



Audit Committee Attribute and Corporate Social Impact

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Abstract

This study evaluated the effect of audit committee attribute on corporate social impact as reflected in their corporate social performances. The population and sample of study is 5 quoted conglomerates in Nigeria. This study adopts ex-post facto research design in extracting data from annual reports of the companies in the period from 2013 to 2022. Ordinary least square regression technique was employed in testing the data so gathered. Results from the analysis revealed that audit committee size has significant positive effect on corporate social performance. Sequel to this, it is concluded that audit committee attribute significantly affect corporate social impact. This study recommends that particular attention should be given to audit attribute while constituting audit committees as this has been revealed to have direct effect on the level of impact a firm makes in the society.

Keywords: Audit committee size; Labour force participation; Legitimacy theory; corporate social performance; Social responsibility performance

Introduction

Corporate social impact has over the years earned more attention in academic, corporate environment, government and international communities with the shift of emphasis from shareholder wealth creation to stakeholder wealth creation through value creation. This is due to the fact that financial performance emphasis by corporations has caused more harms than good to the stakeholders [1,2]. Currently there is heightened focus on sustainability performance of business entities than on how much a business reports in its economic bottom-line. Corporate social performance is therefore one of the nexus of sustainability performances which measures corporate social impact of a company within its social environment. Corporate social performances and corporate and corporate social responsibility have been used interchangeably in past studies as they both aim to achieve certain obligations and accountability towards the society [3]. Even though there are legal requirements in some countries for social responsibility performances, firms are still expected to voluntarily perform more than these expected requirements which social performance disclosure is one of such in line with the performance reporting

Guidelines provided by the Global Reporting Initiatives [4,5]. This study extends the frontiers of the relationship between corporate governance and sustainability performance of firms. The most critical role of corporate governance (CG) is to ensure good reporting quality including disclosure of social performance information of a firm [6].

Audit committee is one of the bodies that make up the corporate governance structure of business entities. The Audit Committee is an independent auditing body established to supervise management by controlling its reporting activities, to improve the transparency and quality of information disclosure. It is asserted that an audit committee with the right attributes ensures that corporations adequately involve in social responsibility performances and quality information disclosure relating to such performances [7]. An effective audit committee is therefore expected to curb under-performance and poor disclosure of social performance, opportunities behaviour, facilitate the diffusion of innovative practices and increase the credibility of annual performance reports [8-11]. Argued that firms with smaller audit committee size perform better in terms of compliance with information disclosure. Some other studies have been conducted more recently to explain

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the relationship between audit committee and corporate social performances in Korea, European countries, China, Australia [12,13]. However, evidences from other countries may not be generally applicable to underdeveloped economy like Nigeria where the monitoring of corporate social performance is still debatable as these are noted to be affected by the peculiarities of both social and cultural environment of each of the country in which a firm operates. Sequel to this, this current study therefore extends the research on the relationship between audit committee and corporate social performance from the perspective of an underdeveloped economy, with particular attention on Nigeria. This is achieved by investigating the extent to which audit committee size affects the level of corporate social performance.

Literature Review

Audit committee attribute

Audit committee is a committee of the Board of Directors, charged with the responsibility to oversee financial reporting processes and quality reporting. Corporate board of directors establishes an audit committee to assist in discharging its fiduciary responsibilities. How the committee fulfills that mandate varies according to its clarity of the committee's mission, the abilities of the committee's members, and the tone set at the top of the governance structure. An audit committee that operates effectively is a key feature in a strong corporate governance culture, and can bring significant benefits to the company. An effective audit committee reflects a procedure which ensures that the external auditor achieves the fundamental objective of obtaining reasonable assurance that the financial report as a whole is free of material misstatement and that the financial reporting system follows stipulated guidelines and meets stakeholders' expectations. In other words, the primary role of an audit committee is to conduct the internal audit of a business, including the financial reporting quality and evaluation of areas where judgment and decisions are significant, with the aim of minimizing information asymmetry between management and various stakeholders [14]. Audit committee attributes are the qualities, factors or characteristics which distinguish and describes a given audit committee. The different measures of audit committee attributes as have been used in past researches include, audit committee independence, audit committee gender diversity, academic qualification of members of the committee, work experiences, number of committee meetings and audit committee size.

This study measures audit committee characteristic using audit committee size. The numbers of persons that are members of an audit committee make up audit committee size. Committee size is an attribute considered pertinent to the successful discharge of a company's reporting duties (Cadbury Committee 1992; CIMA 2000). As contained in Companies and Allied Matters Act, the

audit committee size for a Nigerian public company should have five (5) members comprising three shareholders and 2 non-executive directors one of which must belong to a professional accounting body [15]. This is however in line with the provisions of the Nigerian Code of Corporate Governance 2018 which also requires one of the members of an audit committee to be a financial expert. The essence of the professional and financial background of the committee is to help in identifying relevant disclosure requirements and applicable standards, thus, ensure effective and efficient delivery of the expected duties. In addition, it will help the committee keep abreast of information regarding additional performance or disclosure requirements and Guidelines like the current demand for sustainability reporting which includes corporate social performance reporting. Before the enactment of CAMA 2020, the earlier version required the committee to be made up of 6 members as committee size equally comprised of directors and shareholders. The contentious issue here is whether the size of audit committee has any effect on delivery especially as it relates to corporate social performance and its disclosure. Some researchers have tried to provide answers to this but the outcomes remain inconclusive. Larger audit committees are perceived as having increased organizational status and authority [16]. It is also possible that an audit committee can become too large to effectively carry out its duties because of process losses and diffusion of responsibility. In a study, it was reported that higher number of directors in the audit committee aid faster resolution of internal issues relating to reporting, including corporate social responsibility performance reporting [17]. Opines that "A large-size audit committee possesses more members to gather information and expend monitoring effort. It is also more difficult for the management to exercise influence over a large-size audit committee". In another study, found that required disclosures in financial statement reporting were higher for companies with smaller audit committees. Found support for the efficiency of smaller committees when they showed that companies with smaller audit committees were more likely to make earnings forecasts than those with larger committees [18]. Therefore, audit committees require sufficient members to generate a critical mass, but become ineffective if they are too large. Emanating from this, our hypothesis for this study is developed as;

Ho: Audit committee size has no significant effect on corporate social performances.

Corporate social impact

Corporate social impact is a term reflective of a business ability to operate its activities with the least negative impact while creating maximum value for the stakeholders. It reconciles the social performance of an enterprise with its corporate social responsibilities. Corporate social performance is the deliberate actions of a business towards its stakeholders (people within and

outside the business, including the business environment) as backed by organizational rules and principles. Corporate social performance is a broad term which includes stakeholder relations and corporate social reporting. This reporting aspect of corporate social performance is where the audit committee comes into play as an effective audit committee prevents the reporting of social activities that do not reflect a true and fair view of the relationship between the business and its stakeholders. The concept of corporate social performances stems from corporate social responsibilities. Corporate social responsibility is a concept which allows corporate organizations to integrate social and environmental concerns into their business operations and external relations with stakeholders. Developments in social responsibilities overtime with the introduction of the sustainability management into business management have standardized the concept of corporate social responsibilities, hence the focus on corporate social performance. Social responsiveness is viewed by as involving the “intra organizational factors affecting the implementation of social performance within firms and make it possible to carry out wide-scale business models”. In a release by the Global Reporting Initiative (GRI, 2019), on sustainability disclosure, Corporate Social Performance (CSP) is considered as business performances revolving around: labour force participation and employee welfare, abolition of child labour and forced labour, security practices, protection of rights of indigenous people, impact assessments, remediation of human right violations, social safety of local communities, corruption, public policy, anti-competitive behaviour, compliance with laws and regulations, assessment of product health and safety, product or service labelling, etc. Emanating from these, this study chooses to measure corporate social performance using their performance metrics as Labour force participation and Employment distribution.

Legitimacy theory

In organization’s perspective legitimacy has been defined by Lindblom (1994; as cited in Deegan, 2007) as a condition or status which exists when an entity’s system is congruent with the value system of the larger social system of which the entity is a part. When a disparity, actual or potential, exists between the two value systems, there is a threat to the entity’s legitimacy. Legitimacy theory is derived from political economy theory and relies on the idea that the legitimacy of a company to operate in society depends on an implicit social contract between the company and society. Managers continually attempt to ensure that their company complies with its social contract by operating within society’s expectations. This suggests that managers have incentives to disclose information that indicates that the company is not in breach of the norms and expectations of society (Deegan & Blomquist, 2006 as cited in Kent & Stewart, 2008). Organizational legitimacy is summarized by Lindblom (1983, as cited in Mathews

& Perera, 1996) as not synonymous with economic success or legality but determined to exist when the organization goals, output, and methods of operation are in conformance with societal norms and values. Its challenges are related to size of the organisation and to the amount of social and political support it receives with the more visible being most likely to be challenged. Legitimacy challenges may involve legal, political or social sanctions. Mathews and Perera states further that the implications which the notion of organisational legitimacy have for the management of corporation include better communication with society. This enlarged accounting or accountability may be essential for the continued existence of the corporation in its present form. Guthrie & Parker (1989 as cited in Naser, Al-Hussaini Al-Kwari & Nuseibeh (2006) emphasize that under legitimacy theory therefore, the company attempts to maintain its survival and continuity by voluntarily disclosing detailed information to society to prove it is a good citizen. In line with this, the audit committee is expected to focus on ensuring the proper reporting of social performances within stipulated Guidelines.

Empirical reviews

The profusion of empirical studies in line with our concepts of study include the work which examined the relationship between audit committee, Corporate Social Responsibility and Earnings Quality of firms in Korea. The multiple regression analysis carried out on generated data showed that earnings management in areas of social performances is restrained. The study also reported that audit committee is more effective when they are made up of independent directors, active participation and relative power (large number is assumed to strengthen the committee). Investigated the moderating role of audit quality in the relationship between ESG factors and financial performance of 620 firms in Western European countries (Austria, France, Belgium, Germany, Luxembourg, Netherlands, Monaco, Europe and Switzerland from 2010 to 2019). The panel data regression analyses revealed that audit quality has significant effect of CSR but no relationship with financial performance. Examined the role and relationship of audit committees in social responsibility with environmental disclosures of Chinese energy firms. A balanced panel data set was used in the study and tested using fixed-effect models and regression analysis. Findings from this study indicated that female representation has significant positive effect on the likelihood of firms to issue social responsibility reports. Further evidence shows that audit committee independence, effectiveness has no positive effect on corporate social responsibility performance and disclosure. However the variables used in the study failed to cover audit committee size and its effect on CSR performance and disclosure. Investigated the impact of audit committee characteristics on biodiversity disclosure of listed Chinese firms using secondary data from 2012 to 2018. Fixed- effect panel data regression was used in testing the

formulated hypotheses and it was shown that committee size, number of meetings, financial expertise and gender diversity significantly and positively impact biodiversity disclosure. Investigated the relationship between audit committee characteristics and CSR disclosures of firms in Australia. Committee size, gender sensitivity (combination of male and female genders in composition), independence and frequency of audit committee meetings were used to measure audit committee characteristics. The data for the study were gathered from 300 listed firms in Australia. The regression analysis revealed that size, gender sensitivity, and others, have significant positive influence on CSR performance and disclosure.

Researched on the social and environmental aspects of business investment and financing that are becoming increasingly important. They contended that most studies on corporate social responsibility (CSR) focus on analysing the relationship between company performance in the financial and social fields. However, the results obtained have not been conclusive, mainly due to the variables used to measure CSR. In order to simplify its measurement, they used an empirical analytical method to determine possible differences between the financial variables of firms considered being socially responsible and those not considered to be such. The results obtained show that socially responsible corporations obtain higher profits for the same level of systematic risk and show greater sensitivity to market changes, leverage levels and company size. Examined whether business performance is affected by the adoption of practices included under the term Corporate Social Responsibility (CSR) by examining the relationship between Corporate Social Responsibility and certain accounting indicators. The study specifically investigated the differences in performance indicators between European firms that have adopted and firms that have not adopted Corporate Social Responsibility accounting and disclosure. The effects of compliance with the requirements of CSR were determined on the basis of firms included in the Dow Jones Sustainability Index (DJSI), and specific accounting indicators were applied to measure performance. They selected one group of firms belonging to the DJSI and another comprised of firms quoted on the Dow Jones Global Index (DJGI) but not on the DJSI. The sample was made up of two groups of 55 firms, studied for the period 1998–2004. Empirical analysis supports the conclusion that differences in performance exist between firms that belong to the DJSI and that these differences are related to CSR practices. They find that a short-term negative impact on performance is produced. In a different way from previous literature, took a new approach to study the factors that affect audit opinion [19]. They examined the corporate governance factors and its role in enhancing audit quality and in turn, the likelihood of receiving qualified audit report. Using logistic regression and matched pair design they tested the influence of ownership concentration, board ownership, board size

and number of family member in the board. The results of study, in one hand support that higher insider ownership provides better corporate governance leading to higher financial reporting quality, thus, the less likelihood to received qualified opinion. It is because the degree of alignment between shareholders and managers' interest which motivate mangers to act in the interest of company and prepare financial statements that are less likely to attract audit qualifications.

Methodology

The population of study was 5 quoted conglomerates in Nigeria and the study covered 10years from 2013 to 2022. The research design employed in this study was the Ex-post Facto research design. The secondary data that relates to relevant information were sourced from annual reports of the companies for the relevant years. The subjected the data generated to empirical testing using the Ordinary Least Square Technique aided with E-views software (V.9). The below model guided the empirical test as formulated for the purpose of this study;

$$LFP_{it} = \beta_0 + \beta_1 AUC_{it} + E_{it}$$

Equa- 1

Where:

β_0 = Constant term (intercept)

β_{it} = Coefficients to be estimated for firm i in period t

E_{it} = Error term/unexplained variable(s) for firm i in period t

LFP = Labour force participation/ Employment distribution by company i in period t

AUC = Audit committee

Analysis and Results

Ho: Audit committee size has no significant effect on social measures of selected quoted industrial goods firms in Nigeria.

$$LFP_{it} = \beta_0 + \beta_1 AUC_{it} + E_{it}$$

Interpretation of regression results and discussions

The ordinary least square regression analysis in table 1 was conducted to test the effect of Audit committee size on labour force participation (Table 1). Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable. From the above table, the value of adjusted R squared was 0.602, an indication that there was variation of 60% on the firm sustainability (Social Measures) of Industrial goods companies due to changes in AUC. This shows that only 60% changes in labour force participation of Industrial goods companies could be accounted for by changes in audit committee size. The Durbin-Watson Statistic of 1.484171 suggests that the model does not have serial correlation problem. The F-statistic of the regression is equal to 0.020339 and the associated F-statistic probability is equal to 0.000121. Since the result of the

Prob (F-statistic) of 0.000121 is less than the critical value of 5% significance level, it implies that there is significant positive link between audit committee size and LFP at 5% significant level, hence our formulated hypothesis is rejected as results have shown

that audit committee size has significant positive effect on labour force participation rate of selected quoted industrial goods firms in Nigeria.

Table 1: Ordinary Least Square regression showing the effect of AUC on LFP.

Dependent Variable: LFP				
Method: Least Squares				
Date: 18/05/2023 Time: 05:31				
Sample: 2013 2022				
Included observations: 10				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	3.786982	0.631010	6.001458	0.0003
AUC	-0.017751	0.124472	-0.142615	0.0001
R-squared	0.602536	Mean dependent var		3.700000
Adjusted R-squared	-0.522147	S.D. dependent var		0.483046
S.E. of regression	0.511697	Akaike info criterion		1.674690
Sum squared resid	2.094675	Schwarz criterion		1.735207
Log likelihood	-6.373451	Hannan-Quinn criter.		1.608303
F-statistic	0.020339	Durbin-Watson stat		1.484171
Prob(F-statistic)	0.000121			
Source: Researchers' Computation with E-view 9				

Contrary to our apriori expectation, the result generated is very much in agreement with recent evidences emanating from advanced nations. In Korea, in examining the relationship between audit committee size and corporate social responsibility reported that relative power strengthens the committee. In China similarly reported that committee size significantly affect the disclosure of corporate social impact (bio-diversity disclosure). Further in line with our finding, in Australia also found that committee size have significant positive influence on corporate social performance and disclosure.

Conclusion, Implication and Recommendations

This study examined the effect of audit committee attribute on corporate social impact from the point of social performance. Corporate social performance was narrowed down to the aspect of labour force participation and employment distribution. The findings generated above leads the researchers to the conclusion that audit committee attribute have significant positive effect on corporate social performance. The implication of this is that small sized audit committee may not have the power to ensure adequate performance and reporting of information relating to the social impacts of a company's activities. There is need to improve on corporate governance practice in the West Africa to enhance the sustainability of the institutions. By recommendation, regulatory authorities should ensure that manufacturing firms in general, comply strictly with applicable corporate governance codes on

audit committee constitution and appropriate sanctions should be meted to erring firms. It is further recommended that particular attention should be given to audit attribute while constituting audit committees as this has been revealed to have direct effect on the level of impact a firm makes in the society.

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