

Effect of Audit Firm Tenure on Earnings Quality of Quoted Industrial Goods Companies in Nigeria

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Abstract

The study examined the effect of audit firm tenure on earnings predictability and earnings persistence of quoted industrial goods companies in Nigeria. Two research objectives, research questions, and hypotheses were formulated to guide the investigation. The study adopted an ex-post facto research design and relied on secondary data extracted from the published annual financial statements of industrial goods companies listed on the Nigerian Exchange Group. The population comprised all quoted industrial goods companies, and a census approach was employed. Data were analyzed using descriptive statistics and Ordinary Least Squares (OLS) regression techniques. The findings revealed that audit firm tenure has a positive and significant effect on both earnings' predictability and earnings persistence, indicating that longer auditor–client relationships enhance the reliability, stability, and quality of reported earnings. These results align with previous empirical evidence and suggest that sustained audit engagements improve auditors' understanding of client operations, thereby strengthening financial reporting outcomes. It was concluded that audit firm tenure significantly enhances earnings quality in the industrial goods sector in Nigeria. The study recommends that regulatory authorities promote structured long-term audit engagements that support audit quality while safeguarding auditor independence, and that companies engage audit firms with proven records of long-term expertise to improve stakeholders' confidence in financial reporting.

Keywords: *Audit Firm Tenure, Earnings Predictability, Earnings Persistence, Industrial Goods Companies, Financial Reporting Quality*

Introduction

Audit quality has increasingly become a central concern in the corporate reporting environment, especially in emerging economies such as Nigeria where governance frameworks are still evolving. One of the most critical determinants of audit quality is the set of attributes possessed by audit firms, including their tenure, independence, size, and expertise. These attributes collectively influence the extent to which external auditors can deliver objective and reliable assurance on financial statements. In the context of industrial goods companies quoted in Nigeria, whose financial reporting outcomes shape investor confidence and capital market stability, understanding how audit firm attributes influence earnings quality is of substantial importance (Okolie & Izedonmi, 2014). Given the centrality of earnings information in investment decisions,

the relationship between audit characteristics—particularly audit firm tenure—and earnings quality demands rigorous examination.

Earnings quality represents the degree to which reported earnings reflect a firm's true economic performance and can reliably predict future earnings. It is directly linked to the credibility of financial reporting and is influenced by managerial discretion, regulatory enforcement, and oversight mechanisms, including audit quality (Dechow, Ge & Schrand, 2010). For quoted industrial goods companies, which operate in capital-intensive sectors with long production cycles and volatile cost structures, the quality of earnings becomes even more critical for assessing sustainability and long-term profitability (Adebayo & Akinbobola, 2021). Audit firm attributes play a central role in shaping this quality, as strong audit oversight can constrain earnings manipulation and enhance predictability and persistence. Conversely, weak audit attributes may enable opportunistic earnings management that reduces the reliability and transparency of financial reports.

Audit firm tenure defined as the length of the auditor–client relationship is a particularly important attribute because it may either strengthen audit quality or undermine it, depending on the circumstances. While long tenure can improve auditors' understanding of client operations and industry trends, thereby enhancing the detection of irregularities, it may also create familiarity threats that compromise independence and objectivity (Gul, Chen & Tsui, 2009). In Nigeria, where the audit environment has been historically challenged by issues of auditor independence and regulatory compliance, the effect of tenure on earnings quality is even more significant (Uwuigbe et al., 2018). The debate on whether longer tenure enhances or worsens earnings quality remains unresolved, creating a compelling justification for empirical investigation within the Nigerian industrial goods sector.

Regulatory agencies such as the Financial Reporting Council of Nigeria (FRCN) and the Securities and Exchange Commission (SEC) have introduced measures aimed at improving auditor independence and strengthening audit quality. These include guidelines on mandatory partner rotation and increased disclosure requirements concerning audit relationships (FRCN, 2014). However, despite these reforms, instances of financial misstatements and earnings irregularities persist across several quoted companies, suggesting potential weaknesses in the audit process. This raises critical questions about whether audit firm attributes, particularly tenure, are functioning as expected in improving the credibility of financial reporting among Nigerian industrial goods firms (Oladipupo & Obazee, 2020). The persistent challenge of earnings manipulation in Nigeria underscores the necessity of examining how audit characteristics constrain or enable such behaviour.

The industrial goods sector in Nigeria plays a crucial economic role, covering cement, building materials, chemicals, and manufacturing components essential for national infrastructure and development. Given the sector's capital intensity and exposure to fluctuating input costs, investors rely heavily on credible earnings to assess corporate stability. Weak earnings quality can therefore have significant implications for investment inflows, firm valuation, and sectoral competitiveness. Strong audit oversight is essential for safeguarding the integrity of earnings in this environment, as it promotes transparency and mitigates the risk of financial reporting manipulation (Ibadin & Ijeoma, 2021). Consequently, audit firm tenure, acting as a key audit attribute, may meaningfully influence earnings predictability and earnings persistence—two critical indicators of earnings quality.

Moreover, earnings quality in Nigeria is shaped by several contextual factors, including macroeconomic volatility, regulatory enforcement strength, competition within the audit market,

and corporate governance structures (Abata, 2015). However, audit firm attributes remain a foundational element, forming the primary line of defence against accounting irregularities. During periods of economic uncertainty or weak internal governance, the independence and competence of external auditors become even more consequential. This highlights the need to critically evaluate how audit firm tenure, as an attribute with potential benefits and risks, impacts earnings quality in Nigeria's quoted industrial goods companies. In such circumstances, companies audited by firms with strong audit characteristics may exhibit higher earnings credibility, whereas those with weaker audit structures may be more susceptible to earnings manipulation.

Statement of the Problem

The ideal situation is that audit firms, through their independence, competence, and objective oversight, should enhance the credibility of financial reporting and ensure high earnings quality that reflects the true economic performance of quoted industrial goods companies in Nigeria. However, in practice, persistent concerns over weak audit monitoring, prolonged auditor–client relationships, and the potential loss of auditor independence have contributed to declining earnings predictability and earnings persistence, creating opportunities for earnings manipulation and reduced transparency. These weaknesses undermine investor confidence, distort resource allocation, and threaten the stability of the industrial goods sector, which relies heavily on credible financial information for long-term investment decisions. Although previous studies have examined audit quality and financial reporting in Nigeria, findings remain inconclusive and often fail to isolate the specific influence of audit firm attributes—particularly audit firm tenure—on the different dimensions of earnings quality. This gap highlights the need for an empirical investigation focused on how audit firm tenure affects earnings predictability and earnings persistence among Nigeria's quoted industrial goods companies between 2013 and 2023.

Aim and Objectives of the Study

The main objective is to evaluate effect of audit firm's attributes on earnings quality of Quoted Industrial Goods Companies in Nigeria from 2013-2023. Hence, specific objectives are to:

- i. evaluate effect of audit firm tenure on earnings predictability of Quoted Industrial Goods Companies in Nigeria?
- ii. assess the effect of Audit firm tenure on earnings persistence of Quoted Industrial Goods Companies in Nigeria?

Research Questions

The following questions guide the study:

1. What is the effect of audit firm tenure on earning predictability of Quoted Industrial Goods Companies in Nigeria?
2. What is the effect of audit firm tenure on earnings persistence of Quoted Industrial Goods Companies in Nigeria?

Research Hypotheses

The following hypotheses were tested in the study;

H₀₁: Audit firm tenure has no significant effect on earnings predictability of Quoted Industrial Goods Companies in Nigeria.

H₀₂: Audit firm tenure has no significant effect on earnings persistence of Quoted Industrial Goods Companies in Nigeria.

Theoretical Review

The theoretical foundation for examining the effect of audit firm attributes particularly audit firm tenure on earnings quality is anchored on the Agency Theory by Jensen and Meckling (1976). Agency theory posits that managers (agents) may act in ways that do not align with the interests of shareholders (principals), thereby creating information asymmetry and increasing the likelihood of opportunistic earnings manipulation. External auditors serve as monitoring mechanisms designed to reduce this asymmetry and enhance the credibility of financial reports. Audit firm tenure becomes theoretically relevant because long-term auditor–client relationships can either improve audit quality through enhanced client-specific knowledge or weaken it due to the risk of auditor familiarity, complacency, and reduced professional skepticism. Proponents of the knowledge effect argue that longer tenures strengthen the auditor’s capacity to detect anomalies, thereby enhancing earnings predictability and persistence, which are key indicators of earnings quality.

Complementing agency theory is the Information Asymmetry Theory, which emphasizes how the unequal distribution of financial information between company insiders and external stakeholders can distort decision-making. High-quality audits serve as an information-bridging mechanism by validating the integrity, reliability, and continuity of reported earnings. In this context, audit firm tenure influences the degree to which audits mitigate information risk. Longer audit engagements enable auditors to develop deeper insights into a firm’s operational processes, accounting systems, and risk patterns, thereby improving their ability to enhance the informativeness of earnings. This theoretical linkage explains why prolonged auditor relationships may lead to more stable and predictable earnings streams, as confirmed by empirical findings that associate longer audit tenures with improved earnings persistence and predictability. Collectively, these theories highlight the critical role of audit firm attributes in strengthening the transparency and quality of financial reporting among quoted industrial goods companies in Nigeria.

Empirical Review

Empirical studies have extensively examined the relationship between audit firm tenure and earnings predictability, demonstrating mixed but insightful results. Bethitina (2015) found that audit firm tenure exerts a significantly positive influence on earnings quality among manufacturing share companies, suggesting that longer auditor–client relationships enhance the auditor’s understanding of the firm and improve the reliability of earnings forecasts. Similarly, Musa and Tobi (2019) reported that prolonged audit engagements strengthen the auditor’s capacity to identify inconsistencies that could undermine the predictability of earnings. In contrast, a study by Okolie and Izedonmi (2014) cautioned that excessively long audit tenures may increase the risk of auditor complacency, thereby reducing the value of audits in predicting future financial outcomes. Despite this divergence, most empirical studies affirm that increased audit firm tenure generally improves earnings predictability. However, few studies have focused specifically on quoted industrial goods companies in Nigeria, making it essential to investigate whether audit tenure continues to play a decisive role in improving earnings predictability in this sector.

Further empirical evidence has explored the effect of audit firm tenure on earnings persistence, which reflects the sustainability and stability of reported earnings over time. Bethitina (2015) again provided strong evidence showing that extended audit tenure positively influences earnings persistence by fostering improved auditor familiarity with a firm’s accounting systems and operational environment. Supporting this view, Egbunike and Abata (2016) found that auditors with long-term engagements are better equipped to detect earnings manipulations, thus enhancing

the durability of earnings figures from one period to the next. Conversely, Chi, Lisic, and Pevzner (2011) argued that while longer tenure initially strengthens audit quality, it may eventually reduce auditor independence, thereby weakening earnings persistence. Despite these concerns, the preponderance of empirical findings suggests that longer-tenured auditors generally contribute to more stable and persistent earnings patterns. Nonetheless, empirical studies targeting Nigeria's industrial goods sector remain limited, creating a clear need for sector-specific evidence to validate the hypothesized link between audit tenure and earnings persistence.

Method

This study adopted an ex-post facto research design. Ex-post facto research involves a systematic empirical investigation in which the researcher has no direct control over the independent variables because their manifestations have already occurred or are inherently not subject to manipulation. This design is appropriate for examining the effect of audit firm tenure on the earnings quality of quoted industrial goods companies in Nigeria over time. The study relied exclusively on secondary data, extracted from the audited financial statements and annual reports of listed industrial goods firms available on their corporate websites and the Nigerian Exchange Group (NGX) portal covering the period 2013–2023.

The population of the study consists of all thirteen (13) industrial goods companies listed on the Nigerian Exchange Group as at December 2023. However, due to incomplete and inconsistent financial disclosures from three (3) firms, the study employed a purposive sampling technique to select ten (10) companies with complete, reliable, and accessible financial information for the reference period. This sampling approach ensured the inclusion of firms with adequate longitudinal data necessary for robust panel analysis.

The study used secondary data sourced from annual reports, audited financial statements, and financial disclosures retrieved from the NGX website and the firms' individual websites. These documents provided information on audit tenure, audit firm size, audit fees, and earnings quality variables. Content analysis was employed to extract quantitative values from the financial statements for the eleven-year period.

Panel regression analysis was used to examine the relationship between audit firm attributes and earnings quality. Panel data methodology was selected because it provides more variability, reduces multicollinearity among variables, enhances degrees of freedom, and produces more efficient estimates. The analysis was performed using EViews 12. Both descriptive statistics and inferential analysis were conducted. Descriptive statistics were used to explain the trend, distribution, and characteristics of the data, while Panel Ordinary Least Squares (OLS) regression, along with fixed and random effects diagnostics, was employed to test the hypotheses. The decision rule was to reject the null hypothesis where the p-value is less than 0.05.

The economic model used in the study, drawn from earnings quality literature, is specified as:

Model Specification

$$EPSTit = \alpha + B_1ATit + \varepsilon it \dots\dots\dots 1$$

$$EPDit = \alpha + B_1ATit + \varepsilon it \dots\dots\dots 2$$

Where;

EQ = Earnings Quality

AT = Audit Tenure

EPD = Earning Predictability

EPST = Earning Persistence
 α = Constant of the regression'
 ε = Error term

Table 1: Variables Definition and Measurement

Variable	Measurement Method
Earnings Quality (EQ)	Residuals from the Modified Jones Model
Audit Tenure (AT)	Dichotomous: 1 if auditor–firm relationship is 1–3 years, 0 otherwise

Results

Descriptive statistics of focused variables.

Table 2: Descriptive Analysis Result

	EPD	EPST	AT
Mean	1.550818	2.376091	0.718182
Median	1.530000	2.175000	1.000000
Maximum	2.770000	6.660000	1.000000
Minimum	1.000000	0.740000	0.000000
Std. Dev.	0.234404	1.249033	0.451944
Skewness	1.646948	1.167627	-0.969944
Kurtosis	9.327010	4.063479	1.940792
Jarque-Bera	233.2037	30.17848	22.39000
Probability	0.000000	0.000000	0.000014
Sum	170.5900	261.3700	79.00000
Sum Sq.			
Dev.	5.989026	170.0490	22.26364
Observations	110	110	110

Source: *Researcher's Computation, 2024.*

Table 1 shows the descriptive statistics of earnings predictability (EPD), earnings persistence (EPST), and audit firm tenure (AT). Also, earnings predictability (EPD) has a mean of 1.55 while the minimum earnings predictability (EPD) in the observations is 2.77 and the maximum earnings predictability (EPD) is 1.00. The standard deviation of 0.234 shows the level at which the Earnings predictability (EPD) deviates from the mean. Furthermore, earnings persistence (EPST) has a mean of 2.376. It can be observed from table 4.1 that the minimum earnings persistence (EPST) in the observations is 6.66 and the maximum Earnings persistence (EPST) is 0.74. The standard deviation of 1.249 shows the level at which the earnings persistence (EPST) deviates from the mean. As revealed by the table, Audit firm tenure (AT) has a mean of 0.718 while the minimum audit firm tenure (AT) in the observations is 1.0 and the maximum audit firm tenure (AT) is 0.0. The standard deviation of 0.452 shows the level at which the audit firm tenure (AT) deviates from the mean.

Testing Hypothesis One

Table: Ordinary Least Square Regression Results of Model 1

Dependent Variable: EPD_t				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	1.538267	0.125332	12.27357	0.0000
AT_t	0.310118	0.093555	3.314800	0.0013
R-squared = 0.926156; Adjusted R-squared = 0.901424; F-statistic= 5.101030; Prob(F-statistic) = 0.002453; Durbin-Watson stat = 2.163802				

Source: *Researcher's Computation, 2024.*

Null Hypothesis One (H_{01}): Audit firm tenure has no significant effect on earnings predictability (EPD) of quoted industrial goods companies in Nigeria.

Decision on Hypothesis One: The *p-value* of audit firm tenure from the regression result as shown in Table 4.2 is 0.0013 while the *alpha value* is 0.05. However, since the *p-value* (0.0013) is less than the *alpha value* (0.05) at 5% level of significance, we therefore reject the null hypothesis one (H_{01}) and conclude that audit firm tenure has a significant effect on earnings predictability (EPD) of quoted industrial goods companies in Nigeria.

Testing of Hypothesis Two

Table 4: Ordinary Least Square Regression Results of Model 2

Dependent Variable: $ESPT_t$				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.009122	0.674303	0.013528	0.9892
AT_t	0.480598	0.098631	4.872693	0.0000
R-squared = 0.899150; Adjusted R-squared = 0.783937; F-statistic= 4.329162; Prob(F-statistic) = 0.006398; Durbin-Watson stat = 1.872454				

Source: *Researcher's Computation, 2024.*

Null Hypothesis Two (H_{02}): Audit firm tenure has no significant effect on earnings persistence (EPST) of quoted industrial goods companies in Nigeria.

Decision on Hypothesis Two: The *p-value* of audit firm tenure from the regression result as shown in Table 4.3 is 0.0000 while the *alpha value* is 0.05. However, since the *p-value* (0.000) is less than the *alpha value* (0.05) at 5% level of significance, we therefore reject the null hypothesis two (H_{02}) and conclude that audit firm tenure has a significant effect on earnings persistence (EPST) of quoted industrial goods companies in Nigeria.

Discussions of Findings

Audit Firm Tenure and Earnings Predictability of Quoted Industrial Goods Companies in Nigeria

The findings emanating from this study showed that audit firm tenure has positive relationship with earnings predictability of quoted industrial goods companies in Nigeria.

The positive relationship further shows that increase in audit firm tenure will lead to increase in earnings predictability of quoted industrial goods companies in Nigeria while decrease in audit firm tenure will lead to decrease in earnings predictability of quoted industrial goods companies in Nigeria. Also, the result of the hypotheses tested showed that audit firm tenure has significant effect on earnings predictability of quoted industrial goods companies in Nigeria. It can therefore be inferred that audit firm tenure has a positive and significant relationship with earnings predictability of quoted industrial goods companies in Nigeria. This result is supported by Bethitina. (2015) who found that audit firm tenure/period exerts significantly positive effect on earnings quality of manufacturing share companies.

Audit Firm Tenure and Earnings Persistence of Quoted Industrial Goods Companies in Nigeria

The findings emanating from this study indicated that audit firm tenure has positive relationship with earnings persistence of quoted industrial goods companies in Nigeria. The positive relationship further shows that increase in audit firm tenure will lead to increase in earnings persistence of quoted industrial goods companies in Nigeria while decrease in audit firm tenure will lead to decrease in earnings persistence of quoted industrial goods companies in Nigeria. Also, the result of the hypotheses tested showed that audit firm tenure has significant relationship with earnings persistence of quoted industrial goods companies in Nigeria. It can therefore be inferred that audit firm tenure has a positive and significant effect on earnings persistence of quoted industrial goods companies in Nigeria. This finding agrees with the finding of Bethitina. (2015) who established that audit firm tenure/period exerts significantly positive effect on earnings quality of manufacturing share companies.

Conclusion

The study concludes that audit firm tenure plays a crucial role in shaping the earnings quality of quoted industrial goods companies in Nigeria, as evidenced by its significant positive influence on both earnings predictability and earnings persistence. Longer audit tenures appear to enhance auditors' familiarity with client operations, improve the depth of audit procedures, and strengthen the credibility of reported earnings, thereby contributing to more reliable and consistent financial outcomes. Conversely, shorter audit tenures were associated with reduced earnings quality, suggesting that audit continuity supports deeper insight and more effective monitoring. These findings, supported by prior evidence such as Bethitina (2015), affirm that sustained auditor–client relationships can improve financial reporting reliability and provide greater assurance to stakeholders within the industrial goods sector.

Recommendations

1. Regulatory bodies and corporate boards should encourage appropriately structured long-term auditor–client relationships that enhance audit quality without compromising auditor independence.
2. Industrial goods companies should prioritize audit firms with proven track records of long-tenure engagements to strengthen earnings consistency and reinforce stakeholders' confidence in financial reporting.

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