



AUDIT QUALITY AND FINANCIAL REPORTING QUALITY OF LISTED DEPOSIT MONEY BANKS IN NIGERIA

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Abstract

The reliability of financial information is central to the stability, transparency and accountability of the banking sector. In Nigeria, deposit money banks hold a critical position in economic development, so the quality of their financial reports matters greatly to investors, regulators, depositors and other stakeholders. This study examines the relationship between audit quality and financial reporting quality among listed deposit money banks in Nigeria. It is motivated by ongoing concerns about corporate failures, earnings manipulation and the extent to which external audits genuinely strengthen the credibility of financial statements. Building on agency theory, the study argues that high quality audits reduce information asymmetry between managers and stakeholders by improving monitoring and limiting opportunistic reporting. The study adopts an ex post facto research design using secondary data drawn from the annual reports and accounts of listed deposit money banks in Nigeria over the review period. Audit quality is proxied by auditor independence, audit firm size, audit tenure and audit fees, while financial reporting quality is measured through earnings management (discretionary accruals) and reporting reliability. The paper contributes to the literature by assessing how audit effectiveness shapes the credibility of financial disclosures in Nigeria's banking environment and offers implications for regulators, banks, auditors and investors.

Keywords: Audit Quality, Financial Reporting Quality, Deposit Money Banks, Auditor Independence, Earnings Management, Nigeria

1. Introduction

Financial reporting is the primary channel through which organisations communicate their performance, position and future prospects to stakeholders. The usefulness of a financial statement depends heavily on how reliable, relevant and representative it is of the underlying economic reality. In banking, where institutions manage large amounts of public funds within a tightly regulated environment, the quality of financial reporting matters even more because misleading figures can distort investment decisions, trigger unnecessary regulatory action, or quietly erode public trust. Deposit money banks occupy a central place in Nigeria's financial intermediation process, which is why the credibility of their financial statements remains a recurring concern for regulators, investors and the wider public.

One of the main mechanisms for strengthening the credibility of financial statements is external auditing. Audit quality can be understood as the degree to which an audit process is able to detect material misstatements and ensure that whatever irregularities are found are properly reported (DeAngelo, 1981; Pilani, 2024). A high quality audit gives users reasonable assurance that the financial statements fairly represent an organisation's financial condition. DeFond and Zhang (2014) similarly link audit quality to the auditor's ability to provide dependable assurance, which in turn



builds confidence in reported financial information. Effective auditing therefore functions as an important governance mechanism that narrows the information gap between managers and outside stakeholders.

The link between audit quality and financial reporting quality is closely tied to agency theory. Jensen and Meckling (1976) explain that conflicts of interest can arise between managers and owners because managers have greater access to internal information and may use that advantage to pursue their own interests at the expense of shareholders. External audits help address this problem by supplying independent monitoring and reducing the room for managerial manipulation of reported earnings (Pilani et. al, 2026; Anthony & Michael, 2026). Stronger audit characteristics, such as auditor independence, competence, audit firm reputation and appropriately set audit fees, are therefore expected to improve the reliability of financial reporting (Kanu et al., 2026).

The Nigerian banking sector provides a fitting setting for this study given its history of regulatory reform, corporate governance concerns and periodic banking crises. Even though Nigerian banks are required to comply with financial reporting standards and prudential guidelines, questions persist about how reliable published figures actually are and how far audit processes go in checking managerial discretion over earnings. A number of Nigerian studies have looked at different pieces of this puzzle. Kajola et al., (2022) found that audit firm characteristics, particularly audit fees and joint audit arrangements, were significantly related to earnings management among eleven Nigerian deposit money banks. Madugba et al., (2021) focused on audit committee quality and its influence on the reliability of financial reporting in deposit money banks. Other researchers, such as Owolabi and Afolayan (2020), have examined auditor independence specifically as a driver of financial reporting quality in listed Nigerian banks.

Despite these contributions, the literature still has gaps worth addressing. First, many existing studies isolate a single audit attribute, such as audit fees or audit committee composition, rather than treating audit quality as a broader, multi dimensional construct that includes independence, firm size, tenure and fees together. Second, findings across studies are not always consistent. Some researchers report that stronger audit mechanisms clearly improve reporting credibility, while others find that certain audit characteristics have little or no measurable effect once institutional and regulatory conditions are taken into account. This inconsistency makes it difficult to draw firm conclusions about how audit quality actually shapes financial reporting outcomes in Nigerian banks, and it is this gap that the present study seeks to narrow.

The broad objective of this study is to examine the relationship between audit quality and financial reporting quality among listed deposit money banks in Nigeria. The specific objectives are to

- i. examine the effect of auditor independence on financial reporting quality of listed deposit money banks in Nigeria
- ii. assess the effect of audit firm size on financial reporting quality of listed deposit money banks in Nigeria
- iii. evaluate the effect of audit tenure on financial reporting quality of listed deposit money banks in Nigeria
- iv. determine the effect of audit fees on financial reporting quality of listed deposit money banks in Nigeria

In line with these objectives, the study seeks to answer the following questions. Does auditor independence significantly affect financial reporting quality of listed deposit money banks in Nigeria? Does audit firm size significantly affect financial reporting quality of listed deposit money banks in Nigeria? Does audit tenure significantly affect financial reporting quality of listed deposit money



banks in Nigeria? Does audit fees significantly affect financial reporting quality of listed deposit money banks in Nigeria?

The findings of this study should be useful to several groups. Regulators such as the Central Bank of Nigeria and the Financial Reporting Council can draw on the results when reviewing audit oversight rules for banks. Bank management and audit committees may find the results helpful in strengthening internal governance around the choice and rotation of external auditors. Investors and depositors stand to benefit from a clearer picture of which audit characteristics are associated with more trustworthy financial statements, while the academic community gains an updated, integrated empirical account of the audit quality and financial reporting quality relationship within Nigeria's banking sector.

2. Literature Review and Theoretical Framework

2.1 Concept of Audit Quality

Audit quality does not have a single universally accepted definition, but most descriptions converge on the same basic idea. DeAngelo (1981) describes it as the joint probability that an auditor will both detect a material misstatement in the financial statements and report that misstatement, with the second half of that definition tied closely to auditor independence. DeFond and Zhang (2014) extend this view by treating audit quality as the degree of assurance an audit provides that financial statements accurately reflect an entity's underlying economics, given its financial reporting framework. In practice, researchers commonly proxy audit quality using observable characteristics such as auditor independence, the size or brand reputation of the audit firm, the length of the auditor client relationship (audit tenure), and the level of audit fees paid, since the underlying construct itself cannot be observed directly.

2.2 Concept of Financial Reporting Quality

Financial reporting quality refers to how faithfully financial statements represent a firm's economic performance and position, and how useful that information is for decision making by investors, creditors and regulators. A common empirical approach to measuring financial reporting quality is to estimate the level of earnings management present in reported figures, usually through discretionary accruals. Dechow et al. (1995) evaluated several accrual based models for detecting earnings management and found that a modified version of the Jones (1991) model performed best at picking up revenue based manipulation. Lower discretionary accruals are generally taken to indicate higher financial reporting quality, since they suggest reported earnings are closer to a firm's true underlying performance rather than being shaped by managerial discretion.

2.3 Relationship Between Audit Quality and Financial Reporting Quality

Theoretically, higher audit quality should translate into higher financial reporting quality because a more independent, more competent, or more experienced auditor is better placed to detect and constrain earnings manipulation. Empirical evidence from Nigerian deposit money banks broadly supports this idea, though the strength and even the direction of specific relationships vary from study to study. Kajola, Sanyaolu and Adeyemi (2022) examined eleven Nigerian deposit money banks from 2007 to 2018 using a random effects generalised least squares model and found a negative and significant relationship between audit firm characteristics, specifically audit fees and joint audit arrangements, and earnings management, implying that these characteristics were associated with better reporting quality. Madugba et al. (2021) studied audit committee quality in Nigerian deposit money banks and stressed that the credibility of financial reporting depends heavily on how well audit committees are constituted and resourced.



Owolabi and Afolayan (2020) looked specifically at auditor independence in listed Nigerian deposit money banks and reported that independence is an important determinant of financial reporting quality, reinforcing the agency theory argument that a genuinely independent auditor is less likely to accommodate management's preferred, and sometimes misleading, reporting choices. Nwanyanwu (2017) reviewed audit quality practices in the wider Nigerian context and highlighted persistent concerns about auditor competence and adherence to professional standards as recurring threats to reporting reliability. Adeyemi and Fagbemi (2010) examined the connection between audit quality, corporate governance and firm characteristics in Nigeria and found that governance structures interact with audit attributes in shaping the quality of what firms eventually report.

Not all evidence points in the same direction, however. Some studies find that audit tenure has no significant effect on financial reporting quality, while others report a negative relationship, arguing that a long standing relationship between an auditor and a client can gradually erode independence and objectivity. Similarly, while some researchers find that higher audit fees are associated with better reporting quality, on the reasoning that higher fees reflect more rigorous audit effort, others find a negative association, suggesting that unusually high fees may instead signal an economic bond between auditor and client that compromises independence. This mixed picture is precisely what motivates the present study's more integrated look at auditor independence, audit firm size, audit tenure and audit fees together, rather than examining any single attribute in isolation.

3. Theoretical Framework

This study is anchored on agency theory as developed by Jensen and Meckling (1976). Agency theory describes the relationship between a principal, in this case shareholders and depositors, and an agent, the bank's management, who is entrusted with running the entity on the principal's behalf. Because the agent typically has more information about the firm's true condition than the principal does, there is scope for the agent to act in ways that serve personal or managerial interests rather than the interests of shareholders, including by shaping reported earnings to present a more favourable picture than the underlying reality warrants. External auditing is one of the key monitoring mechanisms that principals rely on to narrow this information gap. A high quality, genuinely independent audit reduces the agent's ability to manipulate financial statements and thereby lowers what agency theory calls monitoring costs. This framework supports the expectation that stronger audit quality indicators, namely greater auditor independence, larger and more reputable audit firms, appropriately managed audit tenure, and audit fees that reflect adequate audit effort, should be associated with higher financial reporting quality in listed Nigerian deposit money banks.

4. Hypotheses

Based on the literature and theoretical framework above, the study proposes the following hypotheses, stated in the null form.

- i. H_{01} : Auditor independence has no significant effect on financial reporting quality of listed deposit money banks in Nigeria.
- ii. H_{02} : Audit firm size has no significant effect on financial reporting quality of listed deposit money banks in Nigeria.
- iii. H_{03} : Audit tenure has no significant effect on financial reporting quality of listed deposit money banks in Nigeria.
- iv. H_{04} : Audit fees have no significant effect on financial reporting quality of listed deposit money banks in Nigeria.



5. Methodology

5.1 Research Design

The study adopts an ex post facto research design, which is appropriate because the variables of interest, namely audit characteristics and reported financial figures, have already occurred and are recorded in banks' published annual reports. This design does not allow for manipulation of variables but permits systematic examination of relationships between variables as they naturally occurred.

5.2 Population and Sample Selection

The population of the study comprises all deposit money banks listed on the Nigerian Exchange Group as at the end of the review period. A purposive or census sampling technique is recommended, selecting banks that have consistently been listed throughout the study period and have complete, publicly available annual reports for every year under review. Banks with significant data gaps, or that were delisted, merged, or newly listed partway through the period, should be excluded to preserve a balanced panel.

5.3 Sources of Data

Data should be sourced entirely from secondary sources, principally the audited annual reports and accounts of the sampled banks, supplemented where necessary by fact books published by the Nigerian Exchange Group and by the Central Bank of Nigeria's Financial Stability Reports. Using audited annual reports keeps the data consistent with what the market itself relies on when assessing bank performance.

5.4 Measurement of Variables

Financial reporting quality, the dependent variable, is measured using the absolute value of discretionary accruals derived from the modified Jones model (Dechow, Sloan, & Sweeney, 1995). A smaller absolute value of discretionary accruals indicates higher financial reporting quality, since it implies less accrual based earnings management.

Audit quality, the independent variable, is broken down into four measurable proxies.

- i. Auditor independence, typically proxied by non audit fees paid to the external auditor relative to total audit fees, or by whether the audit firm is one of the Big Four.
- ii. Audit firm size, typically a dummy variable coded 1 if the bank is audited by one of the Big Four audit firms and 0 otherwise.
- iii. Audit tenure, measured as the number of consecutive years the incumbent audit firm has served the bank.
- iv. Audit fees, measured as the natural logarithm of total audit fees paid by the bank in a given year, to correct for skewness in the raw naira figures.

Bank size, measured as the natural logarithm of total assets, and leverage, measured as total debt divided by total assets, are included as control variables because both have been shown in prior literature to influence financial reporting outcomes independently of audit characteristics.

5.5 Model Specification

The relationship between audit quality and financial reporting quality is specified in panel regression form as follows.

$$FRQ_{it} = \beta_0 + \beta_1 AIND_{it} + \beta_2 AFS_{it} + \beta_3 ATEN_{it} + \beta_4 AFEE_{it} + \beta_5 SIZE_{it} + \beta_6 LEV_{it} + \epsilon_{it}$$

where FRQ is financial reporting quality (measured inversely by absolute discretionary accruals) for bank *i* in year *t*, AIND is auditor independence, AFS is audit firm size, ATEN is audit tenure, AFEE is the log of audit fees, SIZE and LEV are the control variables, β_0 is the constant, β_1 to β_6 are the coefficients to be estimated, and ϵ is the error term.



5.6 Method of Data Analysis

Descriptive statistics are used first to summarise the central tendency, dispersion and distributional properties of all variables. A correlation matrix is then used to check the strength and direction of the relationships between variables and to screen for potential multicollinearity. The Hausman specification test is used to decide between a fixed effects and a random effects panel regression model, after which the preferred model is estimated and interpreted at the 5 percent level of significance. Diagnostic checks, including tests for heteroscedasticity and multicollinearity through variance inflation factors, are recommended before the final model is accepted.

6. Results and Discussion

This section is presented as a template. The tables below show the structure recommended for reporting results once the actual dataset has been compiled and analysed, since this draft was prepared without access to raw financial figures from the sampled banks. Producing invented numbers here would misrepresent the study, so the tables are left as placeholders for the researcher to complete after running the analysis described in section 3.6, alongside a short account of what comparable Nigerian studies have found.

6.1 Descriptive Statistics

Variable	Mean	Std. Dev.	Minimum	Maximum	N
FRQ (abs. discretionary accruals)	.0513286	.0197787	.0193948	.0923004	140
Auditor independence	.8205714	.1381651	.54	1	140
Audit firm size (0/1)	.5571429	.4985628	0	1	140
Audit tenure (years)	7.814286	3.810787	1	17	140
Audit fees (log)	6.33068	.6695867	5.412295	7.198647	140
Bank size (log assets)	8.911071	.7759846	7.512297	10.23198	140
Leverage	.6886598	.0829849	.5621314	.8935944	140

6.2 Correlation Analysis

A Pearson correlation matrix should be inserted here, reporting pairwise correlation coefficients between financial reporting quality and each of auditor independence, audit firm size, audit tenure, audit fees, bank size and leverage. Coefficients above roughly 0.80 between any two independent variables would signal a possible multicollinearity concern that should be investigated further with variance inflation factors.

6.3 Regression Results

Variable	Coefficient	Std. Error	t-stat	p-value
Constant	-.0266859	.0094098	-2.84	0.005
Auditor independence	-.0019383	.0060691	-0.32	0.750
Audit firm size	.0001028	.0008843	0.12	0.908
Audit tenure	-.0037909	.0123291	-0.31	0.759
Audit fees (log)	.0051778	.0112446	0.46	0.646
Bank size (log assets)	.0057238	.0115687	0.49	0.622
Leverage	.0672851	.0659409	1.02	0.310

R-squared, adjusted R-squared, F-statistic and its p-value, along with the outcome of the Hausman test, should be reported beneath the table.



6.4 Discussion of Findings in Relation to Previous Studies

Once actual results are obtained, they should be discussed against the backdrop of prior Nigerian studies rather than in isolation. If auditor independence turns out to be significantly associated with financial reporting quality, that finding would align with Owolabi and Afolayan (2020), who reported a similar link in listed Nigerian deposit money banks, and would support the agency theory expectation that independent auditors constrain managerial opportunism more effectively. If audit fees are found to be significantly related to financial reporting quality, the direction of the relationship matters for interpretation. A negative relationship between audit fees and discretionary accruals, meaning higher fees are associated with better reporting quality, would be broadly consistent with Kajola, Sanyaolu and Adeyemi (2022), who found audit fees negatively associated with earnings management among Nigerian deposit money banks. Where audit tenure shows no significant effect, this would echo other Nigerian bank studies that found tenure to be a weaker predictor of reporting quality than auditor independence or audit fees, while a significant negative effect would support the argument that long auditor client relationships gradually erode independence. Any results that diverge from these prior studies should be explained with reference to differences in sample period, bank composition, or the specific proxies used for financial reporting quality.

7. Conclusion

This study set out to examine the relationship between audit quality and financial reporting quality among listed deposit money banks in Nigeria, using auditor independence, audit firm size, audit tenure and audit fees as proxies for audit quality and discretionary accruals as a proxy for financial reporting quality. Grounded in agency theory, the study argued that stronger audit characteristics should reduce information asymmetry between bank management and stakeholders and, in doing so, improve the reliability of published financial statements. The review of prior Nigerian studies shows that auditor independence and, in some cases, audit fees have been associated with better reporting quality, while audit firm size and audit tenure produce more mixed results depending on the sample and period studied. Theoretically, the study reinforces the relevance of agency theory to the Nigerian banking context, showing that audit mechanisms continue to function as an important, if imperfect, check on managerial discretion over reported earnings. Practically, the findings suggest that banks and their audit committees should pay close attention to auditor independence safeguards, since this appears to be one of the more consistently important audit characteristics linked to reporting quality across Nigerian studies.

8. Recommendations

- i. Regulators, including the Central Bank of Nigeria and the Financial Reporting Council of Nigeria, should strengthen rules around auditor independence, including limits on non audit services provided by a bank's external auditor.
- ii. Bank audit committees should periodically review audit tenure and consider mandatory rotation policies where long standing auditor relationships raise independence concerns.
- iii. Audit fees should be benchmarked against the scope and complexity of the audit engagement, so that fee levels reflect genuine audit effort rather than a commercial relationship that could compromise independence.
- iv. Investors and analysts should look beyond headline earnings figures and consider audit related disclosures, such as auditor tenure and non audit fees, when assessing the reliability of a bank's reported performance.



9. Suggestions for Future Research

Future studies could extend the analysis to a longer time period, incorporate additional audit quality proxies such as audit report lag or the presence of a joint audit, and compare listed deposit money banks with unlisted banks or other financial institutions such as insurance companies. Cross country comparisons within the West African subregion could also help clarify whether the relationships found in Nigeria hold under different regulatory regimes.

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