THE NEXUS BETWEEN AUDIT COMMITTEE ATTRIBUTES AND KEY AUDIT MATTERS: EVIDENCE FROM INSURANCE INDUSTRY

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ABSTRACT
Key audit matters (KAMs) are important for financial statement users as they provide clarity and in-depth understanding of financial statement audits. Empirical research on KAMs remains at an early stage particularly in Nigeria. Therefore, this study aims to investigate the effect of audit committee attributes on KAMs of the listed insurance companies in Nigeria. The study sample consists of 24 insurance companies from 2016-2022. The data for the study which was generated from annual reports and accounts of the insurance companies was analyzed using random effect regression. The findings show that audit committee independence and audit committee financial expertise have a negative and positive relationship with the number of KAMs respectively. Consequently, the result provides support on the agency problem between manager and shareholders. Based on result, the *study recommends that regulatory bodies such as the National Insurance Commission (NAICOM) should continue to engage the insurance companies in the area of good corporate governance practices. This will go a long way in mitigating non-disclosure of vital information in the financial statements. Furthermore, the implication of this issue is that the financial statements cannot be relied for informed decision making.*

Keywords: Audit Committee Attributes, Key Audit Matters, Audit Committee Independence; Audit Committee Financial Expertise

INTRODUCTION

The introduction of International Standard on Auditing (ISA,701) is expected to provide relevant and useful information to the capital market, minimize uncertainty regarding company performance and encourage understanding of financial statements. The increasing argument as it relates to key Audit Matters have been adduced to the negative publicity that surround the service provided by the auditor. Such negative publicities are seen from the experience of corporate scandals witnessed globally. This has raised questions about the value of auditing and the role of auditors, particularly the quality of auditors' report. Consequently, resulted in the introduction of reforms meant to restore market confidence and enhance the credibility of the audit service and auditor report.

Following the widely publicised financial scandals, regulating bodies as well as accounting professionals and academics were engaged on how to enhance the quality of audits. They focus on the idea of extending audit reporting such that it will increase the information content thereby reducing the information asymmetry that prevails between auditors and users of the information (Pinto & Morais, 2019). Hence, this led to ISA 701 (Communicating Key Audit Matters in Independent Auditor's Report) which became effective for audits of financial statements for periods ending on or after December 15, 2016 in the European Union. Furthermore, the KAMs are expected to enhance the decision of user of financial information. According to a report Nigeria is ranked as the country with lowest number of KAM of 1.9 compared to Zimbabwe 3.2, Kenya 2.7 and South Africa 2.5 (Association of Chartered Certified Accountants, 2018).

Attributes of audit committees play a crucial role in enhancing good corporate governance, firm performance, mitigating financial statement manipulation, and corporate disclosures among others (Bala et al., 2020; Cohen et al., 2014; Jaffar, 2020; Kang, 2019; Sheidu et al., 2023). Research indicates that factors such as independence and financial expertise are relevant in the modern corporate entities and therefore, these factors can be employed to examines KAMs.

Several studies have investigated the consequences of KAMs on the decisions of investors or the liability of auditors (Bepari, 2023; Jaffar, 2020; Mah'd & Mardini, 2022; Wuttichindanon & Issarawornrawanich, 2020; Zaman et al., 2021; Zhang & Shailer, 2022). However, most of these studies are from the American, Europe, Asia and South American markets. Also, the literature has varying opinions on the influence audit committee attributes on KAMs. Furthermore, research to date indicates that the relationship between KAMs and audit committee characteristics has received less attention and inclusive. This study addressed a research vacuum by investigating the effect of audit committee attributes on KAM in Nigeria.

LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

Audit committee financial expertise and key audit matters

According to prior evidence, audit committee is important mechanisms for regulating opportunistic tendencies of agents (managers), and provide credibility to the financial reporting framework (Sheidu et al., 2023). Previous literature noted that audit committee is more effective when its members have financial or industry experience (Velte, 2018). We argue that the presence of financial expertise within audit committees will enhance their collaboration with external auditors, as supported by previous empirical findings (Cassell et al., 2012; Cohen et al., 2014; P Velte, 2018) Consistent with the agency viewpoint that an audit committee provides more oversight and demands better coverage of the audit, which results in a higher quality of audit, as well as better disclosure (Schrader & Sun, 2019).

Bepari (2023) examined the effect of audit committee members' accounting and finance backgrounds on KAMs. The study employed a sample of 1112 firm-year-observations spanning for the period 2017–2020. The study found that audit committee members' accounting and finance backgrounds has a positive effect on KAMS. Hence, encouraging the production of more readable KAMs. Also, Velte, (2020) conducted an analysis on the relationship between the financial and industry expertise of audit committee members and key audit matters within UK premium listed companies for the fiscal years 2014–2017. The study documented a positive and statistically significant correlation between audit committee expertise and significant key audit matters. Wuttichindanon and Issarawornrawanich, (2020) examined the determining factors of key audit matters in SET-listed firms for the fiscal year-ends 2016 and 2017. The study revealed a positive but insignificant association between audit committee expertise and key audit matters. Moreover, Mah'd and Mardini (2022) investigated the extent of the disclosure of key audit matters (KAMs) and the factors that affect the level of KAMs' disclosure in the audit reports of the Middle East (ME) region. Using a sample of 281 firms from four countries (Oman, the UAE, Bahrain, and Jordan) for four years (2017–2020), comprising 1124 observations. The findings show that audit committee financial expertise positive and significant association with key audit matters. Suggesting that financial expertise in audit committee support more disclosures of KAMs.

However, the result reported by Zhang and Shailer (2022) indicate that audit committee accounting expertise reduces the level key audit matters. In a

Malaysian Jaffar (2020) in their study reported an insignificant relationship between audit committee accounting expertise level key audit matters.

Based on extant studies, it is conceivable that financial expert in audit committee may cooperate more with the outside auditor and have greater motivation in terms of decision that are useful in audit reporting. In Nigeria, the Securities and Exchange Commission Corporate Governance of 2011 and the financial reporting council of Nigeria mandated that all listed companies to have member(s) who has knowledge in accounting. Velte (2020) argued that since stockholders demand a readable KAM section in the audit report, the audit committee's financial expertise may likely encourage lower information asymmetry and less conflicts of interest. Consequently, the study hypothesised that

H1: There is a significant relationship between audit committee financial expertise and key audit matter.

Audit committee independence and key audit matters

Independent directors in the audit committee are expected to play a significant role in strengthening firms internal control systems and financial statement oversight. Jaffar (2020) posited that independent directors in the audit committee improves the monitoring efficacy and fairness when assessing the internal control, accounting, and reporting procedures of the business. Additionally, having more independent audit committee members decrease the likelihood that a company will receive the modified audit opinion (Carcello & Neal, 2003). Members of the independent audit committee are supposed to suggest mitigation strategies in the event that businesses experience financial difficulties or that an external auditor runs into issues while conducting the audit. The tendency of receiving higher quality sustainability becomes more as companies have more independent directors in audit committee (Zaman et al., 2021). Sheidu et al. (2023) in the study found strong evidence that independent directors on audit committee have a negative impact on audit lag. Indicating that these directors on the audit committee diminishes the likelihood of delaying financial statements reporting. Consequently, improves financial reporting processes. Al-Shaer and Zaman (2018) provide evidence that audit committee independence positively influences the demand for sustainability assurance. Corporate officers can make decisions that are best for the company and its stakeholders when they have independent directors and this constitutes one of their crucial attributes. Previous research demonstrates that the independence of an audit committee is crucial for encouraging the careful oversight and monitoring of financial audits (Zaman et al., 2021). Consistent with agency theory, Zaman et al. (2021) revealed that audit committee independence, improves the quality of sustainability assurance statement.

Numerous studies have shown that the audit committee is crucial to both monitoring the integrated reporting process and enhancing the calibre of audit reports (Schrader & Sun, 2019; Velte & Issa, 2019; Mah'd & Mardini, 2022). For example, Velte and Issa (2019) reported that audit committee independence improved audit reporting. Wuttichindanon and Issarawornrawanich (2020) documented a positive association between independent directors in audit committee and key audit matters. In line with previous studies, independent directors in audit committee are expected to have an influence on key audit matter. Therefore, the study hypothesised that

H2: There is a significant correlation between independent directors in audit committee and key audit matter.

Material and Methods

This study uses data from secondary source. Panel data regression was used to conduct the analysis. The population of the study consist of all insurance companies listed on the Nigerian Exchange Group (NGX). Out of which 24 companies were selected based on the availability of data to be used during the analysis. The study covers a period of seven (7) years from 2016 to 2022 and the data were collected from the annual reports and accounts of the listed insurance companies downloaded at websites of the NGX and the companies.

In line with the prior studies, this research uses KAMs as a dependent variable. The study focuses on less explored variables in the study of KAMs. These variables are audit committee financial expertise and independent directors in audit committee. In addition to these variables and consistent with previous studies, firm size and audit firm were used as two control variables for the study. Detail information about these variables is presented in table 1 below.

Table 1. Variable measurement and source

S/N	Variables	Acronyms	Measurement and source
Dependent variable			
1	Key Audit Matters	KAMs	KAM is the number of disclosed KAMs at fiscal year end divided by the number of KAMs of the sampled firms (Jaffar, 2020; Pinto & Morais, 2019)
Independent variables			
2	Audit committee Independence	ACIND	Percentage of independent members on the audit committee (Sheidu et al., 2023)
3	Audit Committee Financial expertise	ACFEX	Number of members of the audit committee with a background in accounting and/or finance (Wuttichindanon & Issarawornrawanich, 2020)
Control variable			
4	Audit firm Size	AUDF	Dichotomous variable equal to 1 if the company is audited by Big four auditor and 0 otherwise (Mah'd & Mardini, 2022)
5	Fim Size	FSZE	Natural log of total assets (Mah'd & Mardini, 2022)

Model of the study

The following model is employed to test two hypotheses developed in this study.

$KAMs_{it} = \beta o + \beta_1 ACIND_{it} + \beta_2\ ACFEX_{\ it} + \beta_4 AUDF_{it} + \beta_3 FSZE_{it} + e_{it}$

Where:

$KAMs_{it}$ = Key audit matters

$\beta 0$ = Constant

$ACIND_{it}$ = Audit Committee Independence

$ACFEX_{it}$ = Audit Committee Financial Expertise

$AUDF_{\ it}$ = Audit Firm Size

$FSZE_{it}$ = Firm Size

ε_{it} = Error term

RESULTS AND DISCUSSION

Summary statistics

Table 2 shows the summary statistics of the variables used in the study. The key audit matters (KAMs) have a mean value of 84.5% with a minimum and maximum values of 65.5% and 99.9% respectively. From the result of the summary statistics in Table 2, it shows that the sample firms have on the average 49% members in the audit committee who are independent (ACIND). However, the minimum percentage of these members are 16% and a maximum of 85.7%. regarding the second independent variable, Table 2 reveals that the mean value of audit committee expertise (ACFEX) is 28.3% with a minimum value of 0 and a maximum of 100%.

Table 2. Summary statistics

Variable	Obs.	Mean	Std. Dev.	Min	Max
KAMs	168	0.845	0.088	0.665	0.999
ACIND	168	0.490	0.104	0.167	0.857
ACFEX	168	0.283	0.281	0.25	0.900
AUDF	168	0.560	0.498	0.000	1.000
FSZE	168	5.375	0.840	3.247	6.684

Note: all the measurements of the variables are captured in Table 1. KAMs = key audit matters, ACIND = audit committee independence; ACFEX = audit committee financial expertise; AUDF = Audit firm; FSZE = firm size.

Correlation matrix and VIF test

From Table 3 there is a negative correlation between key audit matters and audit committee independence with a value of -0.099. However, the correlation between key audit matters and audit committee financial expertise is 0.038 which is positive. With reference to the control variables, audit firms (AUDF) and firm size (FSZE) have a positive and negatively correlation with key audit matters respectively.

Table 3 correlation matrix and VIF results

VAR	KAMs	ACIND	ACFEX	AUDF	FSZE	VIF	1/VIF
KAMs	1.000					-	-
ACIND	-0.099	1.000				1.09	0.917
ACFEX	0.038	-0.081	1.000			1.05	0.950
AUDF	0.126	0.128	0.086	1.000		1.08	0.926
FSZE	-0.017	-0.089	-0.1773*	0.069	1.000	1.05	0.950

Note: all the measurements of the variables are captured in Table 1. KAMs = key audit matters, ACIND = audit committee independence; ACFEX = audit committee financial expertise; AUDF = Audit firm; FSZE = firm size.

Apart from the correlation between the dependent and independent variables reported in Table 3. it also presents the correlation among the independent variables. From the results in this Table, there is a low correlation on the average. While the observed correlations reveal useful information about the relationships between variables, it is important to remember that correlation does not indicate causation. The discovered associations point to trends in the data but establishing a cause-and-effect relationship requires further rigorous analysis.

The results of regression analysis can be distorted by multicollinearity, resulting in inaccurate standard errors and unreliable coefficient estimates. We increase the robustness and accuracy of our estimations by evaluating and guaranteeing low VIF values, offering more reliable insights into the relationships between the regressors and the dependent variable.

Table 3 shows the findings of a multicollinearity test, evaluating the Variance Inflation Factor (VIF) of each independent variable. From the result, comparatively each variable has low VIF values, ranging from about 1.05 to 1.09. These values imply that the independent variables in the model have no multicollinearity threat. Low VIF values are desirable because they show a lack of strong correlation between the variables. This is essential for precise coefficient estimation and dependable inference in regression analysis.

Table 4. Regression results

VAR.	Coef.	Std. Err.	z	P>z
ACIND	-0.094	0.035	-2.690	0.007
ACFEX	0.035	0.018	1.950	0.051
AUDF	0.020	0.008	2.620	0.009
FSZE	-0.009	0.007	-1.350	0.176
_cons	0.920	0.041	22.230	0.000
Overall R^2	0.0121			
Wald chi2	20.78			
Probability	0.000			
Hausman Chi2	0.99			
Probability	0.912			
Breusch & Pagan LM test				
Chibar2:	276.85			
Probability:	0.000			

Note: all the measurements of the variables are captured in Table 1. KAMs = key audit matters, ACIND = audit committee independence; ACFEX = audit committee financial expertise; AUDF = Audit firm; FSZE = firm size.

Result of the regression

Table 4 reports the impact of audit committee attributes on key audit matters. The estimation is based on random effect model as suggested by the result of Hausman test (Chi2 = 0.99 Prob>chi2 = 0.9119) that favours it. We also conducted Breusch and Pagan LM test and the results supports the use of random effect model. The is presented in the Table 4. Consequently, the result discussion is based on random effect model.

Consistent with hypothesis one, audit committee independence (ACIND) has a coefficient of -0.094, z-statistic of -2.690, and a probability of 0.007, thus negatively impacting key audit matters and being statistically significant at a 1% level. The result indicates that having greater percentage of independent audit committee members may lead to lower disclosure key audit matters. The result is consistent with the findings of Jaffar (2020) but disagrees with Wuttichindanon and Issarawornrawanich (2020) and Velte (2020).

Audit committee financial expertise (ACFEX) has a coefficient of 0.035, z-statistic of 1.950, and a probability of 0.051, hence positively influencing KAMs and being statistically significant at 10% level. This result implies that the greater the number of financial expertise in audit committee the higher the disclosure of the key audit matters. This result lend supports to the hypothesis two. In this regard, the result is in agreement documented in the study conducted by Velte (2020), Bepari (2023), and Mah'd and Mardini (2022). Nevertheless, it contradicted the evidence reported by Zhang and Shailer (2022).

The results of the two control variables are also documented in Table 4. The results reveal that the coefficient of audit firm (AUDF) is 0.020 and a probability of 0.009 indicating its significance at 1% level. This shows that Big four audit firms have a considerable impact on key audit matters on the sample firms. This result goes along with the previous findings (Al Lawati & Hussainey, 2022; Mah'd & Mardini, 2022; Patrick Velte, 2020; Wuttichindanon & Issarawornrawanich, 2020) that reported positive association between audit firm (Big four and non-Big four) and key audit matters. Hence, the result indicates that having Big four audit firm will influence more the disclosure of key audit matters in the financial statements.

The result of the second control variable firm size is tabulated in Table 4. The result shows that firm size has no significant effect on key audit matters even though their relationship is negative. The result corroborates with the findings of (Wuttichindanon & Issarawornrawanich, 2020) in terms of its insignificance. However, it disagree with (Jaffar, 2020) that reported positive and statistically significant relationship between firm size and key audit matters.

CONCLUSION AND RECOMMENDTAIONS

KAMs are important for financial statement users as they provide clarity and in-depth understanding of financial statement audits. The primary aim of this study is to analyze the effect of audit committee attributes on KAMs Using random effect regression, the findings show that audit committee independence and audit committee financial expertise have a negative and positive relationship with the number of KAMs respectively. Consequently, the result provides support on the agency problem between manager and shareholders. Based on result of the study recommends that greater oversight and better coverage of KAMs are necessary.

The study finally recommended that regulatory body should continue to strengthen the composition of the audit committee in the insurance companies This will go a long way in mitigating issues relating to KAMs in the financial statements. Furthermore, companies that failed to comply with the extant regulation with regards to KAMs need to the sanction appropriately.

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