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# EFFECTIVENESS OF AUDIT COMMITTEE PRACTICES AND THE VALUE OF LISTED DEPOSIT MONEY BANKS IN NIGERIA

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**ABSTRACT** *This research study examines the effectiveness of audit committee and as well explores the relationship between audit committee effectiveness and the value of deposit money banks in Nigeria. The followings were identified as audit committee characteristics (Internal control, the integrity of financial reporting, commitment of audit committee members and meeting) and were used in identifying the effectiveness of audit committee. Eight questions-survey questionnaires related to the four identified characteristics were administered to 55 respondents spread amongst the five sampled banks. The questionnaire enables the study to seek the perceptions of the respondents on the effectiveness of audit committee in deposit money banks in Nigeria. The Chi Square statistical tool was used to test the two study's hypotheses. The study finds that the Characteristics of Audit Committee practices relates to the effectiveness of Audit committees' of the deposits money banks in Nigeria, hence portraying the committee's effectiveness in performing its functions, the effectiveness of audit committee does not necessarily improve or otherwise on the value of the deposits money banks and results also indicate that activities as relate meeting of the audit committees' of deposit money banks are not clearly stated in the annual accounts of the banks. It therefore recommends that detail issues of meetings of audit committees be clearly stated and or included in the annual reports of the banks.*

**KEYWORDS:** Corporate Governance, Audit Committee, Deposit Money Banks'

## INTRODUCTION

In response to worldwide corporate scandals, there was a significant increased regulatory demand for accountability in the world business environment. This, according to Sengur, (2007) has in the last decade, brought organizations' risk management and internal control systems into the public policy debates on corporate governance. Originated in the 19th century, corporate governance came up in response to the separation of ownership and control, following the formation of common stock companies (Berle & Means, 1932) as cited in Tankiso (2008). The separation between ownership and control resulted in the agency relationship which refers to the situation where shareholders own the firm while managers control it.

Managers mostly do not always pursue the best interests of the company, but rather their own interests. This situation leads to the agency problem, which forms the theoretical framework for current corporate governance practices. The existence of the agency problem results from the owner's inability to run the company on a day-to-day basis. Managers are hired to manage the affairs of company owners, with the instruction of pursuing the owners' objective (Tankiso, 2008). Deviation from these objectives and instructions results in the agency problem.



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Good corporate governance is used as a measure for solving the agency problem, where the board of directors is regarded as the focal point of the governance system and therefore is accountable to shareholders and responsible for the performance and the affairs of the company (IOD 2002). The practice of corporate governance is a combination of a number of mechanisms, amongst which is the audit committee. Audit committee effectiveness has been a focus of international corporate governance reform for many years. Kalbers and Fogarty (1998) asserted that the genesis of audit committees as a part of corporate governance structure is rooted in the reactions to the abuse of power by corporate management which led to financial scandals, financial reporting defalcations, and unjustifiable manipulation of accounting policies.

Audit committee is a key factor of efficient corporate control systems. Companies around the world have been required by their various corporate regulations to have audit committee which primarily is to ensure the integrity of financial reporting and the audit process by ensuring that the external auditor is independent, objective and does a thorough job. An effective audit committee practice is for good corporate governance. It ensures that the statement of affairs presented by the agent is accurate or rather that the report can be trusted and also to ensure that the performance reported is aligned with the goals of the principal. A lot of research has been carried out in the field of corporate governance looking at different ways an organisation is governed and managed to ensure that the interest of all stakeholders, most especially shareholders are been protected, however, the purpose of this paper is to examine the effectiveness of audit committee practices and its effect on the value of listed deposit money banks in Nigeria.

## LITERATURE AND CONCEPTUAL FRAMEWORK

### Corporate governance

Although the focus of the paper is Audit Committee, there is need for the understanding of the concept of corporate governance. The vast amount of literature available on the subject matter ensures that there exist innumerable definitions of corporate governance. This paper however, has identified the following authors’ perception of the meaning and concept of corporate governance.

Mayer (1997) looked at corporate governance as ways of bringing the interests of investors and managers into line and ensuring that firms are run for the benefit of investors. Deakin and Hughes (1997) viewed corporate governance as the relationship between the internal governance mechanisms of corporations and society’s conception of the scope of corporate accountability. It has also been defined by Keasey, Thomas & Wright (1997) to include the structures, processes, cultures and systems that engender the successful operation of organizations. Robins & Coutler (2005) noted that the system used in corporate governance is to ensure that the interests of the corporate owners are protected. Kyereboah-Coleman (2007), opined that corporate governance is represented by the structures and processes lay down by a corporate entity to minimize the extent of agency problems as a result of separation between ownership and control.

Badejo-Okusanya (2011) however defines corporate governance in the context of public



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sector as an embodiment of processes and systems by which corporate entities are controlled and held to account, including the relationship amongst the many stakeholders involved in each corporation and the goals for which they were established. It must also be indicated that different systems of corporate governance will embody what are considered to be legitimate lines of accountability by defining the nature of the relationship between the company and key corporate constituencies.

In summary, the central idea in all these definitions is the position of the shareholder and the overriding objective of maximization of shareholders wealth. What is important is how to manage the organization to achieve shareholders objective of profit maximization. Thus, the key aspects of good corporate governance include transparency of corporate structures and operations; the accountability of managers and the boards to shareholders; and corporate responsibility towards stakeholders.

**Audit committee**

This is the committee of company's board of directors vested with important responsibilities to on behalf of the company shareholders, to oversee the financial reporting process, the integrity of companies' financial statement, the company's compliance with legal requirements, the external auditor's qualification, independence and performance and the internal audit function.

Audit committee has been understood by various authors as it relates to what they perceived of the committee. Birkett (1986), Cadbury Committee (1992) and Collier (1992) defines audit committee as a sub-committee of the main board comprised mostly of non- executive or independent directors with responsibility for oversight of auditing activities. Elaborately defined, Rezaee (2009) looked at audit committee as a committee composed of independent, non-executive directors charged with oversight functions of ensuring responsible corporate governance, a reliable financial reporting process, an effective internal control structure, a credible audit function, an informed whistleblower complaint process and an appropriate code of business ethics with the purpose of creating long-term shareholder value while protecting the interests of other stakeholders.

Although the later is elaborate, a common feature existed in all these definitions. They all described the status, composition and anticipated roles of the committee. Firstly, the committee is described as a sub-committee of the board who considers and takes decisions in the best interests of the shareholders. It then implies that the Audit Committee derives its existence, power, structure and terms of reference from the BOD acting on behalf of the shareholders. This according to Adelopo (2010) is partly comparable to the idea of delegated authority in politics and governance, except that BOD do not have to debate and vote on the decisions of the Audit Committees as is the case in the parliaments in politics and governance with respect to delegated authorities.

Secondly, definitions of the Audit Committee also focus on its composition. All the definitions mentioned above described the Audit Committee as a committee comprising of mainly independent non-executive directors. It is imperative that the membership of the committee is independent in order to be able to defend the interests of the shareholders and look at issues in a pragmatic and unbiased way. Lastly, the committee has been defined in



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terms of its anticipated roles and responsibilities which have changed significantly over time.

In Nigeria, the CBN code of corporate governance for banks post consolidation 2006, provide for the establishment of an audit committee which shall compose of at least two (2) non executive directors and one (1) ordinary shareholders appointed at AGM to review the integrity of the bank's financial reporting and oversees the independence and objectivity of the external auditors.

**Deposit Money Banks:** These are otherwise known as commercial banks, central in financing economic activity in any economy, most especially the developing countries like Nigeria. The Deposit money banks have played significant role through their crucial functions of financial intermediation, provision of an efficient payments system and facilitating the implementation of monetary policies. Governments the world over have evolved an efficient banking system, not only for the promotion of efficient intermediation, but also for the protection of depositors, encouragement of efficient, competition, maintenance of public confidence in the system stability of the system and protection against systemic risk and collapse.

For the industry to be efficient, it must be regulated and supervised in view of the failure of the market system to recognize social rationality and the tendency for market participants to take undue risks which could impair the stability and solvency of their institutions.

## THEORETICAL FRAMEWORK

**The Agency Theory**- the agency theory is used in this paper as such that underpins effective audit committee's function. It states that the separation of corporate management and ownership results in an agency problem: the management (agents) may not always act in the interests of the shareholders (principals) (Fama and Jensen, 1983). In order to solve the agency problem, boards of directors through it oversight role involves appointing the CEO, approving business strategy, monitoring control systems, liaising with external auditors, etc. Given its diverse responsibilities, the board of directors typically delegates its oversight activities to different committees. One of these committees is the audit committee vested mainly with the responsibility to oversee financial reporting. In line with the agency theory, effectiveness of audit committee is associated with the monitoring and control need of that firm. For instance, the work of Klein (2002) finds that audit committee independence is negatively associated with growth opportunities. While we believe that independence of audit could be tight to its effectiveness, Klein (2002) interprets that investors in high growth firms rely less on financial statements, and therefore demand less monitoring functions from audit committee their by derailing its effectiveness. Similarly Beasley and Salterio (2001) find that voluntary increases in the number of outside audit committee members are positively associated with board size and the separation of the CEO and board chair roles. This also relates to how effective the audit committee will function. To buttress this, Matthew (2011) in determining the impact of more outsiders on the effectiveness of audit committee, has found that the more the number of outside directors, the better effective is the audit committee.


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## METHODOLOGY

This study examines the effectiveness of audit committee practices and its effects on the value of deposit money banks in Nigeria. Two hypotheses were formulated in null form and tested. Related studies have adopted varying methods of data analysis; Muhamad-Sori, Abdul-Hamid, Mohd-Saad, and Evans (2007) used the Mann Whitney test together with postal questionnaires in carrying out their survey research; Phuangthip and Phaproke (2010) applied the ordinary least square regression analysis (OLS) while carrying out their research. However, this study applies a simple percentage analysis tools to analyse responses from an eight questions survey questionnaire with a response options of Strongly Agreed, Agreed, Undecided, Disagreed, and Strongly Disagreed distributed to 50 respondents spread amongst the five sampled banks. The Chi Square statistical tool was used to test the study's hypotheses; this was adopted from the work of Austine, Edosa & Henry (2013) who examines Audit Committee Report in Corporate Financial Statements: Users' perception in Nigeria. The sample procedure was judgmental, based on the following: that they are listed in the Nigeria stock exchange as 31$^{st}$ December 2013; that they have a minimum shareholder's fund of two hundred billion naira (N200bil) and that they have their 2013 annual accounts published on or before June 30, 2014. The following banks meets up the conditions: Zenith bank Plc, First bank Nig. Plc, United Bank For Africa Plc, Guarantee Trust Bank Plc and Access Bank Nigeria Ltd. (NDIC Annual Report, 2013). They are therefore considered as the sampled banks. However, for the purpose of data, each bank was conveniently administered ten (10) questionnaires to staff at the managerial level and as well one (1) to each of the sampled bank's auditor. This gives a total of 55 respondents.

### The study Hypothesis

$Ho_1$ The Characteristics of Audit Committee practices does not relate to the effectiveness of Audit committee.

$Ho_2$ Effective Audit Committee practices does not significantly relate to the value of deposit money banks in Nigeria.

## ANALYSIS, RESULTS AND DISCUSSIONS

The fifty five questionnaires distributed to the fifty five respondents were all returned completed and the analysis using a simple percentage is shown below.

Table 1 Audit Committee regularly reviews the integrity of financial statements, accounting policy change, disclosure and compliance with accounting standards.

| **Responses** | **Frequency** | **Percent** | **Valid Percent** | **Cumulative Percent** |
|---|---|---|---|---|
| Strongly Agreed | 4 | 7.27 | 7.27 | 7.27 |
| Agreed | 18 | 32.73 | 32.73 | 40.00 |
| Undecided | 28 | 50.91 | 50.91 | 90.91 |
| Disagreed | 4 | 7.27 | 7.27 | 98.18 |
| Strongly Disagreed | 1 | 1.82 | 1.82 | 100.00 |
| Total | 55 | 100.00 | 100.00 | |

Source: Field Survey, 2014.


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Analysis from the table above indicates that 50.91% of the respondents are not sure if the audit committees regularly review the integrity of financial statements, accounting policy change, disclosure and compliance with accounting standards. Although 7.72% strongly agreed and 32.73% agreed with the assertion, it is not enough to convince the study to accept it. Were as 7.24% and 1.82% respectively disagreed and strongly disagreed.

Table 2 Audit Committee regularly reviews auditor's report and financial highlights of your bank

| **Responses** | **Frequency** | **Percent** | **Valid Percent** | **Cumulative Percent** |
|---|---|---|---|---|
| Strongly Agreed | 6 | 10.91 | 10.91 | 10.91 |
| Agreed | 20 | 36.36 | 36.36 | 47.27 |
| Undecided | 26 | 47.27 | 47.27 | 94.54 |
| Disagreed | 2 | 3.64 | 3.64 | 98.12 |
| Strongly Disagreed | 1 | 1.82 | 1.82 | 100.00 |
| Total | 55 | 100.00 | 100.00 | |
| Total | 55 | 100.00 | 100.00 | |

Source: Field Survey, 2014.

Analysis from the table above has shown no significant difference with the result from table 1 which did not fully support the fact that Audit Committee regularly reviews auditor's report and financial highlights of the bank. Confirming from the fact that strongly agreed (10.91%) and agreed (36.36%) are combined to give a total response of 47.27% which is equal to the 47.27% responses for undecided. 3.64% and 1.82% respectively disagreed and strongly disagreed with the assertion. From the above, we can therefore deduce that it is not certain that Audit Committee regularly reviews auditor's report and financial highlights of the bank.

Table 1 Audit Committee monitors the effectiveness of internal control function in your banks

| **Responses** | **Frequency** | **Percent** | **Valid Percent** | **Cumulative Percent** |
|---|---|---|---|---|
| Strongly Agreed | 20 | 36.36 | 36.36 | 36.36 |
| Agreed | 26 | 47.27 | 47.27 | 83.63 |
| Undecided | 3 | 5.46 | 5.46 | 89.09 |
| Disagreed | 4 | 7.27 | 7.27 | 96.36 |
| Strongly Disagreed | 2 | 3.64 | 3.64 | 100.00 |
| Total | 55 | 100.00 | 100.00 | |

Source: Field Survey, 2014.

From table 3 above, analysis has shown that the combination of strongly agreed (36.36%) and agreed(47.27) has given an 83.63% overwhelming support to the fact that Audit Committee monitors the effectiveness of internal control function in the banks. the percentage response for undecided is 5.46% while disagreed and strongly disagreed is 7. 27% and 3.64% respectively.


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Table 4 Management of your bank usually responds to the internal auditor's findings and recommendations when observed by the audit committee?

| **Responses** | **Frequency** | **Percent** | **Valid Percent** | **Cumulative Percent** |
|---|---|---|---|---|
| Strongly Agreed | 22 | 40.00 | 40.00 | 40.00 |
| Agreed | 28 | 50.90 | 50.90 | 90.90 |
| Undecided | 1 | 1.82 | 1.82 | 92.72 |
| Disagreed | 2 | 3.64 | 3.64 | 96.36 |
| Strongly Disagreed | 2 | 3.64 | 3.64 | 100.00 |
| Total | 55 | 100.00 | 100.00 | |

Source: Field Survey, 2014.

Analysis of responses from Table 4 above, agreed that Management of the bank usually respond to the internal auditor's findings and recommendations when observed by the audit committee as shown. Strongly agreed (40.00%) and agreed (50.90%) while the percentage response for undecided is 1.82%, disagreed and strongly disagreed is 3.64% and 3.64% respectively.

Table 5 Audit Committee members in your banks have shown willingness to be effective in their responsibilities.

| **Responses** | **Frequency** | **Percent** | **Valid Percent** | **Cumulative Percent** |
|---|---|---|---|---|
| Strongly Agreed | 10 | 18.18 | 18.18 | 18.18 |
| Agreed | 12 | 21.82 | 21.82 | 40.00 |
| Undecided | 18 | 32.73 | 32.73 | 72.73 |
| Disagreed | 10 | 18.18 | 18.18 | 90.91 |
| Strongly Disagreed | 5 | 9.09 | 9.09 | 100.00 |
| Total | 55 | 100.00 | 100.00 | |

Source: Field Survey, 2014.

From table 5 above, analysis has shown that 18.18% strongly agreed and 21.82 agreed to give a combination of 40.00% of the respondents supporting the fact that Audit Committee members in the bank have shown willingness to be effective in their responsibilities. However, (32.73%) are undecided, 18.18% disagreed while 9.09% strongly disagreed.

Table 6 Audit Committee members are devoted to affairs of the Committee.

| **Responses** | **Frequency** | **Percent** | **Valid Percent** | **Cumulative Percent** |
|---|---|---|---|---|
| Strongly Agreed | 10 | 18.18 | 18.18 | 18.18 |
| Agreed | 15 | 27.27 | 27.27 | 45.45 |
| Undecided | 18 | 32.72 | 32.73 | 78.18 |
| Disagreed | 12 | 21.82 | 21.82 | 100.00 |
| Strongly Disagreed | 0 | 0.00 | 0.00 | |
| Total | 55 | 100.00 | 100.00 | |

Source: Field Survey, 2014.

Analysis from the table above has shown a similar response to that of table 5 where about 45.45% respondent has strongly agreed (18.18%) and or agreed (27.27%) to the fact that Audit Committee members are devoted to affairs of the Committee in the bank. While


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32.73% are undecided and 21.82% disagreed. However, it shall be deduced that there are indications that the audit committee members devote to the affairs of the committee in the bank.

Table 7 Audit Committee in your bank holds meetings as at when due.

| Responses | Frequency | Percent | Valid Percent | Cumulative Percent |
|---|---|---|---|---|
| Strongly Agreed | 5 | 9.09 | 9.09 | 9.09 |
| Agreed | 15 | 27.27 | 27.27 | 36.36 |
| Undecided | 26 | 47.27 | 47.27 | 83.63 |
| Disagreed | 8 | 14.55 | 14.55 | 98.18 |
| Strongly Disagreed | 1 | 1.82 | 1.82 | 100.00 |
| Total | 55 | 100.00 | 100.00 | |

Source: Field Survey, 2014.

Table 7 shows that majority of the respondents 26(47.27%) have no idea whether audit committee meets as at when due or not, a total of 20(36.36%) covering strongly agreed 5(9.09%) and agreed 15(27.27%) believed the fact that audit committee meets as at when due. 8(14.55%) and 1(1.82%), disagreed and strongly disagreed respectively. This implies that audit committee meetings may not be regular.

Table 8 Audit committee members express their views freely and independently during meetings

| Responses | Frequency | Percent | Valid Percent | Cumulative Percent |
|---|---|---|---|---|
| Strongly Agreed | 8 | 14.55 | 14.55 | 14.55 |
| Agreed | 12 | 21.82 | 21.82 | 36.37 |
| Undecided | 25 | 45.45 | 45.45 | 81.82 |
| Disagreed | 8 | 14.55 | 14.55 | 96.37 |
| Strongly Disagreed | 2 | 3.63 | 3.63 | 100.00 |
| Total | 55 | 100.00 | 100.00 | |

Source: Field Survey, 2014.

While 8(14.55%) strongly agreed that audit committee members express their views freely and independently during meeting, 12(21.82%) agreed, 8(14.55%) disagreed and 2(3.63%) strongly disagreed. However it is deduced that audit committee members are not freely allowed to express their view during meetings, hence 25(45.45%) of the respondents are undecided on whether the audit committee members freely express their views during meetings.

**Hypotheses Testing**

This section relates to the testing of hypotheses earlier stated. For the sake of understanding, the hypotheses will be restated before presenting the result analyses. The decision rule is to reject the null hypothesis and accept the alternative if the $X^2$ calculated is greater than the critical value of $X^2$ at 5% significant level with degree of freedom of 4

$Ho_1$ the Characteristics of Audit Committee practices does not relate to the effectiveness of Audit committee.


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Table 9: testing Hypothesis 1

| **Responses** | **Q4.1.1** | **Q4.1.2** | **Total observations** | **Expected Observation** | **(o-e)** | **$(o-e)^2$** |
|---|---|---|---|---|---|---|
| Strongly Agreed | 4 | 6 | 10 | 22 | -12 | 144 |
| Agreed | 18 | 20 | 38 | 22 | 16 | 256 |
| Undecided | 28 | 26 | 54 | 22 | 32 | 1024 |
| Disagreed | 4 | 2 | 6 | 22 | -16 | 256 |
| Strongly Disagreed | 1 | 1 | 2 | 22 | -20 | 400 |
| Total<br>**$X^2$ Cal $=\sum(o-e)^2/\sum e$**<br>**$X^2$ 0.95,4** | | | 110 | 110 | | 2080<br>18.909<br>9.488 |

From the above analysis, the null hypothesis is rejected and the alternate accepted since the $X^2$ calculated value 18.909 is greater than the critical value of 9.488 at 95% confidence interval. This therefore means that the effectiveness of audit committee is confined on the existence of its major characteristics

$Ho_2$ Effective Audit Committee Practices does not significantly relate to the value of deposit money banks in Nigeria.

Table 9: testing Hypothesis 2

| **Responses** | **Q4.1.5** | **4.1.6** | **Total observations** | **Expected Observation** | **(o-e)** | **$(o-e)^2$** |
|---|---|---|---|---|---|---|
| Strongly Agreed | 10 | 10 | 20 | 22 | -2 | 4 |
| Agreed | 12 | 15 | 27 | 22 | 5 | 25 |
| Undecided | 18 | 18 | 36 | 22 | 14 | 196 |
| Disagreed | 10 | 12 | 22 | 22 | 0 | 0 |
| Strongly Disagreed | 5 | 0 | 5 | 22 | -17 | 289 |
| Total<br>**$X^2$ Cal $=\sum(o-e)^2/\sum e$**<br>**$X^2$ 0.95,4** | | | 110 | 110 | | 514<br>4.672<br>9.488 |

From the above analysis, the null hypothesis is accepted since the $X^2$ calculated value of 4.672 is lower than the critical table value of 9.488 at 95% confidence interval. This therefore means that, effective audit committee practice does not significantly relate to the growth of the value of deposits money banks in Nigeria.

## SUMMARY/DISCUSSION OF FINDINGS

Having presented the statistical analysis, sorting to examine the effectiveness of Audit committee as well as its effect on the value of deposit money banks, the following findings were discovered:

(i) The Characteristics of Audit Committee practices relates to the effectiveness of Audit committees' of the deposits money banks in Nigeria, hence portraying the committee's effectiveness in performing its functions.

(ii) That the effectiveness of audit committee does not relates to the value of deposit money banks in Nigeria, it therefore does not necessarily improve or otherwise on the value of the deposits money banks.


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(iii) Meeting of audit committee has been rated as one of those basic characteristics of audit committee (Ojulari, 2012). Results indicate that activities as relate meeting of the audit committees' of deposit money banks are not clear.

Although result has shown that effectiveness of audit committee has no significant relationship with the value of the deposit money banks in Nigeria, Ojulari (2012) proved that the characteristics of audit committee influences the performance of firms, Ibrahim and Saidin (2009) found that audit committees' effectiveness do impact on the quality of unaudited financial reports, this study have also proved that the audit committees' effectiveness is positively related to firms performances and Brown and Caylor (2007) on the general note have identified that corporate governance can lead to better performance clearly indicating a link between the two. This disagreement could result from the fact that this study specifically concerns the deposits money banks, whose value mostly is dependants on the quality of services rendered to customers (Ojunwa, 2013).

## CONCLUSION/RECOMMENDATIONS

The paper however concludes that audit committees' of deposits money banks are effective in their functions and responsibilities and that the effectiveness of the committees' will not impact positively and or negatively on the value change of the banks in Nigeria. The study haven also noted that activities as relate meeting of the audit committees' of deposit money banks are not clear, concludes that meetings are not held by the committee as expected. The paper therefore recommends that detail issues of meetings of audit committees be clearly stated and or included in the annual reports of the banks.

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