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AUDIT QUALITY AND EARNINGS MANAGEMENT OF LISTED INDUSTRIAL GOODS FIRMS IN NIGERIA

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ABSTRACT

This paper investigated the effect of audit quality on earnings management of listed industrial goods firms in Nigeria. The study used a correlational research approach, with secondary data gathered from eight (8) selected Nigerian industrial goods manufacturers for ten years (2010-2019). Stata version 11 was used to do multiple regression analysis on the data. The study discovered that audit firm size and earnings management of listed industrial goods firms (IGFs) in Nigeria are not significantly associated; auditor sector specialization has not significantly associated with earnings management of Nigeria's listed IGFs; auditor tenure has significantly affected earnings management of listed IGFs, and auditor client importance has significantly affected earnings management of listed IGFs in Nigeria. Based on the findings, it was recommended that the size of audit firms should not be the basis for hiring services of audit firms; there should be strict adherence to the recommendation by the Securities and Exchange Commission (SEC) that no company should retain an audit firm for a period longer than ten years consecutively. Since audit fees affect client importance, regulatory bodies such as the SEC and Financial Reporting Council of Nigeria (FRCN) should make the disclosure of all audit fees a mandatory requirement for all listed industrial goods firms in Nigeria.

Keywords: Audit quality, Earnings management, Audit firm size, Auditor tenure, Client importance

1. INTRODUCTION

The increasing waves of globalization and fierce competition have put pressure on organizations to strengthen their good corporate governance mechanisms. The inherent differences of interest that existed between the shareholders and management of corporations brought about this scandal. This conflict necessitates

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the establishment of rules to regulate the actions of parties involved in the management of companies. With the recent high-profile scandals in accounting, investors have indicated an interest in the issue of quality financial reporting.

To ensure that financial statements reflect a true and fair view of the financial affairs of business enterprises, certain mechanisms have been put in place. One of such mechanisms is a financial statements audit. Auditing came in as control and quality assurance following the divorce between ownership and control in the modern corporate world. Audit quality is seen as a monitoring system that can help managers and shareholders align their interests and limit the risk of opportunistic manager behavior (Abbott, Parker & Peters, 2004).

Earnings management occurs when executives use their judgment in financial reporting and transaction structuring to change financial reports to deceive some stakeholders about the company's underlying economic performance or to influence contractual outcomes based on reported accounting figures (Al Momani & Obeidat, 2013). It reduces the quality of reported earnings and their usefulness for investment decisions, thus reducing investors' and other financial information users' confidence in the financial reports.

Because of the importance of industrial goods corporations to the Nigerian economy and the claims of manipulative tendencies leveled against them, it is critical to investigate their earnings management behavior and the amount to which audit quality influences that behavior. This is in addition to jurisdictional and sectoral differences noticed in prior research resulting in inconsistent and mixed findings. The inconsistencies in the findings, coupled with the lack of local empirical studies on the link between audit quality and earnings management methods in the sector, make a fresh study of the nature and scope of the relationship more desirable. As a result, this study investigates the relationship between audit quality and earnings management of listed IGFs in Nigeria. The study's specific objectives were to; determine the relationship between audit firm size and earnings management of listed IGFs in Nigeria; ascertain whether the auditor's industry specialisation has any effect on the earnings management of listed IGFs in Nigeria; determine whether the auditor's tenure has a significant effect on earnings management of listed IGFs in Nigeria, and investigate whether auditor's client importance has any significant effect on earnings management of listed IGFs in Nigeria.

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2. LITERATURE REVIEW

2.1 Conceptual Framework

The basic concepts that are relevant to this study are audit quality and earnings management. These concepts are hereby clarified.

2.1.1 Audit Quality

Most audit scholars cite DeAngelo's (1981) definition of audit quality, which stipulates that audit quality is the market-assessed joint chance that a specific auditor would both (a) identify and (b) report a substantial mistake in the organization's accounting system. The definition identifies two key characteristics of audit quality: (i) the audit firm's competence, which affects how likely a breach will be identified, and (ii) the auditor's independence and objectivity, which defines what the auditor will do if a breach is detected. The ability of the auditor to discover and eradicate material misstatements, according to Davidson & Neu (1993), is the concept of audit quality.

2.1.1.1 Measures of audit quality

This research considers the following audit quality factors:

i) Audit Firm size

Audit quality is difficult to measure, thus, many academics rely on audit firm size as a proxy. Large audit companies are thought to conduct more thorough checks. As a result, if everything else is equal, bigger audit companies are more likely to be linked with more detailed information than smaller audit firms (Beatty, 1989; Titman & Trueman, 1986). Big audit firms are in a better position to constrain earnings management because they invest more in reputation capital and expertise than small audit firms (DeAngelo, 1981; Piot & Janin, 2007). Providing quality-differentiated audit services is, therefore, necessary for big audit firms to protect and maintain their investment in reputation capital.

ii) Audit Firm Tenure

Another proxy of audit quality often associated with earnings management in accounting literature is auditor tenure. There are two contending arguments concerning the link between auditor tenure and earnings management. The first argument suggests that an excessively long auditor-client relationship threatens the auditor's independence due to closer ties and familiarity with the client. Long auditor

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tenure is, therefore, likely to make the auditor lose his objectivity and make the audit engagement become a routine exercise (Piot & Janin, 2007). In contrast, proponents of longer auditor tenure contend that it leads to more audit efficiency and experience as the length of the auditor-client relationship increases. This makes auditors more effective in the detection of questionable accounting practices of the client than they were in the early years of the audit engagement. The second argument suggests that longer auditor tenure is likely to be linked with less earnings management of firms.

iii) Auditor's Client Importance

Client importance is another proxy of audit quality that extant literature associates with the earnings management behaviour of firms. Auditors are to a greater extent likely to overlook clients' accounting irregularities when the client is a very important one (economically big in terms of revenue contribution to its total fees) than when the client is less important to them. Auditor's objectivity is, therefore, likely to be compromised when he faces the risk of losing an important client and not reporting accounting irregularities of the same client (Ebrahim, 2001).

iv) Auditor’s Industry specialization

Accounting literature also suggests a positive link between auditor industry specialists and audit quality. Specialist auditors possess industry-specific knowledge and experience which makes them more effective in identifying accounting irregularities than non-specialist auditors. Industry specialist auditors also invest more in relevant audit technology than their counterparts. This gives them an advantage over other auditors in the detection of unethical accounting practices such as earnings management (Balsam, Krishnan & Yang, 2003; Tyokoso & Tsegba, 2015)

2.1.2 Earnings Management

Earnings management, according to Merchant and Rockness (1994), is any management action that affects reported income and delivers no genuine economic benefit to the business in the long run. Earnings management in this study is defined as both intentional and unintentional actions that managers take which affect financial reporting by misleading some information users. That is, it involves any transformation of financial records using accounting choices, estimates, and other practices allowed by accounting regulation.

Auditors, by giving reasonable assurance that the financial statements are free of substantial misstatements, eliminate information asymmetry between management and stakeholders (Becker, DeFond, Jiambalvo & Subramanyam,1998). Quality audits should be more likely to successfully detect and prevent earnings management.

2.2 Theoretical framework

Stewardship theory, the stakeholder theory, and the agency theory are reviewed.

2.2.1 The Stakeholders Theory

The stakeholder theory was propounded by Freeman in 1984. The theory views the firm as comprising more than two stakeholders. A stakeholder, according to Freeman (1984), is an individual or group of people who can affect or is influenced by the attainment of an organization's goals. The connection between the company and its internal stakeholders (such as employees, managers, and owners) is governed by both official and informal rules that have evolved. While management receives finance from shareholders, they depend upon employees to accomplish the productive purpose of the company. External stakeholders (such as consumers, suppliers, and the community) are equally essential, and they are likewise bound by statutory and informal rules that must be followed by businesses. The stakeholder theory recognizes that the firm and society are interdependent.

The stakeholder theory is also heavily criticized because of the difficulty to treat equally and satisfy the competing demands of the multiple stakeholders in the firm as proposed by the stakeholder theory. The theory, therefore, fails to adequately explain the association between audit quality and earnings management practices.

2.2.2 The Agency Theory

The agency theory was developed by Jensen and Meckling in 1976. It is based on the principal's (shareholder's) and agent's (manager's) relationship. The separation of ownership from management and control in modern-day business corporations provides the basis for the function of agency theory. This separation provides the opportunity for an agent (manager) to be appointed to manage the daily operations of the company. This relationship, however, creates the potential for conflicts of interest between the agent and principal and requires monitoring costs involved in resolving these conflicts (Jensen & Meckling, 1976).

Agency theory, therefore, suggests monitoring techniques such as high-quality audits to decrease these conflicts and align the interests of managers and shareholders. The self-seeking interest of managers, therefore, increases costs to the firm such as costs of contract formation, loss due to decisions taken by the agents, and the costs of observing and controlling the actions of the agents. In light of the above, managers cannot be fully trusted by shareholders. This study, therefore, draws on agency theory to test the link between audit quality and the incidence of earnings management industrial goods firms in Nigeria. Agency theory is chosen because it better explains the motivation for earnings management and the link between audit quality as a monitoring mechanism, and earnings management than the other theories.

2.3 Review of Related Empirical Studies

Memis (2012) used a sample of 1507 firm-year observations for 2008-2009 to study the connection between audit quality and earnings management in eight emerging nations. Discretionary accruals- a proxy for earnings management were examined using the modified Jones model (MJM). The study's findings revealed that, except for Brazilian and Mexican firms, there is a significant link between discretionary accruals and audit quality as measured by the Big Four auditors. Though the study covers eight emerging countries, the fact that it excluded Nigeria makes its findings unlikely to apply to industrial goods firms in Nigeria due to environmental factors.

Ahmadzade, Hassanzadeh, Pooryegane, and Ebrahimi (2012) investigated audit quality and earnings management by using a sample of 73 firms listed on the Tehran Stock Exchange from the years 2008-2011. According to the regression analysis, audit firm tenure and audit firm industry specialization are inversely associated with Iranian firm earnings management over the study period. However, the fact that the study focused on listed companies in Iran generally and not specifically concerning industrial goods firms may likely affect the application of the findings to listed industrial goods firms in Nigeria due to sectoral differences.

Inaam, Khmoussi and Fatma (2012) investigated audit quality and earnings management of Tunisian firms using 319 firm-year observations for the period 2000-2010. Using the modified Jones model (Dechow, Sloan & Sweeney 1995) to measure discretionary accruals, the study showed that auditor industry specialty and auditor size measured by Big 4 auditors are negatively linked with earnings management of their clients. Auditor tenure had a negative but insignificant association with discretionary accruals. The study is limited because even though

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Tunisia and Nigeria are developing nations with several similarities, the study was not directly concerning industrial goods firms making the findings unlikely to apply to industrial goods firms in Nigeria.

Rohaida (2011) investigated the link between audit quality and earnings management of companies in the UK. The Jones and modified Jones 1991 model, in addition to the Kothari, Lcone, and Wasley, 2005 model, were used to estimate earnings management, which is represented by discretionary accruals. For all metrics of earnings management, the study discovered that both audit fees and industry specialist auditors are related to less earnings management of the sampled enterprises. Similarly, the size and independence of the audit committee had no significant negative link with the various indicators of earnings management. The various indicators of earnings management, audit committee financial skills, and audit committee meetings yielded varied results. The study findings may, however, not apply in Nigeria due to legal and economic considerations such as the high litigation risk faced by external auditors in the UK compared to the low litigation risk of external auditors in Nigeria

In another study, Yasar (2013) examined audit quality and earnings management of companies listed on the Turkish Stock Exchange for the period 2003-2007. Empirical evidence from the regression analysis shows a positive link between audit firm size and discretionary accruals of manufacturing firms in Turkey. The study result is, however, limited because given the economic differences between Turkey and Nigeria findings from the study are not likely to apply to firms in Nigeria.

Pouraghajan, Tabari, Emamgholipour, and Mansourinia (2013) studied audit quality and earnings management links involving 140 firms listed on the TSE from 2006 to 2011. The MJM was utilized in estimating discretionary accruals which is a proxy of earnings management. The data analysis revealed a non-significant positive link between the audit firm size and discretionary accruals. The study is limited because even though Iran and Nigeria are developing economies with a lot of similarities, since the study was not specifically on industrial goods firms, its findings are not likely to apply to industrial goods firms in Nigeria due to sectoral and some jurisdictional differences.

Also, Ching, Teh and San (2015) investigated audit quality and earnings management using a sample of one hundred (100) industrial products and consumer products companies listed on the main board of Bursa Malaysia covering 2008-2013. Audit quality was proxy by audit firm size, audit fees, and audit partner

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tenure. Earnings management, represented by absolute discretionary accruals was estimated by the modified Jones (1991) model. According to the results of data analysis using the regression technique, audit firm size and audit fees have a negligible negative link with earnings management of Malaysian listed industrial and consumer products businesses. However, findings from this study may not apply to listed industrial goods firms in Nigeria because of some legal and economic differences between Nigeria and Malaysia such as the level of capital market development.

Zhou and Guan (2014) investigated the relationship between audit quality and earnings management of companies in China for the period 2008-2011. Discretionary accruals were estimated using the MJM for a sample of 4,640 firm-year observations. The study revealed that audit firm size has a significant negative effect on earnings management in China, especially for firms with income-increasing abnormal accruals. A positive relationship was found between the auditor industry specialty and earnings management of the companies. The relationship, however, turns negative in firms with income decreasing earnings management in China. Given the different nature of the sampled companies in China, findings from the study may likely not apply to industrial goods films in Nigeria due to sectoral and economic differences.

Also, Karimi and Gerayli (2014) investigated audit quality (as measured by auditor industry specialty and tenure) and earnings management in 91 businesses listed on the Tehran Stock Exchange (TSE) from 2008 to 2012. According to the findings of the study, the auditor industry specialty is linked to less earnings management of firms listed on the TSE. The sampled companies' earnings management exhibited a negative but negligible relationship with auditor tenure. The study only looked at auditor industry expertise and tenure, presenting only a partial picture of the relationship between audit quality and corporate earnings management. Many research from developing economies have looked at the connection between audit quality and corporate earnings management methods.

Aliyu, Musa and Zachariah (2015) studied the effect of audit quality (represented by audit firm size, joint audit, and auditor financial dependence- a measure of client importance) on earnings management of listed deposit money banks (DMBs) in Nigeria using a sample of seven (7) DMBs listed in Nigeria between 2006 and 2013 while data analysis was done using ordinary least square (OLS) regression technique. Findings from data analysis indicated that both audit firm size and joint audit have a significant negative effect on earnings management of listed DMBs in

Nigeria. Though this study is from Nigeria, it is limited because given the peculiar nature of the banking sector; it is likely that its earnings management will be different from other sectors such as industrial goods firms not captured in the study sample.

Tyokoso and Tsegba (2015) investigated the audit quality and earnings management association involving listed oil marketing companies in Nigeria covering 2004-2013. The dependent variable earnings management represented by discretionary accruals (DA) was estimated using the MJM while the independent variable, audit quality was represented by audit firm size, auditor industry specialization, and auditor tenure. The study findings show that audit firm size and auditor industry specialization have an insignificant negative effect on the DA of the sampled listed oil marketing companies in Nigeria.

3. METHODOLOGY

3.1 Research Design

The paper employs a correlational research design and the study population is comprised of all the twenty-one (16) industrial goods firms listed on the floor of the Nigerian Stock Exchange (NSE) as of 31st December 2019. A sample size of Eight (8) industry goods firms listed on the NSE was used based on the following filters: The company must have been listed on the NSE on or before 1st January 2010 and stay listed throughout the Ten (10) years under study. The company must have complete data values for each financial year covered in the study period.

The paper used secondary data. These data were extracted from the financial statements (statement of comprehensive income, Statement of financial position, statement of cash flows, and non-financial information) of industrial goods companies listed on the NSE for the period of ten (10) years (2010-2019) for analysis. The study used descriptive statistics and multiple regression analysis with the aid of Stata version 11 for data analysis.

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3.2 Measurement of Variables

Variable	Nature of Variable	Proxy	Measurement
Earnings Management	Dependent	modified Jones model (MJM)	Net income amount of firm minus amount of cash flow from operations of the firm
Audit Firm Size	Independent	AudSIZE	Measured by dichotomous variable (1 if a firm is audited by any of the big4 and 0, if otherwise).
Audit industry Specialisation	Independent	SPEC	Measured by a dummy variable 1 if market size (MS) ≥20 percent and 0 otherwise.
Audit Firm Tenure	Independent	TENURE	Measured by a dummy variable 1 is attached for 3 years and above, and 0 is recorded if otherwise
Client Importance	Independent	CI	This is measured as the Ratio of client's sales to the sum of all clients' sales audited by an auditor within the sample size.

3.3 Model Specification

The study uses MJM. The model is as follows:

$DA_{it}=b_O+b_1AudSIZE_{it}+b_2SPEC_{it}+b_3TENURE_{it}+b_4CI_{it} + e_{it}$------------i

Where:

DA_{it} = Discretionary accruals

AudSIZE$_{it}$ = Audit firm size for firm i in time t

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$SPEC_{it}$ = Auditor industry specialization for firm i in time t

$TENURE_{it}$ = Audit firm tenure for firm i in time t

CI_{it} = Client importance for firm i in time t

b_O = Constant

e = error term

4. RESULTS AND DISCUSSION

4.1 Descriptive Statistics

The descriptive statistics of the dataset from the sampled industrial firms in Nigeria are presented in table 1.

Table 1. Descriptive Statistics

Variable	Mean	Std. Dev	Min.	Max.
DA	0.0996	0.0517	0.0002	0.2789
AUDSIZE	0.6500	0.4800	0	1
SPEC	0.5500	0.5006	0	1
TENURE	0.5750	0.4975	0	1
CI	0.5550	0.3620	0.0280	1

Source: Output from Stata, Version 11

Table 1 reveals a mean value of 0.0996 for discretionary accruals which is an indication that the sampled companies were involved in minimal earnings manipulations during the study period. The minimum and maximum values of discretionary accruals during the study period are 0.0002 and 0.2789 respectively.

The Table further reveals an average value of 0.6500 for audit firm size. The value implies that 65% of the sampled industrial goods firms were audited by the big 4 audit firms in Nigeria during the study period. Auditor industry specialization has a mean value of 0.5500 during the study period. This value implies that 55% of the

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sampled companies were audited by industry specialist auditors during the period of the study. Auditor tenure has a mean value of 0.5750 during the study period. This value indicates that about fifty-eight percent (58%) of the sampled firms retained their auditors for three years and above. The minimum and maximum values of auditor tenure during the study period are zero and one respectively. Client importance has a mean value of 0.5550. What this suggests is that on average, auditors' financial dependence on the sampled companies was 55%. The minimum and maximum values of client importance during the study period are 0.0280 and 1 respectively.

4.2 Correlation Analysis

It is needful to determine whether the variables used are associated. Given this, table 2 presents correlation values between dependent and independent variables and the correlation among the independent variables themselves.

Table 2 Correlation Matrix

Variable	DAC	AUDSIZE	SPEC	TENURE	CLI
DA	.0000				
AUDSIZE	-0.1253	1.0000			
SPEC	-0.1389	0.4952	1.0000		
TENURE	-0.3357	0.1113	0.1881	1.0000	
CI	0.2373	-0.4706	-0.4295	0.0357	1.0000

Source: Output from Stata Version 11

The Table indicates that AUDSIZE and SPEC, AUDSIZE and TENURE, SPEC and TENURE, TENURE and CI are positively correlated. This implies that the paired variables move in the same direction. The Table also shows that AUDSIZE and CI, SPEC and CI, are negatively correlated. This means that the paired variables move in the opposite direction, as one increases, the other decreases.

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4.3 Regression Results

Table 3: Summary of Random Effect Regression Results

Variable	Beta Coeff	Z-values	Prob.>t
AUDSIZE	0.0046	0.34	0.734
SPEC	0.0110	0.83	0.406
TENURE	-0.0362	-3.31	0.001
CI	0.0324	1.83	0.067
R^2			0.5733
F-value			23.19
Prob.>F			0.0007

Output from Stata Version 11

Table 3 reveals an R^2 value of 0.57. The R^2, which represents the coefficient of multiple determination, implies that 57% of the total variation in the dependent variable (discretionary accruals) of listed industrial firms in Nigeria is jointly explained by the explanatory variables (audit firm size, auditor industry specialization, auditor tenure, and client importance). The value of R^2 also shows that 43% of the variation in the dependent variable is explained by factors not captured in the model.

This suggests that apart from audit quality, other factors are linked to the earnings management of firms studied. The Wald- statistics value of 23.19 (Prob.>F = 0.00) indicates that the model is fit to describe the relationship represented in the research model and that the explanatory variable has been properly chosen, combined, and used. The nature and extent of the relationship between the dependent variable and each of the independent variables of the study in terms of coefficients, t- values, and p- values are explained below.

Table 3 reports a positive relationship between audit firm size and earnings management. The table reveals that the coefficient of AUDIZE is 0.0046. The coefficient of 0.0046 implies that a unit increase in AUDIZE leads to about a 0.0046

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increase in discretionary accruals (earnings management) of listed industrial goods in Nigeria. It is reported in Table 3 that SPEC has a coefficient of 0.011 which means that it has a positive relationship with earnings management of listed industrial firms in Nigeria to the extent that a unit increase in SPEC leads to about a 0.011 increase in earnings management of listed industrial firms in Nigeria.

From Table 3 it can be observed that TENURE has a coefficient of -0.0362 which means that it negatively affects the earnings management of listed industrial firms in Nigeria. The relationship is such that a unit increase in TENURE leads to about a 0.0362 decrease in earnings management of listed industrial firms in Nigeria. Table 3 also indicates that the coefficient of CI is 0.0138 which is an indication that a unit increase in CI leads to a corresponding increase in discretionary accruals (earnings management) of listed industrial goods by 0.0138.

4.4 Discussion of Findings

Based on the result, the first hypothesis of the study which states that audit firm size has no significant effect on earnings management of listed IGFs firms in Nigeria is not rejected. The present finding is consistent with those of Yasar (2013) and Pouraghajan, Tabari, Emamgholipour, and Mansourinia (2013) who found a positive link between audit firm size and earnings management of firms. The result, however, contradicts the findings of Inaam, Khmoussi and Fatma (2012), Zhou and Guan (2014), Tyokoso and Tsegba (2015), Aliyu, Musa and Zachariah (2015), and Ching, Teh and San (2015) who documented a negative link between audit firm size and earnings management of firms.

The result of hypothesis two supports the finding of Zhou and Guan (2014) who found a positive relationship between auditor industry specialization and earnings management of firms. The result, however, is not in line with the finding of Inaam, Khmoussi and Fatma (2012), Ahmadzade, Hassanzadeh, Pooryegane and Ebrahimi (2012), Karimi & Gerayli (2014), and Tyokoso and Tsegba (2015) who documented a negative association between industry specialist auditors and earnings management of firms. Based on the empirical evidence, the second hypothesis of the study which states that auditor industry specialization has no significant effect on earnings management of listed IGFs is not rejected.

Based on the results, hypothesis three which states that Auditor tenure has no significant effect on Earnings Management of the IGFs in Nigeria is rejected. The finding is consistent with the finding of Ahmadzade, Hassanzadeh, Pooryegane and Ebrahimi (2012), Inaam, Khmoussi and Fatma (2012), Karimi and Gerayli (2014), and Tyokoso and Tsegba (2015) who documented a negative relationship between auditor tenure and earnings management of firms. The result is, however, inconsistent with those of Ching, Teh and San (2015) who documented evidence of a positive association between auditor tenure and earnings management of firms.

The finding in hypothesis four corroborates the finding of Aliyu, Musa & Zachariah (2015) who found a positive association between the financial dependence of auditors and earnings management of Nigerian banks. Based on the empirical evidence, the hypothesis of the study which states that the auditor's client importance does not affect the Earnings Management of the IGFs in Nigeria is rejected.

5. CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

From the findings of the study, it is concluded that:

i. It was hypothesized that audit firm size has no significant effect on earnings management of listed IGFs firms in Nigeria. This hypothesis was not rejected. Therefore, audit firm size is not the most important factor associated with less earnings management of Nigerian firms. ii. On the hypothesis which states that Auditor’s industry specialization has not significantly affected Earnings Management of listed IGFs in Nigeria, a positive relationship between auditor industry specialization and earnings management of firms was found. Therefore, audit firms that specialize along the industry lines of companies listed on the NSE are more likely to mitigate earnings management due to their specialist competencies in those areas.

iii. It was stated in hypothesis three that Auditor tenure does not affect Earnings Management of the IGFs in Nigeria. This hypothesis was rejected. This implies that the experience of the audit firm arising from longer tenure is more likely to be linked with less earnings management of firms.

iv. The fourth hypothesis stated that the auditor's client importance has not significantly affected the Earnings Management of listed IGFs in Nigeria. This hypothesis was not rejected. This is an indication that the financial dependence of an audit firm on a client would more likely not constrain earnings management.

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5.2 Recommendations

i. In hiring the services of audit firms, companies should judge them based on performance in previous audits and not merely the size of the audit firm. Those who hire audit services in Nigeria should consider the competence and experience of the audit firms rather than the size that are likely to be associated with less earnings management of firms. Also, users of audited financial statements should subject all audited financial statements to the same scrutiny regardless of whether the audit report is from a big 4 or small audit firm. This is to avoid making wrong investment decisions.

ii. Audit firms should create avenues for specializing along the industry lines of companies listed on the NSE. This will boost auditor industry specialization which is significant in mitigating earnings management.

iii. There is a need to visit audit tenure rules. A shorter period may not be appropriate, rather an appropriate longer period should be considered. In considering the longer period, care should be taken to avoid a period that may be too lengthy to impair auditors' independence.

iv. Audit firms should strive to earn revenues from different sources outside of their audit clients. Similarly, audit firms through quality services may likely increase their client base and avoid over-dependence on a particular client.

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