

## **EFFECT OF AUDIT COMMITTEE CHARACTERISTICS ON FINANCIAL RESTATEMENTS IN NIGERIA**

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### **ABSTRACT**

This study examines the effect of audit committee attributes on the incidence of annual financial restatement. A sample of 96 firms (66 of which were restatement firms) was examined for the period 2008 to 2017 and controlled for firm size. Using a logit model regression analyses were carried out to test whether audit committee characteristics are effective in curbing the incidence of a financial restatement. The results indicate that audit committee independence is effective in curbing the likelihood of restatement. Similarly, the results also show that audit committee meeting frequency mitigates the likelihood of restatement. This study finds no cause to associate either audit committee size or audit committee financial expertise to restatement. The findings are robust for the average marginal effects. Notwithstanding, this study has some limitations. First, lack of variation in audit committee characteristics might affect the results. Second, the corporate governance data were hand-collected from the annual reports of listed firms downloaded from the website of the Nigerian Stock Exchange. Third, this research outcome is based on a sample of 960 firm-year observations between 2008 to 2017. Future studies will find subsequent years more comprehensive with financial data available in the Thomson Reuters Eikon database. The findings underlie the regulatory action that strengthens the oversight function of audit committees in financial reporting. It affirms the Financial Reporting Council (FRC) of Nigeria's position for a revised guideline to monitor reporting entities. A listed firm may leverage on its audit committee's independence and meeting frequency profiles to send a signal to investors about its governance quality. This study contributes to the burgeoning

literature on audit committee, by providing evidence from a West African reporting environment.

**Keywords:** Audit committee financial expertise, audit committee independence, audit committee meeting frequency, audit committee size, financial restatement.

## 1. INTRODUCTION

The prevalence of financial restatement in recent times continues to pose serious concern on financial reporting quality. A restatement usually constitutes a clear conceding of material misstatements or omissions in prior-year financial statements (Abbott, Parker, & Peters, 2004), which portends the possibility of litigation (Amoah & Tang, 2010), and the loss of public trust (Wan Mohammad, Wasiuzzaman, Morsali, & Zaini, 2018). Financial restatement concerns the firm, and the individuals entrusted with the responsibility to oversee its financial reporting process. Theory predicts that audit committee effectiveness or otherwise explains the likelihood of restatement. Within the Nigerian corporate environment, audit committee characteristics that affect financial reporting over the years needs investigation.

Motivated by the series of regulatory interventions through guidelines/regulations, issuance of codes of corporate governance, the recurring incidence of restatements, and the burgeoning literature on the issue, this study investigates whether audit committee attributes affect financial restatement of firms in Nigeria. Specifically, the recent Financial Reporting Council (FRC) of Nigeria revised guidelines/regulations for monitoring and inspection of reporting entities 2014 continue to generate debate among stakeholders (Deloitte, 2014). This regulation is perceived to have daunting provisions with a serious consequence on the professionals.

Historically, the Securities and Exchange Commission (SEC) of Nigeria re-issued the code of corporate governance for public entities in the year 2011. A revised and harmonized version was subsequently issued by the FRC in 2018, being an attempt to improve the effectiveness of the corporate governance mechanisms like the audit committees that oversee the financial reporting process. Nigeria offers a unique regulatory setting because the membership composition of statutory audit committees requires an equal share between the directors and the shareholders. At least one member of the committee is required to be a financial expert while the rest should be at least financially literate.

Studies that use restatements or fraudulent financial irregularities as a construct for managerial misrepresentation are viewed to have more validity in comparison to those that use earnings management proxies, such as abnormal accruals (Habib & Hossain, 2013), hence, a case to investigate financial restatement in Nigeria is in the affirmative. Although restatement does not take into account all aspects of misreporting, yet it is adjudged to represent a more objective ex-post measure (Ham, Lang, Seybert, & Wang, 2017). The likelihood that restatement will occur becomes higher as misreporting is detected.

There have been several cases of board reporting issues. For example, the FRC had suspended the registration status of four directors of Stanbic IBTC Holdings Plc, and ordered the withdrawal and restatement of their financial statements for 31st December 2013 and 2014 respectively, for misleading disclosures and other irregularities (FRC, 2015). The FRC imposed a fine of one billion Naira (₦1b equivalent to USD \$5.08m) on the firm for alleged misrepresentation of its financial statements. But the issue has been resolved through litigation. Further, the FRC (2014) guideline and regulation for inspection and monitoring of reporting entities had stipulated penalty for non-compliance to its corporate governance code, where withdrawal of financial statement leads to restatement, with sanctions ranging from five hundred million Naira (₦500m equivalent to USD \$2.5m) to five billion Naira (₦5b equivalent to USD \$25.4m). The sanction is for each year that requires such restatement.

Financial reporting decision processes and the reviews and corrections of prior financial statements vary across jurisdictions on dimensions of financial reporting oversight (Baber, Liang, & Zhu, 2012). Specifically, audit committees are saddled with the responsibility of overseeing the processes of preparing credible and quality financial reports. Some studies from Nigeria in the area of financial reporting have considered accruals and earning quality (Hassan, 2011; Kibiya, Che-Ahmad, & Amran, 2016), discretionary accruals (Abdulmalik & Ahmad, 2016), and disclosure index: qualitative characteristics (Kantudu & Samaila, 2015) as variables that affect the quality of financial reporting, but no evidence that considered accounting restatement. Restatements can potentially impact negatively on the overall investors' confidence which stems from certain corporate accounting practices, thus reflecting

weakness in corporate governance (<sup>1</sup>GAO, 2002). To the best of the authors' knowledge, no study has linked restatement with audit committee in the reporting environment.

The theoretical aspect of corporate activities is well documented in accounting research. Based on signaling theory, firm value may increase if the firm establishes the appropriate signal about its credentials. Signaling theory was originally developed to explain problems of information asymmetry (Morris, 1987). Firms compete against each other to secure resources from the capital market, and this appropriate signal offers additional exposure of the firm to that market. This reduces outsider uncertainty about the firm's prospects. Subsequently, it reduces the firm's capital costs because there is less uncertainty about firms that send a remarkable signal, hence less investment risk, and a lower required rate of return (Wolk, Tearney, & Dodd, 2001). This means the ability of a firm to raise capital is improved if the firm has a good reputation in its corporate activity (Holthausen & Leftwich, 1983). As for this study, audit committee characteristics may be used by a high-quality reporting firm to signal this reporting quality to the market (Felo, Krishnamurthy, & Solieri, 2003). On the other hand, some firms with material weakness might use their audit committees as signal to overcome their internal control weaknesses (Hoitash, Hoitash, & Bedard, 2009). Audit committee attributes – size, independence, financial expertise, meeting frequency, and the likes, have signaling effect on market participants. Yet, the mere existence of an audit committee does not sufficiently enhance the quality of financial reports (Bajra & Čadež, 2018).

The purpose of this study is to examine the effect of audit committee on the likelihood of financial restatement occurrence. The results indicate that audit committee independence as well as their meeting frequency are negative and significantly affect restatement. This study contributes to the burgeoning literature on restatement studies. The study has implication for policy makers and regulators.

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<sup>1</sup> GAO is the United States' government accountability office that helped the Congress investigate the trend in financial statements restatements in 2002.

This paper continues with the literature review and hypotheses development in Section 2. The research methodology is in Section 3. And the analysis of results in Section 4, while the last section, Section 5 concludes the paper.

## **2. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT**

### **Financial Restatement**

A financial restatement occurs when a firm either voluntarily or prompted by the auditor or regulators, revises public financial information that was previously reported, arising from whether non-fraudulent or fraudulent misstatement or other financial irregularities. According to Eilifsen and Messier Jr (2000), there exists four conditions upon which audited financial reports can be subsequently restated. First, where a material misstatement occurs because of some inherent risks, involving fraud or error. For example, erroneous application of GAAP or aggressive accounting practices by management. Second, the said material misstatement was neither prevented nor detected by the firm's internal controls. Third, failure of the external auditor to detect the misstatement, hence, the financial statements are issued. Fourth, the misstatement is afterward discovered and, if deemed material, requires the reissuance of corrected financial statements. The audit committee is saddled with the responsibility to oversee this financial reporting process.

### **The Role of the Audit Committee in Financial Reporting**

Audit committee, whether the board audit committee or statutory audit committee is a key component for effective corporate governance. It is saddled with the responsibility of overseeing the financial reporting process of the entity to ensure that managers prepare the report of their firm performance in an ethical manner (Kusnadi, Leong, Suwardy, & Wang, 2016). And that how effective this committee would be, is depended on the members' independence, financial expertise, size, meeting frequency and so on.

Extant literature mostly focused on directors on the audit committee, but in the Nigerian context, the committee comprises of shareholders' representative also. Little attention is given to shareholders' representative attributes. Kibiya et al. (2016) suggested that audit committee variables such as shareholders' representative financial expertise and frequency of meeting be examined, in addition to the committees' size and independence already included in their study. Cohen et al.

(2004) suggested that the spate of regulation could result in unintended consequences that have a negative impact on FRQ. For instance, where regulation emphasizes financial literacy for audit committee members, which drifts focus to financial reporting without proper regard to the entity's strategic and business risk.

Corporate governance code in Nigeria describes an audit committee as a statutory or board committee assigned with the responsibility of overseeing the financial reporting processes (FRC, 2016, 2018; SEC, 2003, 2011) The committee is also responsible for establishing an internal audit unit for a periodic review purpose and the appraisal of its internal control system. Hence, the committee's role enhances the functions of both the internal and external auditors. Several literatures have underscored the importance of audit committee in the financial reporting process (Abbott et al., 2004; Kibiya et al., 2016; Wan Mohammad *et al.*, 2018).

#### ***Audit committee independence***

Extant literature posits that audit committee independence can potentially mitigate the likelihood of financial restatement (Abbott et al., 2004; Wan Mohammad *et al.*, 2018). Their role strengthens the effectiveness and independence of the internal audit. In Nigeria, corporate governance laws require the inclusion of at least one independent director on the audit committee. The code specifically requires that there should be six members (three each drawn from the representatives of the directors and that of the shareholders). The aim of splitting the audit committee membership in two equal parts of representation is to ascertain the committee's independence (Kibiya et al., 2016).

Nevertheless, the mere presence of affiliated independent directors on audit committees may not be effective in the prevention of financial restatements. For example, Loon (2013) found that a sizeable number of independent directors on Malaysian corporate boards are either former politicians or retired civil servants. This indicates that independent directors on audit committees are hired for strategic connection purposes rather than to provide oversight function in the firm's financial reporting process (Wan Mohammad et al., 2018). Accordingly, the existence of independent directors on audit committees may not necessarily curb financial restatements. Based on the preceding argument, it is hypothesized that:

*H<sub>1</sub>: There is a negative association between audit committee independence and financial restatement.*

### ***Audit committee financial expertise***

Researchers suggest that weak audit committees provide a chance for financial restatement, but arguably if the oversight and monitoring function is not strict, it is more likely that restatement will occur (Beasley, 1996; Zhizhong, Juan, Yanzhi, & Wenli, 2011). Agrawal and Chadha (2005) document that the likelihood of restatement is lower for firms with audit committee financial expertise. The presence of a financial expert on the audit committee has a signaling effect that the quality of financial reports will be higher, hence restatement might not likely occur.

From the preceding argument, we assume that an audit committee without the presence of at least one financial expert, it is more likely that the firm would restate its annual financial reports. Further, restatement firms without a financial expert on their audit committee provide more evidence to suspect internal control weakness that would lead to restatement. Therefore, we expect a negative relationship between audit committee financial expertise and the likelihood of restatement. Based on the preceding argument, it is hypothesized that:

*H<sub>2</sub>: There is a negative association between audit committee financial expertise and financial restatement*

### ***Audit committee size***

Arguably, an increase in the size of audit committee is likely going to signal the public thereby instilling confidence in the firm's financial reports. The Nigerian code of corporate governance stipulates that there should be six members (three each drawn from the directors and the shareholders). But can size per se bring about the required effectiveness in financial reporting?

Debate is still on-going among scholars as to whether a larger or smaller audit committee is more effective in preventing financial restatement. Wan Mohammad et al. (2018) argued that the larger-sized audit committee is stronger and more likely to detect and prevent restatement than smaller ones. In their restatement model, however, Huang, Rose-Green, and Lee (2012) showed that the coefficient of audit committee size is not significant at the conventional level. And, Lin, Li, and Yang

(2006) showed evidence of a negative correlation between the size of audit committee and earnings restatement. Based on the preceding argument, it is hypothesized that:

*H<sub>3</sub>: There is a negative association between audit committee size and financial restatement.*

### ***Audit committee meeting***

A previous study suggests that corporate governance variables like audit committee meetings frequency be examined to see their effect on financial restatement (Shamsul, Yusof, & Mohamad, 2010). So, whether the frequency of meeting is systematically associated with restatement has been an empirical question (Abbott et al., 2004). In the <sup>2</sup>post-SOX annual restatement sample, the number of audit committee meetings and the likelihood of financial restatement is negative and significant, but not in the pre-SOX annual restatement sample (Abbott, Parker, & Presley, 2012). However, the frequency of audit committee meeting is significant and positively related to the likelihood of earnings restatement (Lin et al., 2006). Based on the preceding argument, it is hypothesized that:

*H<sub>4</sub>: There is a negative association between audit committee meeting frequency and financial restatement.*

## **3. RESEARCH METHODOLOGY**

### **Research Sample**

The Thomson Reuters Eikon database was used to obtain a sample of listed firms that have restated their annual financial statements from 2008 to 2017. The restatement firms were identified in the database through their financial statements (balance sheet, income statement, and cash flow) for a given year on which the letter “R” was inscribed, referring to “Restatement”. We excluded restatements arising from merger and acquisition, change in accounting policy, and dividend payment, and include only restatements due to fraud, error, irregularities, accounting misrepresentation, and intentional or unintentional misstatements (Wang & Wu,

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<sup>2</sup> The period after implementing the Sarbanes-Oxley (SOX) Act 2002 in the United States.



2011). Within the study period, 66 firms restated their financial reports for one year or the other. The restatement firms were largely drawn from the consumer goods industry and the services industry that got 15 firms each.

For the whole sample of 96 firms, data on audit committee were hand-collected from their annual reports. Only firms that were consistently listed during the period 2008 to 2017 made up the final sample. All other financial data were collected from the Thomson Reuters Eikon. All financial firms were excluded from the study because their industry has a separate code of corporate governance.

### **Model Specification**

This research model was estimated based on prior literature, as shown in Table 1. In this study, logistic regression analysis (consistent with previous literature, Abbott et al., 2004 and Wan Mohammad *et al.*, 2018) was used to test the hypotheses:

$$RES_{it} = \alpha_{0it} + \beta_1 ACIN_{it} + \beta_2 ACFE_{it} + \beta_3 ACSZE_{it} + \beta_4 ACMT_{it} + \beta_5 BSZE_{it} + \beta_6 BIND_{it} + \beta_7 BMT_{it} + \beta_8 DINTS_{it} + \beta_9 BIG4_{it} + \beta_{10} FSZE_{it} + \beta_{11} ROA_{it} + \beta_{12} LEV_{it} + \beta_{13} FAGE_{it} + \beta_{14} LAGE_{it} + \varepsilon_{it}$$

Where;

RES	Restatement
ACIN	Audit committee independence
ACFE	Audit committee financial expertise
ACSZE	Audit committee size
ACMT	Audit committee meeting
BSZE	Board size
BIND	Board independence
BMT	Board meeting
DINTS	Directors' interest in shareholding
BIG4	Big four audit firms
FSZE	Firm size

ROA            Return on asset

LEV            Leverage

FAGE           Firm age

LAGE           Listing age

Consistent with prior restatement studies involving audit committees (Abbott et al., 2004; Wan Mohammad *et al.*, 2018), audit committee independence, size, expertise, and meetings were included. We control for other factors associated with financial restatement, as indicated in prior studies. Firm size (FSZE): a large firm is expected to have a sound system of internal control, and to attract a higher quality auditing service (Huang et al., 2012). Hence, we predict a negative coefficient for FSZE. We also control for Board size (BSZE) and Board Independence (BIND). This study expects a negative association between BSZE and RES, since Alzoubi (2014) showed that larger boards are effective in constraining earnings management activity. Similarly, we expect a negative nexus between BIND and RES, as independent outside directors are better monitors (Abbott et al., 2004; Beasley, 1996). Other control variables include BMT, DINTS, BIG4, ROA, LEV, FAGE and LAGE.

**Table 1**

**Measurement of variables**

<b>Source</b>	<b>Variable</b>	<b>Operationalization</b>
<b>Dependent variable</b>		
Wan Mohammad et al. (2018); Cao et al. (2012)	RES	Restatement equals 1 if annual financial account were restated to correct prior misstatements, and 0 otherwise.
<b>Independent variables</b>		
Kibiya et al. (2016)	ACIN	Proportion of audit committee members who are independent directors
Kibiya et al. (2016)	ACFE	Proportion of audit committee member with financial expertise

Kusnadi et al. (2016)	ACSZE	Number of audit committee members
Kusnadi et al. (2016); Baxter and Cotter (2009)	ACMT	Number of audit committee meetings held in a year
<b>Control variables</b>		
Wan Mohammad et al. (2018); Huang et al. (2012)	BSZE	Log number of board members
Wan Mohammad et al. (2018); Huang et al. (2012)	BIND	The total number of independent non-executive directors scaled by board size
Amoah and Tang (2010)	BMT	The number of board meeting in a year
Abbott et al. (2004); Huang et al. (2012)	DINTS	The proportion of shares held by the board of directors
Kusnadi et al. (2016) Huang et al. (2012)	BIG4	Dummy variable equals 1 if firm is audited by a Big4 audit firm, and 0 otherwise.
Abdulmalik and Ahmad (2016)	FSZE	Log of total assets
Cao et al. (2012); Huang et al. (2012)	ROA	Proportion of net income to total assets at the beginning of the year
Wan Mohammad et al. (2018)	LEV	Proportion of total liabilities to total assets
Huang et al. (2012)	FAGE	Firm age in years
Abbott et al. (2004)	LAGE	Number of years a firm is publicly traded

*Note:* RES = restatement, ACIN = audit committee independence, ACFE = audit committee financial expertise, ACSZE = audit committee size, ACMT = audit committee meeting, BSZE = board size, BIND = board independence, BMT = board meeting, DINTS = directors' interests in shareholding, BIG4 = large four audit firm, FSZE = firm size, ROA = return on assets, LEV = leverage, FAGE = firm age, LAGE = listing age.

## 4. RESULTS AND DISCUSSION

### Descriptive Statistics

Table 2 shows the descriptive statistics for all the sampled firms. The mean average of restated firms is .37, which indicates that 37% of the sample are restatement firms. For the explanatory variables, the average audit committee independence is 16%, and financial expertise on the committee is quite high – 74%. These averages differ with Kibiya et al. (2016) a Nigerian study that shows an average of 99% for independence, and 6% for financial expertise. Recent years and the larger sample period in this study might account for such variation. Nevertheless, an independent audit committee with a higher proportion of financial expertise is associated with a higher quality of financial reporting (Huang et al., 2012). The average size of the audit committee is 5 members, while the number of their meetings is 4 on the average. Corporate governance laws in Nigeria requires an audit committee to meet at least quarterly within a year. Over half of the firms (i.e. 54%) were audited by Big4 firms. Hence, the BIG4 is a signal that most of the firms will present a higher quality financial reporting (Felo et al., 2003).

**Table 2**  
**Descriptive Statistics**

<b>Variables</b>	<b>N</b>	<b>Mean</b>	<b>Std.</b>	<b>Min</b>	<b>Max</b>
RES	960	.37	.48	0	1
ACIN	960	.16	.09	0	.5
ACFE	960	.74	.43	0	1
ACSZE	960	5.29	.77	4	6
ACMT	960	3.50	.91	2	6
BSZE	960	8.63	2.25	4	15
BIND	960	.15	.05	.06	.33
BMT	960	4.62	1.36	2	9
DINTS	960	.20	.22	.00	.75
BIG4	960	.54	.49	0	1
FSZE	960	9.24	1.81	4.48	14.24
ROA	960	.14	.23	-	.79
LEV	960	.52	.20	.02	1.23
FAGE	960	37.9	19.3	2	94
LAGE	960	20	13.2	1	60

Source: Authors' analysis (2020). All variables are as defined in Table 1.

## Correlation Matrix

Table 3 reports the Spearman correlations for all the variables. As expected, the results indicate that RES (restatements) is significant and negatively correlated with ACIN (audit committee independence, -7%). This shows that firms having independent directors on their audit committee are effective in curbing the incidence of a financial restatement. Similarly, the results show a negative insignificant relationship between ACMT (audit committee meeting) and RES. Further, the coefficient ACFE (audit committee financial expertise) is positive but not significant. However, ACSZE (audit committee size) indicates a significant positive coefficient. It means an increase of additional member on the audit committee will cause a corresponding increase in the likelihood of restatement by 7%. The control variables BIND and DINTS are both significant and negatively correlated with RES. This could indicate that both the independent directors and the directors that have shareholding are less likely to become manipulative in their financials. Contrariwise, the positive significance of FSZE shows the likelihood of a restatement by larger firms.

**Table 3**  
**Correlation matrix**

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1 RES	1														
2 ACIN	-0.07*	1													
3 ACFE	0.01	0.14*	1												
4 ACSZE	0.07*	-0.11*	0.09*	1											
5 ACMT	-0.01	0.11*	0.17*	0.41*	1										
6 BSZE	0.06	0.02	0.09*	0.27*	0.20*	1									
7 BIND	-0.07*	0.18*	0.08*	-0.01	0.07*	-0.33*	1								
8 BMT	0.02	-0.02	0.12*	0.31*	0.34*	0.18*	0.08	1							
9 DINTS	-0.08*	-0.06*	-0.12*	-0.13*	-0.14*	-0.10*	-0.04	-0.16*	1						
1 BIG4	0.06	0.11*	0.10*	0.09*	0.18*	0.08*	0.08	0.28*	-0.26*	1					
1 FSZE	0.12*	0.04	0.16*	0.40*	0.30*	0.38*	0.08	0.33*	-0.25*	0.40	1				
1 ROA	-0.02	-0.00	0.08*	0.01	0.06*	0.03	0.07	0.16*	-0.11*	0.19	0.12	1			
1 LEV	0.00	0.01	0.10*	0.10*	0.06	-0.01	0.04	-0.04	-0.09*	0.17	0.19	-0.09*	1		
1 FAGE	0.01	-0.07*	0.11*	0.24*	0.20*	-0.01	0.04	0.12*	-0.33*	0.16	0.09	0.10*	0.29	1	
1 LAGE	-0.02	-0.01	0.06	0.22*	0.22*	0.14*	-0.02	0.09*	-0.31*	0.14	0.01	0.13*	0.23	0.73	1

Source: Authors' analysis

Note: Table 3 reports Spearman correlations of the variables for the sample of 960 firm-year observations from 2008 to 2017. All variables are as defined on Table 1. The asterisk \* represents significance at 5% or lower.

### **Logistic Regression Results**

Table 4 below reports the regression results of the main model in this study. Overall, the model is significant ( $p = 0.000$ ) which indicates that the estimation provides a better data fit than the null model. The low Pseudo R-squared of 4% is rather consistent with prior restatement studies of 4.8% (Wahid, 2019), and 6.8% (Huang et al., 2012). Consistent with expectation, *ACIN* (audit committee independence),

and *ACMT* (audit committee meeting frequency) is significant and negatively associated with restatement at 5% levels. The result of audit committee independence is similar to the finding in a Nigerian study (Kibiya et al., 2016). The significant coefficients indicate that firms with independent audit committees that meet frequently are less likely to have financial restatement. These results, therefore, support the first and the fourth hypotheses respectively.

Contrary to expectation, *ACSZE* (audit committee size) is not significant. The result shows that audit committee size does not matter in the likelihood of restatement. This effect fails to support the  $H_3$  hypothesis. The result of the *ACFE* (audit committee's financial expertise) is insignificant, hence  $H_2$  is also not supported. It means the financial expertise of audit committee members does not necessarily help in curbing the likelihood of a financial restatement. A possible explanation to this is that, since one-half of the financial experts on audit committees in Nigeria are drawn from the shareholders' group, these groups of experts might be busy as CEOs or CFOs of other firms.

A plausible explanation for the lack of consistency between this result and that of other jurisdictions may be due to differences in regulatory environments. Audit committee effectiveness indicates a firm's overall corporate governance quality, which apparently differs between countries (Habbash, Sindezingue, & Salama, 2013). Accordingly, other restatement literature (e.g., Abbott et al., 2004, 2012; Huang et al., 2012; Wan Mohammad et al., 2018) have employed a variation of governance and firm-related control variables, which might affect the relationship between the predictors and the dependent variable.

**Table 4**  
**Regression results**

RES	Predicted Sign	Coef.	Std. Err.	P-value	Average marginal effect	Decision
ACIN	Negative	-1.44	.758	0.057*	0.057*	Supported
ACFE	Negative	.041	.164	0.801	0.801	Not supported
ACSZE	Negative	.157	.108	0.146	0.146	Not supported
ACMT	Negative	-.149	.088	0.090*	0.090*	Supported
BSZE		-.017	.038	0.643	0.643	
BIND		-2.96	1.37	0.031**	0.031**	
BMT		-.033	.057	0.555	0.555	
DINTS		-.724	.343	0.035*	0.035*	
BIG4		.142	.160	0.374	0.374	
FSZE		.152	.052	0.004***	0.004***	
ROA		-.396	.315	0.210	0.210	
LEV		-.335	.364	0.357	0.357	
FAGE		-.000	.005	0.990	0.990	
LAGE		-.004	.008	0.574	0.574	
_cons		-.865	.626	0.167	0.167	
Pseudo R <sup>2</sup>				4%		
Model Chi-squared				40.58		
p-value				0.000***		
Observations				960		
Pearson goodness of fit				0.3752		

Note: Standard errors are \*\*\* p<0.01, \*\* p<0.05, \* p<0.1, one-tailed direction. All variables are as defined on Table 1.

### Additional Analyses

To check for robustness of the results, and the concern for endogeneity problem, some additional analyses were carried out. Agrawal and Chadha (2005) document that “large firms are more likely to restate their earnings”. On this basis the sample was partitioned into two: large firms and small firms, using the mean firm size (FSZE). Then separate regression analyses were carried out as presented in Table 5 and Table 6 respectively. Table 5 reports the regression results for the larger firms. The result on audit committee independence (ACIN)  $p = 0.034$  and that of audit committee meeting (ACMT)  $p = 0.065$  are similar to the findings of the main regression. The rest are insignificant.



**Table 5**  
**Regression results for larger firms**

RES	Coef.	Std. Err.	P-value
ACIN	-2.22	1.04	0.034**
ACFE	.108	.257	0.672
ACSZE	.238	.182	0.191
ACMT	-.249	.135	0.065*
BSZE	.044	.052	0.400
BIND	-3.13	1.72	0.070*
BMT	-.087	.086	0.314
DINTS	-1.07	.534	0.045**
BIG4	.115	.299	0.699
FSZE	.094	.122	0.441
ROA	-.254	.517	0.623
LEV	-.198	.546	0.716
FAGE	3.23	.007	1.000
LAGE	-.005	.012	0.669
_cons	-.449	1.30	0.730
Pseudo R <sup>2</sup>			4%
Observations			455

Note: Standard errors are \*\*\* p<0.01, \*\* p<0.05, \* p<0.1, one-tailed direction. All variables are as defined on Table 1.

Table 6 reports the regression results for the smaller firms. The variables of interest are not significant. This indicates that audit committees of smaller firms are not effective in curbing the likelihood of financial restatement.

**Table 6**  
**Regression results for smaller firms**

RES	Coef.	Std. Err.	P-value
ACIN	-.264	1.26	0.834
ACFE	-.070	.228	0.759
ACSZE	.204	.157	0.195
ACMT	-.069	.126	0.583
BSZE	-.165	.068	0.015***
BIND	-4.69	2.75	0.088*
BMT	.036	.084	0.664
DINTS	-.395	.496	0.426
BIG4	.158	.216	0.463
FSZE	-.029	.106	0.783
ROA	-.814	.415	0.050**
LEV	-.290	.528	0.583
FAGE	-.009	.009	0.309
LAGE	.003	.012	0.756
_cons	1.12	1.31	0.392
Pseudo R <sup>2</sup>			2%
Observations			505

*Note:* Standard errors are \*\*\*  $p < 0.01$ , \*\*  $p < 0.05$ , \*  $p < 0.1$ , one-tailed direction. All variables are as defined on Table 1.

Overall, firm size seems to matter. These additional analyses lend support to that. Interestingly, the results also indicate that larger firms are less effective even with their ability to specifically hire better financial expertise on their audit committees. This affirms the notion that large firms eventually become manipulative in their financials, with their audit mechanisms failing to curb restatement (Zhizhong et al., 2011).

## 5. CONCLUSION

In this study, we examine whether audit committee attributes are associated with the likelihood of financial restatement occurrence. We show that firms with strong audit committees are effective in curbing the possibility of such incidence. In the main regression specifically, we find that firms with higher proportion of independent directors on their audit committee are less likely to restate their financial statements. In our additional analyses, this finding is also true for larger firms, where audit committee independence plays a significant role. This result indicates that the

breadth of knowledge and independence of opinion is higher with additional independent directors on the committee. Similarly, audit committee meeting frequency is negatively associated with restatement, which suggests that the audit committees take proactive measures rather than react to an escalating problem, in overseeing the reporting process. We find no significance for audit committee size, and their financial expertise. To the best of our knowledge, we did not come across any research that associates audit committee attributes to financial restatement in Nigeria.

Based on signaling theory, audit committee attributes – size, independence, financial expertise, meeting frequency, and the likes, have signaling effects on market participants. It is established that high-quality reporting firms use their audit committees to signal this reporting quality to the market (Felo et al., 2003). Likewise, firms with material weakness use their audit committees as a signal to overcome internal control weaknesses (Hoitash et al., 2009). In this study, therefore, our findings show that firms with higher proportion of independent directors serve as signal to market participants that the directors will be effective in curbing the likelihood of financial restatement.

The findings in this study provide useful insights for regulatory agencies to improve on the current provisions on audit committee membership as a governance mechanism. The regulators might consider a uniform standard of audit committee size for all firms and may weigh into the fact that smaller firms lag in ensuring financial expertise on their audit committees. Our results are robust for the average marginal effects. Our study adds to the burgeoning literature on the audit committee as the overseer of financial reporting process.

Notwithstanding, our study has some limitations. First, lack of variation in audit committee attributes might affect our results. Second, our corporate governance data were hand-collected from the annual reports of listed firms downloaded from the website of the Nigerian Stock Exchange. Third, our evidence is based on a sample of 960 firm-year observations between 2008 to 2017. The later years are more comprehensive with financial data available in the Thomson Reuters Eikon database. Future research could add to our sample, as detail corporate information is becoming more available in recent years. Other salient audit committee attributes such as;

Chairman's financial expertise, female gender, tenure, and institutional ownership are areas that could be explored.

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