185</td>
</tr>
<tr>
<td></td>
<td>-2.456902</td>
<td>6.959039</td>
</tr>
<tr>
<td></td>
<td>0.0152</td>
<td>0.0000</td>
</tr>
<tr>
<td>COMPSIZE</td>
<td>0.115824</td>
<td>-0.043600</td>
</tr>
<tr>
<td></td>
<td>1.384650</td>
<td>-0.518210</td>
</tr>
<tr>
<td></td>
<td>0.1683</td>
<td>0.6051</td>
</tr>
<tr>
<td></td>
<td>0.0154</td>
<td>0.3699</td>
</tr>
<tr>
<td></td>
<td>-0.152798</td>
<td>0.062420</td>
</tr>
<tr>
<td></td>
<td>-1.835939</td>
<td>0.742644</td>
</tr>
<tr>
<td></td>
<td>0.0685</td>
<td>0.4589</td>
</tr>
</tbody>
</table>

Source: Researchers' Computation, 2014

To address the basic regression assumptions, we tested for multicollinearity using covariance analysis as presented in Table 2. The results show a combination of positive and negative relationship among the variables. While positive relationship can be seen between company size and audit quality, board independence and audit quality, there appears to be a negative relationship between audit committee independence, audit firm size and audit quality.

The test of multicollinearity was further strengthened using the variance inflation factor test. From the results as presented in Table 3, it was observed that none of the variables tested indicates the presence of multicollinearity as the centered VIF of the variables were all less than 10.

Table 4. Result of the Variance Inflation Factors

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Uncentered</th>
<th>Centered</th>
</tr>
</thead>
<tbody>
<tr>
<td>C</td>
<td>0.018486</td>
<td>11.71220</td>
<td>NA</td>
</tr>
<tr>
<td>AUDIND</td>
<td>0.011014</td>
<td>1.465364</td>
<td>1.412655</td>
</tr>
<tr>
<td>AUDFSIZE</td>
<td>3.45E-09</td>
<td>1.595392</td>
<td>1.522335</td>
</tr>
<tr>
<td>COMPSIZE</td>
<td>1.91E-14</td>
<td>1.210779</td>
<td>1.148320</td>
</tr>
<tr>
<td>BDIND</td>
<td>0.014641</td>
<td>3.014233</td>
<td>1.023982</td>
</tr>
<tr>
<td>AUDTEN</td>
<td>0.018057</td>
<td>10.32051</td>
<td>1.010399</td>
</tr>
</tbody>
</table>

Source: Researchers' Computation, 2014

Table 5. Result of the Heteroskedasticity Test

<table>
<thead>
<tr>
<th>Heteroskedasticity Test: Breusch-Pagan-Godfrey</th>
</tr>
</thead>
<tbody>
<tr>
<td>F-statistic: 1.290284</td>
</tr>
<tr>
<td>Obs*R-squared: 6.430978</td>
</tr>
<tr>
<td>Scaled explained SS: 18.79480</td>
</tr>
<tr>
<td>Variable: Coefficient: 0.233589</td>
</tr>
<tr>
<td>AUDIND: 0.007329</td>
</tr>
<tr>
<td>AUDFSIZE: -5.95E-06</td>
</tr>
<tr>
<td>COMPSIZE: -4.31E-08</td>
</tr>
<tr>
<td>BDIND: -0.029045</td>
</tr>
<tr>
<td>AUDTEN: -0.143522</td>
</tr>
<tr>
<td>R-squared: 0.045289</td>
</tr>
<tr>
<td>Adjusted R-squared: 0.010189</td>
</tr>
</tbody>
</table>

Source: Researchers' Computation, 2014
The Breusch-Pagan-Godfrey test of heteroskedasticity was conducted to test the serial correlation of the error term. The result of the study as presented in Table 4 shows the absence of heteroskedasticity. Hence, we accepted the null hypothesis of homoskedastic error term. This means the error variance is not serially correlated.

Using the Breusch-Godfrey serial correlation (LM) test, the null hypothesis of no serial correlation was accepted. The Durbin-Watson statistic of (1.9981e2) in Table 4/5 indicates the absence of serial correlation since the DW statistic is substantially close to (2.00).

### Table 6. Result of the Breusch-Godfrey Serial Correlation LM Test

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>C</td>
<td>-0.008641</td>
<td>0.148497</td>
<td>-0.058192</td>
<td>0.9537</td>
</tr>
<tr>
<td>AUDIND</td>
<td>0.018730</td>
<td>0.090302</td>
<td>0.207415</td>
<td>0.8360</td>
</tr>
<tr>
<td>AUDFSIZE</td>
<td>-8.05E-07</td>
<td>5.63E-05</td>
<td>-0.014293</td>
<td>0.9886</td>
</tr>
<tr>
<td>COMPSIZE</td>
<td>2.75E-09</td>
<td>7.69E-08</td>
<td>0.035784</td>
<td>0.9715</td>
</tr>
<tr>
<td>BDIND</td>
<td>0.020707</td>
<td>0.101189</td>
<td>0.204640</td>
<td>0.8382</td>
</tr>
<tr>
<td>AUDTEN</td>
<td>0.000760</td>
<td>0.078974</td>
<td>0.034901</td>
<td>0.9722</td>
</tr>
<tr>
<td>AR(1)</td>
<td>-0.033843</td>
<td>0.085348</td>
<td>-0.449257</td>
<td>0.6540</td>
</tr>
<tr>
<td>RESID(-1)</td>
<td>0.000304</td>
<td>0.124806</td>
<td>0.024409</td>
<td>0.9806</td>
</tr>
<tr>
<td>RESID(-2)</td>
<td>0.132277</td>
<td>0.111050</td>
<td>1.191152</td>
<td>0.2357</td>
</tr>
</tbody>
</table>

The results of the binary probit are presented in Table 6. The McFadden R-squared value of (0.183181) shows explanatory power of 18.3%. On the basis of the performance of the individual variables, it was discovered that about three variables appear to be statistically insignificant. More specifically, the variable of board independence was found to be statistically significant and positive with a robust coefficient of (1.2756 12) and a significant z-statistic of (2.744730). The implication of this is that board independence has the likelihood of influencing...
audit quality. That means an independent board is likely to enhance quality audit in any organization. This is because the oversight function of the board is likely to be forceful with an independent board. In the same vein, the control variable of company size is seen to be significant and positive. The implication of this is that with larger company size, the quality of audit is likely to increase. Bigger companies are likely to attract more professionals that will positively affect the reporting quality of the organization and by extension, quality audit. The variable of audit tenure was negative and statistically significant having reported a t-value of (1.944456) and a robust coefficient of (-0.764762). This means audit tenure is more likely to have a negative effect on audit quality. The implication of this is that the long run relationship is likely to threaten the independence of the auditor and by extension audit quality. The result is consistent with the negative relationship reported by Davis, Warring and Rasmussen (2009).

Audit firm size was also found to be negative though statistically insignificant. This means a large audit firm is more likely to produce lesser quality audit. This is liken to the ‘too big to fail’ syndrome of Nigeria banks which saw the demise of large banks such as Intercontinental, Oceanic, to mention a few. The case of Arthur Anderson is still fresh in our memory; therefore, the negative relationship between the size of the audit firm and audit quality is not unexpected. This finding disagreed with the findings of previous studies (e.g. Teoh & Wong, 1993, Francis & Krishman, 1999, Reynolds & Francis, 2000). The variable of audit independence was positive but not statistically significant. This means the independence of the auditor is likely to increase audit quality. This position is consistent with Alim, Trisni and Lilik (2007), Windsor, Warring and Rasmussen (2009).

The result of the binary logit is not significantly different from the result of the binary probit. The McFadden R-squared value of the binary logit is estimated to be (0.81354) which means an explanatory power of (0.18 1354). The variable of board independence has a positive coefficient of (2.035709) which is considered very robust. The z-statistic is (2.662990) which is statistically significant. This means board independence has the likelihood of increasing the quality of audit in an organization that appears to be the same result reported in the binary probit presentation.

Similarly, audit tenure was found to be significant with a coefficient of (- 0.764762) though negative but significant with a probability value of (0.005). This means longer audit tenure may likely reduce the quality of audit. The result is consistent with the binary probit which also reported negative relationship between audit tenure and audit quality. The variable of audit firm size was found to be negative with a coefficient of (-0.060615) and a z-statistic of (-1.836965) which is considered not significant. As mentioned earlier, it means larger audit firms have the likelihood of delivering lesser quality audit. This is probably the result of divided attention as a result of the larger number of clients being attracted to the big audit firms. Audit independence was also found to be statistically insignificant in the binary logit with a t-value of (0.02390).

5. Summary of Findings, Conclusion and Recommendations

5.1. Summary of Findings

Based on the result the following summary of findings is provided:

1. Board independence has the likelihood of influencing audit quality.
2. Firm size has the likelihood to increase the quality of audit
3. Audit tenure has the likelihood to reduce the quality of audit
4. Audit firm size has likelihood to reduce audit quality
5. Auditor independence is positively associated with firms’ audit quality but not statistically significant
6. Conclusion

This study examines the relationship between firm characteristic and quality of audit. The study reveals that firm size has the likelihood to increase audit quality, audit tenure and audit firm size has the likelihood to reduce audit quality while audit independence increases audit quality.

Recommendations

Against the backdrop of the findings, we advanced the following recommendations
1. Firms in Nigeria should ensure that their boards are independent as this is likely to enhance audit quality.
2. The Nigerian Stock Exchange should relax its stringent listing requirements so that firms can be listed on the first tier since larger firms engage the services of professionals which by extension will positively affect the audit quality.
3. The three years professional requirement for an auditor in Nigeria should be backed up by law and enforced. Since audit tenure has a negative relationship with audit quality
4. Since audit firm size reduces the quality of audit, smaller audit firm should be encouraged as they are likely to carry out a more thorough audit assignment.

Suggestions for Further Studies

The present study spanned a seven-year period covering 2005 to 2012 and the selected samples included only listed food and beverage companies in Nigeria. It is therefore suggested that the study be extended to a longer period and more samples.

References


