Audit Firm Characteristics and Financial Reporting Quality of Deposit Money Banks in Nigeria: The Moderating Role of Audit Committee

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ABSTRACT

This paper investigates whether selected characteristics of external audi t firms are associated with financial reporting quality in Nigerian deposit money banks and, more importantly, whether audit committee oversight changes those associations. The study responds to continuing questions about the reliability of bank financial statements and the inconsistent evidence reported for auditor tenure, audit remuneration and audit-firm size. An ex-post facto design was used, with secondary information obtained from the published annual reports of the sampled banks for 2014–2024. The final balanced panel contains 110 bank-year observations. Descriptive statistics, Pearson correlation and panel regression procedures were applied, while the Hausman test guided the choice of estimator for the principal model. The results indicate that audit firm tenure is positively related to financial reporting quality, but the relationship is not statistically significant ($\beta = 0.108398$; $p = 0.0984$). Audit fees also have a positive but insignificant direct coefficient ($\beta = 0.166818$; $p = 0.1911$), whereas audit firm size has a significant negative coefficient ($\beta = -0.716003$; $p = 0.0038$). Once audit committee interactions are introduced, the tenure interaction remains insignificant ($\beta = -0.116468$; $p = 0.2418$). By contrast, the audit-fee interaction is positive and significant ($\beta = 5.105045$; $p = 0.0132$), while the audit-firm-size interaction is negative and significant ($\beta = -0.482384$; $p = 0.0136$). The moderated specification explains 89.28% of the observed variation in reporting quality. The evidence therefore suggests that audit inputs do not operate independently of governance arrangements; audit committee oversight can alter the reporting consequences of audit fees and audit-firm size.

Keywords: audit firm characteristics; audit tenure; audit fees; audit firm size; audit committee; financial reporting quality; deposit money banks; Nigeria.

INTRODUCTION

Financial statements are a major source of information for investors, lenders, regulators and other users who evaluate the performance and financial position of deposit money banks. This role is especially important in banking because banks intermediate substantial amounts of funds entrusted to them by depositors and other stakeholders. Weak or unreliable reporting can consequently affect not only individual investment decisions but also confidence in the wider financial system. Hasan et al. (2022) emphasised the importance of governance arrangements in supporting credible financial reporting.

External audit is one of the institutional arrangements intended to improve confidence in reported accounting information. Through independent examination and assurance, auditors provide users with an additional basis for relying on financial statements. Nevertheless, audit outcomes may differ according to the circumstances of an engagement and the attributes of the audit provider. Three characteristics have received particular attention in the literature: the length of the auditor-client relationship, the amount paid for audit services, and the size of the audit firm.

Audit tenure presents competing possibilities. A continuing auditor can accumulate detailed knowledge of a bank's operations, information systems and control environment, which may improve the efficiency and depth of audit work. At the same time, a prolonged relationship can create familiarity concerns and weaken professional scepticism if independence is not adequately protected (Ilaboya & Ohiokha, 2014). Audit fees likewise have more than one possible interpretation. A higher fee may reflect a complex or risky engagement and may permit the auditor to commit more personnel and effort; however, a larger fee does not by itself establish that the resulting audit is more effective. Ayoola (2022) provides evidence that the relationship between audit remuneration and audit quality can depend on other features of the engagement.

Audit-firm size is commonly considered in terms of the resources, specialist knowledge, quality-control arrangements and reputational incentives available to larger firms. The classic argument is that large firms have stronger incentives to protect their reputation and therefore have greater capacity to deliver high-quality audits (DeAngelo, 1981; Simunic, 1980). Empirical findings, however, have not been uniform. Khalil (2022), for example, found no significant difference in financial reporting quality associated with auditor choice in the banking setting examined. These mixed outcomes indicate that auditor characteristics may not be adequately understood when examined without reference to the governance arrangements surrounding the audit.

The audit committee is particularly relevant in this regard. It is responsible for important aspects of financial reporting oversight, internal control review and interaction with the external auditor. An effective committee can question management's accounting judgements, examine audit findings and press for corrective action. Badolato et al. (2014) and Kabiru and Usman (2021) provide evidence that audit committee attributes can be associated with reporting outcomes. Yayangida et al. (2023) further show that audit committee independence can condition the association between audit-firm size and financial reporting quality.

Although the literature has considered tenure, audit fees and audit-firm size as possible determinants of audit or reporting quality, fewer studies have directly examined whether audit committee oversight changes these relationships among Nigerian deposit money banks. The distinction is important. A large audit firm, a lengthy audit relationship or a substantial audit fee may have limited reporting benefits if the engagement is poorly monitored. Conversely, strong oversight may allow useful audit resources to be converted more effectively into credible financial information.

This study therefore evaluates audit firm tenure, audit fees and audit firm size as explanatory variables for financial reporting quality and tests audit committee as a moderator of each relationship. The analysis is designed to address the mixed evidence in prior studies and to determine whether the governance context surrounding external audit helps explain the differences in reported outcomes. The study's objectives are to assess the effects of audit tenure, audit fees and audit firm size on financial reporting quality and to determine whether audit committee significantly changes each of those effects.

The study is relevant to bank boards, audit committees, regulators and other users of financial statements because it provides evidence on whether selecting an auditor on the basis of firm size, maintaining an auditor for a particular period, or paying a higher fee is sufficient to improve reporting outcomes. The remainder of the paper covers the literature and theories, methodology, empirical results and discussion, and finally the conclusion, recommendations, contribution and limitations.

LITERATURE REVIEW

This section clarifies the principal concepts used in the study, reviews the theories that explain the expected relationships and considers relevant empirical evidence. Particular attention is given to the possibility that audit committee oversight changes the effects of audit-firm characteristics.

Financial Reporting Quality

Financial reporting quality concerns the extent to which reported accounting information faithfully reflects an entity's underlying economic activities and remains useful to users making decisions. Reporting that is transparent, comparable and sufficiently representative of economic reality reduces information problems and supports more informed allocation of resources. In this study, financial reporting quality is operationalised through total accruals, calculated as net income less cash flow from operations, following the measurement reported in Onatuyeh et al. (2024).

Audit Firm Characteristics

Audit firm characteristics are attributes of the external audit provider that may shape the resources, independence, expertise or monitoring capacity brought to an engagement. The present study concentrates on audit tenure, audit fees and audit-firm size.

Audit Firm Tenure

Audit tenure denotes the continuing period over which an auditor serves the same client. A longer relationship may improve the auditor's familiarity with the client's transactions, controls and reporting processes, potentially reducing the time required to understand the business. The opposite concern is that excessive familiarity can compromise scepticism or independence. Consequently, tenure does not have an unambiguous theoretical prediction, and previous evidence has reported different directions (Ilaboya & Ohiokha, 2014; Yayangida et al., 2023).

Audit Fees

Audit fees are the amounts paid to external auditors for professional audit services. The fee may capture the scale, complexity and risk of an engagement as well as the professional resources devoted to it. Where a higher fee enables more extensive procedures or more experienced personnel, reporting quality may benefit (Ayoola, 2022). The relationship is nevertheless conditional: payment alone cannot ensure an effective audit where oversight and other governance arrangements are weak.

Audit Firm Size

The study represents audit-firm size with a Big Four dummy variable, coded 1 when a bank is audited by a Big Four firm and 0 otherwise. Larger audit practices are commonly expected to possess broader specialist resources and more formal quality-control systems. Their reputational exposure may also encourage stronger audit performance. The negative coefficient obtained in this study, however, demonstrates that firm size should not automatically be interpreted as synonymous with reporting quality.

Audit Committee as a Moderating Mechanism

The audit committee provides an internal governance layer around financial reporting and external audit activities. Its effectiveness may determine whether the potential benefits of an auditor's experience, resources or effort are realised. Accordingly, this study treats audit committee as a moderating variable rather than merely another direct predictor. The moderation test asks whether the strength or direction of each audit-firm characteristic changes as audit committee oversight changes.

Audit Committee Size

This is measured as the number of members serving on the audit committee, as disclosed in the annual reports of the sampled banks. The variable ranges from 3 to 7 members, with a mean of 5.327 members. It is theoretically relevant because committee membership determines the number of individuals available to perform financial reporting oversight, interact with external auditors and scrutinise management's accounting decisions. A committee with sufficient membership may provide broader expertise and monitoring capacity. However, larger committees may also face coordination difficulties and weaker individual accountability.

Theoretical Framework

Three perspectives support the analysis: Auditor Theory of Inspired Confidence, Expectations Gap Theory and Positive Accounting Theory. The first provides the principal theoretical anchor, while the latter two supply complementary explanations for stakeholder expectations and managerial reporting incentives.

Auditor Theory of Inspired Confidence

Limperg's Auditor Theory of Inspired Confidence places the social function of auditing in the confidence users require when they rely on information prepared by management. Users cannot directly observe every transaction or managerial decision, so an independent and competent auditor is expected to provide assurance that makes published information more credible (Limperg, 1932).

The theory fits this study because the characteristics of an audit firm can affect the assurance process. Client knowledge accumulated through tenure, resources financed through audit fees, and the technical capacity associated with firm size may all shape audit work. None, however, guarantees credible reporting in isolation. The audit committee may strengthen the process by challenging management, supervising the auditor and ensuring that weaknesses identified during the engagement are acted upon. The theory therefore provides a basis for expecting the governance setting to matter alongside auditor characteristics.

Expectations Gap Theory

Expectations Gap Theory concerns the difference between what users believe auditors should accomplish and what an audit is designed and reasonably able to deliver. Porter (1993) describes the audit expectation-performance gap in terms of the distance between reasonable expectations and actual audit performance. Users may expect auditors to uncover every instance of fraud or eliminate all errors, even though an audit provides reasonable rather than absolute assurance.

This perspective is relevant because stakeholders may attach too much significance to visible auditor characteristics. A Big Four appointment, a high audit fee or a lengthy client relationship may be interpreted as proof of superior reporting quality. The present results caution against that assumption: tenure and audit fees are not significant in the direct model, while firm size has a significant negative coefficient. The theory therefore helps explain why the presence or apparent strength of an audit arrangement should not be confused with its actual reporting consequences.

Positive Accounting Theory

Positive Accounting Theory explains accounting choices by considering the incentives managers face and the economic consequences of alternative reporting decisions (Watts & Zimmerman, 1986). Compensation arrangements, lending relationships, political considerations and capital-market pressures can create incentives that affect the way managers select and apply accounting policies.

Where such incentives encourage opportunistic reporting, external audit and governance can operate as monitoring mechanisms. Audit-firm characteristics may influence the strength of external monitoring, while an effective audit committee can add another layer of scrutiny over management and the auditor. This provides a useful explanation for why the same audit input may have different consequences across firms depending on governance quality.

The study is anchored principally on Auditor Theory of Inspired Confidence because the theory most directly addresses the auditor's assurance role and the confidence users place in audited information. Expectations Gap Theory and Positive Accounting Theory are retained as complementary perspectives for interpreting stakeholder expectations and managerial incentives.

Empirical Review and Research Gap

Existing empirical evidence does not point to a single pattern for audit-firm characteristics and financial reporting quality. Ilaboya and Ohiokha (2014) reported a negative association between audit tenure and audit quality in Nigeria, whereas Yayangida et al. (2023) found no significant direct tenure effect in Nigerian listed non-financial services firms. Their work also indicates that audit committee independence can affect the association involving audit-firm size.

Evidence concerning audit fees is similarly unsettled. Ayoola (2022), using Nigerian deposit money banks, reported that audit seasonality mediates the association between audit fees and audit quality. Kabiru and Usman (2021) found that audit committee characteristics are relevant to financial reporting quality in Nigerian deposit money banks. These findings imply that remuneration and governance should not necessarily be interpreted separately.

Audit-firm size also generates competing expectations. DeAngelo (1981) associates larger audit firms with stronger incentives and resources for high-quality auditing, while Yayangida et al. (2023) demonstrate the importance of audit committee oversight when considering size. Khalil (2022) reported no significant reporting-quality difference between Big Four and non-Big Four auditors in the Pakistani banking sector.

The gap addressed here is therefore twofold: the study concentrates on Nigerian deposit money banks and simultaneously tests audit committee as a moderator of tenure, audit fees and audit-firm size. Rather than assuming that an auditor characteristic has the same effect in every governance environment, the analysis examines whether internal oversight changes the relationship.

METHODOLOGY

Research Design and Data

An ex-post facto design was adopted because the study relies on historical observations that existed before the analysis and were not subject to experimental manipulation. The population consists of listed deposit money banks on the Nigerian Exchange. Purposive selection was applied to banks that maintained continuous operations and supplied the information required for the study period. Ten banks were retained, giving a balanced panel of 110 firm-year observations covering 2014–2024. This specification follows the econometric output reported in the underlying research work.

Measurement of Variables

Variable	Code	Measurement	Expected direction
Financial reporting quality	FRQ	Total accruals = Net income − Cash flow from operations	Dependent
Audit tenure	AUDT	Auditor-client relationship as operationalised in the study	±
Audit fees	AUDF	Natural logarithm of annual auditor remuneration	+
Audit firm size	AUDFZ	1 = Big Four auditor; 0 = otherwise	+
Audit committee	AUDCOMT	Audit committee governance measure used in the panel dataset	+

Source: Author’s Compilation (2026)

Model Specification

The direct-effects model is stated as:

$$FRQ_{it} = \beta_0 + \beta_1 AUDT_{it} + \beta_2 AUDF_{it} + \beta_3 AUDFZ_{it} + \varepsilon_{it}$$

The moderation model is stated as:

$$FRQ_{it} = \beta_0 + \beta_1 AUDT_{it} + \beta_2 AUDF_{it} + \beta_3 AUDFZ_{it} + \beta_4 AUDCMT_{it} + \beta_5 (AUDT \times AUDCMT)_{it} + \beta_6 (AUDF \times AUDCMT)_{it} + \beta_7 (AUDFZ \times AUDCMT)_{it} + \varepsilon_{it}$$

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FRQ represents financial reporting quality; AUDT denotes audit tenure; AUDF is audit fees; AUDFZ is audit-firm size; AUDCMT is the audit committee measure; and ε_{it} is the idiosyncratic error term.

Estimation Procedure

The analysis began with descriptive statistics and Pearson correlations to establish the distribution of the variables and their pairwise associations. Pooled, fixed-effects and random-effects panel estimators were considered. The Hausman test was subsequently used to select between the fixed- and random-effects approaches. The reported statistic for the principal model is $\chi^2(3) = 12.845893$ with $p = 0.0050$. The null supporting random effects was therefore rejected and the fixed-effects specification was retained. Diagnostic and post-estimation checks were also performed.

RESULTS AND DISCUSSION

Descriptive Statistics

Variable	Mean	Median	Maximum	Minimum	Std. Dev.
FRQ	0.836473	0.988178	2.501396	−0.819271	0.837990
AUDT	0.654545	1.000000	1.000000	0.000000	0.477693
AUDF	10.59485	10.54534	12.10282	9.903488	0.359224
AUDFZ	0.981818	1.000000	1.000000	0.000000	0.134220
AUDCOMT	5.327273	5.000000	7.000000	3.000000	0.743277

Source: Author’s Compilation (2026)

The sample records an average FRQ of 0.8365, with a standard deviation of 0.8380, indicating noticeable dispersion across bank-year observations. Mean audit fees are 10.5949. The audit-firm-size mean of 0.9818 shows that Big Four auditors dominate the sample, leaving relatively little variation for this indicator. Audit committee size/measure records a mean of 5.3273.

Correlation Analysis

Variable	FRQ	AUDT	AUDF	AUDFZ	AUDCOMT
FRQ	1.0000	0.1666	0.5540	−0.0360	0.0600
AUDT	0.1666	1.0000	−0.0137	−0.0989	0.0113
AUDF	0.5540	−0.0137	1.0000	0.0606	−0.0455
AUDFZ	−0.0360	−0.0989	0.0606	1.0000	0.0602
AUDCOMT	0.0600	0.0113	−0.0455	0.0602	1.0000

Source: Author’s Compilation (2026)

FRQ has a weak positive association with audit tenure ($r = 0.1666$) and a moderate positive association with audit fees ($r = 0.5540$). Its correlation with audit-firm size is very small and negative ($r = −0.0360$). The explanatory variables also display relatively small pairwise correlations, providing no preliminary indication of severe multicollinearity.

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Fixed-Effects Regression Results

Variable	Coefficient	t-statistic	p-value	Decision at 5%
AUDT	0.108398	1.668785	0.0984	Not significant
AUDF	0.166818	1.316586	0.1911	Not significant
AUDFZ	−0.716003	−2.969907	0.0038	Significant
Constant	−0.298903	−0.220464	0.8260	Not significant

$R^2 = 0.880157$; Adjusted $R^2 = 0.865331$; F-statistic = 59.36592, p = 0.0000. Source: Author's Compilation (2026).

The coefficient for audit tenure is positive, but its p-value of 0.0984 exceeds the five-percent significance threshold. The direction suggests that longer auditor-client relationships are associated with better reporting quality in the sample, but the evidence is not strong enough to establish an independent effect. The result is compatible with Hasan et al. (2022), although it differs from the negative association reported by Ilaboya and Ohiokha (2014) and the findings of Yayangida et al. (2023).

Audit fees also carry a positive coefficient without statistical significance. Thus, the additional amount paid for audit services does not, on its own, provide sufficient evidence of improved reporting quality. This outcome indicates that the benefits of audit expenditure may depend on how the engagement is managed and supervised.

Audit-firm size is statistically significant and negative. This result runs against the simple assumption that affiliation with a Big Four firm necessarily produces superior reporting quality. In the present sample, the size indicator should therefore be interpreted cautiously; firm-level reputation and resources do not substitute automatically for the quality of the actual engagement or the governance of the client.

Moderating Effect of Audit Committee

Term	Coefficient	t-statistic	p-value	Interpretation
AUDT	0.718844	1.358308	0.1776	Positive, insignificant
AUDT × AUDCOMT	−0.116468	−1.177993	0.2418	No significant moderation
AUDF	2.767833	2.659559	0.0092	Positive, significant
AUDF × AUDCOMT	5.105045	2.525118	0.0132	Positive significant moderation
AUDFZ	−26.16052	−2.588559	0.0112	Negative significant
AUDFZ × AUDCOMT	−0.482384	−2.514111	0.0136	Negative significant moderation

$R^2 = 0.892790$; Adjusted $R^2 = 0.875682$; F-statistic = 52.18556, p = 0.0000. Source: Author's Compilation (2026).

The interaction results provide the main evidence for the study's moderating argument. The audit-tenure interaction is negative but insignificant ($\beta = -0.116468$; $p = 0.2418$). Consequently, the data do not show that audit committee oversight materially changes the tenure–FRQ relationship.

A different pattern emerges for audit fees. The fee variable is positive and significant in the moderated model, and its interaction with audit committee is also positive and significant ($\beta = 5.105045$; $p = 0.0132$). This indicates

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that stronger audit committee oversight is associated with a larger positive contribution of audit fees to reporting quality. A plausible interpretation is that additional audit resources are more likely to yield reporting benefits when an effective committee monitors their use and follows up on audit findings.

The audit-firm-size interaction is significant and negative ($\beta = -0.482384$; $p = 0.0136$). Audit committee oversight therefore changes the relationship between firm size and reporting quality, but the change is in a negative direction. The result cautions against using Big Four status as a stand-alone indicator of reporting quality and suggests that closer governance scrutiny may expose weaknesses that a simple size classification does not capture.

Introducing the interaction terms raises R^2 from 0.880157 to 0.892790. The increase, alongside the significant overall F-statistic, indicates that the governance-conditioned model accounts for more of the variation in FRQ than the direct-effects specification.

DISCUSSION IN RELATION TO THEORY

The findings are compatible with Auditor Theory of Inspired Confidence in the sense that audit characteristics can matter for the credibility of financial reporting, but their effects are conditional rather than automatic. The positive and significant audit-fee interaction suggests that audit resources can have greater value when an effective internal governance mechanism oversees the engagement.

The results also illustrate the logic of Expectations Gap Theory. Users may regard a long auditor relationship or Big Four appointment as sufficient evidence of superior reporting, yet the direct estimates do not support such a blanket conclusion. The evidence reinforces the need to distinguish between having an external audit and having an audit process that produces the level of assurance stakeholders expect.

Positive Accounting Theory offers another explanation. Management may face incentives that affect reported outcomes, making monitoring important. External auditors provide one monitoring layer, while audit committees provide another. The significant interaction for audit fees suggests that governance can influence whether audit inputs are converted into improved reporting outcomes.

CONCLUSION AND IMPLICATIONS

The evidence from Nigerian deposit money banks indicates that the three audit-firm characteristics considered in this study do not have uniform effects on financial reporting quality. Audit tenure and audit fees are positive but statistically insignificant in the direct model, whereas audit-firm size has a significant negative association with FRQ. The moderation analysis adds an important qualification: audit committee oversight does not significantly change the tenure relationship, but it significantly strengthens the positive audit-fee relationship and significantly changes the audit-firm-size relationship in a negative direction.

For bank management and boards, the findings imply that auditor selection should not be based mainly on the size or brand of an audit practice. Attention should also be directed to engagement quality, auditor competence, professional effort and the extent to which the audit committee challenges and monitors the external auditor. Audit expenditure should correspond to the complexity and risk of the engagement, with governance arrangements ensuring that the resources purchased through the fee are effectively deployed.

For regulators, the results suggest that audit oversight should emphasise actual engagement quality, independence, professional performance and audit committee effectiveness instead of treating Big Four status as a sufficient proxy for audit quality.

Policy Implications and Recommendations

The findings have implications for bank boards, audit committees, regulators and external auditors.

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Strengthening Audit Committee Financial Expertise

Banks should ensure that audit committees collectively possess adequate accounting, auditing, risk-management and financial-reporting expertise. Membership should not be determined solely by seniority or board position. At least a meaningful proportion of members should possess demonstrable financial literacy and relevant professional experience.

Strengthening Audit Committee Independence

Banks should maintain sufficient independence between audit committee members, management and the external auditor. Independent members should be empowered to question management's accounting judgements and challenge the external auditor without undue influence.

Improving Monitoring of External Auditors

Audit committees should conduct formal annual evaluations of external auditors. These evaluations should consider audit independence, partner and engagement-team competence, industry expertise, audit planning, significant audit risks, quality of communication and resolution of audit findings.

Auditor selection should therefore not rely primarily on Big Four affiliation.

Linking Audit Fees to Audit Risk and Effort

Audit fees should reflect the size, complexity and risk of the engagement. Audit committees should obtain adequate information concerning the basis of audit remuneration and should assess whether the level of audit effort is proportionate to the risks identified.

The positive audit-fee interaction observed in this study suggests that audit expenditure may produce greater reporting benefits when effective governance mechanisms monitor how audit resources are deployed.

Strengthening Follow-Up of Audit Findings

Audit committees should establish formal tracking mechanisms for significant audit findings. Each material finding should have a responsible management officer, a remediation deadline and evidence of completion. Matters that remain unresolved should be escalated to the board.

Regulatory Oversight

Regulators should place greater emphasis on the effectiveness of audit committees rather than relying primarily on auditor-firm size as an indicator of reporting quality. Periodic regulatory assessments should examine audit committee independence, expertise, meeting frequency, attendance, oversight of external auditors and follow-up of material reporting issues.

Contribution to Knowledge

The study makes three related contributions. First, it adds evidence focused specifically on deposit money banks in Nigeria, a sector in which the credibility of published financial information has wider systemic implications. Second, it extends the audit-firm-characteristics literature by treating audit committee as a conditioning governance variable rather than only as a direct explanatory factor. Third, the results show that the reporting benefit associated with audit fees is stronger when audit committee oversight is considered, while the interaction involving audit-firm size is negative. These findings provide a more nuanced account of how external audit characteristics operate within the governance environment of banks.

Limitations and Suggestions for Further Research

The findings should be interpreted within the scope of the sample. The analysis covers selected Nigerian deposit money banks and should not be extended automatically to manufacturing, insurance, oil and gas or other sectors. In addition, only three audit-firm characteristics were considered, and the analysis depends on information disclosed in annual reports.

Future studies can broaden the model by examining auditor independence, industry specialisation, partner rotation, audit delay and other governance mechanisms. Comparative research involving Nigerian banks and banks in other African emerging markets may also reveal whether the observed moderation patterns are country-specific. Researchers may further test alternative measures of reporting quality, including earnings persistence, accounting conservatism and value relevance.

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